PROFESSIONAL PROGRAMME

GROUP 2
PAPER 6

CORPORATE RESTRUCTURING, VALUATION & INSOLVENCY

PART I – CORPORATE RESTRUCTURING

PART II – VALUATION

PART III – INSOLVENCY, LIQUIDATION & WINDING UP

THE INSTITUTE OF
Company Secretaries of India
भारतीय कम्पनी सचिव संस्थान
IN PURSUIT OF PROFESSIONAL EXCELLENCE
Statutory body under an Act of Parliament
(Under the jurisdiction of Ministry of Corporate Affairs)

STUDY MATERIAL

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PROFESSIONAL PROGRAMME

CORPORATE RESTRUCTURING, VALUATION & INSOLVENCY

Restructuring is an established economic, social and political process. It occurs at different rates, at different times and in different places, taking some forward on the wave and leaving others behind in the wake. Globalisation, fast-moving technological change, and the driving role played by financial markets have all contributed to making today's economy one which accelerates change. Corporate restructuring is a permanent feature of this change and can take different forms such as amalgamation, merger or acquisition and takeover,

In terms of restructuring at company level, although there may be sector and/or company-specific driving forces behind and reasons for restructuring, companies always restructure to improve their performance and profitability. However, restructuring operations in private and public companies not only have an impact on economic and financial performance but also on the quantity and quality of employment, as well as on the environment.

There are a number of situations in which a business or a share or any other property may be required to be valued. Valuation is essential for strategic partnerships, mergers or acquisitions of shares of a company and/or acquisition of a business. The main objective in carrying out a valuation is to conclude a transaction in a reasonable manner without any room for any doubt or controversy about the value obtained by any party to the transaction.

The failure of some business plans is integral to the process of the market economy. When business failure takes place, the best outcome for society is to have a rapid renegotiation between the financiers, to finance the going concern using a new arrangement of liabilities and with a new management team. If this cannot be done, the best outcome for society is a rapid liquidation. When such arrangements can be put into place, the market process of creative destruction will work smoothly, with greater competitive vigor and greater competition. In this backdrop, Parliament enacted Insolvency and Bankruptcy Code, 2016.

In the light of above, this study material has been prepared to provide an understanding of Corporate Restructuring, Valuation and Insolvency which have direct bearing on the functioning of companies. The study material has been divided into three parts consisting of twenty-six study lessons. Part I dealing with Corporate Restructuring consists of Study Lessons I to XI and Part II dealing with Valuation consists of Study Lesson XII to XIII and whereas Part III dealing with Insolvency, Liquidation & Winding Up consists of Study Lesson XIV to XVI.

This study material has been published to aid the students in preparing for the Corporate Restructuring, Valuation and Insolvency paper of the CS Professional Programme. It has been prepared to provide basic understanding of the Corporate Restructuring, Valuation, Insolvency, Liquidation and winding Up which have a bearing on the conduct of corporate affairs. It is part of the educational kit and takes the students step by step through each phase of preparation stressing key concepts, principle, pointers and procedures.

The legislative changes made upto May 31, 2024 have been incorporated in the study material. In addition to Study Material students are advised to refer to the updations at the Regulator's website, supplements relevant for the subject issued by ICSI and ICSI Journal Chartered Secretary and other publications. Specifically, students are advised to read "Student Company Secretary" e-Journal which covers regulatory and other relevant developments relating to the subject, which is available at academic portal *https://www.icsi.edu/student-n/academic-portal/*. In the event of any doubt, students may contact the Directorate of Academics at **academics@icsi.edu**.

The amendments to law made upto 31st May of the Calendar Year for December Examinations and upto 30th November of the previous Calendar Year for June Examinations shall be applicable

Although care has been taken in publishing this study material yet the possibility of errors, omissions and/or discrepancies cannot be ruled out. This publication is released with an understanding that the Institute shall not be responsible for any errors, omissions and/or discrepancies or any action taken in that behalf.

PROFESSIONAL PROGRAMME

Group 2

Paper 6

CORPORATE RESTRUCTURING, VALUATION & INSOLVENCY

SYLLABUS

OBJECTIVE

To provide legal procedural and practical aspects of Corporate Restructuring Valuation Insolvency, Liquidation & Winding-up.

Level of Knowledge: Expert Knowledge

Detailed Contents

PART I : CORPORATE RESTRUCTURING (40 MARKS)

1. **Types of Corporate Restructuring:** ● Key definitions, Compromises, Arrangements, Mergers & Amalgamations ● Demergers & Slump Sale Business Sale ● Joint Venture, Strategic Alliance, Reverse Merger ● Disinvestment Financial Restructuring (Buy-back, Alteration & Reduction)
2. **Acquisition of Company/ Business:** ● Acquisition of Company ● Takeover of Listed Companies: Legal Framework, Process & Compliances
3. **Planning & Strategy:** ● Case Studies pertaining to Merger, Amalgamation, restructuring ● Studies of Judicial ● Planning relating to acquisitions & takeovers ● Protection of minority interestl Succession Planning ● Managing Family Holdings through Trust
4. **Process of M&A transactions:** ● Key Concepts of MBA ● Law & Procedure M&A Due Diligence ● MBA Valuation ● M&A Structure finalization ● Post transaction integration
5. **Documentation-Merger & Amalgamation:** ● Drafting of Scheme ● Drafting of Notice and Explanatory Statement ● Drafting of Application Petition
6. **Accounting in Corporate Restructuring: Concept and Accounting Treatment:** ● Methods of Accounting for Amalgamations AS-14/ IndAS 103 ● Treatment of Reserves, Goodwill ● Pre-Acquisition & Post-Acquisition Profit ● Accounting in Books of Transferor and transferee ● Merger and De-merger ● Acquisition of Business and internal Reconstruction
7. **Taxation & Stamp Duty aspects of Corporate Restructuring:** ● Capital Gain ● Set-off and carry forward under Income Tax Act ● Deemed Dividend ● Payment of Stamp Duty on scheme, payment of stamp duty on movable and immovable properties
8. **Regulation of Combinations:** ● Regulation of combinations under the Competition Act ● Kinds of combinations ● Exempted combinations ● Concept of relevant market and its importance ● Determination of combinations and any appreciable adverse effect ● Role of CCI
9. **Regulatory Approvals of Scheme:** ● From CCI, Income Tax, Stock Exchange, SEBI, RBI, RD, ROC, OL, Sector Regulators such as IRDA, TRAI, etc.

10. **Fast Track Mergers:** ● Small companies ● Holding and wholly owned companies

11. **Cross Border Mergers**

PART II : VALUATION (20 MARKS)

12. **Overview of Business Valuation:** ● Genesis of Valuation ● Need for Valuation ● Hindrances/ Bottlenecks in Valuation ● Business Valuation Approaches ● Principles of Valuation (Cost, Price and Value)

13. **Valuation of Business and Assets for Corporate Restructuring:** ● Type of Valuations ● Valuation Principles & Techniques for Merger ● Amalgamation, Slump Sale, Demerger ● Principles & Techniques of Reporting ● Relative Valuation and Swap Ratio

PART III : INSOLVENCY, LIQUIDATION & WINDING UP (40 MARKS)

14. **Insolvency:** ● Historical Background ● Pillars of IBC, 2016 [IBBI, IPA, IP, AA, IU] ● Key Definitions and Concepts ● Insolvency Initiation/Resolution under sections 7, 8 and 10

15. **Application for Corporate Insolvency Resolution Process:** ● Legal Provisions ● Procedure, Documentation ● Appearance, Approval

16. **Role, Functions and Duties of IP/ IRP/ RP:** ● Public announcement ● Management of affairs and operations of company as a going concern ● Raising of Interim Finance ● Preparation of Information Memorandum

17. **Resolution Strategies:** ● Restructuring of Equity & Debt ● Compromise & Arrangement ● Acquisition, Takeover & Change of Management ● Sale of Assets

18. **Convening and Conduct of Meetings of Committee of Creditors:** ● Constitution of Committee of Creditors ● Procedural aspects for meeting of creditors

19. **Preparation & Approval of Resolution Plan:** ● Contents of resolution plan ● Submission of resolution plan ● Approval of resolution plan

20. **Pre-Packaged Insolvency Resolution Process:** ● Governing Framework ● Eligibility for PPIRP ● Approval of Resolution Plan ● Closure of PPIRP

21. **Cross Border Insolvency:** ● International Perspective and Global Developments ● UNCITRAL Legislative Guide on Insolvency Laws ● US Bankruptcy Code, Chapter 11 reorganization ● Enabling provisions for cross border transactions under IBC

22. **Liquidation on or after failing of Resolution Plan:** ● Initiation of Liquidation ● Distribution of assets ● Dissolution of corporate debtor

23. **Voluntary Liquidation:** ● Procedure for Voluntary Liquidation ● Powers and duties of the Liquidator ● Completion of Liquidation

24. **Debt Recovery & SARFAESI:** ● Non-Performing Assets, Asset Reconstruction Company lsecurity Interest (Enforcement) Rules, 2002 ● Evaluation of various options available to bank-viz. SARFAESI, DRT, Insolvency Proceedings ● Application to the Tribunal/Appellate Tribunal

25 **Winding-up by Tribunal under the Companies Act, 2013:** ● Procedure of Winding-up by Tribunal ● Powers and Duties of the Company Liquidator ● Fraudulent preferences

26 **Strike Off and Restoration of Name of the Company and LLP:** ● Ways of striking off of companies ● Strike off by ROC Suo-Motu ● Strike off by way of Filing an Application by the Company ● Procedure of striking off of the name of the company by wayof an application to ROC ● Restoration of the company ● Appeal to NCLT for restoration of the name of the company ● Restoration of the LLP

ARRANGEMENT OF STUDY LESSONS

CORPORATE RESTRUCTURING, VALUATION & INSOLVENCY

GROUP 2 • PAPER 6

LESSON WISE SUMMARY

CORPORATE RESTRUCTURING, VALUATION & INSOLVENCY

PART I : CORPORATE RESTRUCTURING (40 MARKS)

Lesson 1: Types of Corporate Restructuring

Corporate Restructuring is an expression that connotes a restructuring process undertaken by business enterprise. It is the process of redesigning one or more aspects of a company. Hence, Corporate Restructuring is a comprehensive process by which a company can consolidate its business operations and strengthen its position for achieving its short-term and long-term corporate objectives. A business may grow over time as the utility of its products and services is recognized, but it is a long drawn process. It may also grow through an inorganic process, symbolized by an instantaneous expansion in work force, customers, infrastructure resources and thereby an overall increase in the revenues and profits of the entity. Corporate restructuring is the process of significantly changing a company's business model, management team or financial structure to address challenges and increase shareholder value. Corporate restructuring is an inorganic growth strategy. Often, restructuring plans are necessary simply to meet the constantly changing demands of technology that competitors are embracing, survive a currently adverse economic weather, or poise the corporation to move in an entirely new trend. Some of common ways to carry our Restructuring process are mergers/amalgamations, acquisitions/takeovers, divestitures/demergers, slump sale, business sale; joint venture, strategic alliance, financial restructuring (buy-back, alteration & reduction). This lesson covers the concept of corporate restructuring, its importance, historical background, available tools and emerging trends in restructuring strategies, etc.

Lesson 2: Acquisition of Company/ Business

Takeovers and acquisitions are common occurrences in the business world. In some cases, the terms takeover and acquisition are used interchangeably, but each has a slightly different connotation. A takeover is a special form of acquisition that occurs when a company takes control of another company without the acquired firm's agreement. Takeovers that occur without permission are commonly called hostile takeovers. Acquisitions, also referred to as friendly takeovers, occur when the acquiring company has the permission of the target company's Board of directors to purchase and takeover the company. Acquisition refers to the process of acquiring a company at a price called the acquisition price or acquisition premium. The price is paid in terms of cash or acquiring company's shares or both. This lesson covers the meaning, concept, objectives of takeover, procedural requirements as to takeover of listed/ unlisted companies, takeover defenses etc.

Lesson 3: Planning & Strategy

Strategies play an integral role when it comes to merger and acquisition. A sound strategic decision and procedure is very important to ensure success and fulfilling of expected desires. Every company has different culture and follows different strategies to define their merger. There are various strategic reasons for companies to consider making an acquisition and a successful takeover can help companies achieve their strategic objectives as well as increase cost effectiveness within the business. The process of merging with another company or acquiring a company is complex. In addition to the legal ramifications, companies must be aware of the potential tax implications as well as ensuring that the terms of the deal benefit both parties. Often companies rely on lawyers and professionals to negotiate on their behalf in order to obtain the best possible deal within the framework of the applicable laws. In order to make a merger work, it is pertinent to have a sound strategic planning so that maximum benefit is taken out from the merger. The company doing the acquisition must evaluate the performance, market position, cash flows, future opportunities, technology, regulatory issues of the target company to fix the right price for the deal. It is important to identify synergy between the two companies. This lesson covers the planning and strategy, purchase and protection of minority interests, succession planning and the funding process for mergers and acquisitions.

Lesson 4: Process of M&A transactions

Process of Merger & Acquisition involves corporate control, strategy, corporate finance and management. It involves consolidation of companies i.e. business combination, division and demerger of two or more companies. The merger and amalgamation requires various regulatory approvals and procedures as enunciated in the Companies Act, 2013. Merger being a strategy, it has to be object oriented and it dwells upon the concept of synergy, which means value of two companies together will be more than of an individual company. Merger & Acquisition could be by way of business purchase/share purchase agreement or by way of sanction of Scheme of Arrangement through the court route. In a sense, in the case of merger through a court route, once the scheme is sanctioned by the court/tribunal after due process of law and the scheme is filed with the Registrar of Companies, it is irreversible; it carries the stamp of final approval by a judicial authority and is acceptable to the public, shareholders, stakeholders, registering authority.

This lesson covers the regulatory framework, interpretations of provisions in the Companies Act relating to merger/amalgamation, different approvals, steps involved, integration not only of the financials, accounting and software but also of the human and cultural integration and judicial pronouncements, etc

Lesson 5: Documentation – Merger & Amalgamation

Documentation is an important aspect in fulfilment of legal requirements and obligations in merger and amalgamation for an effective and successful venture. The quantum of such obligations will depend upon the size of company, debt structure and profile of its creditors, compliances under the corporate laws, controlling regulations, etc. In all or in some of these cases legal documentation would be involved. If foreign collaborators are involved, their existing agreements would need a mandatory documentation to protect their interests if their terms and conditions so require. Secured debenture holders and unsecured creditors would also seek legal protection to their rights with new or changed management of the amalgamating company. Regulatory bodies like the RBI, Stock Exchanges, the SEBI, etc. would also ensure adherence to their respective guidelines, regulations or directives. In this way, while drafting the scheme of merger and amalgamation the transferor and transferee would have to ensure that they meet legal obligations in all related and requisite areas. Company Secretary being an expert in drafting has an edge over others, to grab the ample opportunities available in this area of work. The study lesson covers the documentation involved, points to be factored while drafting such documents and general provisions under the Companies Act, 2013 and NCLT Rules with respect to mergers and amalgamations.

Lesson 6: Accounting in Corporate Restructuring – Concept and Accounting Treatment

Accounting for corporate restructuring is dealt with accounting standards. Accounting standard (AS-14) prescribes for accounting and disclosure requirements of merger and acquisition. According to AS14 amalgamation may be either in the nature of merger or in the nature of purchase. IND-AS 103 deals with meaning of business, business combination. According to IND-AS 103, business combination is accounted applying acquisition method. This lesson covers various developments happening in M&A accounting, concepts of demerger and internal reconstruction and also difference between IND-AS 103 and AS-14.

Lesson 7: Taxation & Stamp Duty aspects of Corporate Restructuring

Tax planning in cases of amalgamation of companies is perhaps the most vital aspect of decision-making involved in framing of the scheme of amalgamation. A company planning a merger or a takeover, need to do intensive tax planning before finalising the deal to get the maximum tax concession and benefits in the deal. In India, law provides for ample benefits in the form of various provisions to companies going in for amalgamation. Since a merger or demerger inevitably entails some transfer of property, movable or immovable, it attracts the imposition of stamp duty which is essentially a form of revenue for the government arising out of taxation of various transactions governed under the Indian Stamp Act, 1899. The exposition of stamp duty is a vital aspect because it could substantially increase the costs of a merger deal. In corporate restructuring through amalgamation and merger, stamp duty planning assumes a significant role and all out efforts are made to pay as less a duty on such amalgamations as possible and yet proceed with the acquisitions through mergers and amalgamations. The incidence of stamp duty is an important consideration in the planning of any merger. This lesson covers the regulatory aspects and court decisions as to the stamp duty aspects of mergers, tax advantage on mergers, etc.

Lesson 8: Regulation of Combinations

According to Section 5 of the Competition Act, 2002, combination as (i) acquisition of control, shares, voting rights or assets; or (ii) acquiring of control by a person over an enterprise when such person has already direct or indirect control over another enterprise engaged in production, distribution or trading of a similar or identical or substitutable goods or provision of a similar or identical or substitutable service; or (iii) merger or amalgamation. A combination beyond the prescribed thresholds is regulated under the Act. Section 6 declares a combination as void if it causes or is likely to cause an adverse effect on competition within the relevant market in India.

This lesson covers Regulation of combinations under the competition Act, Kinds of combinations, Exempted combinations, Concept of relevant market and its importance, determination of combinations and any appreciable adverse effect, Role of CCI. It is of utmost importance for Company Secretaries to have thorough knowledge of the precedents, orders and decisions made by the overseas contemporary authorities as well as the leading decisions of the Commission.

Lesson 9: Regulatory Approvals of Scheme

Merger or amalgamation of companies involves various issues including the regulatory approvals. These regulatory approvals are to be obtained not only from the sector in which the company is operating (for example in case of merger of two banks, RBI's approval is needed) but from other departments like Income Tax, SEBI, CCI, RD, ROC, OL and Sector Regulators such as IRDA, TRAI, etc. The merger and takeover involve various issues and compliance depending upon the nature of business of the company and sector under which it is operating. From this point of view, it becomes necessary for a student of professional programme to know various procedural aspects, regulatory approvals required to complete these events. It is to be noted in corporate world such professionals having an expertise in these procedural aspects are in great demand. This lesson covers the various approval required in case of merger/ amalgamation, acquisition/ takeovers, etc.

Lesson 10: Fast Track Mergers

Fast track mergers have been introduced in order to encourage small companies to grow and expand. Small companies should not be dissuaded from entering into mergers just because the process is long, tedious and complicated. Introduction, applicability and procedure for Fast track mergers Covers under Section 233 of the Companies Act, 2013, Rule 25 of Companies (Compromises, Arrangements and Amalgamations) Rules, 2016. Company Secretary plays an important role in the restructuring process and often advises his/her clients as to the procedure to be adopted, forms to be filed, etc. Hence, it is important for them to learn the basic concepts of what is a fast track merger, to whom does it apply, how can it be invoked, what are the requisite steps and which forms are required to be filed. This lesson covers about concept of fast track merger, procedure involved in fast track merger, etc.

Lesson 11: Cross Border Mergers

A company in one country can be acquired by an entity (another company) from other countries. The local company can be private, public, or state-owned company. In the event of the merger or acquisition by foreign investors referred to as cross-border merger and acquisitions will result in the transfer of control and authority in operating the merged or acquired company. Assets and liabilities of the two companies from two different countries are combined into a new legal entity in terms of the merger, while in terms of acquisition, there is a transformation process of assets and liabilities of local company to foreign company (foreign investor), and automatically, the local company will be affiliated. Since the cross-border M&As involve two countries, according to the applicable legal terminology, the state where the origin of the companies that acquire (the acquiring company) in other countries refer to as the Home Country, while countries where the target company is situated refers to as the Host Country. Section 234 of the Companies Act, 2013 and Rule 25A of the Companies (Compromises, Arrangements and Amalgamation) Rules, 2016 which provide for the basic legal framework involved in cross border mergers is discussed. This lesson covers concept of cross border mergers, legal framework surrounding cross border mergers, concepts of inbound and outbound mergers, risks and benefits associated with a cross border merger, etc.

PART II : VALUATION (20 MARKS)

Lesson 12: Overview of Business Valuation

Valuation is a process of appraisal or determination of the value of certain assets, i.e., tangible or intangible, securities, liabilities and a specific business as a going concern or any company listed or unlisted or company undergoing liquidation or other forms of organization, partnership or proprietorship. 'Value' is a term signifying the material or monetary worth of a thing, which can be estimated in terms of medium of exchange. In other words, it is an assessment resulting in an expression of opinion rather than arithmetical exactness. Business valuation requires a working knowledge of a variety of factors, and professional judgment and experience. This includes recognizing the purpose of the valuation, the value drivers impacting the subject company, and an understanding of industry, competitive and economic factors, as well as the selection and application of the appropriate valuation approach (es) and method(s). This lesson covers genesis, Principles and need of Valuation, Process of valuation and Business Valuation Approaches.

Lesson 13: Valuation of Business and Assets for Corporate Restructuring

Valuation models are used to determine the true value of a business mostly by financial market participants. Business valuation can be for the entire company or a part of the operations of a company. There are tools and methods used for valuation. Usually the valuation is done by analysing the financial statements, the cash flows and other market factors. Valuation involves financial modelling. This financial model can be different for different entities, as because one financial model for an industry may not be suitable for another industry and the choice of model to use for the industry is subjective. An important aspect in the merger/amalgamation/takeover activity is the valuation aspect. The method of valuation of business, however, depends to a great extent on the acquisition motives. The acquisition activity is usually guided by strategic behavioural motives. This lesson covers Business Valuation and its types, Circumstances when valuation becomes essential, Method of Valuation, Valuation for Slump Sale and Principles and techniques of Reporting.

PART III: INSOLVENCY, LIQUIDATION & WINDING-UP

Lesson 14: Insolvency

The Insolvency and bankruptcy Code, 2016 is one of the biggest economic reforms which provides a uniform and comprehensive insolvency legislation covering corporates, partnerships and individuals (other than financial firms). The Code gives both the creditors and debtors the power to initiate proceeding. It has helped India achieve a historic jump in the ease of doing business rankings by consolidating the law and providing for resolution of insolvencies in a time-bound manner. The objective of the Insolvency and Bankruptcy Code is to consolidate and amend the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner. An effective legal framework for timely resolution of insolvency and bankruptcy will not only encourage entrepreneurship but will also improve Ease of Doing Business, and facilitate more investments leading to higher economic growth and development. This study lesson has made an endeavour to focus on key aspects of insolvency, like, Pillars of IBC, 2016; Key Definitions and Concepts; Insolvency Initiation / Resolution; Regulatory framework governing Insolvency in various foreign countries etc.

Lesson 15: Application for Corporate Insolvency Resolution Process

The Insolvency and Bankruptcy Code, 2016 provides a simple test to initiate corporate insolvency resolution process. The Code adopts a default-based test for initiating the corporate insolvency resolution process. A default based test for initiating the insolvency resolution process permits early intervention when the corporate debtor shows early signs of financial distress. Early recognition of financial distress is very important for timely resolution of insolvency. In corporate insolvency resolution process, the financial creditors assess the viability of debtor's business and the options for its revival and rehabilitation. If the corporate insolvency resolution process fails or the financial creditors decide that the business of the debtor cannot be carried on in a profitable manner and it should be wound up, the debtor's business undergoes the liquidation process. Since Corporate Insolvency Resolution Process holds paramount significance, this study lesson throws ample light on the following key areas- Persons who may Initiate Corporate Insolvency Resolution Process; Financial and Operational Creditor; Operational debt etc.

Lesson 16: Role, Functions and Duties of IP / IRP / RP

The Insolvency and Bankruptcy Code, 2016 (Code) provides a market process, popularly known as called corporate insolvency resolution process (CIRP), for time bound revival of viable corporate debtors (CD) and closure of unviable ones. An insolvency professional (IP) is a key driver of CIRP - he acts as interim resolution professional (IRP) in the initial days of CIRP and then as resolution professional (RP) till its completion. He runs the operations of the CD as going concern and assists the stakeholders to find out the best resolution plan, while protecting and preserving the value of assets of the CD and ensuring compliance with all the applicable laws to the business of the CD and the CIRP. The law facilitates and empowers the IP to discharge his responsibilities effectively. Insolvency professionals play a vital role in the insolvency and bankruptcy resolution process as envisaged under IBC. In view of the above, this study lesson has made an attempt to explore the critical facets, like, Definitions in the Insolvency and Bankruptcy Code, 2016; Enrolment and Registration of Insolvency Professionals; Functions and Obligations of Insolvency Professionals etc

Lesson 17: Resolution Strategies

The legislative framework in India for insolvency and bankruptcy proceedings provides for a wide range of resolution measures, viz. re-organisation by way of a merger or amalgamation, acquisition of control and change of management, demerger, slump sale and reconstruction or financial, capital and business/ operational restructuring and as such a resolution strategy may consist of one or more of such measures and/or any measure other than the said measures. Failure to reach an understanding/ resolution with the creditors under the Code could lead to liquidation of the corporate debtor. The procedure for restructuring encompasses schemes of mergers, amalgamations, demergers, transfer/ sale of assets, restructuring of capital by way of cancellation/ delisting or any other modification in share capital, and restructuring of debts by ways of satisfaction or modification of security charge/ interest as suggested in Regulation 37 of the CIRP Regulations by way of which the liabilities of the distressed companies can be restructured and the state of insolvency can be resolved. In the event of initiation of a Corporate Insolvency Resolution Process against the Corporate Debtor under IBC 2016, the Resolution Professional shall invite resolution plans from the prospective resolution applicants, subject to the compliance of the conditions as laid down under the IBC, 2016 read with CIRP regulations. This study lesson focuses on key topics like, Organisational Restructuring, Financial Restructuring, Debt restructuring, Formal Restructuring and Insolvency Proceedings etc.

Lesson 18: Convening and Conduct of Meetings of Committee of Creditors

Committee of Creditors is a committee typically consisting of the financial creditors of the Corporate Debtor. It is the supreme decision-making body in a Corporate Insolvency Resolution Process (CIRP). Decisions regarding the administration of the corporate debtor are taken at the meetings of the Committee, based on a requisite vote of the members. It is responsible for giving approval to the IRP/ RP to carry out actions that might affect the CIRP. Section 21 and 24 of the Insolvency and Bankruptcy Code, 2016 make provisions relating to the committee of creditors. Section 21 deals with the constitution of committee of creditors while section 24 prescribes the modalities for the meeting of the committee of creditors. Section 28 of the Code lists out certain actions that may be taken by the resolution professional only with the prior approval of the committee of creditors by a vote of 66 per cent of the voting shares. Thus, in light of the soaring importance of the Committee of Creditors, this study lesson has laid emphasis on various elements of the Committee of Creditors; Exclusion of Related Party; Authorized Representative etc.

Lesson 19: Preparation & Approval of Resolution Plan

The Insolvency and Bankruptcy Code, 2016 (Code) aims at resolving the woes of insolvent companies through the corporate insolvency resolution process (CIRP), wherein the assets or business of the corporate debtor are transferred as a going concern to the most eligible party approved by the Committee of Creditors. Such an eligible party is willing to take up the management of the Corporate Debtor as well as to service its debts. The parties that are willing to take over the corporate debtor are called resolution applicants and they participate in the CIRP by submitting a document called a resolution plan. It is a comprehensive document which covers, inter alia, overview of the eligible party, how does the party plan to take over the corporate debtor, debt repayment schedule etc. This study lesson encompasses the vital components of the Insolvency and Bankruptcy Code (Amendment) Act, 2018, such as, an undischarged insolvent; wilful defaulter; related party etc.

Lesson 20: Pre-Packaged Insolvency Resolution Process

Section 54A to 54P of the Insolvency and Bankruptcy Code, 2016 ('Code') read with the Insolvency and Bankruptcy Board of India (Pre-packaged Insolvency Resolution Process) Regulations,2021 lays down the provisions of a pre-packaged insolvency resolution process with respect to its initiation, manner of carrying out the process, appointment of resolution professional, termination etc. It consolidates the benefit of both formal and informal proceedings of resolution, thus broadening the options for stakeholders and enables faster resolution as the corporate debtor can prepare a settlement plan or resolution plan with the creditors before going to NCLT. Pre-packaged Insolvency Resolution Process reduced burden on NCLT due to out of court settlements and provide relief to promoters and corporate debtors. It allows the corporate debtor retain control till a settlement is reached with the creditors. This study lesson throws light on governing framework and approval resolution plan etc.

Lesson 21: Cross Border Insolvency

Cross-border insolvency (sometimes called international insolvency) regulates the treatment of financially distressed debtors where such debtors have assets or creditors in more than one country. In recent times, the number of cross-border insolvency cases has increased significantly. The increasing frequency of cross-border insolvencies reflects the continuing expansion of global trade and investment. In its current form, the Insolvency and Bankruptcy Code contains only two provisions that may possibly enable and assist the liquidator with respect to a company having assets in a foreign jurisdiction. Section 234 of the Code allows the union government to enter into reciprocal agreements with other countries to enforce the provisions of the Code. Section 235 envisages a 'letter of request' by the liquidator for action on the assets of the company situated in another country. However, there must exist a reciprocal arrangement with such country. It is important to appreciate that the Code does not envisage the adoption of the UNCITRAL Model law or any cross-border insolvency regime. This study lesson covers enabling provisions of cross border insolvency under the Code.

Lesson 22: Liquidation on or after failing of Resolution Plan

Sections 33 to 54 in Chapter III of Part II of the Insolvency and Bankruptcy Code, 2016 lays down the law relating to liquidation process for corporate persons. An attempt is first made to resolve the insolvency of corporate debtor through corporate insolvency resolution process laid down in Chapter II of Part II of the Code. The provisions relating to liquidation in Chapter III of Part II of the Code comes into effect if the attempts to resolve corporate insolvency under Chapter II of the Code fail. A corporate debtor may witness liquidation under the following scenarios such as where the Adjudicating Authority does not receive a resolution plan, where the Adjudicating Authority rejects the resolution plan, where, at any time before confirmation of resolution plan, the committee of creditors resolve to liquidate corporate debtor and where the corporate debtor violates the terms of the resolution plan. This study lesson covers initiation of liquidation, distribution of assets, dissolution of corporate debtor etc.

Lesson 23: Voluntary Liquidation

A corporate person who intends to liquidate itself voluntarily and has not committed any default may initiate voluntary liquidation proceedings under the provisions of Chapter V of Part II of the Insolvency and Bankruptcy Code, 2016. The Insolvency and Bankruptcy Board of India has made the Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations, 2017 to regulate the voluntary liquidation of corporate persons. This study lesson made an endeavour to explore various important angles, like, Procedural requirements; Conditions for voluntary liquidation proceedings of corporate person registered as company; Requirement of notification etc.

Lesson 24: Debt Recovery & SARFAESI

The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 enacted with a view to regulate securitisation and reconstruction of financial assets and enforcement of security interest and for matters connected therewith or incidental thereto. The Act enables the banks and financial institutions to realise long-term assets, manage problems of liquidity, asset liability mismatch and improve recovery by exercising powers to take possession of securities, sell them and reduce non- performing assets by adopting measures for recovery or reconstruction. The said Act further provides for setting up of asset reconstruction companies which are empowered to take possession of secured assets of the borrower including the right to transfer by way of lease, assignment or sale and realise the secured assets and take over the management of the business of the borrower. This study lesson covers non-performing assets, Asset Reconstruction Companies, Enforcement of security interest by creditors, Debt Recovery, Debt Recovery Tribunals (DRT) etc.

Lesson 25: Winding-up by Tribunal under the Companies Act, 2013

Winding up is a means by which the dissolution of a company is brought about. The main purpose of winding up of a company is to realize the assets and pay the company's debts expeditiously and fairly in accordance with the law. Iif any surplus is left, it is distributed among the members in accordance with their rights. The entire procedure for bringing about a lawful end to the life of a company is divided into two stages i.e., 'winding up' and 'dissolution'. Winding up is the first stage in the process whereby assets are realised, liabilities are paid off and the surplus, if any, distributed among its members. Dissolution is the final stage whereby the existence of the company is withdrawn by the law. Dissolution brings about an end to the legal entity of the company. This study lesson covers procedure of winding up by Tribunal under the ComaniesAct,2013.

Lesson 26: Strike Off and Restoration of Name of the Company and LLP

A company can be struck off by Suo moto by the ROC under Section 248(1) of the Act; or an application by the company for removal of name/ strike off of company under Section 248(2) of the Companies Act. A company which is undergoing the process of 'Striking Off' either voluntarily or by an action of the ROC is given the status as 'Striking Off'. The provisions of Sections 248 to 252 of the Companies Act, 2013 read with Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016 deal with the removal of names of companies from the Register of Companies. This study lesson covers circumstances under which name of the company Struck off from the Register, circumstances under which name of the LLP is Struck off from the Register, Procedure for Striking off the Name and Restoration of the Name.

CONTENTS

PART I

CORPORATE RESTRUCTURING

LESSON 1

TYPES OF CORPORATE RESTRUCTURING

LESSON 2

ACQUISITION OF COMPANY/BUSINESS

LESSON 3

PLANNING & STRATEGY

LESSON 4

PROCESS OF MERGER AND ACQUISITION TRANSACTIONS

LESSON 5

DOCUMENTATION – MERGER & AMALGAMATION

LESSON 6

ACCOUNTING IN CORPORATE RESTRUCTURING: CONCEPT AND ACCOUNTING TREATMENT

LESSON 7

TAXATION & STAMP DUTY ASPECTS OF CORPORATE RESTRUCTURING

LESSON 8

REGULATION OF COMBINATIONS

LESSON 9

REGULATORY APPROVALS OF SCHEME

LESSON 10

FAST TRACK MERGERS

LESSON 11

CROSS BORDER MERGERS

PART II

VALUATION

LESSON 12

OVERVIEW OF BUSINESS VALUATION

LESSON 13

VALUATION OF BUSINESS AND ASSETS FOR CORPORATE RESTRUCTURING

PART III

INSOLVENCY, LIQUIDATION & WINDING-UP

LESSON 14

INSOLVENCY

LESSON 15

APPLICATION FOR CORPORATE INSOLVENCY RESOLUTION PROCESS

LESSON 16

ROLE, FUNCTIONS AND DUTIES OF INSOLVENCY PROFESSIONAL, INTERIM RESOLUTION PROFESSIONAL AND RESOLUTION PROFESSIONAL

LESSON 17

RESOLUTION STRATEGIES

LESSON 18

CONVENING AND CONDUCT OF MEETINGS OF COMMITTEE OF CREDITORS

LESSON 19

PREPARATION & APPROVAL OF RESOLUTION PLAN

LESSON 20

PRE-PACKAGED INSOLVENCY RESOLUTION PROCESS

LESSON 21

CROSS BORDER INSOLVENCY

LESSON 22

LIQUIDATION ON OR AFTER FAILING OF RESOLUTION PLAN

LESSON 24

DEBT RECOVERY & SARFAESI

LESSON 25

WINDING-UP BY TRIBUNAL UNDER THE COMPANIES ACT, 2013

LESSON 26

STRIKE OFF AND RESTORATION OF NAME OF THE COMPANY AND LLP

PART I

CORPORATE RESTRUCTURING

Types of Corporate Restructuring

Lesson 1

KEY CONCEPTS

■ Corporate Restructuring ■ Amalgamation ■ Merger ■ Takeover

Learning Objectives

To understand:

- Types of Restructuring
- The Concept of Corporate Restructuring
- Types of Mergers
- The Concept of Merger and Acquisition in India
- Legal Framework of Corporate Restructuring
- Reduction of Capital and Scheme of Compromise and Arrangement
- Buy-Back Procedure for Listed Securities

Lesson Outline

- Meaning of Corporate Restructuring
- Historical Background
- Need & Scope of Corporate Restructuring
- Various Modes of Restructuring
- Commonly applied tools of Corporate Restructuring
- Planning, formulation and execution of various Restructuring Strategies
- Financial Restructuring
- Reduction of capital
- Buy-back
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

- Companies Act, 2013
- The Companies (Compromises, Arrangements and Amalgamations) Rules, 2016
- The National Company Law Tribunal Rules, 2016
- Foreign Exchange Management Act, 1999
- Competition Act, 2002

INTRODUCTION

There are primarily two ways of growth of business organization, i.e. organic and inorganic growth.

Organic growth is through internal strategies, which may relate to business or financial restructuring within the organization that results in enhanced customer base, higher sales, increased revenue, without resulting in change of corporate entity.

Inorganic growth provides an organization with an avenue for attaining accelerated growth enabling it to skip few steps on the growth ladder. Restructuring through mergers, amalgamations etc., constitute one of the most important methods for securing inorganic growth.

Growth can be organic or inorganic

A company is said to be growing organically when the growth is through the internal sources without change in the corporate entity. Organic growth can be through capital restructuring or business restructuring.

Inorganic growth is the rate of growth of business by increasing output and business reach by acquiring new businesses by way of mergers, acquisitions and take-overs and other corporate restructuring strategies that may create a change in the corporate entity.

Mergers and Acquisitions (M&A) offers an alternative to organic growth for buyers seeking to achieve their strategic goals, while offering sellers the option to cash in or share the risks and rewards of a newly formed business. A company may grow either by internal expansion or by external expansion. For internal expansion, a company grows gradually over time in the normal course of business. Acquisitions are part of corporate restructuring, or inorganic growth, so companies are looking for opportunities to grow outside rather than keep profits in-house. Indian companies have often outperformed their foreign counterparts in corporate restructuring both within and outside their borders.

The business environment is rapidly changing with respect to technology, competition, products, people, geographical area, markets, customers. It is not enough if companies keep pace with these changes but are expected to beat competition and innovate in order to continuously maximize shareholder value. Inorganic growth strategies like mergers, acquisitions, takeovers and spinoffs are regarded as important engines that help companies to enter new markets, expand customer base, cut competition, consolidate and grow in size quickly, employ new technology with respect to products, people and processes. Thus, the inorganic growth strategies are regarded as fast track corporate restructuring strategies for growth

Corporate Restructuring is an expression that connotes a restructuring process undertaken by business enterprise. It is the process of redesigning one or more aspects of a company. Hence, Corporate Restructuring is a comprehensive process by which a company can consolidate its business operations and strengthen its position for achieving its short-term and long-term corporate objectives. A business may grow over time as the utility of its products and services is recognized, but it is a long drawn process. It may also grow through an inorganic process, symbolized by an instantaneous expansion in work force, customers, infrastructure resources and thereby an overall increase in the revenues and profits of the entity.

Restructuring as per Oxford dictionary means reorganization of a company with a view to achieve greater efficiency and profit, or to adapt to a changing market. According to Peter F Drucker, the management guru, the greatest change in corporate culture and the way business is being conducted, is the strategic intervention and relationship based not on ownership, but on partnership. Corporate restructuring play a major role in enabling enterprises to achieve economies of scale, global competitiveness, right size, reduction of operational costs and administrative costs. The process of reorganizing one or more aspects of the business of a company or financial structure for increasing its efficiency and profitability is known as corporate restructuring. It is a strategic tool used by the corporate houses to boost value to the organization as well as to the investors. The need for reorganizing a company may be felt due to a number of different factors such as to make the company more competitive, to overcome a currently adverse economic climate, or for moving towards an entirely new direction. The process of corporate restructuring essentially involves significant reorganization of assets and liabilities of the organization so as to conduct the business operations in an efficient, effective and competitive manner with the underlying objective of improving the quality and quantity of the future cash flow streams and thereby increasing the organization's market share, brand power, and synergies. In a nutshell, corporate restructuring is a comprehensive process by which a company can consolidate its business operations and strengthen its financial position for achieving its short-term and long-term corporate objectives.

> Corporate restructuring is the process of significantly changing a company's business model, management team or financial structure to address challenges and increase shareholder value. Corporate restructuring is an inorganic growth strategy.

On the other hand, "Amalgamation" as the merger of one or more companies with another company, or the merger of two or more companies to form one company. In the case of *Religare Finvest Limited {Appellant(S)} vs. State of NCT of Delhi & Anr. {respondent(s)}, Criminal Appeal No(s). 2242 of 2023 with Criminal Appeal No(s). 2243 of 2023, judgement dated September 11, 2023,* Hon'ble Supreme Court reliance placed in the case of *M/s. General Radio & Appliances Co. Ltd. vs. M.A. Khader (dead)* by *LR's* (1986 (2) SCR 607), where in Supreme Court held that after the amalgamation of two companies, the transferor company ceases to have any entity, and the amalgamated company acquires a new status, and it is not possible to treat the two companies as partners or jointly liable in respect of their liabilities and assets.

Further the Apex Court observed that according to Stroud's Judicial Dictionary of Words and Phrases (9th edition), "amalgamation" is *"welding or blending of two or more concerns into one."* It also states that *"where there the companies concerned retain separate entities, there is no amalgamation"*. Black's Law Dictionary, Eleventh Edition defines amalgamation as the *"act of combining or uniting; consolidation < amalgamation of two small companies to form a new corporation >..."* The Companies Act, 2013 does not contain any express definition of amalgamation; it rather outlines and regulates the procedure for amalgamation and spells out its legal effect, which results in extinguishment of the corporate identity of the transferor company [read, in this case, LVB]. In *Walker's Settlement* 1935 (1) Ch. D. 567., the term'amalgamation' is defined as:

"The word 'amalgamation' has no definite legal meaning. It contemplates a state of things under which 2 companies are so joined as to form a third entity or one company is absorbed into and blended with another company."

In the Case of *Principal Commissioner of Income Tax (Central) – 2 vs. M/S. Mahagun Realtors (P) Ltd* (*Arising out of special leave petition (c) no. 4063 of 2020) Judgement dated April 05, 2022,* Hon'ble Supreme Court inter alia observed that amalgamation, thus, is unlike the winding up of a corporate entity. In the case of amalgamation, the outer shell of the corporate entity is undoubtedly destroyed; it ceases to exist. Yet, in every other sense of the term, the corporate venture continues – enfolded within the new or the existing transferee entity. In other words, *the business and the adventure lives on but within a new corporate residence, i.e., the transferee company.* It is, therefore, essential to look beyond the mere concept of destruction of corporate entity which brings to an end or terminates any assessment proceedings. There are analogies in civil law and procedure where upon amalgamation, the cause of action or the complaint does not *per se* cease – depending of course, upon the structure and objective of enactment. Broadly, the quest of legal systems and courts has been to locate if a successor or representative exists in relation to the particular cause or action, upon whom the assets might have devolved or upon whom the liability in the event it is adjudicated, would fall.

HISTORICAL BACKGROUND

The concept of merger and acquisition in India was not popular until the year 1988. During that period a very small percentage of businesses in the country used to come together, mostly into a friendly acquisition with a negotiated deal. The key factor contributing to fewer companies involved in the merger was the regulatory and prohibitory provisions of MRTP Act, 1969. According to this Act, a company or a firm has to follow a burdensome procedure to get approval for merger and acquisitions.

The year 1988 witnessed one of the oldest business acquisitions or company mergers attempt in India. It is the well-known ineffective unfriendly takeover bid by Swaraj Paul to overpower DCM Ltd. and Escorts Ltd. Further to that many other non-resident Indians had put in their efforts to take control over various companies through their stock exchange portfolio.

Before 1991 Indian economy was closed economy. Various licenses and registration under various enactments were required to set-up an industry. Due to restrictive government policies and rigid regulatory framework there existed very limited scope for restructuring. However, after 1991, the main thrust of Industrial Policy, 1991 was on relaxations in industrial licensing, foreign investments, and transfer of foreign technology, etc. With the economic liberalization, globalization and opening-up of economies, the Indian corporate sector started restructuring businesses to meet the opportunities and challenges.

In the era of hyper competitive capitalism and technological change, industrialists realized that restructuring perhaps is the best route to reach a size comparable to global companies so as to effectively compete.

NEED AND SCOPE

Corporate Restructuring is concerned with arranging the business activities of the Corporate as a whole so as to achieve certain pre-determined objectives at corporate level. Objectives may include the following:

- To enhance shareholders value
- Deploying surplus cash from one business to finance profitable growth in another
- Exploiting inter-dependence among present or prospective businesses
- Risk reduction
- Development of core-competencies
- To obtain tax advantages by merging a loss-making company with a profit-making company
- Revolution in information technology has made it necessary for companies to adopt new changes for improving corporate performances.
- To become globally competitive
- To increase the market share
- Convertibility of rupee has attracted medium-sized companies to operate in the global markets.
- Competitive business necessitated to have sharp focus on core business activities, to gain synergy benefits, to minimize the operating costs, to maximize efficiency in operation and to tap the managerial skill to the best advantage of the firm.
- By diversification of business activities, the minimization of business risk is possible and it enables the firm to achieve at least the minimum targeted rate of return
- With the integration of sick unit into the successful unit, the adjustment of unabsorbed depreciation and write off of accumulated loss is possible and thereby the successful unit can have strategic tax planning.

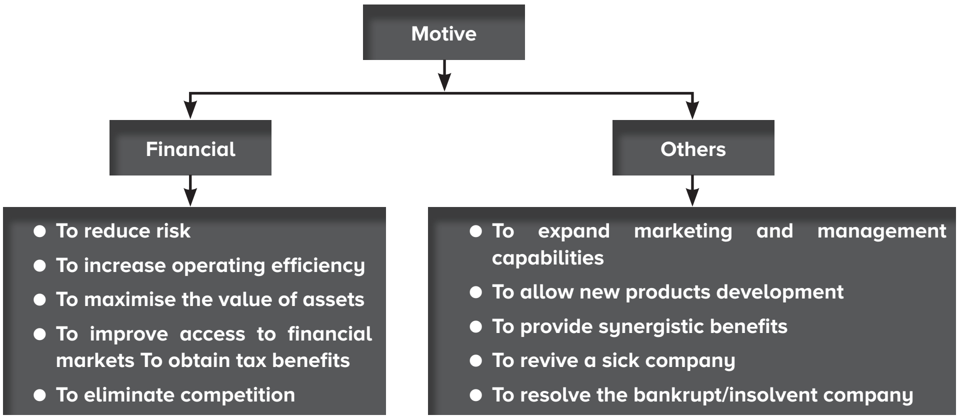
Restructuring aims at improving the competitive position of an individual business and maximizing its contribution to corporate objectives. It also aims at exploiting the strategic assets accumulated by a business i.e., monopolies, goodwill, exclusivity through licensing, etc. to enhance the competitiveness advantages. Thus, restructuring helps in bringing an edge over competitors.

In highly competitive world, cost cutting and value addition are very important to get highlighted.

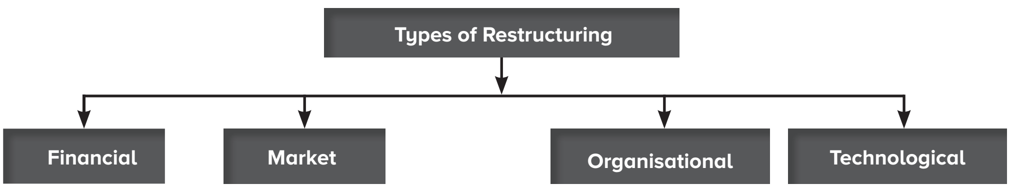
Corporate Restructuring : An Example

ABC Limited has surplus funds but it is not able to consider any viable projects. Whereas XYZ Limited has identified viable projects but has no money to fund the cost of the project. The merger of ABC Limited and XYZ Limited is a mutually beneficial option and would result in positive synergies for both the Companies.

Motives behind Corporate Restructuring



TYPES OF RESTRUCTURING



I. Financial Restructuring

Financial restructuring deals with restructuring of capital base and raising finance for new projects. Financial restructuring helps a firm to revive from the situation of financial distress without going into liquidation.

Financial restructuring is done for various business reasons:

- Poor financial performance
- External competition
- Erosion or loss of market share
- Emerging market opportunities

It involves Equity Restructuring like buy-back, Alteration/Reduction of capital and Debt Restructuring like restructuring of the secured long-term borrowing, long-term unsecured borrowings, Short term borrowing which are explained in detail in further later.

II. Market and Technological Restructuring

Market Restructuring involves decisions with respect to the product market segments where the company plans to operate on its core competencies and technological restructuring occurs when a new technology is developed that changes the way an industry operates. This type of restructuring usually affects employees, and tends to lead to new training initiatives, along with some layoffs as the company improves efficiency. This type of restructuring also involves alliances with third parties that have technical knowledge or resources.

Indian technology major Tata Consultancy Services Limited has embarked upon the process of restructuring and focusing on three core areas Cloud, agile and automation. The restructuring plan of the company focuses on the manufacturing capacity and on product, technical and technological, financial, employment, organizational, purchasing and management restructuring activities.

Disney's global technology group, parks-and-resorts division is undergoing a reorganization which results in some employees losing their jobs. It is eliminating some positions and replacing them with others that help the company reach more long-term technology goals.

Joint Venture, Strategic Alliances, Franchising are some of the examples of market and technological restructuring.

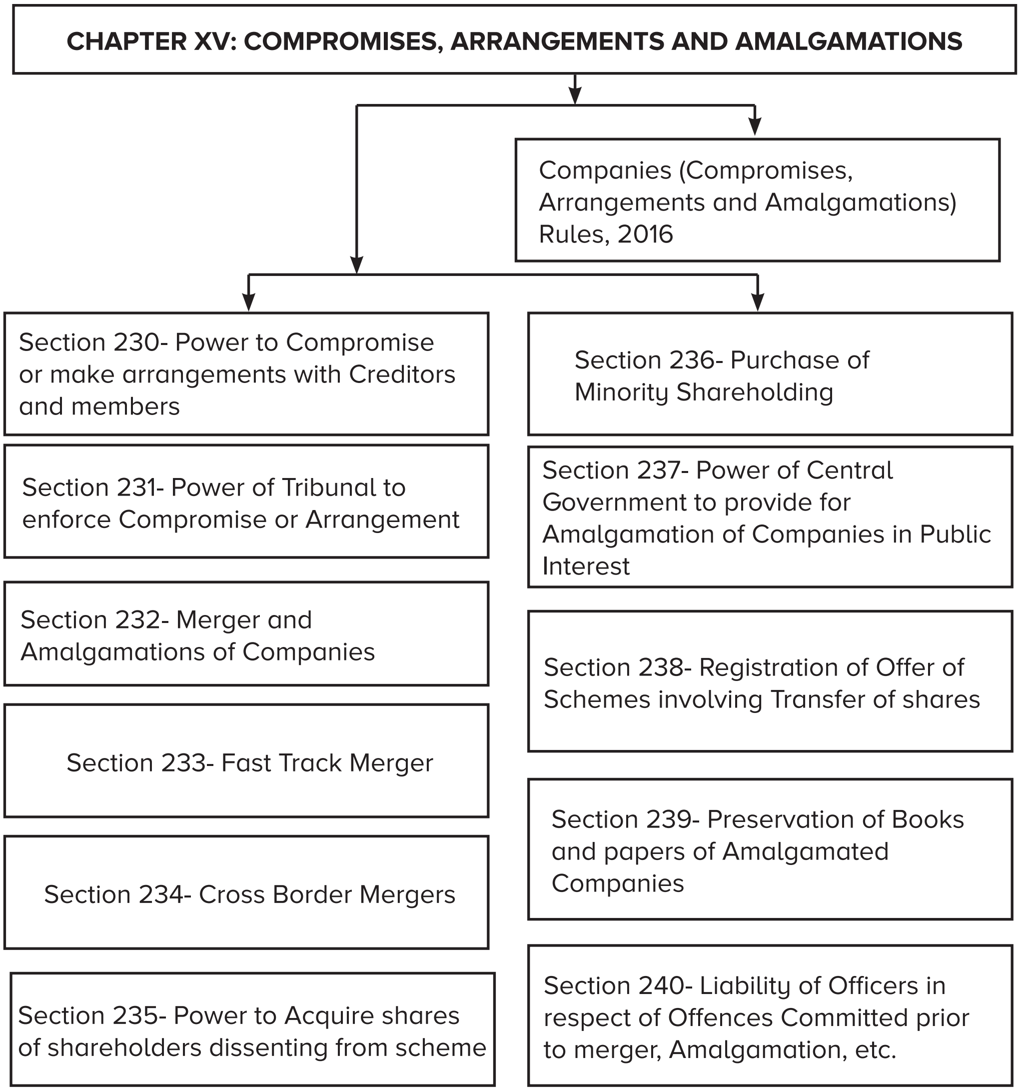
III. Organisational Restructuring

Organizational Restructuring involves establishing internal structures and procedures for improving the capability of the personnel in the organization to respond to changes. These changes need to have the cooperation of all levels of employees. Some companies shift organizational structure to expand and create new departments to serve growing markets. Other companies reorganize corporate structure to downsize or eliminate departments to conserve overheads.

LEGAL FRAMEWORK OF CORPORATE RESTRUCTURING

Corporate Restructuring in India is governed by the following Acts, Rules, etc.:

- Chapter XV of The Companies Act, 2013 (the Act) The Companies (Compromises, Arrangements and Amalgamations) Rules, 2016
- Chapter IV of the Companies Act, 2013 the Companies (Share Capital and Debentures) Rules, 2014 - Buy Back of shares/ purchase of own securities
- The National Company Law Tribunal (Procedure for reduction of share capital of Company) Rules, 2016 -Reduction of share capital
- The Companies (Compromises, Arrangements, and Amalgamations) Rules, 2016
- Income Tax Act, 1961
- Accounting Standards
- Foreign Exchange Management Act, 1999
- Competition Act, 2002
- Indian Stamp Act, 1899
- State Stamp Acts
- Insolvency and Bankruptcy Code, 2016 and Rules & Regulations thereon
- Intellectual Property Rights.



MOST COMMONLY APPLIED TOOLS OF CORPORATE RESTRUCTURING

Mergers/Acquisitions and Amalgamation

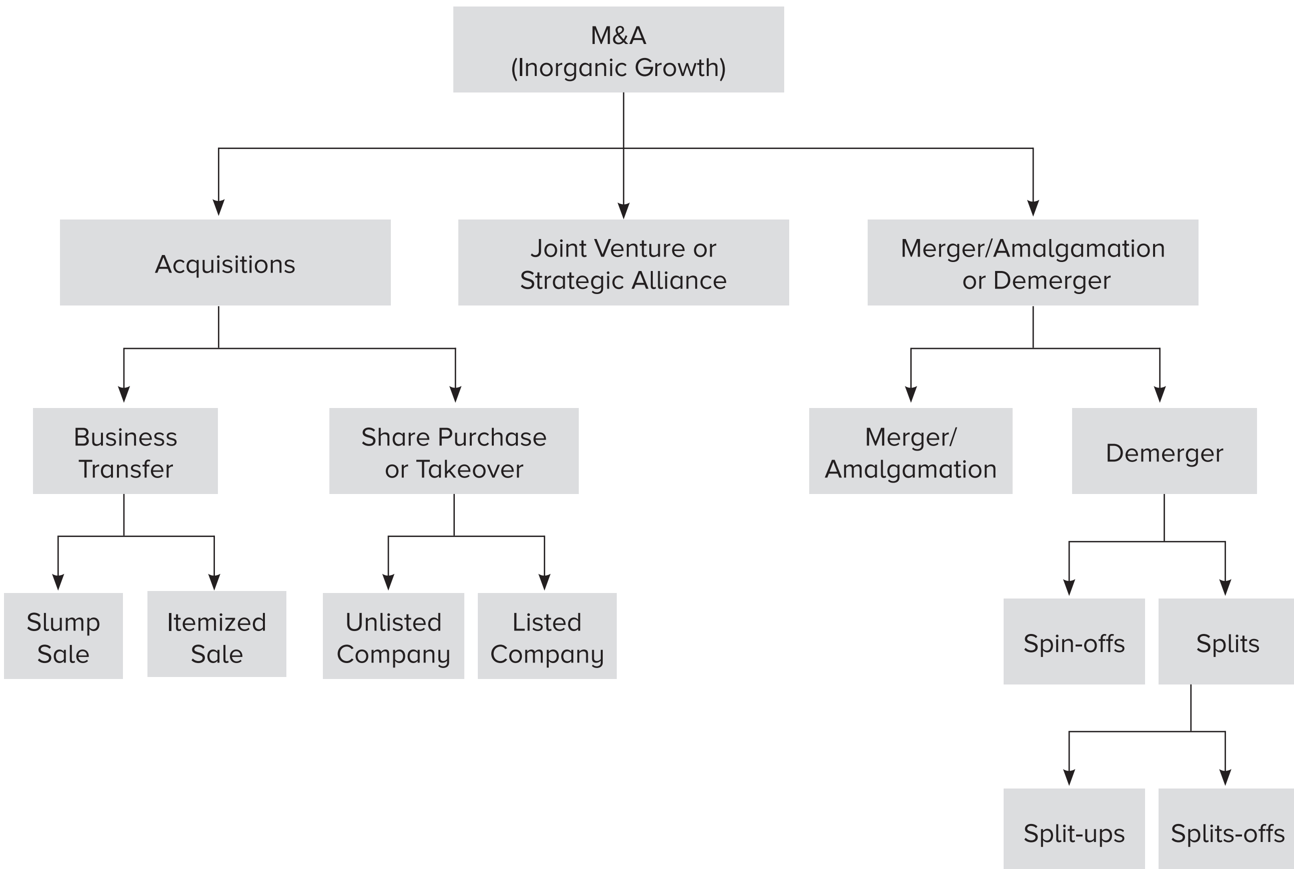
Mergers and Acquisitions (M&A) are transactions in which the ownership of companies, other business organizations or operating units are transferred or combined. As an aspect of strategic management, M&A allow enterprises to grow, shrink, and change the nature of the business or competitive position. It refers to the consolidation of two companies.

The reasoning behind M&A is that two separate companies together create more value compared to being on an individual stand. With the objective of wealth maximization, companies keep evaluating different opportunities through the route of merger or acquisition.

Mergers and Acquisitions (M&A) is a critical strategy for growth in the new economy. M&A are transactions in which the ownership of companies, other business organizations or operating units are transferred or combined. As an aspect of strategic management, M&A allow enterprises to grow, shrink and change the nature of the business or competitive position. It refers to the consolidation of two companies. The reasoning behind M&A is that two separate companies together create more value compared to being on an individual stand. With the objective of wealth maximization, companies keep evaluating different opportunities through the route of merger or acquisition.

M& A help the aspiring entities to expand geographically and assists them to reach the greater height and become market leaders. Also, M & As would increase the entity's ability to distribute goods or services on a wider scale which allows the entity to reach a wider market of consumers. This also helps to expand brand recognition and increase sales. The consumer also gets competitive products with improved technology.

The terms M & As is a term for company consolidation when two or more companies merge into one entity is called a merger. When we refer the term acquisition, it means to the purchase of one entity by another and in this case, instead of starting a new company, one company becomes part of another company. Mergers and acquisitions are an important part of strategic management that is included in corporate finance. we could also say that it is a type of restructuring of the company with the aim of growing rapidly thereby increasing the profitability and also gaining more market share.



Reasons for Mergers & Acquisitions

Regardless of their category or structure, all mergers and acquisitions have one common goal: they are all meant to create synergy that makes the value of the combined companies greater than the sum of the two parts.

The success of a merger or acquisition depends on whether this synergy is achieved. Synergy takes the form of revenue enhancement and cost savings. By merging, the companies hope to benefit from the following:

- **Becoming bigger**: Many companies use M&A to grow in size and leapfrog their rivals. While it can take years or decades to double the size of a company through organic growth, this can be achieved much more rapidly through mergers or acquisitions.

- **Pre-empted competition**: This is a very powerful motivation for mergers and acquisitions, and is the primary reason why M&A activity occurs in distinct cycles.
- **Domination**: Companies also engage in M&A to dominate their sector. However, since a combination of two behemoths would result in a potential monopoly, such a transaction would have to face regulatory authorities.
- **Tax benefits**: Companies also use M&A for tax purposes, although this may be an implicit rather than an explicit motive.
- **Economies of scale**: Mergers also translate into improved economies of scale which refers to reduced costs per unit that arise from increased total output of a product.
- **Acquiring new technology**: To stay competitive, companies need to stay on top of technological developments and their business applications. By buying a smaller company with unique technologies, a large company can maintain or develop a competitive edge.
- **Improved market reach and industry visibility**: Companies buy other companies to reach new markets and grow revenues and earnings. A merger may expand two companies' marketing and distribution, giving them new sales opportunities. A merger can also improve a company's standing in the investment community: bigger firms often have an easier time raising capital than smaller ones.

M&A take place:

- by purchasing assets
- by purchasing common shares
- by exchange of shares for assets
- by exchanging shares for shares

M&A include a number of different transactions such as:

1. Mergers
2. Acquisitions
3. Amalgamation
4. Consolidations
5. Tender offers
6. Purchase of assets
7. Management buy-out

1. MERGERS

The term merger and amalgamation has not been defined under the Act. M&A is often known to be a single terminology. However, there is a thin difference between the two. 'Merger' is the fusion of two or more companies, whereby the identity of one or more is lost resulting in a single company whereas 'Amalgamation' signifies the blending of two or more undertaking into one undertaking, blending enterprises loses their identity forming themselves into a separate legal identity.

There may be amalgamation by the transfer of two or more undertakings to a new or existing company. 'Transferor company' means the company which is merging also known as amalgamating company in case of amalgamation and 'transferee company' is the company which is formed after merger or amalgamation also known as amalgamated company in case of amalgamation.

A merger is a legal consolidation of two entities into one entity which can be merged together either by way of amalgamation or absorption or by formation of a new company. The Board of Directors of two companies approve the combination and seek shareholders' approval. After the merger, the acquired company ceases to exist and becomes part of the acquiring company. Some recent examples are acquisition of eBay India by Flipkart, Vodafone-Idea merger and Axis Bank's acquisition of free charge, State Bank of India merger with all its subsidiary banks etc.

Types of Mergers

Horizontal Merger	Vertical Merger	Conglomerate Merger	Congeneric Merger	Reverse Merger

(a) Horizontal Merger

Horizontal Merger is a merger between companies selling similar products in the same market and in direct competition and share the same product lines and markets. It decreases competition in the market. The main objectives of horizontal merger are to benefit from economies of scale, reduce competition, achieving monopoly status and control of the market.

Example:

Facebook's acquisition of Instagram for a reported $1 billion. Both Facebook and Instagram operated in the same industry and were in similar production stages in regard to their photo-sharing services. Facebook, looking to strengthen its position in the social media and social sharing space, saw the acquisition of Instagram as an opportunity to grow its market share, increase its product line, reduce competition and access potential new markets.

Disney bought Lucas firm and both companies were involved in production of film and running the TV shows.

(b) Vertical Merger

Vertical Merger is a merger between companies in the same industry, but at different stages of production process. In another words, it occurs between companies where one buys or sells something from or to the other.

To illustrate, suppose XYZ Ltd. produces shoes and ABC Ltd. produces leather. ABC has been XYZ's leather supplier for many years, and they realize that by entering into a merger together, they could cut costs and increase profits. They merge vertically because the leather produced by ABC is used in XYZ's shoes.

Microsoft bought Nokia to support its software and provide hardware necessary for the smartphone.

(c) Conglomerate Merger

Conglomerate merger is a merger between two companies that have no common business areas. It refers to the combination of two firms operating in industries unrelated to each other. The business of the target company is entirely different from the acquiring company. The main objective of a conglomerate merger is to achieve big size e.g., a watch manufacturer acquiring a cement manufacturer, a steel manufacturer acquiring a software company, etc.

Example:

Berkshire Hathway acquired Lubrizol: Berkshire Hathaway and its subsidiaries engage in diverse business activities including property and casualty insurance and reinsurance, utilities and energy, freight rail transportation, finance, manufacturing, retailing and services. Berkshire's common stock is listed on the New York Stock Exchange.

The Lubrizol Corporation is an innovative specialty chemical company that produces and supplies technologies to customers in the global transportation, industrial and consumer markets. These technologies include lubricant additives for engine oils, other transportation-related fluids and industrial lubricants, as well as fuel additives for gasoline and diesel fuel.

(d) Congeneric Merger

Congeneric merger is a merger between two or more businesses which are related to each other in terms of customer groups, functions or technology e.g., combination of a computer system manufacturer with a UPS manufacturer.

PVR/INOX Merger

India's two leading cinema franchises, PVR and INOX, merged in 2022 to create the largest multiplex chain in the country with over 1500 screens. The PVR and INOX merger will result in synergies in the form of advertising revenues, reduced rental costs, and convenience fees for the merged entity, which will be called PVR-INOX.

HDFC LTD/HDFC BANK Merger

India's largest housing finance company, HDFC Ltd and the largest private sector bank, HDFC Bank, merged in 2022 in one of the biggest financial deals in India. The $40 billion deal will result in a single entity, but the services of HDFC Ltd and HDFC Bank will continue to be provided separately.

An example of a congeneric merger is when banking giant Citicorp merged with financial services company Travelers Group in 1998. In a deal valued at $70 billion, the two companies joined forces to create Citigroup Inc. While both companies were in the financial services industry, they had different product lines.

(e) Reverse Merger

A **reverse merger** is a **merger** in which a private company becomes a public company by acquiring it. It saves a private company from the complicated process and expensive compliance of becoming a public company. Instead, it acquires a public company as an investment and converts itself into a public company.

Example of a reverse merger was when ICICI merged with ICICI Bank in 2002. The parent company's balance sheet was more than three times the size of its subsidiary at the time.

2. ACQUISITION

Acquisition occurs when one entity takes ownership of another entity's stock, equity interests or assets. It is the purchase by one company of controlling interest in the share capital of another existing company. Even after the takeover, although there is a change in the management of both the firms, companies retain their separate legal identity. The companies remain independent and separate; there is only a change in control of the companies. When an acquisition is 'forced' or 'unwilling', it is called a takeover.

Examples:

- Snapdeal and Freecharge ($400 million)
- Flipkart and Myntra ($300 to 330 million)
- Ola and Taxi ForSure ($200 million)

Difference between a Merger and an Acquisition:

Merger	Acquisition
A merger occurs when two separate entities, usually of comparable size, combine forces to create a new, joint organization in which both are equal partners	An acquisition refers to the purchase of one entity by another (usually, a smaller firm by a larger one)
Old company cease to exist and a new company emerges	A new company does not emerge

It requires two companies to consolidate int a new entity with a new ownership and management structure	It occurs when one company takes over all of the operational management decisions of another
It the takeover is friendly, it is called merger	If the takeover is hostile, it is called as an acquisition

From a commercial and economic point of view, both types of transactions generally result in the consolidation of assets and liabilities under one entity, and the distinction between a "merger" and an "acquisition" is less clear. A transaction legally structured as an acquisition may have the effect of placing one party's business under the indirect ownership of the other party's shareholders, while a transaction legally structured as a merger may give each party's shareholders partial ownership and control of the combined enterprise.

Contemporary corporate restructurings are usually referred to as merger and acquisition (M&A) transactions rather than simply a merger or acquisition. The practical differences between the two terms are slowly being eroded by the new definition of M&A deals. In other words, the real difference lies in how the purchase is communicated to and received by the target company's board of directors, employees and shareholders.

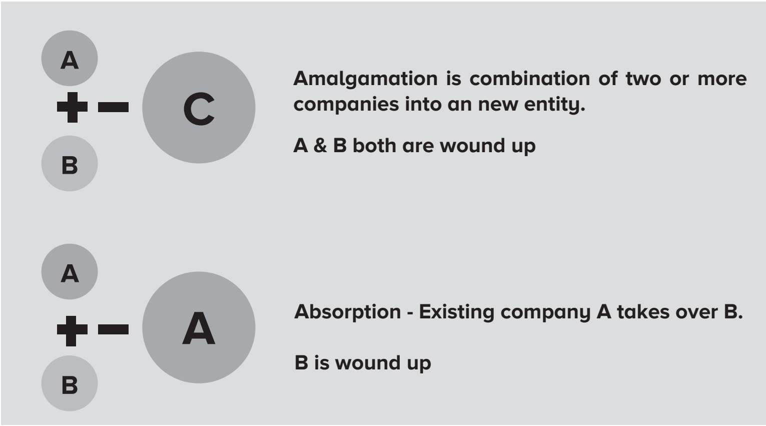
A stock swap occurs when shareholders' ownership of the target company's shares are exchanged for shares of the acquiring company as part of a merger or acquisition. During a stock swap, each company's shares must be accurately valued in order to determine a fair swap ratio.

3. AMALGAMATION

Amalgamation is defined as the combination of one or more companies into a new entity. It includes:

(i) Two or more companies join to form a new company.

(ii) Absorption or blending of one by the other.



Amalgamation is a legal process by which two or more companies are joined together to form a new entity or one or more companies are to be absorbed or blended with another as a consequence the amalgamating company loses its existence and its shareholders become the shareholders of new company or amalgamated company. In other words, property, assets, liabilities of one or more companies is taken over by another or are absorbed by and transferred to an existing company or a new company.

Therefore, the essence of amalgamation is to make an arrangement thereby uniting the undertakings of two or more companies so that they become vested in, or under the control of one company which may or may not be the original of the two or more of such uniting companies.

The word "amalgamation" is not defined under the Companies Act 2013 whereas section 2(1B) of Income Tax Act, 1961 defines Amalgamation as:

"amalgamation", in relation to companies, means the merger of one or more companies with another company or the merger of two or more companies to form one company (the company or companies which so merge being referred to as the amalgamating company or companies and the company with which they merge or which is formed as a result of the merger, as the amalgamated company) in such a manner that –

(i) all the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation;

(ii) all the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation;

(iii) shareholders holding not less than three-fourths in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee for, the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of the amalgamation.

Otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first-mentioned company.

Amalgamation includes absorption. The Institute of Chartered Accountants of India has issued Accounting Standard (AS) 14 on Accounting for Amalgamations.

Illustration

Process	Result
Existing companies A and B are wound-up and a new company C is formed to takeover the businesses of A and B	Amalgamation
Existing company A takes over the business of another existing company B which is wound-up	Absorption
A new Company X is formed to take over the business of an existing company Y which is wound-up.	External reconstruction

Reasons for Amalgamation :

(a) To acquire cash resources
(b) To eliminate competition
(c) Tax savings/advantages
(d) Economies of large scale operations
(e) To Increase shareholders value
(f) To reduce the degree of risk by diversification
(g) Managerial effectiveness
(h) To achieve growth and financial gain
(i) Revival of weak or sick or insolvent/bankrupt company
(j) Survival
(k) Sustaining growth.

4. CONSOLIDATION

A consolidation creates a new company. Stockholders of both companies approve the consolidation, and subsequent to the approval, receive common equity shares in the new firm.

Example: In 1998 Citicorp and Traveler's Insurance Group announced a consolidation, which resulted in Citigroup. Facebook's acquisition of Instagram & Disney's acquisition of Fox.

5. TENDER OFFER

One company offers to purchase the outstanding stock of the other firm at a specific price. The acquiring company communicates the offer directly to the other company's shareholders.

Example: ABC Ltd is a publicly listed company whose share price is trading at $15 per share. Michael is a venture capitalist who wants to take over the company and offers $18 per share provided his firm secures at least 51% of ABC Ltd.

6. ACQUISITION OF ASSETS

In a purchase of assets, one company acquires the assets of another company. The company whose assets are being acquired, obtain approval from its shareholders. The purchase of assets is typical during bankruptcy proceedings, where other companies bid for various assets of the bankrupt company, which is liquidated upon the final transfer of assets to the acquiring firm(s).

7. MANAGEMENT BUYOUT

A management buyout (MBO) is a transaction where a company's management team purchases the assets and operations of the business they manage. MBO is appealing to professional managers because of the greater potential rewards from being owners of the business rather than employees.

According to global consultancy giant Grant Thornton, the overall deal activity - including both mergers and acquisitions and PE (private equity) - was about $59 billion in the January-November period of 2017, a 9 per cent rise from the previous year 2016.

When looking to exit, a business owner has a number of options. One of these is to sell the company to the existing management team.

A sale to management may be preferred to a trade sale for a variety of reasons, for example, the number of potential trade buyers may be limited, the vendors may be nervous about approaching competitors and disclosing sensitive information or they may feel strongly that the company and its staff carry on independently in what they believe to be "safe hands".

In its simplest form, a management buyout (MBO) involves the management team of a company combining resources to acquire all or part of the company they manage. Most of the time, the management team takes full control and ownership, using their expertise to grow the company and drive it forward.

Factors that makes a succesful MBO:

- A company with a good track record of profitability;
- Good future prospects for the company without high risk factors;
- A strong committed management team with a mixture of skills;
- A vendor who is willing to explore a sale to the management team and who will accept a realistic price;
- A deal structure that can be funded, and supported by the future cashflows of the company.

8. PURCHASE OF COMPANY AS RESOLUTION APPLICANT UNDER IBC LAW

The basic objective behind the Insolvency and Bankruptcy Code 2016 is to revive the insolvent company by approving the effective resolution plan and maximization of assets of the corporate debtor. As per the Code, the company under insolvency can be purchased by the resolution applicant by participating in the bid process by submitting the most effective resolution plan. This way the insolvent company can be revived by some other company/group/individuals.,

Example: Tata Steel has taken over the bankrupt Bhushan Steel for ₹ 35,200 crore,

EXAMPLE-MERGERS AND ACQUISITIONS IN INDIA

Tata Group/Air India

Tata Group, India's largest conglomerate, acquired the nationalised airline Air India in 2022. Tata also announced the merger of Air India with Vistara, a joint venture between Tata Sons and Singapore Airlines. Air India had been struggling for years, and the travel restriction during the COVID-19 pandemic only added to its woes. However, Tata is doing everything possible to restore Air India to its former glory.

Adani Group/Ambuja Cement

Gautam Adani is fast-rising in the world. In a span of a few years, he has claimed a spot as one of the richest people in the world. Along with the acquisition of NDTV, the Adani Group also acquired a majority stake in Ambuja Cements and its subsidiary, ACC Ltd. Adani is now the second largest cement manufacturer in the country after Aditya Birla Group's UltraTech.

Zomato – Blinkit Merger

Zomato and Blinkit have reached an agreement for a merger. The all-stock deal values Blinkit between $700 million and $750 million. Blinkit, formerly known as Grofers, has revamped itself to focus on an instant grocery delivery portal.

Zomato Acquisition of Uber Eats

Zomato acquired Uber Eats for an all-stock acquisition deal during the year 2020. The acquisition deal provided great discounts to customers and it was the most beneficial to the customer during the Covid pandemic time. The stock deal was done by the companies operating in the same line of business. Which resulted Zomato becoming number one in food marketing and food supply. In other words, Zomato became the megastar of the food business and in turn Uber Eats could invest their money in other growing business.

Vodafone India and Idea Cellular

Vodafone India and Idea Cellular decided to merge and form country's largest telecom operator 'Vodafone India Ltd.' worth of more than $23 billion with a 35 per cent market share and it is the top M&Adeal of 2017-18.

Vodafone and the Aditya Birla Group will have a joint control of this combined company. Combining the Vodafone and idea customers, the merged entity is the biggest telecom company in India.

The merged entity have over 408 million customers, nearly 42% customer market share (CMS) and nearly 33% revenue market share (RMS), leaving it stronger placed to take on competitive pressures triggered by Jio, with 160 million subscribers and over 16% CMS and 15.3% RMS. Airtel has a CMS of 29.5% and an RMS of 31.5%.

The Idea-Vodafone merger has been cleared by the stock exchanges, Securities and Exchange Board of India, Competition Commission of India, foreign direct investment clearance from the department of industrial policy and promotion, approval given by DoT as licensor and the merger after approval of NCLTis complete in August 2018.

Flipkart and eBay

Indian e-commerce major Flipkart acquired the Indian wing of eBay. The transaction was announced in April 2017 and completed in August 2017. eBay and Flipkart have also entered into an agreement for cross-border sale. In exchange of equity stake in Flipkart, eBay had made cash investment of $500 million and sold its eBay. in business to Flipkart.

As a result, Flipkart customers get expanded product choices with the wide array of global inventory available on eBay while eBay customers will have access to a more unique Indian inventory from Flipkart sellers.

DEMERGER

It is a business strategy in which a single business is broken into components, either to operate on their own, to be sold or to be dissolved. A demerger allows a large company, such as a conglomerate, to split off its various brands to invite or prevent an acquisition, to raise capital by selling off components that are no longer part of the business's core product line, or to create separate legal entities to handle different operations.

Demerger is an arrangement whereby some part / undertaking of one company is transferred to another company which operates completely separate from the original company. Shareholders of the original company are usually given an equivalent stake of ownership in the new company.

The contracts relating to the demerged undertaking would get automatically transferred to the resulting company, unless the underlying contract has stipulated specific restrictions. A demerged company is said to be one whose undertakings are transferred to the other company, and the company to which the undertakings are transferred is called the resulting company. It is a process of reorganizing a corporate structure whereby a capital stock of a division or subsidiary of corporation or of a newly affiliated company is transferred to the stakeholders of existing company.

Demerger under Section 2(19AA) of the Income tax Act, 1961 means the transfer, pursuant to a scheme of arrangement under section 230 to 232 of the Act, by a demerged company of its one or more undertakings to the resulting company in such a manner that:-

(i) All the property of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the property of the resulting company by virtue of demerger;

(ii) All the liabilities relatable to the undertaking, being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger;

(iii) The property and the liabilities of the undertaking or undertakings, being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger;

(iv) The resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis except where the resulting company itself is a shareholder of the demerged company;

(v) The shareholders holding not less than three-fourth in value of shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or, its subsidiary) become shareholders of the resulting company or companies by virtue of the demerger; otherwise than as a result of the acquisition of the property or assets of the demerged or any undertaking thereof by the resulting company;

(vi) the transfer of the undertaking is on a going concern basis;

(vii) Demerger in accordance with the conditions notified under Section 72A(5) of Income Tax Act, 1961.

"Undertaking" includes any part of an undertaking, or a unit or division of an undertaking or a business activity taken as a whole, but does not include individual assets or liabilities or any combination thereof not constituting a business activity.

"Liabilities" referred to in sub-clause (ii), shall include:

(a) the liabilities which arise out of the activities or operations of the undertaking;

(b) the specific loans or borrowings (including debentures) raised, incurred and utilised solely for the activities or operations of the undertaking; and

(c) in cases, other than those referred to in clause (a) or clause (b), so much of the amounts of general or multipurpose borrowings, if any, of the demerged company as stand in the same proportion which the value of the assets transferred in a demerger bears to the total value of the assets of such demerged company immediately before the demerger.

As per provisions of Section 72A(4) of Income Tax Act, 1961, in the case of a demerger, the accumulated loss and the allowance for unabsorbed depreciation of the demerged company shall

(a) where such loss or unabsorbed depreciation is directly relatable to the undertakings transferred to the resulting company, be allowed to be carried forward and set-off in the hands of the resulting company;

(b) where such loss or unabsorbed depreciation is not directly relatable to the undertakings transferred to the resulting company, be apportioned between the demerged company and the resulting company in the same proportion in which the assets of the undertakings have been retained by the demerged company and transferred to the resulting company, and be allowed to be carried forward and set-off in the hands of the demerged company or the resulting company, as the case may be.

Examples:

- In April 2023, Competition Commission of India approves the proposed combination involving **demerger** of FMCG business of Haldiram Snacks and Haldiram Foods into Haldiram Snacks Food and acquisition of 56% and 44% shareholding in Haldiram Snacks Food by existing shareholders of Haldiram Snacks and Haldiram Foods.

  Haldiram Snacks Private Limited (HSPL/Haldiram Snacks) is engaged in the manufacture and distribution of packaged food products in India such as snacks, namkeen, sweets, ready to eat / premix food, frozen food, biscuits, non-carbonated ready to drink beverages, pasta etc. Headquartered in Delhi, HSPL's operations are primarily run by Mr. Manohar Agarwal and Mr. Madhu Sudan Agarwal (Delhi Family).

  Haldiram Foods International Private Limited (HFIPL/ Haldiram Foods) is similarly engaged in the manufacture and distribution of packaged foods products such as snacks, namkeen, sweets, ready to eat / pre-mix food, biscuits, cookies, non-carbonated ready to drink beverages, pasta etc. Headquartered in Nagpur, HFIPL's operations are primarily run by Mr. Kamalkumar Shivkisan Agrawal (Nagpur Family).

  Haldiram Snacks Food Private Limited (HSFPL/ Haldiram Snacks Food) is a newly incorporated entity that currently does not undertake any business operations. Post the Proposed Transaction, HSFPL would undertake the FMCG Business that is currently undertaken by HFIPL and HSPL, respectively

  The FMCG business (i.e., the packaged foods business) would comprise collectively of the FMCG business currently undertaken by HSPL and HFIPL and their respective subsidiaries / affiliates.

  The proposed combination involves the following steps:

  i. **A demerger** of the respective FMCG businesses of HSPL and HFIPL (currently housed under HSPL and HFIPL and their various associates / subsidiaries), through NCLT approved Scheme of Arrangement (Scheme);

  ii. Pursuant to the Scheme, the acquisition of 56% and 44% shareholding in HSFPL by the shareholders of HSPL and HFIPL (collectively, Proposed Combination).

- Reliance Industries demerged to Reliance Industries and Reliance Communications Ventures Ltd, Reliance Energy Ventures Ltd, Reliance Capital Ventures Ltd, Reliance Natural Resources Ltd.

- In April 2018, Whitbread plc. announced to de-merge Costa Coffee from their stable of businesses.

- Pfizer sold their infant nutrition business to Nestle.

Types of Demerger

1. Divestiture

Divestiture means selling or disposal of assets of the company or any of its business undertakings/ divisions, usually for cash (or for a combination of cash and debt).

2. Spin-offs

The shares of the new entity are distributed to the shareholders of the parent company on a pro-rata basis. The parent company also retains ownership in the spun-off entity. There are two approaches in which Spin offs may be conducted. In the first approach, the company distributes all the shares of the new entity to its existing shareholders on a pro rata basis. This leads to the creation of two different companies holding the same proportions of equity as compared to the single company existing previously. The second approach is the floatation of a new entity with its equity being held by the parent company. The parent company later sells the assets of the spun off company to another company.

A spinoff may occur for various reasons. A company may conduct a spinoff so it can focus its resources and better manage the division that has more long-term potential. Businesses wishing to streamline their operations often sell less productive or unrelated subsidiary businesses as spinoffs. For example, a company might spin off one of its mature business units that are experiencing little or no growth so it can focus on a product or service with higher growth prospects.

Alternatively, if a portion of the business is headed in a different direction and has different strategic priorities from the parent company, it may be spun off so it can unlock value as an independent operation.

A company may also separate a business unit into its own entity if it has been looking for a buyer to acquire it but failed to find one. For example, the offers to purchase the unit may be unattractive, and the parent company might realize that it can provide more value to its shareholders by spinning off that unit.

A corporation creates a spinoff by distributing 100% of its ownership interest in that business unit as a stock dividend to existing shareholders. It can also offer its existing shareholders a discount to exchange their shares in the parent company for shares of the spinoff. For example, an investor could exchange $100 of the parent's stock for $110 of the spinoff's stock. Spinoffs tend to increase returns for shareholders because the newly independent companies can better focus on their specific products or services.

The downside of spinoffs is that their share price can be more volatile and can tend to under perform in weak markets and outperform in strong markets. Spinoffs can also experience high selling activity; shareholders of the parent may not want the shares of the spinoff they received because it may not fit their investment criteria. The share price may dip in the short term because of this selling activity, even if the spinoff's long-term prospects are positive.

Key Takeaways

- A spinoff is the creation of an independent company through the sale or distribution of new shares of an existing business or division of a parent company.
- The spun-off companies are expected to be worth more as independent entities than as parts of a larger business.
- When a corporation spins off a business unit that has its own management structure, it sets it up as an independent company under a renamed business entity.

3. Splits/divisions

Splits involve dividing the company into two or more parts with an aim to maximize profitability by removing stagnant units from the mainstream business. Splits can be of two types, Split-ups and Split-offs.

Split-ups: It is a process of reorganizing a corporate structure whereby all the capital stock and assets are exchanged for those of two or more newly established companies resulting in the liquidation of the parent corporation.

Split-offs: It is a process of reorganizing a corporate structure whereby the capital stock of a division or subsidiary of corporation or of a newly affiliated company is transferred to the stakeholders of the parent corporation in exchange for part of the stock of the latter. Some of the shareholders in the parent company are given shares in a division of the parent company which is split off in exchange for their shares in the parent company.

Key Takeaways

- Split-offs are a method that can be used for a corporate divestiture.

- Split-offs do not mandate a proportioned pro rata share distribution but rather offer shareholders the option to exchange shares.
- Split-offs are motivated by the desire to create greater value for shareholders through the shedding of assets and offering of a new, separate company.

Comparison Between Spin-off and Split-off

Basis for comparison	Spin-Off	Split-Off
Meaning	Spin-off implies a business action, wherein a company disjoins a division and creates new business entity, which is separately listed in the stock exchange and has independent board of directors.	Split-off refers to a corporate divestiture process in which a company's subsidiary turnout as a separate entity, with independent listing of its capital stocks.
Shares	Shares of the subsidiary company are distributed to all the shareholders.	Holding company's shareholders are required to exchange their shares, to get shares in the subsidiary.
Reason	To create a separate identity of the new firm.	To create a distinction between the core business and the new one.

4. Equity Carve-Outs

Equity carve-outs are referred to a percentage of shares of the subsidiary company being issued to the public. This method leads to a separation of the assets of the parent company and the subsidiary entity. Equity carve outs result in publicly trading the shares of the subsidiary entity.

Examples:

1. Indiabulls carved out commercial office business into a separate firm under the name of Indiabulls Commercial Assets Limited.
2. India's largest engineering and construction company Larsen and Toubro Ltd (L&T) adopted "asset-light strategy" by separating business units into independent subsidiaries by selling a stake in businesses. The company, which is considered a corporate proxy for the broader economy, divested its assets as a way to generate capital for investing in fresh projects.
3. In January 2017, the Government of India divested 10 per cent stake in Coal India Limited through the offer-for-sale (OFS) route at Rs. 358 per share and brought its holding down to 79.65 per cent.

SLUMP SALE

The transfer of the undertaking concerned as going concern is called "Slump sale". Slump sale is one of the methods that are widely used in India for corporate restructuring where the company sells its undertaking. The main reasons of slump sale are generally undertaken in India due to following reasons:

- It helps the business to improve its poor performance.
- It helps to strengthen financial position of the company.
- It eliminates the negative synergy and facilitates strategic investment.
- It helps to seek tax and regulatory advantage associated with it.

Section 2 (42C) of the Income Tax Act, 1961, recognizes 'Slump-sale' as a transfer of an 'undertaking' i.e. a part or a unit or a division of a company, which constitutes a business activity when taken as a whole. It is a transfer of one or more undertakings as a result of sale for a lump sum consideration, without values being assigned to the individual assets and liabilities in such sale. Sale includes transfer of an asset from one person to another for some consideration, where consideration can be in kind or cash.

'Undertaking' shall include any part of an undertaking or a unit or division of an undertaking or a business activity taken as a whole, but does not include individual assets or liabilities or any combination thereof not constituting a business activity.

The term 'sale' is not defined in the Income Tax Act, 1961. The term "Sale" is defined in the Section 4 of the Sales of Goods Act, 1930. Sale is a contract whereby the seller transfers the property in goods to a buyer for a price.

In *CIT v R.R. Ramkrishna Pillai (66 ITR 725)*, the Supreme Court made the clear distinction between sale and exchange. In this case, the assessee was carrying on the business and had transferred the assets of the business to a company in consideration for the allotment of the shares of that company. The issue was whether it was exchange or sale because on that basis the transaction will be identified as slump sale. The Supreme Court held that where the assets are transferred for money consideration and the liability of consideration so determined is discharged by any mode whether money or other assets then the said transaction is sale.

In that case, there are in truth two transactions, one transaction of sale and the other of contract under which the shares are allotted in satisfaction of the liability to pay the price. However where the assets are transferred for a consideration of another asset other than money the said transaction is exchange. On the basis of this distinction the Supreme Court held that transfer of assets in consideration for the allotment of shares of that company is 'exchange' and not sale.

The Act does not define a slump sale but has included in its ambit slump sale by way of section 180(1) and provides for the procedure and approval required for selling, leasing or disposing of the whole or substantially whole of the undertaking of the company or where the company owns more than one undertaking, of the whole or substantially the whole of any such undertakings.

"Undertaking" means an undertaking in which the investment of the company exceeds twenty per cent. of its net worth as per the audited balance sheet of the preceding financial year or an undertaking which generates twenty per cent. of the total income of the company during the previous financial year.

"Substantially the whole of the undertaking" in any financial year shall mean twenty per cent. or more of the value of the undertaking as per the audited balance sheet of the preceding financial year.

BUSINESS SALE/DIVESTITURE

Divestiture means selling or disposal of assets of the company or any of its business undertakings/ divisions, usually for cash (or for a combination of cash and debt) and not against equity shares to achieve a desired objective, such as greater liquidity or reduced debt burden. Divestiture is normally used to mobilize resources for core business or businesses of the company by realizing value of non-core business assets.

For example: XYZ Ltd. is the parent of a food company, a car company, and a clothing company. If XYZ Ltd. wishes to go out of the car business, it may divest the business by selling it to another company, exchanging it for another asset, or closing down the car company.

Reasons for Divestitures

- Huge divisional losses
- Continuous negative cash flows from a particular division
- Difficulty in integrating the business within the company
- Unable to meet the competition
- Better alternatives of investment
- Lack of technological upgradations due to non-affordability

- Lack of integration between the divisions
- Legal pressures.

E.g. Nestle is selling its US chocolate business, which includes brands such as Baby Ruth, Butterfinger, and Crunch to Ferrero for $2.8 billion. The deal is part of Nestle's strategy to sell under performing brands and refocus on healthier products and fast-growing markets.

JOINT VENTURE

A joint venture (JV) is a business or contractual arrangement between two or more parties which agree to pool resources for the purpose of accomplishing a specific task may be a new project or any other business activity. In a joint venture (JV), each of the participants is responsible for profits, losses and costs associated with it. Company enters into a joint venture when it lacks required knowledge, human capital, technology or access to a specific market that is necessary to be successful in pursuing the project on its own.

For example: A Ltd. may own technology, manufacturing and production facilities that B Ltd. needs to create and ultimately distribute a new product. A joint venture between the two companies gives B Ltd. access to the equipment without purchasing or leasing it, while A Ltd. is able to participate in production of a product without incurring costs to develop. Each company benefits when the joint venture is successful, and neither is left to complete the project alone.

Types of Joint Ventures

(a) **Equity-based joint ventures** is a type of joint venture in which two or more parties set-up a separate legal company to act as the vehicle for carrying out the project. This new company would usually be located in the same country as one of the two partner companies, with the purpose of mutually establishing an activity with its own objectives: marketing and distribution, research, manufacturing, etc. It benefits foreign and/or local private interests, or members of the general public through capital.

(b) **Non-equity joint ventures** also known as cooperative agreements, seek technical service arrangements, franchise, brand use agreements, management contracts, rental agreements, or one-time contracts, e.g., for construction projects, non-equity arrangements in which some companies are in need of technical services or technological expertise than capital. It may be modernizing operations or starting new production operations.

Example:

- Vistara airlines is an Indian Joint Venture with a foreign company. Vistara is the brand name of Tata SIA Airlines Ltd, a JV between India's corporate giant Tata Sons and Singapore Airlines (SIA).
- Tata Starbucks Pvt. Ltd is a joint venture of Tata with Starbucks Corporation, USA which runs a chain of Starbucks brand coffee shops across India.

STRATEGIC ALLIANCE

Nike, the world's largest producer of athletic foot-wear, does not produce a single shoe. Boeing, the giant aircraft company, makes little more than cockpits and wing bits. These organizations, like a number of other businesses nowadays, have created strategic alliances with their suppliers to do much of their actual production for them.

A strategic alliance is an arrangement between two companies that have decided to share resources to undertake a specific, mutually beneficial project. It is an excellent vehicle for two companies to work together profitably. It can help companies develop and exploit the unique strengths. Organizations get an opportunity to widen customer base or utilize the surplus capacity.

E.g. Etihad Airways, based in Abu Dhabi, has completed an investment in India's Jet Airways. This alliance will provide considerable benefits for both carriers, as it opens Etihad to 23 cities in India, and offers Jet Airways passengers connection possibilities to the US, Europe, Middle East and Africa that were previously unavailable.

ICICI Bank and Vodafone India entered into a strategic alliance to launch a unique mobile money transfer and payment service called 'm-pesa'.

REVERSE MERGER

A reverse merger is a merger in which a private company becomes a public company by acquiring it. It saves a private company from the complicated process and expensive compliance of becoming a public company. Instead, it acquires a public company as an investment and converts itself into a public company.

However, there is another angle to the concept of a reverse merger. When a weaker or smaller company acquires a bigger company, it is a reverse merger. In addition, when a parent company merges into its subsidiary or a loss-making company acquires a profit-making company, it is also termed as a reverse merger.

The reason for reverse merger are:

- To carry forward tax losses of the smaller firm, this allows the combined entity to pay lower taxes. Tax savings under Income Tax Act, 1961
- Economies of scale of production
- Marketing network
- To protect the trademark rights, licence agreements, assets of small/loss making company.

Examples:

1. In 2023, the reverse merger of HDFC with its subsidiary HDFC Bank, resulting in a combined business worth over 41 lakh crore.
2. Merging of Oil exploration company Cairn India with parent Vedanta India.
3. In 2002 Merging of ICICI with its arm ICICI Bank. The parent company's balance sheet was more than three times the size of its subsidiary at the time. The rational for the reverse merger was to create a universal bank that would lend to both industry and retail borrowers.
4. Merging of Godrej Soaps, profitable and with a turnover of ₹437 crore with loss-making Gujarat Godrej Innovative Chemicals with a turnover of ₹ 60 crore, the resulting firm was named Godrej Soaps.

FINANCIAL RESTRUCTURING

Corporate financial restructuring is any substantial change in a company's financial structure, or ownership or control, or business portfolio, designed to increase the value of the firm, i.e., debt and equity restructuring. Internal reconstruction of a company is the simplest form of financial restructuring. Under this, various liabilities are reduced after negotiating with various stakeholders such as banks, financial institutions, creditors, debenture holders and shareholders. It deals with the restructuring of capital base and raising finance for new projects.

Debt Restructuring

It involves a reduction of debt and an extension of payment terms or change in terms and conditions, which is less expensive. It is nothing but negotiating with bankers, creditors, vendors. It is the process of reorganizing the whole debt capital of the company. It involves the reshuffling of the balance sheet items as it contains the debt obligation of the company. Debt capital of the company includes secured long term borrowing, unsecured long-term borrowing, and short term borrowings.

- Restructuring of the secured long-term borrowing for improving liquidity and increasing the cash flows for a sick company and reducing the cost of capital for healthy companies. Restructuring of the unsecured long-term borrowings.

- Restructuring of the long-term unsecured borrowings can be in form of public deposits and/or private loans (unsecured) and privately placed, unsecured bonds or debentures.
- Restructuring of other short-term borrowings: the borrowings that are very short in nature are generally not restructured these can indeed be renegotiated with new terms. These types of short-term borrowings include inter-corporate deposits clean bills & clean overdraft.
- Best method for corporate debt restructuring is Debt-equity swap. In the case of an debt-equity swap, specified shareholders have right to exchange stock for a predetermined amount of debt (i.e. bonds) in the same company. In debt-equity swap debt /bonds are exchanged with shares/stock of the company.

CASE STUDY

Gammon India Ltd. invoked the Strategic Debt Restructuring (SDR) mechanism in the 2015-2016. A total of 16 banks, led by ICICI Bank, decided to convert a part of their loan into 63.07 per cent equity. The SDR Scheme, an improved version of the erstwhile Corporate Debt Restructuring, or CDR, mechanism, wherein lenders have sweeping powers to throw out managements of companies whose assets have turned bad. However, the bankers could not find a buyer for the entire Gammon India and instead decided to restructure it into three parts - Power Transmission & Distribution (T&D), Engineering, Procurement & Construction (EPC), and the residual business. The Thailand-based GP Group has acquired the EPC assets while Ajanma Holdings bought stake in the T&D business.

Gammon India is one among two dozen companies where bankers have invoked the SDR Scheme, to make the process of debt recovery faster and smoother. The list includes Alok Industries, Usher Agro, Diamond Power, Monnet Ispat, Jaiprakash Power and IVRCL.

Equity Restructuring

It is a process of reorganizing the equity capital. It includes a reshuffling of the shareholders capital and the reserves that are appearing on the balance sheet. Restructuring equity means changing how the firm's residual cash flows are divided and distributed among the firms shareholders, with the goal of increasing the overall market value of the firms common stock. Restructuring of equity and preference capital becomes complex process involving a process of law and is a highly regulated area.

The following comes under equity restructuring:

- Alteration of share capital
- Reduction of share capital
- Buy-back of shares.

ALTERATION OF SHARE CAPITAL

The capital of a company is separated into units of a fixed denomination and such unit is a share. A share means a share in the share capital of a company and includes stock as defined under Section 2(84) of Companies Act, 2013. Alteration of share capital means, increase or decrease in or rearrangement of share capital as permitted in Articles of Association. An increase or decrease in the share capital of a company may be carried out as and when the company requires thus leading to an alteration in the company's share capital.

According to section 61 of the Companies Act, 2013 a limited company having a share capital derives its power to alter its share capital through its articles of association. As per the section the company may, if so authorised by its articles, alter its memorandum in its general meeting to –

1. increase its authorised share capital by such amount as it thinks expedient;
2. consolidate and divide all or any of its share capital into shares of a larger amount than its existing shares;

The proviso to Section 61(1)(b) clarifies that No consolidation and division which results in changes in the voting percentage of shareholders shall take effect unless it is approved by the Tribunal on an application made in the prescribed manner;

3. convert all or any of its fully paid-up shares into stock, and reconvert that stock into fully paid-up shares of any denomination;
4. sub-divide its shares, or any of them, into shares of smaller amount than is fixed by the memorandum, so, however, that in the sub-division the proportion between the amount paid and the amount, if any, unpaid on each reduced share shall be the same as it was in the case of the share from which the reduced share is derived;
5. cancel shares which, at the date of the passing of the resolution in that behalf, have not been taken or agreed to be taken by any person, and diminish the amount of its share capital by the amount of the shares so cancelled;
6. The cancellation of shares shall not be deemed to be a reduction of share capital.

If a company increases its capital beyond the amount of authorised capital, it shall increase its authorised capital by the amount of new shares. Section 2(8) of the Companies Act 2013, defines that “Authorised capital” or “nominal capital” means such capital which is authorized by the memorandum of a company to be the maximum amount of share capital of the company.

If consolidation and division, results in changes in the voting percentage of shareholders, it shall be approved by the Tribunal.

Legal Provisions

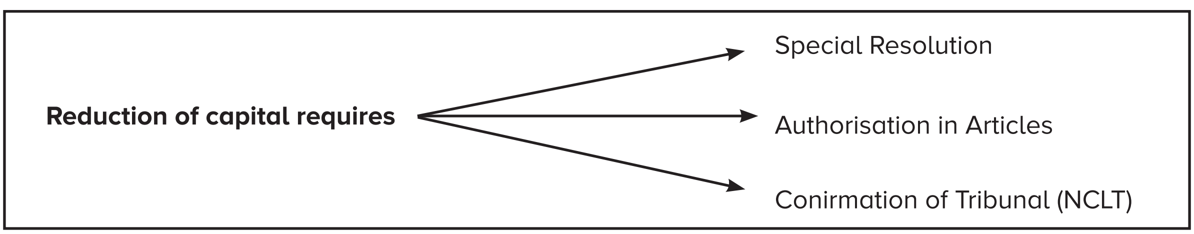
- Section 61 to 64 read with Section 13 and 14 of the Companies Act, 2013
- The Companies (Share Capital and Debentures) Rules, 2014
- National Company Law Tribunal Rules, 2016.

REDUCTION OF SHARE CAPITAL

Capital Reduction is the process of decreasing a company’s shareholder’s equity through share cancellations and share repurchases. The reduction of share capital means reduction of issued, subscribed and paid up share capital of the company. In simple words it can be regarded as ‘Cancellation of Uncalled Capital’ i.e. part of subscribed share capital. The act of capital reduction is enacted by reducing the amount of issued share capital in a response to a permanent reduction in a company’s operations or a revenue loss that cannot be recovered from a company’s future earnings.

The need of reducing share capital arise in following situations:

- Returning of surplus to shareholders;
- Eliminating losses, which may be preventing the payment of dividends;
- As part of scheme of compromise or arrangements.



Legal Provisions

- Section 66 of the Companies Act, 2013; Reduction by way of cancellation of shares
- Rule 2 to 6 of the National Company Law Tribunal (Procedure for Reduction of Share Capital of Company) Rules, 2016
- SEBI (LODR) Regulations, 2015.

Example:

- The shares of face value of INR 125 each of which INR 100 paid, the company may reduce them to INR 100 fully paid-up shares and thus relieve the shareholders from liability on the uncalled capital of INR 25 per share.
- The shares of face value of INR 100 each fully paid-up is represented by INR 75 worth of assets. In such a case, reduction of share capital may be effected by cancelling INR 25 per share and writing off similar amount of shares.
- The shares of face value of INR 100 each fully paid-up reduced to face value of INR 75 each by paying back INR 25 per share.

Modes of Reduction of Capital

A company limited by shares or a company limited by guarantee and having a share capital may, if authorised by its articles, by special resolution, and subject to its confirmation by the Tribunal on petition, reduce its share capital in any way and in particular:

(a) extinguish or reduce the liability on any of its shares in respect of the share capital not paid-up; or

(b) either with or without extinguishing or reducing liability on any of its shares;

(c) cancel any paid-up share capital which is lost or is unrepresented by available assets; or

(d) pay off any paid-up share capital which is in excess of the wants of the company,

alter its memorandum by reducing the amount of its share capital and of its shares accordingly.

Reduction of capital without sanction of the Tribunal

The following are cases which amount to reduction of share capital but where no confirmation by the Tribunal is necessary:

(a) Surrender of shares – "Surrender of shares" means the surrender of shares already issued, to the company, by the registered holder of shares. Where shares are surrendered to the company, whether by way of settlement of a dispute or for any other reason, it will have the same effect as a transfer in favour of the company and amount to a reduction of capital. But if, under any arrangement, such shares, instead of being surrendered to the company, are transferred to a nominee of the company then there will be no reduction of capital [*Collector of Moradabad v. Equity Insurance Co. Ltd., (1948) 18 Com Cases 309: AIR 1948 Oudh 197*]. Surrender may be accepted by the company under the same circumstances where forfeiture is justified. It has the effect of releasing the shareholder whose surrender is accepted for further liability on shares.

The Companies Act contains no provision for surrender of shares. Thus surrender of shares is valid only when Articles of Association provide for the same and:

(i) where forfeiture of such shares is justified; or

(ii) when shares are surrendered in exchange for new shares of same nominal value.

Both forfeiture and surrender lead to termination of membership. However, in the case of forfeiture, it is at the initiative of company and in the case of surrender it is at the initiative of member or shareholder.

(b) Forfeiture of shares – A company may if authorised by its articles,forfeit shares for non-payment of calls and the same will not require confirmation of the Tribunal.

(c) Diminution of capital – Where the company cancels shares which have not been taken or agreed to be taken by any person.

(d) Redemption of redeemable preference shares.

(e) Buy-back of its own shares within the specified percentage of capital permitted by the Act.

Creditors' right to object to reduction

After passing the special resolution for the reduction of capital, the company is required to apply to the Tribunal by way of petition for the confirmation of the resolution under Section 66 of the Companies Act, 2013. Where the proposed reduction of share capital involves either (i) diminution of liability in respect of unpaid share capital, or (ii) the payment to any shareholder of any paid-up share capital, or (iii) in any other case, if the Tribunal so directs, the following provisions shall have effect:

The creditors having a debt or claim admissible in winding-up are entitled to object. To enable them to do so, the Tribunal will settle a list of creditors entitled to object. If any creditor objects, then either his consent to the proposed reduction should be obtained or he should be paid off or his payment be secured. The Tribunal, in deciding whether or not to confirm the reduction will take into consideration the minority shareholders and creditors.

The Tribunal shall give notice of every application made to it under sub-section (1) of section 66 to the Central Government, Registrar and to the Securities and Exchange Board, in the case of listed companies, and the creditors of the company and shall take into consideration the representations, if any, made to it by that Government, Registrar, the Securities and Exchange Board and the creditors within a period of three months from the date of receipt of the notice:

Provided that where no representation has been received from the Central Government, Registrar, the Securities and Exchange Board or the creditors within the said period, it shall be presumed that they have no objection tothe reduction.

There is no limitation on the power of the Court to confirm the reduction except that it must first be satisfied that all the creditors entitled to object to the reduction have either consented or been paid or secured [*British and American Trustee and Finance Corpn. v. Couper,* (1894) AC 399, 403: (1991-4) All ER Rep 667].

When exercising its discretion, the Tribunal must ensure that the reduction is fair and equitable. In short, the Court shall consider the following, while sanctioning the reduction:

(i) The interests of creditors are safeguarded;

(ii) The interests of shareholders are considered; and

(iii) Lastly, the public interest is taken care of.

Confirmation and Registration

Section 66(3) of the Companies Act, 2013 states that if the Tribunal is satisfied that either the creditors entitled to object have consented to the reduction, or that their debts have been determined, discharged, paid or secured, it may confirm the reduction of share capital on such terms and conditions as it deems fit.

Provided that no application for reduction of share capital shall be sanctioned by the Tribunal unless the accounting treatment, proposed by the company for such reduction is in conformity with the accounting standards specified in section 133 or any other provision of this Act and a certificate to that effect by the company›s auditor has been filed with the Tribunal.

Section 66(4) of the Companies Act, 2013 states that the order of confirmation of the reduction of share capital by the Tribunal under sub-section (3) shall be published by the company in such manner as the Tribunal may direct.

Section 66(5) of the Companies Act, 2013 states that the Company shall deliver a certified copy of Tribunal order confirming the reduction together with the minutes giving the details of the company's

(a) amount of share capital;

(b) number of shares into which it is to be divided;

(c) amount of each share; and

(d) amount, if any, at the date of registration deemed to be paid-up on each share,

to the Registrar within 30 days of receipt of the order of Tribunal who will register them. The reduction takes effect only on registration of the order and minutes, and not before. The Registrar will then issue a certificate of registration which will be a conclusive evidence that the requirements of the Act have been complied with and that the share capital is now as set out in the minutes. The Memorandum has to be altered accordingly.

Conclusiveness of certificate for reduction of capital

Where the Registrar had issued his certificate confirming the reduction, the same was held to be conclusive although it was discovered later that the company had no authority under its articles to reduce capital [*Re Walkar & Smith Ltd., (1903) 88 LT 792 (Ch D)*]. Similarly, in a case where the special resolution for reduction was an invalid one, but the company had gone through with the reduction, the reduction was not allowed to be upset [*Ladies's Dress Assn. v. Pulbrook, (1900) 2 QB 376*].

Liability of members in respect of reduced share capital

On the reduction of share capital, a member of the company, past or present, shall not be liable to any call or contribution in respect of any share held by him exceeding the amount of difference, if any, between the amount paid on the share, or reduced amount, if any, which is to be deemed to have been paid thereon, as the case may be, and the amount of the share as fixed by the order of reduction.

In the case of Reckitt Benckiser *(India)* Ltd. (2005) the reduction was objected to by a group of shareholders on the grounds that there was no necessity to reduce capital and the reduction was discriminatory as it would extinguish the class of public shareholders. Ultimately, Reckitt Benckiser *(India)* Ltd. offered to let the objectors remain as shareholders and consequently, the Delhi High Court approved the capital reduction.

If, however the name of any creditor entitled to object to the reduction of share capital under this section is, by reason of his ignorance of the proceedings for reduction or of their nature and effect with respect to his debt or claim, not entered on the list of creditors, and after such reduction, the company commits a default, within the meaning of section 6 of the Insolvency and Bankruptcy Code, 2016, in respect of the amount of his debt or claim –

(a) every person, who was a member of the company on the date of the registration of the order for reduction by the Registrar, shall be liable to contribute to the payment of that debt or claim, an amount not exceeding the amount which he would have been liable to contribute if the company had commenced winding-up on the day immediately before the said date; and

(b) if the company is wound up, the Tribunal may, on the application of any such creditor and proof of his ignorance as aforesaid, if it thinks fit, settle a list of persons so liable to contribute, and make and enforce calls and orders on the contributories settled on the list, as if they were ordinary contributories in a winding up.

Penalties

If any officer of the company

(a) Knowingly conceals the name of any creditor entitled to object to the reduction;

(b) knowingly misrepresents the nature or amount of the debt or claim of any creditor; or

(c) abets or is privy to any such concealment or misrepresentation as aforesaid,

he shall be liable under section 447.

Reduction of capital and Scheme of Compromise and Arrangement

Arrangement includes ‘a reorganisation of share capital of the company’ and reorganisation can involve reduction of share capital. However, as part of the scheme of compromise or arrangement, distinct formalities as prescribed under section 100 do not have to be observed [*Maneckchowk and Ahmedabad Mfg. Co. Ltd., Re (1970) 2 Comp LJ 300 (Guj); also Vasant Investment Corporation Ltd. v. Official Liquidator (1981) 51 Comp Cas 20 (Bom); Mcleod & Co.Ltd. v. S.K. Ganguly (1975) 45 Comp Cas 563 (Cal)*]. It may however be noted that, in all such cases involving reduction of share capital in the scheme of compromise or arrangement, the petition seeking confirmation of the Tribunal with respect to the scheme must also expressly mention that the company is also seeking, at the same time, the confirmation of the Tribunal with respect to the reduction of share capital, and that, while seeking the consent of the members to the scheme, the consent of the members with respect to the reduction of share capital had also been obtained.

The power of Tribunal to give to creditors an opportunity of raising objections to the reduction of capital is discretionary. In an appropriate case, for example, where the interests of creditors are duly and fully protected, the Tribunal may exercise its discretion against calling upon the creditors to raise objections.

BUY-BACK

According to Section 68(1) of the Companies Act, 2013, a company whether public or private, may purchase its own shares or other specified securities (hereinafter referred to as “buy-back”) out of:

(i) its free reserves; or

(ii) the securities premium account; or

(iii) the proceeds of any shares or other specified securities.

However, no buy-back of any kind of shares or other specified securities can be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities. Thus, the company must have at the time of buy-back, sufficient balance in any one or more of these accounts to accommodate the total value of the buy-back.

The term Buy-back has two meanings. Firstly, when a person sells shares or any specified securities and then buys again according to a fixed agreement, the buying back by a company of its shares/securities from an invest or who put venture capital up for the formation of the company.

Secondly, buying of its own stock from open market in order to reduce the number of outstanding shares. It is one of the prominent modes of capital restructuring. It is a corporate action in which a company buys back its shares from the existing shareholders usually at a price higher than market price. When it buys back, the number of shares outstanding in the market reduces. By reducing the number of shares outstanding in the market, buy-backs increase the proportion of shares a company owns.

Modes of Buy-Back

1. **Tender Offer**

   In tender offer, the company makes an offer to buy a certain number of shares/securities at a specific price directly from security holders on proportionate basis. Share buyback ensures all shareholders are treated equally, however small they are.

2. Open Market Purchase

In open market purchase, the company acquires a certain number of shares. Fixes a price cap and buy for any price up to the upper limit. Most companies prefer the open market route. The biggest difference between the two - tender offer and open market purchase- is that the price in the tender route is fixed.

Buy-back from open market can be made through:

- Book Building Process
- Stock exchange.

Advantages of buy-back

- It is an alternative mode of reduction in capital without requiring approval of the National Company Law Tribunal
- To improve the earnings per share
- To improve return on capital, return on net worth and to enhance the long-term shareholders value
- To provide an additional exit route to shareholders when shares are undervalued or thinly traded
- To enhance consolidation of stake in the company
- To prevent unwelcome takeover bids
- To return surplus cash to shareholders
- To achieve optimum capital structure
- To support share price during periods of sluggish market condition
- To serve the equity more efficiently.

Legal Framework for Buy-back

- Companies Act, 2013.
- The Companies (Share Capital and Debentures) Rules, 2014.
- Securities and Exchange Board of India (Buy-back of Securities) Regulations, 2018.

Examples

In June 2023, WIPRO Limited came out with a public announcement of buy back of its equity shares through tender offer upto 26,96,62,921 fully paid up equity shares.

In the year 2017, Infosys decided to utilize cash reserves of USD 6 billion either through share buy-back or generous dividend. Cognizant and TCS announced mega buy-back offers worth USD 3.4 billion and ₹ 16,000 crore, respectively, to return surplus cash to shareholders. HCL Technologies also approved a buy-back of up to 3.50 crore shares worth ₹ 3,500 crore.

Authorisation

The primary requirement is that the articles of association of the company should authorise buy-back. In case, such a provision is not available, it would be necessary to alter the articles of association to authorise buy-back. Buy-back can be made with the approval of the Board of directors at a meeting and/or by a special resolution passed by shareholders in a general meeting, depending on the quantum of buy-back. In case of a listed company, approval of shareholders shall be obtained only by postal ballot.

Quantum of Buy-back

(a) Board of directors can approve buy-back up to 10% of the total paid-up equity capital and free reserves of the company and such buyback has to be authorized by the board by means of a resolution passed at the meeting.

(b) Shareholders by a special resolution can approve buy-back up to 25% of the total paid-up capital and free reserves of the company. In respect of any financial year, the shareholders can approve by special resolution up to 25% of total equity capital in that year.

Post buy-back debt-equity ratio

The ratio of the aggregate of secured and unsecured debts owed by the company after buy-back should not be more than twice the paid-up capital and its free reserves i.e. the ratio shall not exceed 2:1. However, the Central Government may, by order, notify a higher ratio of the debt to capital and free reserves for a class or classes of companies;

All the shares or other specified securities for buy-back are to be fully paid-up.

Buy-back by listed/unlisted companies

The buy-back of the shares or other specified securities listed on any recognized stock exchange is in accordance with the regulations made by the Securities and Exchange Board in this behalf; and

The buy-back in respect of shares or other specified securities other than listed securities is in accordance with such rules made under Chapter IV of the Companies Act, 2013.

Time gap

No offer of buy-back under this sub-section shall be made within a period of one year reckoned from the date of the closure of the preceding offer of buy-back, if any.

Explanatory statement [Section 68(3) & Rule 17(1)]

The notice of the meeting at which the special resolution is proposed to be passed shall be accompanied by an explanatory statement stating—

(a) a full and complete disclosure of all material facts;

(b) the necessity for the buy-back;

(c) the class of shares or securities intended to be purchased under the buy-back;

(d) the amount to be invested under the buy-back; and

(e) the time-limit for completion of buy-back.

(f) the date of the board meeting at which the proposal for buy-back was approved by the board of directors of the company;

(g) the objective of the buy-back;

(h) the number of securities that the company proposes to buy-back;

(i) the method to be adopted for the buy-back;

(j) the price at which the buy-back of shares or other securities shall be made;

(k) the basis of arriving at the buy-back price;

(l) the maximum amount to be paid for the buy-back and the sources of funds from which the buy-back would be financed;

(m) (i) the aggregate shareholding of the promoters and of the directors of the promoter, where the promoter is a company and of the directors and key managerial personnel as on the date of the notice convening the general meeting;

(ii) the aggregate number of equity shares purchased or sold by persons mentioned in sub-clause (i) during a period of twelve months preceding the date of the board meeting at which the buy-back was approved and from that date till the date of notice convening the general meeting;

(iii) the maximum and minimum price at which purchases and sales referred to in sub-clause (ii) were made along with the relevant date.

(n) if the persons mentioned in point (l) & (m) intend to tender their shares for buy-back –

(i) the quantum of shares proposed to be tendered;

(ii) the details of their transactions and their holdings for the last twelve months prior to the date of the board meeting at which the buy-back was approved including information of number of shares acquired, the price and the date of acquisition.

(o) a confirmation that there are no defaults subsisting in repayment of deposits, interest payment thereon, redemption of debentures or payment of interest thereon or redemption of preference shares or payment of dividend due to any shareholder, or repayment of any term loans or interest payable thereon to any financial institution or banking company;

(p) a confirmation that the Board of directors have made a full enquiry into the affairs and prospects of the company and that they have formed the opinion-

(i) that immediately following the date on which the general meeting is convened there shall be no grounds on which the company could be found unable to pay its debts;

(ii) as regards its prospects for the year immediately following that date, that, having regard to their intentions with respect to the management of the company's business during that year and to the amount and character of the financial resources which will in their view be available to the company during that year, the company shall be able to meet its liabilities as and when they fall due and shall not be rendered insolvent within a period of one year from that date; and

(iii) the directors have taken into account the liabilities(including prospective and contingent liabilities), as if the company were being wound up under the provisions of the Companies Act, 2013.

(q) a report addressed to the Board of directors by the company's auditors stating that-

(i) they have inquired into the company's state of affairs;

(ii) the amount of the permissible capital payment for the securities in question is in their view properly determined;

(iii) that the audited accounts on the basis of which calculation with reference to buy back is done is not more than six months old from the date of offer document; and

Provided that where the audited accounts are more than six months old, the calculations with reference to buy back shall be on the basis of un-audited accounts not older than six months from the date of offer document which are subjected to limited review by the auditors of the company.

(iv) the Board of directors have formed the opinion as specified in clause (m) on reasonable grounds and that the company, having regard to its state of affairs, shall not be rendered insolvent within a period of one year from that date.

Buy-back Procedure for Private & Unlisted Public Companies

Rule 17 of the Companies (Share Capital and Debentures) Rules, 2014

According to Rule 17(2) the company which has been authorized by a special resolution shall, before the buy-back of shares, file with the Registrar of Companies a letter of offer in Form No. SH-8, along with the fee as prescribed. Such letter of offer shall be dated and signed on behalf of the Board of directors of the company by not less than two directors of the company, one of whom shall be the managing director, where there is one.

Filing Declaration of Solvency with SEBI/ROC [Rule 17(3)]

When a company proposes to buy-back its own shares or other specified securities under this section in pursuance of a special resolution or board resolution as the case may be, it shall, before making such buy- back, file with the Registrar and the Securities and Exchange Board (in case of listed companies), a declaration of solvency in Form No.SH-9 signed by atleast two directors of the company, one of whom shall be the managing director, if any, in such form as may be prescribed and verified by an affidavit as specified in said form.

Dispatch of letter of Offer [Rule 17(4)]

The letter of offer shall be dispatched to the shareholders or security holders immediately after filing the same with the Registrar of Companies but not later than 21 days from its filing with the Registrar of Companies.

The letter of offer shall contain true, factual and material information and shall not contain any misleading information and must state that the directors of the company accept the responsibility for the information contained in such document; [Rule17(10)(a)]

Validity [Rule 17(5)]

The offer for buy-back shall remain open for a period of not less than15 days and not exceeding 30 days from the date of dispatch of the letter of offer.

Provided that where all members of a company agree, the offer for buy-back may remain open for a period less than fifteen days.

Acceptance on proportional basis [Rule 17(6)]

In case the number of shares or other specified securities offered by the shareholders or security holders is more than the total number of shares or securities to be bought back by the company, the acceptance per shareholder shall be on proportionate basis out of the total shares offered for being bought back.

Time limit for verification [Rule 17(7)]

The company shall complete the verifications of the offers received within 15 days from the date of closure of the offer and the shares or other securities lodged shall be deemed to be accepted unless a communication of rejection is made within 21 days from the date of closure of the offer.

Payment of consideration/returning of share certificates

The company shall within seven days of the time limit of verification:

(a) make payment of consideration in cash to those shareholders or security holders whose securities have been accepted, or

(b) return the share certificates to the shareholders or security holders whose securities have not been accepted at all or the balance of securities in case of part acceptance.

Separate Account [Rule 17(8)]

The company shall immediately after the date of closure of the offer, open a separate bank account and deposit there in, such sum, as would make-up the entire sum due and payable as consideration for the shares tendered for buy-back.

The company shall confirm in its offer the opening of a separate bank account adequately funded for this purpose and to pay the consideration only by way of cash. [Rule 17(10)(c)]

Other conditions [Rule 17(10)]

The rules further provide that the company shall ensure that—

(a) the company shall not issue any new shares including by way of bonus shares from the date of passing of special resolution authorizing the buy-back till the date of the closure of the offer under these rules, except those arising out of any outstanding convertible instruments;

(b) the company shall not withdraw the offer once it has announced the offer to the shareholders;

(c) the company shall not utilize any money borrowed from banks or financial institutions for the purpose of buying back its shares; and the company shall not utilize the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities for the buy-back.

Time limit for completion of buy-back [Section 68(4)]

Every buy-back shall be completed within a period of one year from the date of passing of the special resolution, or as the case may be, the resolution passed by the Board.

Methods of buy-back [Section 68(5)]

The buy-back may be —

(a) from the existing shareholders or security holders on a proportionate basis;

(b) from the open market;

(c) by purchasing the securities issued to employees of the company pursuant to a scheme of stock option or sweat equity.

Extinguishment of securities bought back [Section 68(7)]

When a company buys back its own shares or other specified securities, it shall extinguish and physically destroy the shares or securities so bought back within seven days of the last date of completion of buy-back.

Prohibition of further issue of shares or securities [Section 68(8)]

When a company completes a buy-back of its shares or other specified securities it shall not make a further issue of the same kind of shares or other securities including allotment of new shares under clause (a) of sub-section (1) of section 62 or other specified securities within a period of six months except by way of a bonus issue or in the discharge of subsisting obligations such as conversion of warrants, stock option schemes, sweat equity or conversion of preference shares or debentures into equity shares.

Register of buy-back [Section 68(9)]

When a company buys back its shares or other specified securities , it shall maintain a register of the shares or securities so bought, the consideration paid for the shares or securities bought back,the date of cancellation of shares or securities, the date of extinguishing and physically destroying the shares or securities and such other particulars as may be prescribed.

According to the rules the register of shares or securities bought back shall be maintained in Form SH-10, at the registered office of the company and shall be kept in the custody of the secretary of the company or any other person authorized by the board in this behalf. Entries in the register shall be authenticated by the secretary of the company or by any other person authorized by the Board for the purpose. [Rule 17(12)].

Return of buy back [Section 68 (10)]

A company shall, after the completion of the buy-back under this section, file with the Registrar and the Securities and Exchange Board (in case of listed companies) a return containing such particulars relating to the buy-back within thirty days of such completion, as may be prescribed.

The company shall file with the Registrar, and in case of a listed company with the Registrar and the SEBI, a return in the Form No. SH-11 along with the 'fee'. There shall be annexed to the return filed with the Registrar in Form No. SH-11, a certificate in Form No. SH-15 signed by two directors of the company including the managing director, if any, certifying that the buy-back of securities has been made in compliance with the provisions of the Act and rules made thereunder. [Rule 17(13) and Rule 17(14)]

Penal Provisions [Section 68 (11)]

If a company makes any default in complying with the provisions of this section or any regulation made by the Securities and Exchange Board, in case of listed companies, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees.

Transfer to and application of Capital Redemption Reserve Account (Section 69)

When a company purchases its own shares out of free reserves or securities premium account, a sum equal to the nominal value of the shares so purchased shall be transferred to the capital redemption reserve account and details of such transfer shall be disclosed in the balance sheet. The capital redemption reserve account may be applied by the company, in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares.

Circumstances prohibiting buy back (Section 70)

No company shall directly or indirectly purchase its own shares or other specified securities—

(i) through any subsidiary company including its own subsidiary companies;

(ii) through any investment company or group of investment companies; or

(iii) if a default, is made by the company, in the repayment of deposits accepted either before or after the commencement of this Act, interest payment thereon, redemption of debentures or preference shares or payment of dividend to any shareholder, or repayment of any term loan or interest payable thereon to any financial institution or banking company:

However, the buy-back is not prohibited, if the default is remedied and a period of three years has lapsed after such default ceased to subsist.

No company shall, directly or indirectly, purchase its own shares or other specified securities in case such company has not complied with the provisions of sections 92 (Annual Return), 123 (Declaration of Dividend), 127 (punishment for failure to distribute dividend) and section 129 (Financial Statement) of the Companies Act, 2013.

Income Tax Aspects

Section 46A of the Income-tax Act, 1961 provides that any consideration received by a security holder from any company on buy back shall be chargeable to tax on the difference between the cost of acquisition and the value of consideration received by the security holder as capital gains.

The computation of capital gains shall be in accordance with the provisions of Section 48 of the Income-tax Act, 1961.

In respect of Foreign Institutional Investors (FIIs), as per the provisions of Section 196D (2) of the Income Tax Act,1961 no deduction of tax at source shall be made before remitting the consideration for equity shares tendered under the offer by FIIs as defined under Section 115AD of the Income Tax Act, 1961. NRIs, OCBs and other non-resident shareholders (excluding FIIs) will be required to submit a No Objection Certificate (NOC) or tax clearance certificate obtained from the Income Tax authorities under the Income Tax Act. In case the aforesaid NOC or tax clearance certificate is not submitted, the company should deduct tax at the maximum marginal rate as may be applicable to the category of shareholders on the entire consideration amount payable to such share holders.

BUY-BACK FOR LISTED SECURITIES

A listed company proposing to undertake a buy-back is required to primarily comply with the provisions of the Companies Act, 2013 (the "Companies Act") and the Securities and Exchange Board of India (Buy-Back of Securities) Regulations, 2018 (the "SEBI Regulations"). However, a listed company is also required to ensure compliance with the requirements of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (the "SEBI Takeover Regulations"), the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, the Foreign Exchange Management Act, 1999, the Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015 and other applicable securities laws including in other jurisdictions.

In exercise of powers, SEBI notified Securities and Exchange Board of India (Buy-back of Securities) Regulations, 2018 w.e.f. September 11, 2018. Notification No. SEBI/LAD-NRO/GN/2018/32. All the listed companies are required to comply with SEBI (Buy Back of Securities) Regulations, 2018, in addition to the provisions of the Companies Act, 2013. These regulations broadly cover the following aspects:

1. Special resolution and its additional disclosure requirements.
2. Methods of buy back including buy back through reverse book building, from existing shareholders through tender offer, etc.
3. Filing of offer documents, public announcement requirements.
4. Offer procedure/opening of escrow account, etc.
5. General obligations of company, merchant banker, etc.

Special Resolution and its additional disclosure requirements (Regulation 5)

Sub-regulation (iv) of Regulation 5 of the Regulations, lays down that for the purposes of passing a special resolution the explanatory statement to be annexed to the notice for the general meeting shall contain disclosures as specified in Schedule I to the Regulations.

Sub-regulation (v) provides that a copy of the above resolution passed at the general meeting shall be filed with SEBI and the stock exchanges where the shares or other specified securities of the company are listed, within seven days from the date of passing of the resolution.

In case of Board approval

Regulation 5(vii) of the Regulations, provides that a company, authorized by a resolution passed by the Board of Directors at its meeting to buy back its shares or other specified securities, shall file a copy of the resolution, with the SEBI and the stock exchanges, where the shares or other specified securities of the company are listed,within two working days of the date of the passing of the resolution.

Disclosures under Schedule I (Contents of Explanatory Statement)

An explanatory statement containing full and complete disclosure of all the material facts and the following disclosures prescribed in Schedule I of the Regulations should be annexed to the notice where the buy-back is pursuant to shareholders' approval:

(i) Date of the Board meeting at which the proposal for buy back was approved by the Board of Directors of the company;

(ii) Necessity for the buy back;

(iii) Maximum amount required under the buy back and its percentage of the total paid up capital and free reserves;

(iv) Maximum price at which the shares or other specified securities are proposed be bought back and the basis of arriving at the buy back price;

(v) Maximum number of securities that the company proposes to buy back;

(vi) Method to be adopted for buy back as referred in sub-regulation (iv) of regulation 4;

(vii) (a) the aggregate shareholding of the promoter and of the directors of the promoters, where the promoter is a company and of persons who are in control of the company as on the date of the notice convening the General Meeting or the Meeting of the Board of Directors;

(b) aggregate number of shares or other specified securities purchased or sold by persons including persons mentioned in (a) above from a period of six months preceding the date of the Board Meeting at which the buy back was approved till the date of notice convening the general meeting;

(c) the maximum and minimum price at which purchases and sales referred to in (b) above were made along with the relevant dates.

(viii) Intention of the promoters and persons in control of the company to tender shares or other specified securities for buy-back indicating the number of shares or other specified securities, details of acquisition with dates and price;

(ix) A confirmation that there are no defaults subsisting in repayment of deposits, redemption of debentures or preference shares or repayment of term loans to any financial institutions or banks;

(x) A confirmation that the Board of Directors has made a full enquiry into the affairs and prospects of the company and that they have formed the opinion-

(a) that immediately following the date on which the General Meeting or the meeting of the Board of Directors is convened there will be no grounds on which the company could be found unable to pay its debts;

(b) as regards its prospects for the year immediately following that date that, having regard to their intentions with respect to the management of the company's business during that year and to the amount and character of the financial resources which will in their view be available to the company during that year, the company will be able to meet its liabilities as and when they fall due and will not be rendered insolvent within a period of one year from that date; and

(c) in forming their opinion for the above purposes, the directors shall take into account the liabilities as if the company were being wound up under the provisions of the Companies Act, 1956 or Companies Act or the Insolvency and Bankruptcy Code, 2016 (including prospective and contingent liabilities).

(xi) Areport addressed to the Board of Directors by the company's auditors stating that–

(a) they have inquired into the company's state of affairs;

(b) the amount of the permissible capital payment for the securities in question is in their view properly determined; and

(c) the Board of Directors have formed the opinion as specified in clause(x) on reasonable grounds and that the company will not, having regard to its state of affairs, will not be rendered insolvent within a period of one year from that date.

(xii) Prior approval obtained from the unders of the company in case of a breach of any covenant with such unders.

Methods of Buy-Back (Regulation 4)

According to Regulation 4 of the Regulations, a company may buy back its own shares or other specified securities by any one of the following methods:

(a) from the existing shareholders or other specified securities holders on a proportionate basis through the tender offer;

(b) from the open market through:

   (i) book-building process

   (ii) stock exchange.

It may be noted that no offer of buy back for 15% or more of paid up capital and free reserves, shall be made from the open market.

In terms of Regulation 4(vii), a company shall not make any offer of buy-back within a period of one year reckoned from the date of expiry of buy-back period of the preceding offer of buy-back, if any.

Regulation 4(vi) does not permit buy-back through negotiated deals (of and on stock exchange), private arrangement, spot transactions.

Regulation 4(v) prohibits a company to buy-back its shares or other specified securities so as to delist its shares or other specified securities from the stock exchange.

Buy-back from existing security-holders through tender offer (Regulation 6)

According to Regulation 6 of the Regulations, a company may buy-back its securities from its existing security-holders on a proportionate basis in accordance with the provisions of the Regulations. It may be noted that fifteen per cent of the number of securities which the company proposes to buy back or number of securities entitled as per their shareholding, whichever is higher, shall be reserved for small shareholders.

Additional Disclosures (Regulation 5(iv)(c))

In addition to disclosure required under Schedule I, where the buy-back is through tender offer from existing securities holders, following additional disclosures are required to be made to the explanatory statement:

(a) the maximum price at which the buy-back of shares or other specified securities shall be made and whether the Board of Directors of the company is being authorized at the general meeting to determine subsequently the specific price at which the buy-back may be made at the appropriate time;

(b) if the promoter intends to offer their shares or others pacified securities, the quantum of shares or other specified securities proposed to be tendered, and the details of their transactions and their holdings for the last six months prior to the passing of the special resolution for buy-back including information of number of shares or other specified securities acquired, the price and the date of acquisition.

Public Announcement and Filing of Offer Documents (Regulation 7 & 8)

The company which has been authorized by a special resolution or a resolution passed by the Board of Directors at its meeting shall make a public announcement within two working days from the date of declaration of results of the postal ballot for special resolution/board of directors resolution in at least one English National Daily, one Hindi National Daily and a Regional language daily all with wide circulation at the place where the Registered office of the company is situated and shall contain all the material information as specified in Schedule II.

A copy of the public announcement in electronic mode file with the Board and stock exchanges on which its shares/securities are listed.

The company shall within two working days of the public announcement file with the Board a letter of offer, containing disclosures as specified in Schedule III through a merchant banker who is not associated with the company, a declaration of solvency in the prescribed form and in a manner provided in section 68(6) of the Companies Act, 2013.

Offer Procedure (Regulation 9)

1. A company making a buyback offer shall announce a record date in the public announcement for the purpose of determining the entitlement and the names of the security holders, who are eligible to participate in the proposed buy- back offer.

2. The letter of offer along with the tender form shall be dispatched to the security holders who are eligible to participate in the buy-back offer.

   Even if an eligible public shareholder does not receive the tender offer/offer form, he may participate in the buy-back offer and tender shares in the manner as provided by the Board.

   An unregistered shareholder may also tender his shares for buy-back by submitting the duly executed transfer deed for transfer of shares in his name, along with the offer form and other relevant documents as required for transfer, if any.

3. The date of the opening of the offer shall be not later than four working days from the date of dispatch of letter of offer.

4. The offer for buy back shall remain open for a period of five working days.

5. The company shall accept shares or other specified securities from the security holders on the basis of their entitlement as on record date.

6. The shares proposed to be bought back shall be divided in to two categories; (a) reserved category for small shareholders and (b) the general category for other shareholders, and the entitlement of a shareholder in each category shall be calculated accordingly.

   Explanation: Holdings of multiple demat accounts would be clubbed together for identification of small shareholder if sequence of Permanent Account Number for all holders is matching. Similarly, in case of physical shareholders, if the sequence of names of joint holders is matching, holding under such folios should be clubbed together for identification of small shareholder.

7. After accepting the shares or other specified securities tendered on the basis of entitlement, shares or other specified securities left to be bought back, if any in one category shall first be accepted, in proportion to the shares or other specified securities tendered over and above their entitlement in the offer by security holders in that category and thereafter from security holders who have tendered over and above their entitlement in other category.

Payment to the Security holders (Regulation 10)

Regulation lays down that—

1. The company shall immediately after the date of closure of the offer, open a special account with a SEBI registered banker to an issue and deposit therein, such sum as would, together with ninety percent of the amount lying in the escrow account make up the entire sum due and payable as consideration for the buy-back and for this purpose, may transfer the funds from the escrow account.

2. The company shall complete the verifications of offers received and make payment of consideration to those security holders whose offer has been accepted and return the remaining shares or other specified securities to the security holders within five working days of the closure of the offer.

Extinguishing of bought-back securities (Regulation 11)

The company shall extinguish and physically destroy the security certificates so bought back in the presence of a Registrar to issue or the Merchant Banker and the Secretarial Auditor within fifteen days of the date of acceptance of the shares or other specified securities. The company shall also ensure that all the securities bought-back are extinguished within seven working days of expiry of buy-back period. The aforesaid period of fifteen days shall in no case extend beyond seven days of expiry of buy-back period.

The shares or other specified securities offered for buy-back if already dematerialised shall be extinguished and destroyed in the manner specified under the Securities and Exchange Board of India (Depositories and Participants) Regulations,1996, and the bye-laws, the circulars and guidelines framed thereunder.

The company shall, furnish a certificate to the Board certifying compliance as specified above and duly certified and verified by-

(i) the registrar and whenever there is no registrar by the merchant banker;

(ii) two directors of the company one of whom shall be a managing director where there is one;

(iii) the Secretarial auditor of the company.

The certificate shall be furnished to the Board within seven days of extinguishment and destruction of certificates.

The company shall furnish, the particulars of the security certificates extinguished and destroyed, to the stock exchanges where the shares of the company are listed within seven days in which the securities certificates are extinguished and destroyed. The company shall also maintain a record of security certificates which have been cancelled and destroyed as prescribed in Section 68(9) of the Companies Act.

CASE STUDY

Merger of HDFC & HDFC Bank

India's largest housing finance company, HDFC Ltd and the largest private sector bank, HDFC Bank, merged in 2022 in one of the biggest financial deals in India. The $40 billion deal will result in a single entity. Let us discuss details about HDFC LTD/HDFC BANK Merger.

Brief about the Companies

HDFC Investments Limited (Transferor Company No.1) is a Systemically Important Non-Deposit Taking Non-Banking Financial Company registered with the Reserve Bank of India (RBI) and is primarily engaged in the business of making investments in equity shares, preference shares, venture funds, mutual funds and other securities.

HDFC Holdings Limited (Transferor Company No.2) is also a Systemically Important Non-Deposit Taking Non-Banking Financial Company registered with the RBI and is primarily engaged in the business of making investments in equity shares, preference shares, venture funds, mutual funds and other securities.

Housing Development Finance Corporation Limited (Transferee Company/ Amalgamating Company) is principally engaged in the business of providing finance to individuals, corporates and developers for the purchase, construction, development and repair of houses, apartment and commercial properties in India through its branches in India and overseas offices supported by network of agents for sourcing loans as well as deposits.

HDFC Bank Limited (Amalgamated Company) is registered with RBI as a banking company under the provisions of the Banking Regulation Act, 1949.

Transferor Companies are wholly-owned subsidiaries of the Transferee Company/ Amalgamating Company and that the entire paid-up share capital of the respective Transferor Companies are held by the Transferee

Company/ Amalgamating Company. Transferor Companies and Transferee Company/ Amalgamating Company are promoter companies of the Amalgamated Company.

Transferee Company/ Amalgamating Company and the Amalgamated Company are both listed on BSE Limited (“BSE”) and National Stock Exchange Limited (“NSE”)

Composite Scheme of Amalgamation

Sanction of Composite Scheme of Amalgamation among Transferor Companies, Transferee Company and Amalgamated Company sought before the Hon’ble NCLT under Sections 230 to 232 and other applicable provisions of the Companies Act, 2013 and in compliance with the provisions of the Income Tax Act, 196

The Scheme, inter alia, provides for the:

(a) Amalgamation of the Transferor Company No. 1 and the Transferor Company No. 2 (together referred to as the “Transferor Companies”) with and into the Transferee Company/Amalgamating Company, with effect from the Appointed Date and the consequent dissolution of the Transferor Companies without being wound up; and

(b) Amalgamation of the Transferee Company/Amalgamating Company with and into the Amalgamated Company, with effect from the Appointed Date and the consequent dissolution of the Transferee Company/Amalgamating Company without being wound up, and the issuance of the New Equity Shares (as defined in the Scheme) to the equity shareholders of the Transferee Company/ Amalgamating Company as on the Record Date (as defined in the Scheme) in accordance with the Share Exchange Ratio.

Rationale and Benefits of the Scheme

- the Amalgamation, through the Scheme, shall enable the Amalgamated Company to build its housing loan portfolio and enhance its existing customer base;
- the Amalgamation is based on leveraging the significant complementarities that exist amongst the parties to the Scheme. The Amalgamation would create meaningful value for various stakeholders including respective shareholders, customers, employees, as the combined business would benefit from increased scale, comprehensive product offering, balance sheet resiliency and the ability to drive synergies across revenue opportunities, operating efficiencies and underwriting efficiencies, amongst others;
- the Amalgamated Company is a private sector bank and has a large base of over 6.8 Crore customers. The bank platform will provide a well-diversified low cost funding base for growing the long tenor loan book acquired by the Amalgamated Company pursuant to the Amalgamation;
- the Amalgamated Company is a banking company with a large distribution network that offers product offerings in the retail and wholesale segments. The Amalgamating Company is a premier housing finance company in India and provides housing loans to individuals as well as loans to corporates, undertakes lease rental discounting and construction finance apart from being a financial conglomerate. A combination of the Amalgamating Company and the Amalgamated Company is entirely complementary to, and enhances the value proposition of, the Amalgamated Company;
- the Amalgamated Company would benefit from a larger balance sheet and networth which would allow underwriting of larger ticket loans and also enable a greater flow of credit into the Indian economy;
- the Amalgamating Company has invested capital and developed skills and has set up approximately 464 (Four Hundred and Sixty Four) offices across the country. These offices can be used to sell the entire product suite of both the Amalgamating Company and the Amalgamated Company;
- the loan book of the Amalgamating Company is diversified having cumulatively financed over 90 lakh dwelling units. With the Amalgamating Company’s leadership in the home loan arena, developed

over the past 45 years, the Amalgamated Company would be able to provide to customers flexible mortgage offerings in a cost-effective and efficient manner;

- the Amalgamated Company has access to funds at lower costs due to its high level of current and savings accounts deposits (CASA). With the amalgamation of the Amalgamating Company with the Amalgamated Company, the Amalgamated Company will be able to offer more competitive housing products;
- the Amalgamating Company's rural housing network and affordable housing lending is likely to qualify for Amalgamated Company as priority sector lending and will also enable a higher flow of credit into priority sector lending, including agriculture;
- the Amalgamation will result in reducing the Amalgamated Company's proportion of exposure to unsecured loans;
- the Amalgamating Company has built technological capabilities to evaluate the credit worthiness of customers using analytical models and has developed unique skills in financing various customer segments. The models have been tested and refined over the years at scale and the Amalgamated Company will benefit from such expertise in underwriting and financing of mortgage offerings;
- the Amalgamated Company can leverage on the loan management system, comprising rule engines, IT tools and rules, agents connected through a central system;
- the Amalgamation is expected to result in bolstering the capital base and bringing in resiliency in the balance sheet of the Amalgamated Company;
- the Transferor Companies are Systemically Important Non - Deposit Taking Non - Banking Financial Companies and are also wholly owned subsidiaries of the Amalgamating Company. The Amalgamation shall result in a simplified corporate structure.
- the Amalgamation would therefore be in the best interest of the shareholders of the respective parties to the Scheme and shall not in any manner be prejudicial to the interests of the concerned shareholders or the creditors or general public at large.

Chronological Events & Regulatory Approvals of Merger

- Board of Directors of the Transferor Company No. 1, the Transferor Company No. 2, the Transferee Company/Amalgamating Company and the Amalgamated Company in their respective meetings held on April 3, 2022, April 3, 2022, April 4, 2022 and April 4, 2022 have approved the proposed Scheme.
- The Transferee Company/Amalgamating Company and the Amalgamated Company had entered into an Implementation Agreement dated April 4, 2022, setting out the manner of effecting the Scheme and the rights and obligations of the respective parties in relation to the Scheme. The principal objectives of the Implementation Agreement are to
  - set out the agreement between the parties in relation to the Scheme;
  - provide the detailed mechanism for giving effect to the Scheme and the related matters upon the Scheme coming into effect or being terminated/withdrawn; and
  - provide appropriate representations and warranties by the parties.
- BSE Limited ("BSE") and National Stock Exchange Limited ("NSE") by their separate letters all dated July 2, 2022 have respectively given their "no adverse observation/ no-objection" to the Transferee Company/ Amalgamating Company and the Amalgamated Company to file the Scheme with this Tribunal.
- Transferee Company/ Amalgamating Company and the Amalgamated Company had jointly filed the necessary notification form with the Competition Commission of India on June 20, 2022. The

Competition Commission of India vide its letter dated August 12, 2022 has provided its approval to the Scheme.

- Pursuant to the application made by the Amalgamated Company to the RBI, RBI by its letter dated July 4, 2022 has granted its 'no-objection' to the Scheme.
- Hon'ble National Company Law Tribunal, Mumbai Bench, Mumbai on October 14, 2022 in its Order has directed convening of a meeting of the Equity Shareholders of HDFC Bank Limited ("Amalgamated Company") for the purpose of considering, and if thought fit, approving the arrangement embodied in the Composite Scheme of Amalgamation among HDFC Investments Limited and HDFC Holdings Limited and Housing Development Finance Corporation Limited and the Amalgamated Company and their respective shareholders and creditors (hereinafter referred to as the "Scheme") pursuant to the provisions of Sections 230-232 of the Companies Act, 2013 and the other applicable provisions thereof and applicable rules thereunder.
- Meeting of the equity shareholders of the Amalgamated Company held on Friday, November 25, 2022.
- Pursuant to the application made by the Transferee Company/Amalgamating Company under Regulation 59 of Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 (hereinafter referred to as "SEBI Listing Regulations"), BSE and NSE, by their separate letters both dated December 13, 2022, have granted their in-principle approval under Regulation 59 of SEBI Listing Regulations for transfer of non-convertible debentures issued by Transferee Company/Amalgamating Company to Amalgamated Company.
- The Company Scheme Petition is filed before the Hon'ble NCLT in consonance with Sections 230 to 232 of the Act along with the Order dated October 14, 2022 passed in CA(CAA) No.200/MB/2022 read with Order dated December 16, 2022 passed in CP(CAA) No.243 of 2022 of NCLT.
- The Regional Director, Ministry of Corporate Affairs has filed his Report dated December 21, 2022 setting out his observations on the Scheme. In response to the observations made by the Regional Director, the Transferor Companies, Transferee Company & Amalgamated Company have given necessary clarifications and undertakings by way of a Joint Affidavit dated January 9, 2023.
- Regional Director satisfied with the undertakings given by the Petitioners and states that the Scheme is otherwise not prejudicial to the interests of the shareholders/creditors and the public. The said undertakings are accepted.
- The Official Liquidator had sought for certain clarifications by its letter dated January 4, 2023. The same was replied to by the Transferor Companies/Transferee Company by their letter dated January 9, 2023. The Official Liquidator has duly recorded/ referred to the said reply in its report dated January 12, 2023. Based on the reply given by the Transferor Companies/Transferee Company, amongst others, it has been observed/noticed by the Official Liquidator in its report that the affairs of the Transferor Companies have been conducted in a proper manner.
- Transferor Companies, Transferee Company & Amalgamated Company have complied with all the requirements as per the directions of NCLT and have filed the necessary affidavits all dated January 7, 2023 before the NCLT showing compliance.

Approval of Scheme by NCLT

Hon'ble NCLT Mumbai Bench, (Court-II) in the Company Scheme Petition No.243 of 2022 connected with Company Scheme Application No.200 of 2022 vide its Order delivered on 17.03.2023 inter alia order that *the Company Scheme Petition appears to be fair and reasonable and is not violative of any provisions of law and is not contrary to public policy.*

The Petitioners are directed to lodge a copy of this Order and Scheme duly certified by the Deputy Registrar, National Company Law Tribunal, Mumbai Bench, with the concerned Superintendent of Stamps, for the purpose *of adjudication of stamp duty payable on the same, if any, within 60 (sixty) days from the date of the Scheme becoming effective in terms of Clause 5.1 (o) of Part B of the Scheme.*

Petitioner Companies are directed to file a copy of this Order alongwith a copy of the Scheme with the concerned Registrar of Companies electronically in addition to physical copies within 30 days from the receipt of the certified copy of the order along with additional fees, if any.

Parties are at liberty to apply to this Tribunal for any directions that may be necessary, including for an extension of the above period.

All concerned regulatory authorities to act on a copy of this Order alongwith the Scheme duly authenticated by the Deputy Registrar, National Company Law Tribunal, Mumbai Bench.

HDFC Ltd & HDFC Bank Merge Effective from July 1, 2023

HDFC Bank in its news release dated June 30, 2023 inter alia stated that HDFC Bank, India's leading private sector bank announced the successful completion of merger of HDFC Ltd., India's premier housing finance company with and into HDFC Bank, following the receipt of all requisite shareholder and regulatory approvals. HDFC Bank and HDFC Ltd. had announced a decision to merge on April 4, 2022, subject to obtaining the requisite consent and approvals and had indicated a time frame of 15 to 18 months for the process to be concluded. The Boards of both the companies at their respective meetings held and noted that the merger would be effective from July 1, 2023.

The merged entity inter-alia brings together significant complementarities that exist between both the entities and is poised to create meaningful value for various stakeholders, including respective customers, employees, and shareholders of both the entities from increased scale, comprehensive product offering, balance sheet resiliency and ability to drive synergies across revenue opportunities, operating efficiencies and underwriting efficiencies............. .

The merger of India's largest Housing Finance Company, HDFC Ltd. with the largest private sector bank in India combines the strengths of a trusted home loan brand with an institution that enjoys a lower cost of funds. The larger net-worth would allow greater flow of credit into the economy. It will also enable underwriting of larger ticket loans, including infrastructure loans and contribute further to nation building and employment generation.

Source:

1. https://www.hdfcbank.com/
2. https://www.hdfcbank.com/content/bbp/repositories/723fb80a-2dde-42a3-9793-7ae1be57c87f/?path=/Footer/About%20Us/Corporate%20Governance/Composite%20Scheme%20of%20Amalgamation/NCLT-ORDER.pdf
3. https://www.hdfcbank.com/content/bbp/repositories/723fb80a-2dde-42a3-9793-7ae1be57c87f/?path=/Footer/About%20Us/News%20Room/Press%20Release/Content/2023/pdf/Press_Release_HDFC_Ltd_to_merge_into_HDFC_Bank_effective_July_1_2023.pdf

Demerger of Reliance Industries Limited 's Financial Arm

Brief of the Demerger Scheme

Reliance Industries Ltd. announced the demerger of its financial services arm Reliance Strategic Investments, which would be renamed later on **as Jio Financial Services Ltd. (JFSL).**

The Hon'ble National Company Law Tribunal, Mumbai Bench, vide its order dated June 28, 2023, sanctioned the Scheme of Arrangement between Reliance Industries Limited ("RIL" or "Company") and its shareholders and creditors & Reliance Strategic Investments Limited ("RSIL") and its shareholders and creditors ("Scheme") providing, inter alia, for demerger, transfer and vesting of the Financial Services Business (Demerged Undertaking as defined in the Scheme) from the Company into RSIL on a going concern basis and issue of equity shares by

RSIL to the shareholders of the Company, in consideration thereof, in accordance with the provisions of Section 2(19AA) of the Income Tax Act, 1961.

In accordance with provisions of the Scheme, RSIL shall issue and allot 1 (One) fully paid-up equity share of RSIL having face value of Rs 10 (Rupees Ten) each for every 1 (One) fully paid-up equity share of Rs 10 (Rupees Ten) each of the Company to the shareholders of the Company whose names are recorded in the register of members and / or records of the depository as on the Record Date (i.e., Thursday, July 20, 2023).

Brief about the Companies

Reliance Industries Limited (RIL) ***(Demerged Company)***, was incorporated on May 8, 1973, under the provisions of the Companies Act, 1956 under the name 'Mynylon Limited'. This name of 'Mynylon Limited' was subsequently changed to 'Reliance Textile Industries Limited' on March 11, 1977. A certificate of incorporation consequent upon change of name has been issued by the Registrar of Companies, Karnataka, Bangalore. The registered office of the RIL was changed from the State of Karnataka to the State of Maharashtra, and certificates of registration of the order of the Company law Board confirming such transfer of registered office had been issued by the Registrar of Companies, Maharashtra, Bombay on August 4, 1977, and by the Registrar of Companies, Karnataka, Bangalore on August 5, 1977. The name 'Reliance Textiles Industries Limited' was subsequently changed to the present name, 'Reliance Industries Limited' on June 27, 1985. A certificate of incorporation consequent upon change of name had been issued by the Registrar of Companies, Maharashtra, Mumbai.

The RIL, *inter alia,* has multiple undertakings viz., digital services, retail, financial services, advanced materials and composites, renewables (solar and hydrogen), exploration & production and oil to chemicals. The equity shares and non-convertible debentures of the RIL are listed on BSE Limited and National Stock Exchange of India Limited. The global depository receipts of the RIL are listed on Luxembourg Stock Exchange and are traded on the International Order Book (IOB) (London Stock Exchange) and amongst qualified institutional investors on the over-the-counter (OTC) market in the United States of America. The foreign currency bonds of the RIL are listed on the Singapore Exchange Limited, Luxembourg Stock Exchange and India International Exchange (IFSC) Limited.

Reliance Strategic Investments Limited (RSIL) ***(Resulting Company)***, a company incorporated under the provisions of the Companies Act, 1956 and is a wholly-owned subsidiary of RIL. The resulting company is a registered Non-Banking Financial Company (NBFC) (systemically important non-deposit taking non-banking financial company). The name of the Company stands changed from Reliance Strategic Investments Limited to "Jio Financial Services Limited" effective July 25, 2023.

Scheme of Arrangement

Reliance announced the demerger of its financial services arm Reliance Strategic Investments Limited as part of its group restructuring. The Scheme of Arrangement provides for:

(a) demerger, transfer and vesting of the Demerged Undertaking from the Reliance Industries Limited (RIL) into the Reliance Strategic Investments Limited (RSIL) on a *going concern* basis, and issue of 1 (One) fully paid-up equity share of the Reliance Strategic Investments Limited (RSIL) having face value of Rs 10 (Rupees Ten) each for every 1 (One) fully paid-up equity share of Rs 10 (Rupees Ten) each of the Reliance Industries Limited (RIL), in consideration thereof, in accordance with the provisions of Section 2(19AA) of the Income Tax Act; and

(b) reduction and cancellation of the entire pre-Scheme share capital of the Reliance Strategic Investments Limited (RSIL).

The Scheme also provides for various other matters consequent and incidental thereto.

Rationality of Demerged Scheme

(i) The Demerged Company is India's biggest conglomerate with interests in multiple businesses. One amongst the multiple businesses carried on by the Demerged Company is the Financial Services Business which is carried on by the Demerged Company directly and through its subsidiaries and joint ventures.

(ii) Further growth and expansion of the Financial Services Business would require differentiated strategy aligned to its industry specific risks, market dynamics and growth trajectory.

(iii) The nature and competition involved in the financial services business is distinct from the other businesses and it is capable of attracting a different set of investors, strategic partners, lenders and other stakeholders.

Apportionment of Cost of Acquisition of Equity Shares of Reliance Industries Limited and Reliance Strategic Investments Limited

As per the Reliance Industries Ltd.'s stock exchange filings, the company informed the shareholders to apportion pre demerger cost of acquisition of equity shares in the Company in the following manner:

Sr No.	Name of Company	% of Cost of Acquisition of Equity Shares of the Company
	Reliance Industries Limited	95.32%
	Reliance Strategic Investments Limited	4.68%

For example, suppose a person purchased a share of Reliance Industries Ltd. on February 10, 2021, at Rs 2,000. Then, post-demerger, the cost of acquisition for the share of Reliance Industries Ltd. will be Rs 1,906.4 (95.32 per cent of Rs 2,000), and cost of acquisition for allotted share of Reliance Strategic Investments Limited will be Rs 93.6 (4.68 per cent of Rs 2,000).

Chronological Events & Regulatory Approvals of Merger

1. In October, 2022, Reliance Industries Limited (RIL) has announced that it would demerge and list its financial services business - Reliance Strategic Investments Limited (RSIL) - which will be renamed Jio Financial Services (JFS). Reliance shareholders would get one share of Jio Financial Services for holding one share of Reliance.

2. The sanction of Hon'ble Tribunal has been sought under Sections 230 to 232 and other applicable provisions of the Companies Act, 2013 to the Scheme of Arrangement between RIL and its shareholders and creditors of RSIL and its shareholders and creditors ("Scheme").

3. Observation letters dated February 27, 2023 issued by BSE Limited and dated February 28, 2023 issued by National Stock Exchange of India Limited received by RIL respectively.

4. Application Order passed by Hon'ble Tribunal on March 27, 2023.

5. As per the Scheme "Appointed Date" is closing business hours of March 31, 2023 or such other date as may be approved by the Boards of the Demerged Company and the Resulting Company.

6. As directed by this Hon'ble Tribunal *vide* the Application Order, the meetings of the secured creditors, the unsecured creditors and the equity shareholders of the RIL were duly convened and held on May 2, 2023.

7. A meeting of the equity shareholders, secured creditors & unsecured creditors of the RIL convened on 2nd May, 2023 respectively for approving the Scheme of Arrangement.

8. Meeting of equity shareholders (7), preference shareholder (1), secured creditors (Nil) & unsecured creditor (1) of RSIL was dispensed with due to a smaller number of shareholder and creditors and received consents from all the equity shareholders secured creditors & unsecured creditors in the form of affidavits approving the Scheme.

9. The Chairperson appointed for the said meetings of the secured creditors, the unsecured creditors and the equity shareholders of the RIL has filed his report dated May 4, 2023 showing the conduct and results of the said meetings.

10. Hon'ble Tribunal admitted the Company Scheme Petition on May 12, 2023 and fixed June 22, 2023 as the date for hearing and final disposal of the Company Scheme Petition.

11. The Central Government through the Regional Director has filed its report dated May 30, 2023 and has presented certain information derived from the records of the case and has prayed for kind consideration and disposal of the case as the Hon'ble Tribunal may deem fit and proper.

12. The RIL & RSIL were directed to publish the notice of hearing of the Company Scheme Petition in newspapers on June 2, 2023.

13. RIL & RSIL have also served notice of hearing and final disposal of Company Scheme Petition upon: (i) the Central Government through the Regional Director (ii) the Registrar of Companies (iii) the Income Tax Authorities (iv) Goods & Services Tax Authority.

14. RIL & RSIL have filed an Affidavit dated June 8, 2023 confirming, *inter alia*, the publication of newspaper advertisements and service of notice upon the abovementioned regulatory authorities.

15. Since all the requisite statutory compliances have been fulfilled by the Demerged and Resultant Company & Company Scheme Petition appears to be fair and reasonable and is not violative of any provisions of law and is not contrary to public policy, Hon'ble NCLT has sanctioned the Demerger Scheme vide its Order dated June 28, 2023.

16. The name of the Company stands changed from Reliance Strategic Investments Limited to "Jio Financial Services Limited" effective July 25, 2023 and the certificate of incorporation issued by the Registrar of Companies, Mumbai dated July 25, 2023.

The demerger of Reliance Industries Ltd. of its financial services arm Reliance Strategic Investments, which is now **Jio Financial Services Ltd.,** will accrue the benefits such as creation of an independent company focusing exclusively on financial services and exploring opportunities in the said sector; the independent company can attract different sets of investors, strategic partners, lenders and other stakeholders having a specific interest in the financial services business; a financial services company can have a higher leverage (as compared to the Demerged Company) for its growth; and unlocking the value of the Demerged Undertaking for the shareholders of the Demerged Company. The Scheme is in the interests of all stakeholders of the Demerged Company and the Resulting Company.

References:

1. https://nclt.gov.in/gen_pdf.php?filepath=/Efile_Document/ncltdoc/casedoc/2709138055732023/04/Order-Challenge/04_order-Challange_004_16885467751197370623564a52dd7e2cf5.pdf

2. https://nclt.gov.in/gen_pdf.php?filepath=/Efile_Document/ncltdoc/casedoc/2709138079292023/04/Order-Challenge/04_order-Challange_004_1691733978209715247064d5cfda82c19.pdf

Demerger of ITC 's Hotel Business

Case study is based on Scheme of Arrangement amongst ITC Limited ('Demerged Company') and ITC Hotels Limited ('Resulting Company') and their respective shareholders and creditors under Sections 230 to 232 read with other applicable provisions of the Companies Act, 2013 ('Scheme').

The Scheme of Arrangement involves the demerger of the Demerged Undertaking comprising the Hotels Business of the Demerged Company into the Resulting Company on a going concern basis and in consideration, the consequent issuance of equity shares by the Resulting Company to all the shareholders of the Demerged Company in accordance with the Share Entitlement Ratio i.e. *"for every 10 (Ten) Ordinary Shares of face and paid-up value of Re. 1 each held in the Demerged Company, 1 (One) equity share of face and paid-up value of Re. 1 in the Resulting Company".*

Brief Details of the Company

ITC is one of India's foremost private sector companies and a diversified conglomerate with businesses spanning Fast Moving Consumer Goods, Hotels, Paperboards and Packaging, Agri Business and Information Technology. The Company is acknowledged as one of India's most valuable business corporations with a Gross Revenue of ₹ 69,481 crores and Net Profit of ₹ 18,753.31 crores (as on 31.03.2023). ITC was ranked as India's most admired company, according to a survey conducted by Fortune India, in association with Hay Group.

ITC is the country's leading FMCG marketer, the clear market leader in the Indian Paperboard and Packaging industry, a globally acknowledged pioneer in farmer empowerment through its wide-reaching Agri Business, a pre-eminent hotel chain in India that is a trailblazer in 'Responsible Luxury'. ITC's wholly-owned subsidiary, ITC Infotech, is a specialized global digital solutions provider.

Over the last decade, ITC's new Consumer Goods Businesses have established a vibrant portfolio of 25+ world-class Indian brands that create and retain value in India. ITC's world class FMCG brands including Aashirvaad, Sunfeast, Yippee!, Bingo!, B Natural, ITC Master Chef, Fabelle, Sunbean, Fiama, Engage, Vivel, Savlon, Classmate, Paperkraft, Mangaldeep, Aim and others have garnered encouraging consumer franchise within a short span of time. While several of these brands are market leaders in their segments, others are making appreciable progress.

Established in 1910, ITC Limited is a diversified conglomerate with businesses spanning Fast Moving Consumer Goods comprising Foods, Personal Care, Cigarettes and Cigars, Education & Stationery Products, Incense Sticks and Safety Matches; Hotels, Paperboards and Packaging, Agri Business and Information Technology. The Company was incorporated on August 24, 1910 under the name Imperial Tobacco Company of India Limited. As the Company's ownership progressively Indianised, the name of the Company was changed to India Tobacco Company Limited in 1970 and then to I.T.C. Limited in 1974. In recognition of the ITC's multi-business portfolio encompassing a wide range of businesses, the full stops in the Company's name were removed effective September 18, 2001. The Company now stands rechristened 'ITC Limited,' where 'ITC' is today no longer an acronym or an initialised form.

In 1975, the Company launched its Hotels Business with the acquisition of a hotel in Chennai which was rechristened ‹ITC-Welcomgroup Hotel Chola' **(**now renamed Welcomhotel by ITC Hotels, Cathedral Road, Chennai**).** The objective of ITC's entry into the hotels business was rooted in the concept of creating value for the nation. ITC chose the Hotels business for its potential to earn high levels of foreign exchange, create tourism infrastructure and generate large scale direct and indirect employment. The business also launched The two new brands: Mementos by ITC Hotels - A new brand of luxury hotels & resorts that offers those rarest of luxuries i.e Great Memories and Storii by ITC Hotels- A collection of handpicked boutique properties, offering bespoke stays & immersive experiences. Since then ITC's Hotels business has grown to occupy a position of leadership, with over 115 owned and managed properties spread across India under six brands namely, ITC Hotels, Mementos, Welcomhotel, Storii, Fortune Hotels and WelcomHeritage. ITC Hotels recently took its first step toward international expansion with an upcoming super premium luxury hotel in Colombo, Sri Lanka.

Demerged Undertaking comprising the Hotels Business of the Demerged Company ". Hotels Business" includes the business of owning, licensing, operating, managing, servicing, marketing, accommodating and supervising the operations of hotels and includes dining and banqueting services, etc.

Rationale for Demerger

ITC is a diversified company engaged in various businesses including hotels. The Hotels Business of ITC includes ownership/ licensing/ management of several hotel properties and providing services including accommodation, dining, banqueting, etc.

The Hotels Business of ITC has matured over the years and is well poised to chart its own growth path and operate as a separate listed entity in the fast-growing hospitality industry whilst continuing to leverage ITC's institutional strengths, strong brand equity and goodwill. Therefore, the Scheme is being proposed to segregate Hotels Business from Remaining Business of ITC and demerge it into the Resulting Company.

Indicative Timelines & Key Approvals

1. 24 July 2023- In-Principal approval demerger Scheme - The Board of Directors ("the Board") of ITC Limited accorded its in-principal approval to the demerger of the Hotels Business under a scheme of arrangement; with the Company holding a stake of about 40% in the new entity and the balance shareholding of about 60% to be held directly by the Company's shareholders proportionate to their shareholding in the Company.
2. 14 August 2023-Final Board Approval of demerger Scheme
3. September, 2023- Filing of scheme with Stock Exchanges under Regulation 30 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 read with the SEBI Circular dated 13th July, 2023,
4. December 2023 -Receipt of Stock Exchanges approval and filing with NCLT
5. December 2023 -Filing of Scheme with NCLT
6. March 2024- Shareholders / creditors meeting
7. August 2024- NCLT / other regulatory process
8. September 2024-Receipt of NCLT order
9. September 2024-Filing with ROC
10. September 2024- Appointed / Effective date for Demerger
11. November 2024- Issuance and Listing of equity shares of ITC Hotels
12. November 2024- Listing of shares of ITC Hotels

As per ITC, Scheme of demerger is subject to necessary approval from shareholders, creditors, stock exchanges, SEBI, NCLT and other regulatory authorities, as required and Indicative timeline for listing of ITC Hotels is ~15 months.

The proposed Scheme would be in the best interests of the Companies and their respective shareholders, employees, creditors and other stakeholders for the following reasons:

a. The confluence of favourable factors such as rising societal aspirations, strong macro-economic fundamentals of the country, Government of India's thrust on the Travel & Tourism industry and infrastructure creation along with rapid digitalization present immense opportunities for the Hotels Business going forward, though distinct from the other businesses of the Demerged Company.

b. In light of the distinctive profile of the hospitality industry, housing the Hotels Business in a separate listed entity would enable crafting of the next horizon of growth and sustained value creation for shareholders through sharper focus on the business anchored on a differentiated strategy aligned with industry specific market dynamics.

c. The Resulting Company is a newly incorporated entity which will have the ability to raise capital from equity and debt markets towards funding its growth requirements.

d. The Resulting Company as a focused entity would attract the right sets of investors, strategic partners and collaborations, whose investment strategies and risk profiles are aligned more sharply with the hospitality industry.

e. The Scheme would unlock value of the Hotels Business for existing shareholders of the Demerged Company through independent market driven valuation of their shares in the

   Resulting Company which will be listed pursuant to the Scheme, along with the option and flexibility to remain invested in a pure play hospitality focused listed entity.

f. The Scheme will ensure long term stability and strategic support to the Resulting Company and also enable the leveraging of cross synergies between the two Companies.

Sources:

1. https://www.itcportal.com/about-itc/profile/index.aspx
2. https://www.itcportal.com/about-itc/profile/history-and-evolution.aspx
3. https://www.itcportal.com/about-itc/shareholder-value/pdf/lodr-14aug23c.pdf

Amalgamation of IDFC Ltd with IDFC FIRST Bank

The Board of Directors of IDFC FIRST Bank Limited and IDFC Limited, at their respective meetings held on July 03, 2023, have approved the Scheme of Amalgamation of IDFC limited with IDFC FIRST Bank.

The Scheme is subject to the receipt of requisite approvals from the Reserve Bank of India ("RBI"), Securities and Exchange Board of India ("SEBI"), the Competition Commission of India, the National Company Law Tribunal, BSE Limited and the National Stock Exchange of India Limited (collectively, the "Stock Exchanges") and other statutory and regulatory authorities, and the respective shareholders, under applicable law. The following are the details of the proposed scheme:

1. The Share Exchange Ratio for the amalgamation of IDFC Limited with IDFC FIRST Bank shall be 155 equity shares of face value of ₹ 10/- each fully paid-up of IDFC FIRST Bank for every 100 equity shares of face value of ₹ 10/- each fully paid-up of IDFC Limited.
2. According to the amalgamation scheme, 264.64 crore shares of IDFC FIRST Bank held by IDFC Ltd will get extinguished, and based on the share exchange ratio mentioned above, 248 crore new shares of IDFC FIRST Bank would be issued to the shareholders of IDFC Ltd based on their respective holdings.
3. Consequent to the merger, the standalone book value per share of the Bank would increase by 4.9%, as calculated on audited financials as of March 31, 2023.
4. The key benefits of this amalgamation scheme are as follows:
   a. The merger will result in value unlocking to IDFC Limited shareholders as, after the merger, they will directly hold shares in IDFC FIRST Bank.
   b. The merger will lead to simplification of the corporate structure of IDFC FHCL, IDFC Limited and IDFC FIRST Bank by consolidating them into a single entity and will help streamline accounting and regulatory compliances of the aforesaid entities.
   c. The merger will help create an institution with diversified public and institutional shareholders, like other large successful Indian private sector banks.
   d. Raising equity capital from time to time will become easier in an institution with diversified set of shareholders.

Background:

IDFC Limited, a premier, successful infrastructure Financing Domestic Financial Institution (DFI) since 1997, was granted "in-principle" approval by the RBI to set up a Bank in April 2014, leading to the creation of IDFC Bank Limited. The Bank started its operation in October 2015. The loan assets and liabilities of IDFC Limited, which were mostly infrastructure and corporate loans, were transferred to IDFC Bank. Capital First Limited was a successful consumer and MSME financing institution since 2012 with a strong track record of growth, profits, and asset quality. On December 18, 2018, the IDFC Bank and Capital First merged, and subsequently renamed IDFC FIRST Bank. As of June 30, 2023, IDFC Limited through its non-financial holding company has 39.93% shareholding of IDFC FIRST Bank.

IDFC FIRST Bank is operating as a full-service universal bank with pan-India presence. The Bank has transformed from infrastructure financing to a universal banking franchise in the last four years. The Bank has built a strong deposit franchise, which has grown at a 4-year CAGR of 36% since the merger to reach Rs. 136,812 crore, by March 31, 2023. The Bank has increased CASA ratio from 8.6% at the time of merger with Capital First in December 2018, to 49.77% (March 31, 2023) and has set up 809 branches and 925 ATMs as of March 31, 2023.

In terms of assets, the Bank has a well-diversified loan book of Rs. 1,60,599 crore with a balance sheet size of Rs. 239,942 crore as on March 31, 2023. The Bank recorded a PAT of Rs. 2,437 crore in FY23, with strong Capital Adequacy of 16.82% as of March 31, 2023.

The Bank maintains high asset quality with Gross NPA of retail loans at 1.65% and Net NPA at 0.55% as of March 31, 2023. At the overall Bank level, GNPA 2.51% and NNPA is 0.86%. Infrastructure financing has higher NPA with GNPA of 25.11% and NNPA of 15.73%, but the infrastructure book is in wind down mode. If we exclude infrastructure financing, at the overall bank level, the GNPA is 1.84%, and NNPA is 0.46%. The PCR, including technical write-off, is 80.29% as of March 31, 2023.

The Bank's long term credit rating was upgraded last month by two rating agencies, CRISIL and India ratings, to AA+.

In summary, with strong foundations of good deposit franchise, customer friendly products, strong capital buffer, profitability, and high corporate governance, we look ahead, beyond the merger, to grow our bank in a safe and steady manner.

We are happy to welcome all shareholders of IDFC Limited to become direct shareholders of IDFC FIRST Bank. We will seek approval from the RBI and all other stakeholders and look forward to completing the exercise within 6 to 9 months.

The Reserve Bank of India approved the reverse merger of IDFC Ltd and its banking unit, IDFC First Bank. In July, the board of IDFC First Bank and IDFC authorized the reverse merger.

Source: https://www.idfcfirstbank.com/merger-of-idfc-ltd-and-idfc-first-bank

Amalgamation of Fincare Small Finance Bank Ltd. – AU Small Finance Bank Ltd

The Reserve Bank of India has sanctioned the Scheme of Amalgamation of Fincare Small Finance Bank Ltd. (Transferor Bank) with AU Small Finance Bank Ltd. (Transferee Bank). The Scheme has been sanctioned in exercise of the powers contained in sub-section (4) of Section 44A of the Banking Regulation Act, 1949. The effective date of the amalgamation shall be April 01, 2024. All the branches of Fincare Small Finance Bank Ltd. will function as branches of AU Small Finance Bank Ltd. with effect from April 01, 2024.

Source: https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=57445

LESSON ROUND-UP

- Corporate restructuring is a change in the business strategy of an organization resulting in diversification, closing parts of the business, etc. to increase its long-term profitability.
- It can be driven by external factors requiring change in the organizational structure or business model of a company, or it can be driven by the necessity to make financial adjustments to its assets and liabilities.
- Corporate Restructuring is an inorganic business strategy that results in faster pace of growth, effective utilization of resources, fulfillment of increasing expectations of stakeholders, managing competition, etc.
- Restructuring may be financial restructuring, technological, market and organizational restructuring.
- Corporate Restructuring process in India is governed by the Companies Act, 2013, Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 and various other laws.

- The most commonly applied tools of corporate restructuring are amalgamation, merger, demerger, acquisition, joint venture, disinvestments, etc.
- Corporate financial restructuring is any substantial change in a company's financial structure, or ownership or control, or business portfolio, designed to increase the value of the firm, i.e., debt and equity restructuring.
- Debt restructuring involves a reduction of debt and an extension of payment terms or change in terms and conditions, which is less expensive.
- Capital Reduction is the process of decreasing a company's shareholder's equity through share cancellations and share repurchases.
- According to section 61 of the Companies Act 2013 a company limited by shares or a company limited by guarantee and having a share capital may, if authorised by its articles, by special resolution, and subject to its confirmation by the Tribunal on petition, reduce its share capital.
- "Surrender of shares" means the surrender of shares already issued to the company by the registered holder of shares. Where shares are surrendered to the company, whether by way of settlement of a dispute or for any other reason, it will have the same effect as a transfer in favour of the company and amount to a reduction of capital.
- According to Section 68(1) of the Companies Act, 2013 a company whether public or private, may purchase its own shares or other specified securities out of: (i) its free reserves; or (ii) the securities premium account; or (iii) the proceeds of any shares or other specified securities.
- When a company buys back its shares or other specified securities, it shall maintain a register of the shares or securities so bought, the consideration paid for the shares or securities bought back, the date of cancellation of shares or securities, the date of extinguishing and physically destroying the shares or securities and such other particulars as may be prescribed.
- Section 46A of the Income Tax Act, 1961 provides that any consideration received by a security holder from any company on buy back shall be chargeable to tax on the difference between the cost of acquisition and the value of consideration received by the security holder as capital gains.
- All the listed companies are required to comply with SEBI (Buy Back of Securities) Regulations, 2018, in addition to the provisions of the Companies Act, 2013.

GLOSSARY

Corporate Restructuring : is the process of significantly changing a company's business model, management team or financial structure to address challenges and increase shareholder value. Corporate restructuring is an inorganic growth strategy.

Merger : is the fusion of two or more companies, whereby the identity of one or more is lost resulting in a single company.

Amalgamation : is a legal process by which two or more companies are joined together to form a new entity or one or more companies are to be absorbed or blended with another as a consequence the amalgamating company loses its existence and its shareholders become the shareholders of new company or amalgamated company.

Acquisition : occurs when one entity takes ownership of another entity's stock, equity interests or assets. It is the purchase by one company of controlling interest in the share capital of another existing company. Even after the takeover, although there is a change in the management of both the firms, companies retain their separate legal identity.

Demerger : is an arrangement whereby some part / undertaking of one company is transferred to another company which operates completely separate from the original company.

Slump Sale : is a transfer of one or more undertakings as a result of sale for a lump sum consideration, without values being assigned to the individual assets and liabilities in such sale.

Joint Venture (JV) : is a business or contractual arrangement between two or more parties which agree to pool resources for the purpose of accomplishing a specific task may be a new project or any other business activity.

Reverse Merger : is a merger in which a private company becomes a public company by acquiring it. It saves a private company from the complicated process and expensive compliance of becoming a public company.

Financial Restructuring : is any substantial change in a company's financial structure, or ownership or control, or business portfolio, designed to increase the value of the firm, i.e., debt and equity restructuring.

TEST YOURSELF

(These are meant for recapitulation only. Answers to these questions are not required to be submitted for evaluation.)

1. Define Corporate Restructuring.
2. Briefly discuss the scope and modes of Corporate Restructuring.
3. Describe about legal provisions of Corporate Restructuring in India.
4. Explain in detail the types of Merger.
5. Explain the acquisition of Flipcart and ebay.
6. What do you mean by Business Sale? Explain
7. What do you mean by 'buy-back' of shares or specified securities under the Companies Act, 2013?
8. Explain the relevant provisions of the Act.
9. What are the different alternatives available to a public company for 'buy-back'?
10. Enumerate the provisions relating to Escrow account and offer procedure under SEBI (Buy- back of Securities) Regulations, 2018.
11. Discuss the obligations of Merchant Banker under SEBI (Buy-back of Securities) Regulations, 2018.

LIST OF FURTHER READINGS

- Guide to Companies Act by A Ramaiya, Lexis Nexis Butter worths
- The Companies Act, 2013 with Rules and Ready Referencer by S K Kataria, Bloomsbury Publication
- Guide to Takeovers and Mergers by Sridharan and Pradhan, Wadhwa & Co.
- Mergers, Acquisitions and Corporate Restructuring by C Krishna murthi, SAGE Publications

Acquisition of Company/ Business

Lesson 2

KEY CONCEPTS

■ Target Company ■ Persons Acting in Concert ■ Acquirer ■ Shares ■ Acquisition ■ Voluntary Offer ■ Delisting offer ■ Tendering Period ■ Conditional Offer ■ Competing Offer

Learning Objectives

To understand:

- The legal framework provided for law governing acquisition and takeovers.
- The important definitions and concepts contained within Takeovers Regulations.
- Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.
- To familiarize the students with the legal frame work pertaining to direct and indirect acquisition of shares or voting rights in, or control over target company.

Lesson Outline

- Introduction
- Substantial Acquisition of Shares or Voting Rights
- Delisting Offer
- Voluntary Offer
- Offer Size
- Offer Price
- Conditional Offer
- Competing Offer
- Other Obligations
- Disclosures of Shareholding and Control
- Lesson Round-Up
- Test Yourself
- List of Further Readings
- Other References (Including Websites/Video Links)

REGULATORY FRAMEWORK

- Companies Act, 2013
- Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011

INTRODUCTION

Takeover concept in India emerged only around the twentieth century. In fact, Lord Swaraj Paul was one of the first to attempt a hostile takeover when he tried to obtain control over DCM Ltd. and Escorts Ltd. Further, the liberalization and globalisation policy of 1991 in the country, further necessitated the requirement of having legal framework to address takeovers in view of heightened competition amongst business entities and resultant corporate restructuring and M&As.

Where an acquirer takes over the control of the 'target company', it is termed as takeover. When an acquirer acquires 'substantial quantity of shares or voting rights' of the target company, it results into substantial acquisition of shares.

Takeovers and acquisitions are common occurrences in the business world as entities aim for inorganic growth and diversification. In some cases, the terms takeover and acquisition are used interchangeably, but each has a slightly different connotation. A takeover is a special form of acquisition that generally occurs when a company takes control of another company without the acquired company's agreement. Takeovers that occur without consent are commonly called hostile takeovers. Acquisitions, also referred to as friendly takeovers, occur when the acquiring company has the permission of the target company's Board of directors / shareholders to purchase and takeover the company. Acquisition refers to the process of acquiring a company at a price called the acquisition price or acquisition premium. The price is paid in terms of cash or acquiring company's shares or both.

The transaction relating to the acquisition of shares of a target company (listed company in India), undertaken by an existing shareholder of the company or any other independent acquirer company, is governed by the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ("Regulations"). The Regulations' goal is to govern the direct or indirect purchase of shares, voting rights, or the "control" of the target firm and to make sure that such purchases are made in a just and open way. Its objective is to also make the transactions relating to acquisition fairer and more transparent.

Takeover of companies whose securities are listed on one or more recognized stock exchanges in India is regulated by the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011. Therefore, before planning a takeover of a listed company, any acquirer should understand the compliance requirements under the Regulations and also the requirements under the SEBI (LODR) Regulations, 2015 and the Companies Act, 2013. There could also be some compliance requirements under the Foreign Exchange Management Act, 1999 if the acquirer was a person resident outside India.

The Takeover Regulations were notified based on recommendations made by the Takeover Regulations Advisory Committee (TRAC). The TRAC report had inter alia recommended the following relating to completion of transaction that triggered the open offer - "The agreement that attracts an open offer obligation may be acted upon during the pendency of the open offer provided 100 % of the consideration payable under the open offer is placed in escrow." The provisions relating to completion of acquisition during the open offer period were accordingly provided in Regulation 22(1) and (2) of Takeover Regulations in 2011.

In the case of *M/s Nirvana Holdings Private Limited (Appellant) Versus Securities and Exchange Board of India (Respondent), decision dated 8.9.2011,* Securities Appellate Tribunal inter alia observed that the primary object of the takeover code is to provide an exit route to the public shareholders when there is substantial acquisition of shares or a takeover. This right to exit is an invaluable right and the shareholders cannot be deprived of this right lightly. It is only when larger interest of investor protection or that of the securities market demands that this right could be taken away. Therefore, as a normal rule, a direction to make a public announcement to acquire shares of the target company should issue to an acquirer who fails to do that. The Board need not give reasons as to why such a direction is being issued because that is the mandate of Regulations 10, 11 and 12. However, if the issuance of such a direction is not in the interest of the securities market or for the protection of interest of investors, the Board may deviate from the normal rule and issue any other direction as envisaged in Regulation 44 of the takeover code. In that event, the Board should record reasons for deviation. In the case before us no reasons have been recorded for deviating from the normal rule and we find no ground for deviation.

What do we mean by a takeover?

The term 'Takeover' has not been defined under the said Regulations; the term basically envisages the concept of an acquirer acquiring shares with an intention of taking over the control or management of the target company. When an acquirer, acquires substantial quantity of shares or voting rights of the target company, it results in the substantial acquisition of shares. Substantial is again not defined in the Regulations and what is substantial for one company may not be substantial for another company. It can therefore not be quantified in terms of number of shares.

Takeover of companies whose securities are listed on one or more recognized stock exchanges in India is regulated by the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

An acquisition involves purchase of one entity by another (usually, a smaller firm by a larger one). A new company does not emerge from an acquisition; rather, the acquired company, or target firm, is often consumed and ceases to exist, and its assets become part of the acquiring company.

Acquiring an existing business enables a company to speed up its expansion process because they do not have to start from the very scratch. The target company is already established and has all the processes in place. The acquiring company simply has to focus on merging the business with its own and move ahead with its growth strategies.

As the motive is to takeover of other business, the acquiring company offers to buy the shares at a very high premium, that is, the gaining difference between the offer price and the market price of the share. This entices the shareholders and they sell their stake to earn quick money. This way the acquiring company gets the majority stake and takes over the ownership control of the target company.

OBJECTS OF TAKEOVER

The objects of a takeover may *inter alia* include:

- To effect savings in overheads and other working expenses on the strength of combined resources;
- To achieve product development through acquiring firms with compatible products and technological/ manufacturing competence, which can be sold to the acquirer's existing marketing areas, dealers and end users;
- To diversify through acquiring companies with new product lines as well as new market areas, as one of the entry strategies to reduce some of the risks inherent in stepping out of the acquirer's historical core competence;

- To improve productivity and profitability by joint efforts of technical and other personnel of both companies as a consequence of unified control;
- To create shareholder value and wealth by optimum utilisation of the resources of both companies;
- To achieve economies of scale by mass production at economical costs;
- To secure substantial facilities as available to a large company compared to smaller companies for raising additional capital, increasing market potential, expanding consumer base, buying raw materials at economical rates and for having own combined and improved research and development activities for continuous improvement of the products, so as to ensure a permanent market share in the industry;
- To achieve market development by acquiring one or more companies in new geographical territories or segments, in which the activities of acquirer are absent or do not have a strong presence.

KINDS OF TAKEOVER

Takeovers may be broadly classified into three kinds:

1. **Friendly Takeover:** Friendly takeover is with the consent of target company. In friendly takeover, there is an agreement between the management of two companies through negotiations and the takeover bid may be with the consent of majority or all shareholders of the target company. This kind of takeover is done through negotiations between two groups. Therefore, it is also called negotiated takeover.
2. **Hostile Takeover:** When an acquirer company does not offer the target company the proposal to acquire its undertaking but silently and unilaterally pursues efforts to gain control against the wishes of existing management.
3. **Bailout Takeover:** Takeover of a financially sick company by a profit earning company to bail out the former is known as bailout takeover. There are several advantages for a profit making company to takeover a sick company. The price would be very attractive as creditors, mostly banks and financial institutions having a charge on the industrial assets, would like to recover to the extent possible.

Legal aspects of Takeover

The legislations/regulations that mainly govern takeover are as under:

1. Companies Act, 2013
2. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (The Regulations)
3. SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015

As far as Companies Act, 2013 is concerned, the provisions of Section 186 apply to the acquisition of shares through a company. Section 235 and 236 of the Companies Act, 2013 lays down legal requirements for purpose of takeover of an unlisted company through transfer of undertaking to another company. Section 230 (11) also deals with provision that compromise or arrangement may include takeover offer made in such manner as may be prescribed:

Provided that in case of listed companies, takeover offer shall be as per the regulations framed by the Securities and Exchange Board.

Further as per provisions of Section 230(12) An aggrieved party may make an application to the Tribunal in the event of any grievances with respect to the takeover offer of companies other than listed companies in such manner as may be prescribed and the Tribunal may, on application, pass such order as it may deem fit.

Explanation.—For the removal of doubts, it is hereby declared that the provisions of section 66 shall not apply to the reduction of share capital effected in pursuance of the order of the Tribunal under this section.

TAKEOVER OF UNLISTED COMPANIES

Unlisted Entities are governed by the framework stipulated under Companies Act, 2013. Section 236 of the Companies Act contains a compulsory acquisition mode for the transferee company to acquire the shares of minority shareholders of Transferor Company.

Where the scheme has been approved by the holders of not less than nine tenth (90%) in value of the shares of the transferor company whose transfer is involved, the transferee company, may, give notice to any dissenting shareholders that transferee company desires to acquire their shares. The scheme shall be binding on all the shareholders of the transferor company (including dissenting shareholders), unless the Tribunal orders otherwise (i.e. that the scheme shall not be binding on all shareholders).

Accordingly, the transferee company shall be entitled and bound to acquire these shares on the terms on which it acquires under the scheme (the binding provision).

The advantage of going through the route contained in Section 235 of the Companies Act is the facility for acquisition of minority stake. The transferee company shall give notice to the minority dissenting shareholders and express its desire to acquire their shares within a period of 4 months after making an offer as envisaged under Section 235 of the Act.

When a Company intends to takeover another Company through acquisition of 90% or more in value of the shares of that Company, the procedure laid down under Section 235 of the Act could be beneficially utilized. When one Company has been able to acquire more than 90% control in another Company, the shareholders holding the remaining control in the other Company are reduced to a minority. They do not even command a 10% stake so as to make any meaningful utilization of the power. Such minority cannot even call an extra-ordinary general meeting under Section 100 of the Act nor can they constitute a valid strength on the grounds of their proportion of issued capital for making an application to the Tribunal under Section 241 of the Act alleging acts of oppression and/or mismanagement. Hence, the statute itself provides them a meaningful exit route.

The advantage of going through the route is the facility for acquisition of minority stake. But even without going through this process, if an acquirer is confident of acquiring the entire control, there is no need to go through Section 235 of the Act. It is purely an option recognized by the statute.

The merit of this scheme is that without resort to tedious court procedures, the acquisition by takeover is affected. Only in cases where any dissentient shareholder or shareholders exist, the procedures prescribed by this section will have to be followed. It provides machinery for adequately safeguarding the rights of the dissentient shareholders also.

Section 235 lays down two safeguard in respect of expropriation of private property (by compulsory acquisition of majority shares). First the scheme requires approval of a large majority of shareholders. Second the Tribunal's discretion to prevent compulsory acquisition.

The following are the important ingredients of the Section 235 route:

- The Company, which intends to acquire control over another Company by acquiring share, held by shareholders of that another Company is known under Section 235 of the Act as the "Transferee Company".
- The Company whose shares are proposed to be acquired is called the "Transferor Company".
- The "Transferee Company" and "Transferor Company" deliberate and discuss together at the Board level and come out with a scheme or contract.
- Every offer or every circular containing the terms of the scheme shall be duly approved by the Board of Directors of the companies and every recommendation to the members of the transferor Company by its directors to accept such offer. It shall be accompanied by such information as provided under the said Act. The circular shall be sent to the dissenting shareholders in Form No: CAA 14 to the last known address of the dissenting shareholder.
- Rule 26 A of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 deals with purchase of minority shareholding held in DEMAT form. According to Rule 26A:

(1) The company shall within two weeks from the date of receipt of the amount equal to the price of shares to be acquired by the acquirer, under section 236 of the Act, verify the details of the minority shareholders holding shares in dematerialised form.

(2) After verification under sub-rule (1), the company shall send notice to such minority shareholders by registered post or by speed post or by courier or by email about a cut-off date, which shall not be earlier than one month after the date of sending of the notice, on which the shares of minority shareholders shall be debited from their account and credited to the designated DEMAT account of the company, unless the shares are credited in the account of the acquirer, as specified in such notice, before the cut-off date.

(3) A copy of the notice served to the minority shareholders under sub-rule (2), shall also be published simultaneously in two widely circulated newspapers (one in English and one in vernacular language) in the district in which the registered office of the company is situated and also be uploaded on the website of the company, if any.

(4) The company shall inform the depository immediately after publication of the notice under sub-rule (3) regarding the cut-off date and submit the following declarations stating that:

(a) the corporate action is being effected in pursuance of the provisions of section 236 of the Act;

(b) the minority shareholders whose shares are held in dematerialised form have been informed about the corporate action a copy of the notice served to such shareholders and published in the newspapers to be attached;

(c) the minority shareholders shall be paid by the company immediately after completion of corporate action;

(d) any dispute or complaints arising out of such corporate action shall be the sole responsibility of the company.

(5) For the purposes of effecting transfer of shares through corporate action, the Board shall authorise the Company Secretary, or in his absence any other person, to inform the depository under sub-rule (4), and to submit the documents as may be required under the said sub-rule.

(6) Upon receipt of information under sub-rule (4), the depository shall make the transfer of shares of the minority shareholders, who have not, on their own, transferred their shares in favour of the acquirer, into the designated DEMAT account of the company on the cut-off date and intimate the company.

(7) After receiving the intimation of successful transfer of shares from the depository under sub-rule (6), the company shall immediately disburse the price of the shares so transferred, to each of the minority shareholders after deducting the applicable stamp duty, which shall be paid by the company, on behalf of the minority shareholders, in accordance with the provisions of the Indian Stamp Act, 1899.

(8) Upon successful payment to the minority shareholders under sub-rule (7), the company shall inform the depository to transfer the shares of such shareholders, kept in the designated DEMAT account of the company, to the DEMAT account of the acquirer.

Explanation: The company shall continue to disburse payment to the entitled shareholders, where disbursement could not be made within the specified time, and transfer the shares to the DEMAT account of acquirer after such disbursement.

(9) In case, where there is a specific order of Court or Tribunal, or statutory authority restraining any transfer of such shares and payment of dividend, or where such shares are pledged or hypothecated under the provisions of the Depositories Act, 1996, the depository shall not transfer the shares of the minority shareholders to the designated DEMAT account of the company under sub-rule (6).

Explanation: For the purposes of this rule, if “cut-off date” falls on a holiday, the next working day shall be deemed to be the “cut-off date”.

- Every offer shall contain a statement by or on behalf of the Transferee Company, disclosing the steps it has taken to ensure that necessary cash will be available. This condition shall apply if the terms of acquisition as per the scheme or the contract provide for payment of cash in lieu of the shares of the Transferor Company which are proposed to be acquired.
- Any person issuing a circular containing any false statement or giving any false impression or containing any omission shall be punishable with fine.
- After the scheme or contract and the recommendation of the Board of Directors of the transferor Company, if any, shall be circulated and approval of not less than 9/10th in value of "Transferor Company" should be obtained within 4 months from the date of circulation. It is necessary that the Memorandum of Association of the transferee company should contain as one of the objects of the company, a provision to take over the controlling shares in another company. If the memorandum does not have such a provision, the company must alter the objects clause in its memorandum, by convening an extraordinary general meeting. The approval is not required to be necessarily obtained in a general meeting of the shareholders of the Transferor Company.
- Once approval is available, the 'Transferee Company' becomes eligible for the right of compulsory acquisition of minority interest.
- The Transferee Company has to send notice to the shareholders who have not accepted the offer (i.e. dissenting shareholders) intimating them the need to surrender their shares.
- Once the acquisition of shares in value, not less than 90% has been registered in the books of the transferor Company, the transferor Company shall within one month of the date of such registration, inform the dissenting shareholders of the fact of such registration and of the receipt of the amount or other consideration representing the price payable to them by the transferee Company.
- The transferee Company having acquired shares in value not less than 90% is under an obligation to acquire the minority stake as stated aforesaid and hence it is required to transfer the amount or other consideration equal to the amount or other consideration required for acquiring the minority stake to the transferor Company. The amount or consideration required to be so transferred by the transferee Company to the transferor Company, shall not in any way, less than the terms of acquisition offered under the scheme or contract.
- Any amount or other consideration received by the Transferor Company in the manner aforesaid shall be paid into a separate bank account. Any such sums and any other consideration so received shall be held by the transferor Company in trust for the several persons entitled to the shares in respect of which the said sums or other consideration were respectively received.

The takeover achieved in the above process through Section 235 of the Act will not fall within the meaning of amalgamation under the Income Tax Act, 1961 and as such benefits of amalgamation provided under the said Act will not be available to the acquisition under consideration. The takeover in the above process will not enable carrying forward of unabsorbed depreciation and accumulated losses of the transferor Company in the transferee Company for the reason that the takeover does not result in the transferor Company losing its identity.

Check-list

Transferor Company (Documents etc. involved in this process):

1. MOA and AOA
2. Offer of a scheme or contract from the transferee company
3. Minutes of Board meeting containing consideration of the offer and its acceptance or rejection
4. Notice calling general meeting with explanatory statement
5. Form CAA 14 circulated to the members (dissenting)

6. Minutes of general meeting of the company containing approval of the offer by statutory majority in value and in numbers also, if required
7. Court order, if any
8. Register of Members
9. Notice sent by the transferee company to dissenting shareholders for acquiring their shares
10. Duly filled in and executed instrument(s) of transfer of shares held by the dissenting shareholders
11. Bank Passbook or Statement of Account in respect of the amount deposited in the special bank account to be kept in trust for the dissenting shareholders
12. Annual Report.

Transferee Company (Documents etc. involved in this process):

1. MOA and AOA
2. Minutes of Board meeting containing consideration and approval of the offer sent to the transferor company
3. Offer of a scheme or contract sent to the transferor company
4. Notice to dissenting shareholders if any, of the transferor company
5. Notice to the remaining shareholders of the transferor company, who have not assented to the proposed acquisition, if any
6. Form No: CAA14 received from the transferor company, which has been circulated to its members by that company
7. Minutes of general meeting of the company containing approval of the shareholders to the offer of scheme or contract sent to the transferor company
8. Court order, if any
9. Register of Investments
10. Duly filled in and executed instrument(s) of transfer for shares held by the dissenting shareholders
11. Balance Sheets showing investments in the shares of the transferor company.

Development of Takeover Regulations

The SEBI Act, 1992 empowered SEBI to make substantial acquisition of shares and takeovers a regulated activity for the first time. SEBI notified the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1994 in November 1994.

> Being statutory in nature, violation of any of the provisions attracted several penalties. SEBI could initiate criminal prosecution under Section 24 of the SEBI Act, 1992, issue directions under the SEBI Act and could direct any person not to dispose off any securities acquired in violation of the regulations or direct him to sell shares acquired in violation of the Regulations or take action against the intermediary registered with SEBI. The SEBI Act, 1992 also empowered SEBI to initiate adjudications and to impose fines as penalties for certain violations of the Regulations.

SEBI acquired necessary learnings, expertise and insight into the complexities of a Takeover after implementing the same for 2 years and thereafter formed a Committee under the Chairmanship of Justice Bhagwati. The terms of reference of the Committee were:

- to examine the areas of deficiencies in the existing regulations; and
- to suggest amendments in the Regulations with a view to strengthen the Regulations and make them more fair, transparent and unambiguous and also protect the interest of investors and all parties concerned in the acquisition process.

The Committee submitted its report in January 1997 and the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 were notified on February 20, 1997. These Regulations primarily dealt with the issues such as consolidation of holdings, conditional offers, change in control, formation of a Takeover Panel, competitive offers and defined substantial quantity for the purpose of making a disclosure and for the purpose of making an open offer. Takeovers were for the first time regulated in India in full swing. However, the various provisions were again subject to different interpretations and some of the provisions could not give the intended results.

With a view to address all the concerns raised by all concerned, the same committee was reconstituted to review the working of the regulations and to consider suitable suggestions for further refinement of the Regulations in the light of the experience gained so far. The reconstituted Committee submitted its recommendations in 2002 and the Regulations went in for a major amendment in the year 2002.

In 2009, SEBI constituted a Takeover Regulation Advisory Committee (“TRAC Committee”) under the Chairmanship of Late Mr. C Achutan to review the Takeover Regulations of 1997. The committee submitted its report in 2010 and the Regulations, SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 were notified on September 23, 2011 and became effective from October 22, 2011. The major amendments/changes were:

1. Increase in trigger limit for open offer from 15% to 25%
2. Increase in statutory open offer size from 20% of share capital to 26% of total share capital of the company
3. Overhaul of exemptions from open offer:

   Exemptions have been further categorized into the following broad heads:

   (a) Transactions, which trigger a statutory open offer due to substantial acquisition of shares/ voting rights, or due to change in control

   (b) Transactions, which trigger a statutory open offer due to acquisition of shares/ voting rights exceeding prescribed thresholds, provided that there is no change in control.
4. Offer pricing: The new regulations brought in the concept of Volume Weighted Average Market Price.
5. Creeping acquisition: The New Regulations provided that an acquirer could make a creeping acquisition of 5% annually (between April 1 to March 31 of next year) to reach 75% stake such that the minimum public shareholding of 25% is maintained. The manner of computation of the 5% creeping acquisition limit has also been clarified.
6. Non-Compete Fee : The provision of payment of non compete was done away with.
7. Recommendation of independent directors on the open offer to be published in the newspapers in which the detailed public statement was given.

The Regulations, further sought to include the various Securities Appellate Tribunal (“SAT”) judgements, informal guidance given and the experience gained from implementing the Takeover Regulations from the year 1994. They further sought to align itself with the Takeover Regulations as they exist in the rest of the world.

TAKEOVER OF LISTED COMPANIES

Takeover of companies whose securities are listed on one or more recognized stock exchanges in India is regulated by the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

Therefore, before planning a takeover of a listed company, any acquirer should understand the compliance requirements under the Regulations and also the requirements under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("SEBI LODR") and the Companies Act, 2013. There could also be some compliance requirements under the Foreign Exchange Management Act, 1999 if the acquirer is a person resident outside India.

As per Regulation 38 of SEBI LODR, the listed entity shall comply with the minimum public shareholding requirements ("MPS") as specified in Rule 19(2) and Rule 19A of the Securities Contracts (Regulations) Rules, 1957 in the manner as specified by the Board from time to time. In other words, the listed entity shall ensure that the public shareholding shall be maintained at 25% of the total paid up share capital of the listed company failing which the listed company shall take steps to increase the public shareholding to 25% of the total paid up share capital by the methods as specified in Rule 19(2) and Rule 19A of the Securities Contracts (Regulations) Rules, 1957.

This provision shall not apply to entities listed on Innovators Growth Platform without making a public issue.

Substantial Acquisition of Shares or Voting Rights

Regulation 3(1) provides for Substantial acquisition of shares or voting rights. It states that no acquirer shall acquire shares or voting rights in a target company which taken together with shares or voting rights, if any, held by him and by Persons Acting in Concert (PACs) with him in such target company, entitle them to exercise twenty-five percent or more of the voting rights in such target company unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations.

It may be noted that-

"Target Company" means a company and includes a body corporate or corporation established under a Central legislation, State legislation or Provincial legislation for the time being in force, whose shares are listed on a stock exchange. [Regulation 2(1)(z)]

"Persons Acting in Concert" means persons who, with a common objective or purpose of acquisition of shares or voting rights in, or exercising control over a target company, pursuant to an agreement or understanding, formal or informal, directly or indirectly co-operate for acquisition of shares or voting rights in, or exercise of control over the target company. [Regulation 2(1)(q)]

"Acquirer" means any person who, directly or indirectly, acquires or agrees to acquire whether by himself, or through, or with persons acting in concert with him, shares or voting rights in, or control over a target company. [Regulation 2(1)(a)]

"*Shares*" means shares in the equity share capital of a target company carrying voting rights, and includes any security which entitles the holder thereof to exercise voting rights

Explanation— For the purpose of this clause shares will include all depository receipts carrying an entitlement to exercise voting rights in the target company; [Regulation 2(1)(v)]

Regulation 3(2) provides that no acquirer, who together with persons acting in concert with him, has acquired and holds in accordance with these regulations shares or voting rights in a target company entitling them to exercise twenty-five per cent or more of the voting rights in the target company but less than the maximum permissible non-public shareholding, shall acquire within any financial year additional shares or voting rights in such target company entitling them to exercise more than five per cent of the voting rights, unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations:

Provided that the acquisition beyond five per cent but up to ten per cent of the voting rights in the target company shall be permitted for the financial year 2020-21 only in respect of acquisition by a promoter pursuant to preferential issue of equity shares by the target company.

Provided that such acquirer shall not be entitled to acquire or enter into any agreement to acquire shares or voting rights exceeding such number of shares as would take the aggregate shareholding pursuant to the acquisition above the maximum permissible non-public shareholding.

Provided further that, acquisition pursuant to a resolution plan approved under section 31 of the Insolvency and Bankruptcy Code, 2016 [No. 31 of 2016] shall be exempt from the obligation under the proviso to the sub-regulation (2) of regulation 3.

Explanation.— For purposes of determining the quantum of acquisition of additional voting rights under this sub-regulation,—

(i) gross acquisitions alone shall be taken into account regardless of any intermittent fall in shareholding or voting rights whether owing to disposal of shares held or dilution of voting rights owing to fresh issue of shares by the target company.

(ii) in the case of acquisition of shares by way of issue of new shares by the target company or where the target company has made an issue of new shares in any given financial year, the difference between the pre-allotment and the post-allotment percentage voting rights shall be regarded as the quantum of additional acquisition .

It may be noted that-

"Acquisition" means, directly or indirectly, acquiring or agreeing to acquire shares or voting rights in, or control over, a target company. [Regulation 2(1)(b)]

"Maximum permissible non-public shareholding" means such percentage shareholding in the target company excluding the minimum public shareholding required under the Securities Contracts (Regulation) Rules, 1957. [Regulation 2(1)(o)]

How is the maximum permissible non-public shareholding in a listed company defined?

Maximum permissible non-public shareholding is derived based on the minimum public shareholding requirement under the Securities Contracts (Regulations) Rules 1957 ("SCRR"). Rule 19A of SCRR requires all listed companies (other than public sector companies) to maintain public shareholding of at least 25% of share capital of the company. Thus by deduction, the maximum number of shares which can be held by promoters i.e. Maximum permissible non-public shareholding) in a listed companies (other than public sector companies) is 75% of the share capital.

"Promoter" has the same meaning as in the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, and includes a member of the promoter group.

What is the basis of computation of the creeping acquisitions limit under Regulation 3(2) of Takeover Regulations 2011?

For computing acquisitions limits for creeping acquisition specified under regulation 3(2), gross acquisitions/ purchases shall be taken in to account thereby ignoring any intermittent fall in shareholding or voting rights whether owing to disposal of shares or dilution of voting rights on account of fresh issue of shares by the target company.

Whether for the purpose of the creeping acquisition in terms of the Takeover Regulations, 2011, the Creeping Acquisition made during the period 01.04.201 to 22.10.2011 will be considered?

The Takeover Regulations, 2011 have clearly defined the financial year as the period of 12 months commencing on the first day of the month of April. Thus, for the purpose of the creeping acquisitions under Regulation 3(2) of Takeovers Regulations 2011, shares acquired during 1/4/2011 to 22/10/2011 will be taken in to account.

Regulation 3(3) provides that for the purposes of sub-regulation (1) and sub-regulation (2), acquisition of shares by any person, such that the individual shareholding of such person acquiring shares exceeds the stipulated thresholds, shall also be attracting the obligation to make an open offer for acquiring shares of the target company irrespective of whether there is a change in the aggregate shareholding with persons acting in concert.

Regulation 3(4) provides nothing contained in this regulation shall apply to acquisition of shares or voting rights of a company by the promoters or shareholders in control, in terms of the provisions of Chapter VI-A of Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009.

Regulation 3(5) provides for the purpose of this regulation, any reference to “twenty-five per cent” in case of listed entity which has listed its specified securities on Innovators Growth Platform shall be read as “forty-nine per cent”.

Acquisition of Control

Regulation 4 states that irrespective of acquisition or holding of shares or voting rights in a target company, no acquirer shall acquire, directly or indirectly, control over such target company unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations.

What are the typical steps and corresponding timelines, in an open offer process?

- ***Under most scenarios (except in certain types of indirect acquisitions) on the day of the triggering event, the acquirer is required to make a Public Announcement to the stock exchanges where shares of Target Company are listed and to SEBI. Within 5 working days thereafter, the acquirer is required to publish a Detailed Public Statement (DPS) in newspapers and also submit a copy to SEBI, after creation of an escrow account.***
- ***Within 5 working days of publication DPS, the acquirer through the manager to the offer is required to file a draft letter of offer with SEBI for its observations. The letter of offer is dispatched to the shareholders of the target company, as on the identified date, after duly incorporating the changes indicated by SEBI, if there are any.***
- ***The offer shall open not later than 12 working days from the date of receipt of SEBI’s observations. The acquirer is required to issue an advertisement announcing the final schedule of the open offer, one working day before opening of the offer. The offer shall remain open for 10 working days from the date of opening of the offer. Within 10 working days after the closure of the offer, the acquirer shall make payments to the shareholders whose shares have been accepted. A post offer advertisement, giving details of the acquisitions, is required to be published by the acquirer within 5 workings days of the completion of payments under the open offer.***

Indirect Acquisition of Shares or Control

Regulation 5 states that for the purposes of regulation 3 and regulation 4, acquisition of shares or voting rights in, or control over, any company or other entity, that would enable any person and persons acting in concert with him to exercise or direct the exercise of such percentage of voting rights in, or control over, a target company, the acquisition of which would otherwise attract the obligation to make a public announcement of an open offer for acquiring shares under these regulations, shall be considered as an indirect acquisition of shares or voting rights in, or control over the target company.

In the case of an indirect acquisition attracting the provisions of sub-regulation (1) where,—

1. the proportionate net asset value of the target company as a percentage of the consolidated net asset value of the entity or business being acquired;
2. the proportionate sales turnover of the target company as a percentage of the consolidated sales turnover of the entity or business being acquired; or
3. the proportionate market capitalisation of the target company as a percentage of the enterprise value for the entity or business being acquired;

is in excess of eighty per cent, on the basis of the most recent audited annual financial statements, such indirect acquisition shall be regarded as a direct acquisition of the target company for all purposes of these regulations including without limitation, the obligations relating to timing, pricing and other compliance requirements for the open offer.

Explanation.— For the purposes of computing the percentage referred to in clause (c) of this sub-regulation, the market capitalisation of the target company shall be taken into account on the basis of the volume-weighted average market price of such shares on the stock exchange for a period of sixty trading days preceding the earlier of, the date on which the primary acquisition is contracted, and the date on which the intention or the decision to make the primary acquisition is announced in the public domain, as traded on the stock exchange where the maximum volume of trading in the shares of the target company are recorded during such period.

How are the thresholds for the requirement of making an open offer in case of an indirect acquisition computed?

The thresholds for the requirement of making an open offer in case of an indirect acquisition are computed on the basis of the voting rights and/or control acquired in the target company. Further, the quantum of acquisition of the target company in case of an indirect acquisition cannot be computed on a pro rata basis. This is illustrated as below:

- ***If X acquires 40% shares of Y along with majority control of Y which, in turn, holds 70% shares of Z, a listed company along with majority control of Z, then X, in effect, acquires control on 70% shares of Z held by Y. Therefore, X will be required to make an open offer for the shareholders of Z.***
- ***Now; If X, which already holds 40% shares of Y and majority control of Y, further acquires additional 10% shares of Y, then X, in effect, does not acquire control on any shares additional to 70% shares of Z held by Y. Therefore, X will not be required to make an open offer for the shareholders of Z. It may be noted that the computation of quantum of additional shares acquired by X in Z as 10% of 70%, i.e., 7% on pro rata basis is not correct. Here, X does not acquire any additional shares of Z either directly or indirectly by acquiring additional 10% shares of Y.***
- ***Now; if A and B are in joint control of X which holds majority control of Y which, in turn, holds 70% shares of Z along with its majority control and A acquires sole control of X pursuant to cessation of control of X by B, then A, in effect, acquires sole control of Z indirectly through X and Y. Therefore, X will be required to make an open offer for the shareholders of Z.***

Are there special provisions for determining the offer price in case of open offer arising out of indirect acquisition of a target company?

Yes. Since indirect acquisitions involve acquiring the target company as a part of a larger business, SAST Regulations, 2011 have prescribed additional parameters to be taken into account for determination of the offer price. If the size of the target company exceeds certain thresholds as compared to the size of the entity or business being acquired then the acquirer is required to compute and disclose in the letter of offer, the per share value of the target company taken into account for the acquisition, along with the methodology. (Kindly refer to Regulation 5). Further, in indirect acquisitions which are not in the nature of deemed direct acquisition, the offer price shall stand enhanced by an amount equal to a sum determined at the rate of 10% per annum for the period between the date on which primary acquisition was contracted and the date of Detailed Public Statement.

Delisting Offer

Regulation 5A states that notwithstanding anything contained in these regulations and the Delisting Regulations, in the event the acquirer makes a public announcement of an open offer for acquiring shares or voting rights or control of a target company in terms of sub- regulation (1) of regulation 3, regulation 4 or regulation 5, the acquirer may seek the delisting of the target company by making a delisting offer in accordance with this regulation:

Provided that the acquirer shall have declared his intention to so delist the target company at the time of making such public announcement of an open offer as well as at the time of making the detailed public statement. A subsequent declaration of delisting for the purpose of the delisting offer proposed to be made under sub-regulation (1) shall not suffice:

Provided further that if the open offer is for an indirect acquisition that is not a deemed direct acquisition under sub-regulation (2) of regulation 5, the declaration of the intent to so delist shall be made initially only in the detailed public statement.

Explanation 1: The acquirer shall not, in such target company during the preceding two years from the date of the public announcement made under this regulation, be:

i. a promoter / promoter group / person(s) in control, or

ii. directly / indirectly associated with the promoter or any person(s) in control, or

iii. a person(s) holding more than twenty-five percent shares or voting rights.

Explanation 2: The acquirer shall not acquire joint control along with an existing promoter / person in control of the company.

The delisting offer obligations shall be fulfilled by the acquirer in the following manner:

A. the public announcement, the detailed public statement and the letter of offer shall mention the open offer price determined in accordance with regulation 8 of these regulations and the indicative price for delisting:

   Provided that if the open offer is for an indirect acquisition that is not a deemed direct acquisition under sub-regulation (2) of regulation 5, the open offer price and indicative price shall be notified by the acquirer at the time of making the detailed public statement and in the letter of offer:

   Provided further that the indicative price shall include a suitable premium reflecting the price that the acquirer is willing to pay for the delisting offer with full disclosures of the rationale and justification for the indicative price so determined that can also be revised upwards by the acquirer before the start of the tendering period which shall be duly disclosed to the shareholders.

   Explanation: Indicative price shall be in accordance with clause (o) of sub- regulation (1) of regulation 2 of the Delisting Regulations and shall not be less than the book value of the company as computed in accordance with the Explanation to sub-regulation (5) of regulation 22 of the Delisting Regulations.

B. In case the response to the offer leads to the delisting threshold as provided under regulation 21 of the Delisting Regulations :

   i. being met, all shareholders who tender their shares shall be paid the indicative price;

   ii. not being met, all shareholders who tender their shares shall be paid the open offer price.

It may be noted that –

"*Tendering period*" means the period within which shareholders may tender their shares in acceptance of an open offer to acquire shares made under these regulations.[Regulation 2(1)(za)]

Delisting offer made under sub-regulation (1) is said to be not successful when:

a) on account of the non–receipt of the prior approval of shareholders in terms of regulation 11 of the Delisting Regulations; or

b) on account of non-receipt of the prior in-principle approval of the relevant stock exchange in terms of regulation 12 of the Delisting Regulations; or

c) the threshold as specified under Regulation 21 of the Delisting Regulations is not achieved;

the acquirer shall, within two working days in respect of such failure, make an announcement in all the newspapers in which the detailed public statement was made and comply with all the applicable provisions of these regulations in relation to completing of the open offer.

Regulation 5(4) states that where a competing offer is made in terms of sub-regulation (1) of regulation 20 of these regulations:

a) the acquirer shall not be entitled to delist the target company;

b) the acquirer shall not be liable to pay interest to the shareholders on account of delay due to the competing offer; and

c) the acquirer shall comply with all the applicable provisions of these regulations and make an announcement in this regard, within two working days from the date of public announcement made in terms of sub-regulation (1) of regulation 20, in all the newspapers where the detailed public statement was made.

The shareholders who have tendered shares in acceptance of the offer made under sub-regulation (1), shall be entitled to withdraw such shares tendered, within five working days from the date of the announcement under sub-regulation (3).

Regulation 5(6) Where the target company fails to get delisted pursuant to a delisting offer under sub-regulation (1), but which results in the shareholding of the acquirer exceeding the maximum permissible non-public shareholding threshold:

a) the acquirer may undertake a further attempt to delist the target company in accordance with the Delisting Regulations during the period of twelve months from the date of completion of the open offer, subject to the acquirer continuing to exceed the maximum permissible non-public shareholding in the target company.

b) such further delisting attempt shall be successful subject to the following conditions:

   i. the delisting threshold as provided under regulation 21 of the Delisting Regulations is met; and

   ii. fifty percent of the residual public shareholding is acquired.

c) upon failure of the further delisting attempt, the acquirer shall ensure compliance of the minimum public shareholding requirement of the target company under the Securities Contract (Regulation) Rules, 1957 within a period of twelve months from the end of the period referred to at clause (a).

d) the floor price for a further delisting attempt as referred to at clause (a) shall be higher of the following:

   i. the indicative price offered under the first delisting attempt;

   ii. the floor price determined under the Delisting Regulations as on the relevant date of the subsequent attempt; and

   iii. the book value of the company as computed based on the method stated in explanation to clause (a) under sub-regulation 2.

While undertaking delisting for the first or subsequent attempt, all the provisions of the Delisting Regulations shall mutatis-mutandis be applicable, save as otherwise provided in this regulation.

Voluntary Offer

Regulation 6 states that an acquirer, who together with persons acting in concert with him, holds shares or voting rights in a target company entitling them to exercise twenty-five per cent or more but less than the maximum permissible non-public shareholding, shall be entitled to voluntarily make a public announcement of an open offer for acquiring shares in accordance with these regulations, subject to their aggregate shareholding after completion of the open offer not exceeding the maximum permissible non-public shareholding:

Provided that where an acquirer or any person acting in concert with him has acquired shares of the target company in the preceding fifty-two weeks without attracting the obligation to make a public announcement of an open offer, he shall not be eligible to voluntarily make a public announcement of an open offer for acquiring shares under this regulation:

Provided further that during the offer period such acquirer shall not be entitled to acquire any shares otherwise than under the open offer.

It may be noted that –

"*Offer Period*" means the period between the date of entering into an agreement, formal or informal, to acquire shares, voting rights in, or control over a target company requiring a public announcement, or the date of the public announcement, as the case may be, and the date on which the payment of consideration to shareholders who have accepted the open offer is made, or the date on which open offer is withdrawn, as the case may be. [Regulation 2(1)(p)]

Can a person holding less than 25% of the voting rights/ shares in a target company, make an offer?

Yes, any person holding less than 25% of shares/ voting rights in a target company can make an open offer provided the open offer is for a minimum of 26% of the share capital of the company.

An acquirer and persons acting in concert with him, who have made a public announcement under this regulation to acquire shares of a target company shall not be entitled to acquire any shares of the target company for a period of six months after completion of the open offer except pursuant to another voluntary open offer:

Provided that such restriction shall not prohibit the acquirer from making a competing offer upon any other person making an open offer for acquiring shares of the target company.

Shares acquired through bonus issue or stock splits shall not be considered for purposes of the dis-entitlement set out in this regulation. For the purpose of this regulation, any reference to "twenty-five per cent" in case of listed entity which has listed its specified securities on Innovators Growth Platform shall be read as "forty-nine per cent".

Regulation 6A states that notwithstanding anything contained in these regulations, no person who is a wilful defaulter shall make a public announcement of an open offer for acquiring shares or enter into any transaction that would attract the obligation to make a public announcement of an open offer for acquiring shares under these regulations:

It may be noted that –

"*Wilful Defaulter*" means any person who is categorized as a wilful defaulter by any bank or financial institution or consortium thereof, in accordance with the guidelines on wilful defaulters issued by the Reserve Bank of India and includes any person whose director, promoter or partner is categorized as such. [Regulation 2(1)(ze)]

Provided that this regulation shall not prohibit the wilful defaulter from making a competing offer in accordance with regulation 20 of these regulations upon any other person making an open offer for acquiring shares of the target company.

Regulation 6B states that notwithstanding anything contained in these regulations, no person who is a fugitive economic offender shall make a public announcement of an open offer or make a competing offer for acquiring shares or enter into any transaction, either directly or indirectly, for acquiring any shares or voting rights or control of a target company.

What are the restrictions on acquirers making a voluntary open offer?

A voluntary offer cannot be made if the acquirer or PACs with him has acquired any shares of the target company in the 52 weeks prior to the voluntary offer. The acquirer is prohibited from acquiring any shares during the offer period other than those acquired in the open offer. The acquirer is also not entitled to acquire any shares for a period of 6 months, after completion of open offer except pursuant to another voluntary open offer.

How is the voluntary offer made by a person holding less than 25% of shares/ voting rights in a target company different from the voluntary offer made by a person holding more than 25% of shares/ voting rights of the target company?

Voluntary offer by a person holding less than 25%	Voluntary offer by a person holding more than 25%
Minimum offer size of 26%.	Minimum offer size of 10%.
Maximum can be for entire share capital of the target company.	The maximum offer size is linked to maximum permissible non-public shareholding permitted under Securities Contracts (Regulations) Rules 1957.
No such conditions	● Acquirer should not have acquired any shares during 52 weeks period prior to Public Announcement. ● Acquirer is not entitled to acquire any shares of the target company for a period of 6months after the completion of the open offer except for a voluntary open offer.

Offer Size

Regulation 7(1) states that the open offer for acquiring shares to be made by the acquirer and persons acting in concert with him under regulation 3 and regulation 4 shall be for at least twenty six per cent of total shares of the target company, as of tenth working day from the closure of the tendering period:

Provided that the total shares of the target company as of tenth working day from the closure of the tendering period shall take into account all potential increases in the number of outstanding shares during the offer period contemplated as of the date of the public announcement:

Provided further that the offer size shall be proportionately increased in case of an increase in total number of shares, after the public announcement, which is not contemplated on the date of the public announcement.

Regulation 7(2) states that the open offer made under regulation 6 shall be for acquisition of at least such number of shares as would entitle the holder thereof to exercise an additional ten per cent of the voting rights in the target company, and shall not exceed such number of shares as would result in the post-acquisition holding of the acquirer and persons acting in concert with him exceeding the maximum permissible non- public shareholding applicable to such target company:

Provided that in the event of a competing offer being made, the acquirer who has voluntarily made a public announcement of an open offer under regulation 6 shall be entitled to increase the number of shares for which the open offer has been made to such number of shares as he deems fit:

Provided further that such increase in offer size shall have to be made within a period of fifteen working days from the public announcement of a competing offer, failing which the acquirer shall not be entitled to increase the offer size.

Regulation 7(3) states that upon an acquirer opting to increase the offer size under sub-regulation (2), such open offer shall be deemed to have been made under sub-regulation (2) of regulation 3 and the provisions of these regulations shall apply accordingly.

Regulation 7(4) states that in the event the shares accepted in the open offer were such that the shareholding of the acquirer taken together with persons acting in concert with him pursuant to completion of the open offer results in their shareholding exceeding the maximum permissible non-public shareholding, the acquirer shall be required to bring down the non-public shareholding to the level specified and within the time permitted under Securities Contract (Regulation) Rules, 1957.

Provided that if the open offer has been made by an acquirer under sub- regulation (1) of regulation 3, regulation 4 or regulation 5 and the acquirer has stated upfront his intention to retain the listing of the target company in the public announcement and the detailed public statement issued pursuant to an open offer in accordance with these regulations, the acquirer may alternatively undertake a proportionate reduction of the shares or voting rights to be acquired pursuant to the underlying agreement for acquisition/ subscription of shares or voting rights and the purchase of shares so tendered, upon the completion of the open offer process such that the resulting shareholding of the acquirer in the target company does not exceed the maximum permissible non-public shareholding prescribed under the Securities Contract (Regulation) Rules, 1957:

Provided further that in case of a preferential allotment pursuant to a Share Subscription Agreement which may trigger an open offer as envisaged in the above proviso, the Board Resolution and shareholder resolution shall be appropriately worded, so as to include the effective date of allocation/allotment and the quantum thereof.

Notwithstanding anything contained in regulation 170 of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018, in case of undertaking a scale down of subscription of shares or voting rights from the agreement, the period of fifteen days for allotment of shares shall be counted from the date of the closure of the tendering period for the open offer.

Explanation 1: The acquirer who is undertaking a scale down shall not, in such target company during the preceding two years from the date of the public announcement, be:

i. a promoter / promoter group / person(s) in control, or

ii. directly / indirectly associated with the promoter or any person(s) in control, or

iii. a person(s) holding more than twenty-five percent shares or voting rights.

Explanation 2: The acquirer who is undertaking a scale down shall not acquire joint control along with an existing promoter / person in control of the company.

Regulation 7(5) states that subject to regulation 5A, the acquirer whose shareholding exceeds the maximum permissible non-public shareholding, pursuant to an open offer under these regulations, shall not be eligible to make a voluntary delisting offer under the Delisting Regulations, unless a period of twelve months has elapsed from the date of the completion of the offer period.

Regulation 7(6) states that any open offer made under these regulations shall be made to all shareholders of the target company, other than the acquirer, persons acting in concert with him and the parties to any underlying agreement including persons deemed to be acting in concert with such parties, for the sale of shares of the target company.

What is the stipulated size of an open offer?

An open offer, other than a voluntary open offer under Regulation 6, must be made for a minimum of 26% of the target company's share capital. The size of voluntary open offer under Regulation 6 must be for at least 10% of the target company's share capital. Further the offer size percentage is calculated on the fully diluted share capital of the target company taking in to account potential increase in the number of outstanding shares as on 10th working day from the closure of the open offer.

Offer Price

Regulation 8(1) states that the open offer for acquiring shares under regulation 3, regulation 4, regulation 5 or regulation 6 shall be made at a price not lower than the price determined in accordance with sub-regulation (2) or sub-regulation (3), as the case may be.

Regulation 8(2) states that in the case of direct acquisition of shares or voting rights in, or control over the target company, and indirect acquisition of shares or voting rights in, or control over the target company where the parameters referred to in sub-regulation (2) of regulation 5 are met, the offer price shall be the highest of,—

a) the highest negotiated price per share of the target company for any acquisition under the agreement attracting the obligation to make a public announcement of an open offer;

b) the volume-weighted average price paid or payable for acquisitions, whether by the acquirer or by any person acting in concert with him, during the fifty-two weeks immediately preceding the date of the public announcement;

c) the highest price paid or payable for any acquisition, whether by the acquirer or by any person acting in concert with him, during the twenty- six weeks immediately preceding the date of the public announcement;

d) the volume-weighted average market price of such shares for a period of sixty trading days immediately preceding the date of the public announcement as traded on the stock exchange where the maximum volume of trading in the shares of the target company are recorded during such period, provided such shares are frequently traded;

Provided that the price determined as per clause (d) shall not apply in the case of disinvestment of a public sector undertaking by the Central Government or a State Government, as the case may be:

Provided further that this proviso shall apply only in case of a change in control in the public sector undertaking.

It may be noted that –

"*Disinvestment*" means the direct or indirect sale by the Central Government or any State Government or by a government company, as the case may be, of shares or voting rights in, or control over, a target company, which is a public sector undertaking. [Regulation 2(1)(g)]

"Public Sector Undertaking" means a target company in which, directly or indirectly, majority of shares or voting rights or control is held by the Central Government or any State Government or Governments, or partly by the Central Government and partly by one or more State Governments [Regulation 2(1)(u)]

"Frequently Traded Shares" means shares of a target company, in which the traded turnover on any stock exchange during the twelve calendar months preceding the calendar month in which the public announcement is required to be made under these regulations, is at least ten per cent of the total number of shares of such class of the target company:

Provided that where the share capital of a particular class of shares of the target company is not identical throughout such period, the weighted average number of total shares of such class of the target company shall represent the total number of shares [Regulation 2(1)(j)]

e) where the shares are not frequently traded, the price determined by the acquirer and the manager to the open offer taking into account valuation parameters including, book value, comparable trading multiples, and such other parameters as are customary for valuation of shares of such companies; and

f) the per share value computed under sub-regulation (5), if applicable.

Regulation 8(3) states that, in the case of an indirect acquisition of shares or voting rights in, or control over the target company, where the parameter referred to in sub-regulation (2) of regulation 5 are not met, the offer price shall be the highest of,—

a) the highest negotiated price per share, if any, of the target company for any acquisition under the agreement attracting the obligation to make a public announcement of an open offer;

b) the volume-weighted average price paid or payable for any acquisition, whether by the acquirer or by any person acting in concert with him, during the fifty-two weeks immediately preceding the earlier of, the date on which the primary acquisition is contracted, and the date on which the intention or the decision to make the primary acquisition is announced in the public domain;

c) the highest price paid or payable for any acquisition, whether by the acquirer or by any person acting in concert with him, during the twenty-six weeks immediately preceding the earlier of, the date on which the primary acquisition is contracted, and the date on which the intention or the decision to make the primary acquisition is announced in the public domain;

d) the highest price paid or payable for any acquisition, whether by the acquirer or by any person acting in concert with him, between the earlier of, the date on which the primary acquisition is contracted, and the date on which the intention or the decision to make the primary acquisition is announced in the public domain, and the date of the public announcement of the open offer for shares of the target company made under these regulations;

e) the volume-weighted average market price of the shares for a period of sixty trading days immediately preceding the earlier of, the date on which the primary acquisition is contracted, and the date on which the intention or the decision to make the primary acquisition is announced in the public domain, as traded on the stock exchange where the maximum volume of trading in the shares of the target company are recorded during such period, provided such shares are frequently traded;

Provided that the price determined as per clause (e) shall not apply in the case of disinvestment of a public sector undertaking by the Central Government or a State Government, as the case may be:

Provided further that this proviso shall apply only in case of a change in control in the public sector undertaking; and

f) the per share value computed under sub-regulation (5).

Regulation 8(4) states that, in the event the offer price is incapable of being determined under any of the parameters specified in sub-regulation (3), without prejudice to the requirements of sub-regulation (5), the offer price shall be the fair price of shares of the target company to be determined by the acquirer and the manager to the open offer taking into account valuation parameters including, book value, comparable trading multiples, and such other parameters as are customary for valuation of shares of such companies.

Regulation 8(5) states that, in the case of an indirect acquisition and open offers under sub-regulation (2) of regulation 5 where,—

a) the proportionate net asset value of the target company as a percentage of the consolidated net asset value of the entity or business being acquired;

b) the proportionate sales turnover of the target company as a percentage of the consolidated sales turnover of the entity or business being acquired; or

c) the proportionate market capitalization of the target company as a percentage of the enterprise value for the entity or business being acquired;

is in excess of fifteen per cent, on the basis of the most recent audited annual financial statements, the acquirer shall, notwithstanding anything contained in sub-regulation (2) or sub-regulation (3), be required to compute and disclose, in the letter of offer, the per share value of the target company taken into account for the acquisition, along with a detailed description of the methodology adopted for such computation.

Explanation.— For the purposes of computing the percentages referred to in clause (c) of this sub-regulation, the market capitalisation of the target company shall be taken into account on the basis of the volume-weighted average market price of such shares on the stock exchange for a period of sixty trading days preceding the earlier of, the date on which the primary acquisition is contracted, and the date on which the intention or the decision to make the primary acquisition is announced in the public domain, as traded on the stock exchange where the maximum volume of trading in the shares of the target company are recorded during such period.

How is the offer price calculated in case shares are frequently traded on the stock exchange?

If the target company's shares are frequently traded then the open offer price for acquisition of shares under the minimum open offer shall be highest of the following:

- ***Highest negotiated price per share under the share purchase agreement ("SPA") triggering the offer;***
- ***Volume weighted average price of shares acquired by the acquirer during 52 weeks preceding the public announcement ("PA");***
- ***Highest price paid for any acquisition by the acquirer during 26 weeks immediately preceding the PA;***
- ***Volume weighted average market price for sixty trading days preceding the PA.***

Regulation 8(6) states that for the purposes of sub-regulation (2) and sub-regulation (3), where the acquirer or any person acting in concert with him has any outstanding convertible instruments convertible into shares of the target company at a specific price, the price at which such instruments are to be converted into shares, shall also be considered as a parameter under sub-regulation (2) and sub-regulation (3).

Regulation 8(7) states that for the purposes of sub-regulation (2) and sub-regulation (3), the price paid for shares of the target company shall include any price paid or agreed to be paid for the shares or voting rights in, or control over the target company, in any form whatsoever, whether stated in the agreement for acquisition of shares or in any incidental, contemporaneous or collateral agreement, whether termed as control premium or as non-compete fees or otherwise.

Regulation 8(8) states that where the acquirer has acquired or agreed to acquire whether by himself or through or with persons acting in concert with him any shares or voting rights in the target company during the offer period, whether by subscription or purchase, at a price higher than the offer price, the offer price shall stand revised to the highest price paid or payable for any such acquisition:

Provided that no such acquisition shall be made after the third working day prior to the commencement of the tendering period and until the expiry of the tendering period.

Regulation 8(9) states that the price parameters under sub-regulation (2) and sub-regulation (3) may be adjusted by the acquirer in consultation with the manager to the offer, for corporate actions such as issuances pursuant to rights issue, bonus issue, stock consolidations, stock splits, payment of dividend, de-mergers and reduction of capital, where the record date for effecting such corporate actions falls prior to three working days before the commencement of the tendering period:

Provided that no adjustment shall be made for dividend declared with a record date falling during such period except where the dividend per share is more than fifty per cent higher than the average of the dividend per share paid during the three financial years preceding the date of the public announcement.

Regulation 8(10) states that where the acquirer or persons acting in concert with him acquires shares of the target company during the period of twenty-six weeks after the tendering period at a price higher than the offer price under these regulations, the acquirer and persons acting in concert shall pay the difference between the highest acquisition price and the offer price, to all the shareholders whose shares were accepted in the open offer, within sixty days from the date of such acquisition:

Provided that this provision shall not be applicable to acquisitions under another open offer under these regulations or pursuant to the Delisting Regulations, or open market purchases made in the ordinary course on the stock exchanges, not being negotiated acquisition of shares of the target company whether by way of bulk deals, block deals or in any other form.

Regulation 8(11) states that, where the open offer is subject to a minimum level of acceptances, the acquirer may, subject to the other provisions of this regulation, indicate a lower price, which will not be less than the price determined under this regulation, for acquiring all the acceptances despite the acceptance falling short of the indicated minimum level of acceptance, in the event the open offer does not receive the minimum acceptance.

Regulation 8(12) states that, in the case of any indirect acquisition, other than the indirect acquisition referred in sub-regulation (2) of regulation 5, the offer price shall stand enhanced by an amount equal to a sum determined at the rate of ten per cent per annum for the period between the earlier of the date on which the primary acquisition is contracted or the date on which the intention or the decision to make the primary acquisition is announced in the public domain, and the date of the detailed public statement, provided such period is more than five working days.

Regulation 8(13) states that, the offer price for partly paid up shares shall be computed as the difference between the offer price and the amount due towards calls-in-arrears including calls remaining unpaid with interest, if any, thereon.

Regulation 8(14) states that, the offer price for equity shares carrying differential voting rights shall be determined by the acquirer and the manager to the open offer with full disclosure of justification for the price so determined, being set out in the detailed public statement and the letter of offer:

Provided that such price shall not be lower than the amount determined by applying the percentage rate of premium, if any, that the offer price for the equity shares carrying full voting rights represents to the price parameter computed under clause (d) of sub-regulation 2, or as the case may be, clause (e) of sub-regulation 3, to the volume-weighted average market price of the shares carrying differential voting rights for a period of sixty trading days computed on the same terms as specified in the aforesaid provisions, subject to shares carrying full voting rights and the shares carrying differential voting rights, both being frequently traded shares.

Regulation 8(15) states that, in the event of any of the price parameters contained in this regulation not being available or denominated in Indian rupees, the conversion of such amount into Indian rupees shall be effected at the exchange rate as prevailing on the date preceding the date of public announcement and the acquirer shall set out the source of such exchange rate in the public announcement, the detailed public statement and the letter of offer.

Regulation 8(16) states that, for purposes of clause (e) of sub-regulation (2) and sub-regulation (4), the Board may, at the expense of the acquirer, require valuation of the shares by an independent merchant banker other than the manager to the open offer or an independent chartered accountant in practice having a minimum experience of ten years.

Regulation 8 (17) provides that the effect on the price of the equity shares of the target company due to material price movement and confirmation of reported event or information may be excluded as per the framework specified under sub-regulation (11) of regulation 30 of the listing regulations for determination of the offer price under this regulation.

Mode of payment.

Regulation 9(1) provides the offer price may be paid, —

a) in cash;

b) by issue, exchange or transfer of listed shares in the equity share capital of the acquirer or of any person acting in concert;

c) by issue, exchange or transfer of listed secured debt instruments issued by the acquirer or any person acting in concert with a rating not inferior to investment grade as rated by a credit rating agency registered with the Board;

d) by issue, exchange or transfer of convertible debt securities entitling the holder thereof to acquire listed shares in the equity share capital of the acquirer or of any person acting in concert; or

e) a combination of the mode of payment of consideration stated in clause (a), clause (b), clause (c) and clause (d):

Provided that where any shares have been acquired or agreed to be acquired by the acquirer and persons acting in concert with him during the fifty-two weeks immediately preceding the date of public announcement constitute more than ten per cent of the voting rights in the target company and has been paid for in cash, the open offer shall entail an option to the shareholders to require payment of the offer price in cash, and a shareholder who has not exercised an option in his acceptance shall be deemed to have opted for receiving the offer price in cash:

Provided further that in case of revision in offer price the mode of payment of consideration may be altered subject to the condition that the component of the offer price to be paid in cash prior to such revision is not reduced.

Regulation 9(2) provides that, for the purposes of clause (b), clause (d) and clause (e) of sub-regulation (1), the shares sought to be issued or exchanged or transferred or the shares to be issued upon conversion of other securities, towards payment of the offer price, shall conform to the following requirements, —

(a) such class of shares are listed on a stock exchange and frequently traded at the time of the public announcement;

(b) such class of shares have been listed for a period of at least two years preceding the date of the public announcement;

(c) the issuer of such class of shares has redressed at least ninety five per cent. of the complaints received from investors by the end of the calendar quarter immediately preceding the calendar month in which the public announcement is made;

(d) the issuer of such class of shares has been in material compliance with the listing regulations for a period of at least two years immediately preceding the date of the public announcement:

Provided that in case where the Board is of the view that a company has not been materially compliant with the provisions of the listing regulations, the offer price shall be paid in cash only;

(e) the impact of auditors' qualifications, if any, on the audited accounts of the issuer of such shares for three immediately preceding financial years does not exceed five per cent. of the net profit or loss after tax of such issuer for the respective years; and

(f) the Board has not issued any direction against the issuer of such shares not to access the capital market or to issue fresh shares.

Regulation 9(3) provides that, where the shareholders have been provided with options to accept payment in cash or by way of securities, or a combination thereof, the pricing for the open offer may be different for each option subject to compliance with minimum offer price requirements under regulation 8:

Provided that the detailed public statement and the letter of offer shall contain justification for such differential pricing.

Regulation 9(4) provides that, in the event the offer price consists of consideration to be paid by issuance of securities, which requires compliance with any applicable law, the acquirer shall ensure that such compliance is completed not later than the commencement of the tendering period:

Provided that in case the requisite compliance is not made by such date, the acquirer shall pay the entire consideration in cash.

Regulation 9(5) provides that where listed securities are offered as consideration, the value of such securities shall be higher of:

i. the average of the weekly high and low of the closing prices of such securities quoted on the stock exchange during the six months preceding the relevant date;

ii. the average of the weekly high and low of the closing prices of such securities quoted on the stock exchange during the two weeks preceding the relevant date; and

iii. the volume-weighted average market price for a period of sixty trading days preceding the date of the public announcement, as traded on the stock exchange where the maximum volume of trading in the shares of the company whose securities are being offered as consideration, are recorded during the six-month period prior to relevant date and the ratio of exchange of shares shall be duly certified by an independent merchant banker (other than the manager to the open offer) or an independent chartered accountant having a minimum experience of ten years.

    Explanation.— For the purposes of this sub-regulation, the "relevant date" shall be the thirtieth day prior to the date on which the meeting of shareholders is held to consider the proposed issue of shares under sub-section (1A) of Section 81 of the Companies Act, 2013.

Regulation 9(6) states that the effect on the price of the listed equity shares, which are offered as consideration, due to material price movement and confirmation of reported event or information may be excluded as per the framework specified under sub-regulation (11) of regulation 30 of the listing regulations for determination of the price of such equity shares under this regulation.

General Exemptions

Under Regulation 10(1) the following acquisitions shall be exempt from the obligation to make an open offer under regulation 3 and regulation 4 subject to fulfillment of the conditions stipulated therefor,—

a) acquisition pursuant to inter se transfer of shares amongst qualifying persons, being,—

   i. immediate relatives;

   ii. persons named as promoters in the shareholding pattern filed by the target company in terms of the listing regulations or as the case may be, the listing agreement or these regulations for not less than three years prior to the proposed acquisition;

   iii. a company, its subsidiaries, its holding company, other subsidiaries of such holding company, persons holding not less than fifty per cent of the equity shares of such company, other companies in which such persons hold not less than fifty per cent of the equity shares, and their subsidiaries subject to control over such qualifying persons being exclusively held by the same persons;

   Explanation: For the purpose of this sub-clause, the company shall include a body corporate, whether Indian or foreign.

   iv. persons acting in concert for not less than three years prior to the proposed acquisition, and disclosed as such pursuant to filings under the listing regulations or as the case may be, the listing agreement;

   v. shareholders of a target company who have been persons acting in concert for a period of not less than three years prior to the proposed acquisition and are disclosed as such pursuant to filings under the 35[listing regulations or as the case may be, the listing agreement], and any company in which the entire equity share capital is owned by such shareholders in the same proportion as their holdings in the target company without any differential entitlement to exercise voting rights in such company:

Provided that for purposes of availing of the exemption under this clause,—

(a) If the shares of the target company are frequently traded, the acquisition price per share shall not be higher by more than twenty-five per cent of the volume-weighted average market price for a period of sixty trading days preceding the date of issuance of notice for the proposed inter se transfer under sub-regulation (5), as traded on the stock exchange where the maximum volume of trading in the shares of the target company are recorded during such period, and if the shares of the target company are infrequently traded, the acquisition price shall not be higher by more than twenty- five percent of the price determined in terms of clause (e) of sub-regulation (2) of regulation 8; and

(b) the transferor and the transferee shall have complied with applicable disclosure requirements set out in Chapter V.

b) acquisition in the ordinary course of business by,—

i. an underwriter registered with the Board by way of allotment pursuant to an underwriting agreement in terms of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009;

ii. a stock broker registered with the Board on behalf of his client in exercise of lien over the shares purchased on behalf of the client under the bye-laws of the stock exchange where such stock broker is a member;

iii. a merchant banker registered with the Board or a nominated investor in the process of market making or subscription to the unsubscribed portion of issue in terms of Chapter XB of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009;

iv. any person acquiring shares pursuant to a scheme of safety net in terms of regulation 44 of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009;

v. a merchant banker registered with the Board acting as a stabilising agent or by the promoter or pre-issue shareholder in terms of regulation 45 of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009;

vi. by a registered market-maker of a stock exchange in respect of shares for which he is the market maker during the course of market making;

vii. a Scheduled Commercial Bank, acting as an escrow agent; and

viii. invocation of pledge by Scheduled Commercial Banks or Public Financial Institutions as a pledgee.

c) acquisitions at subsequent stages, by an acquirer who has made a public announcement of an open offer for acquiring shares pursuant to an agreement of disinvestment, as contemplated in such agreement:

Provided that,—

i. both the acquirer and the seller are the same at all the stages of acquisition; and

ii. full disclosures of all the subsequent stages of acquisition, if any, have been made in the public announcement of the open offer and in the letter of offer.

d) acquisition pursuant to a scheme,—

i. made under section 18 of the Sick Industrial Companies (Special Provisions) Act, 1985 or any statutory modification or re-enactment thereto;

ii. of arrangement involving the target company as a transferor company or as a transferee company, or reconstruction of the target company, including amalgamation, merger or demerger;

iii. pursuant to an order of a court or a tribunal under any law or regulation, Indian or foreign; or

iv. of arrangement not directly involving the target company as a transferor company or as a transferee company, or reconstruction not involving the target company's undertaking, including amalgamation, merger or demerger, pursuant to an order of a court or a tribunal or under any law or regulation, Indian or foreign, subject to,—

(a) the component of cash and cash equivalents in the consideration paid being less than twenty-five per cent of the consideration paid under the scheme; and

(b) where after implementation of the scheme of arrangement, persons directly or indirectly holding at least thirty-three per cent of the voting rights in the combined entity are the same as the persons who held the entire voting rights before the implementation of the scheme.

da) acquisition pursuant to a resolution plan approved under section 31 of the Insolvency and Bankruptcy Code, 2016;

e) acquisition pursuant to the provisions of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ;

f) acquisition pursuant to the provisions of the Delisting Regulations;

g) acquisition by way of transmission, succession or inheritance;

h) acquisition of voting rights or preference shares carrying voting rights arising out of the operation of sub-section (2) of section 47 of the Companies Act, 2013;

i) Acquisition of shares by the lenders pursuant to conversion of their debt as part of a debt restructuring implemented in accordance with the guidelines specified by the Reserve Bank of India:

Provided that the conditions specified under sub-regulation (6) of regulation 158 of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 are complied with

Explanation. – For the purpose of this clause, "lenders" shall mean all scheduled commercial banks (excluding Regional Rural Banks) and All India Financial Institutions.

j) increase in voting rights arising out of the operation of sub-section (1) of section 106 of the Companies Act, 2013 or pursuant to a forfeiture of shares by the target company, undertaken in compliance with the provisions of the Companies Act, 2013 and its articles of association.

(2A) An increase in the voting rights of any shareholder beyond the threshold limits stipulated in sub-regulations (1) and (2) of regulation 3, without the acquisition of control, pursuant to the conversion of equity shares with superior voting rights into ordinary equity shares, shall be exempted from the obligation to make an open offer under regulation 3.

(2B) Any acquisition of shares or voting rights or control of the target company by way of preferential issue in compliance with regulation 164A of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 shall be exempt from the obligation to make an open offer under sub- regulation (1) of regulation 3 and regulation 4.

Explanation.- The above exemption from open offer shall also apply to the target company with infrequently traded shares which is compliant with the provisions of sub- regulations (2), (3), (4), (5),(6), (7) and (8) of regulation 164A of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018. The pricing of such infrequently traded shares shall be in terms of regulation 165 of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018.

How is the offer price calculated in case shares are infrequently traded on the stock exchange?

If the target company's shares are infrequently traded, then the open offer price for acquisition of shares under the minimum open offer shall be highest of the following:

- ***Highest negotiated price per share under the share purchase agreement ("SPA") triggering the offer;***
- ***Volume weighted average price of shares acquired by the acquirer during 52 weeks preceding the public announcement ("PA");***
- ***Highest price paid for any acquisition by the acquirer during 26 weeks immediately preceding the PA;***
- ***The price determined by the acquirer and the manager to the open offer after taking into account valuation parameters including book value, comparable trading multiples, and such other parameters that are customary for valuation of shares of such companies.***

It may be noted that the Board may at the expense of the acquirer, require valuation of shares by an independent merchant banker other than the manager to the offer or any independent chartered accountant in practice having a minimum experience of 10 years.

Under Regulation 10(3), an increase in voting rights in a target company of any shareholder beyond the limit attracting an obligation to make an open offer under sub-regulation (1) of regulation 3, pursuant to buy-back of shares by the target company shall be exempt from the obligation to make an open offer provided such shareholder reduces his shareholding such that his voting rights fall to below the threshold referred to in sub-regulation (1) of regulation 3 within ninety days from the date of the closure of the said buy-back offer.

Under Regulation 10(4), the following acquisitions shall be exempt from the obligation to make an open offer under sub-regulation (2) of regulation 3, —

a) acquisition of shares by any shareholder of a target company, upto his entitlement, pursuant to a rights issue;

b) acquisition of shares by any shareholder of a target company, beyond his entitlement, pursuant to a rights issue, subject to fulfillment of the following conditions,—

   i. the acquirer has not renounced any of his entitlements in such rights issue; and

   ii. the price at which the rights issue is made is not higher than the ex-rights price of the shares of the target company, being the sum of,—

      A. the volume weighted average market price of the shares of the target company during a period of sixty trading days ending on the day prior to the date of determination of the rights issue price, multiplied by the number of shares outstanding prior to the rights issue, divided by the total number of shares outstanding after allotment under the rights issue:

      Provided that such volume weighted average market price shall be determined on the basis of trading on the stock exchange where the maximum volume of trading in the shares of such target company is recorded during such period; and

      B. the price at which the shares are offered in the rights issue, multiplied by the number of shares so offered in the rights issue divided by the total number of shares outstanding after allotment under the rights issue:

c) increase in voting rights in a target company of any shareholder pursuant to buy- back of shares:

Provided that,—

i. such shareholder has not voted in favour of the resolution authorising the buy-back of securities under section 68 of the Companies Act, 2013;

ii. in the case of a shareholder resolution, voting is by way of postal ballot;

iii. where a resolution of shareholders is not required for the buy- back, such shareholder, in his capacity as a director, or any other interested director has not voted in favour of the resolution of the board of directors of the target company authorising the buy-back of securities under section 68 of the Companies Act, 2013; and

iv. the increase in voting rights does not result in an acquisition of control by such shareholder over the target company:

Provided further that where the aforesaid conditions are not met, in the event such shareholder reduces his shareholding such that his voting rights fall below the level at which the obligation to make an open offer would be attracted under sub-regulation (2) of regulation 3, within ninety days from the date of closure of the buy-back offer by the target company, the shareholder shall be exempt from the obligation to make an open offer.

d) acquisition of shares in a target company by any person in exchange for shares of another target company tendered pursuant to an open offer for acquiring shares under these regulations;

e) acquisition of shares in a target company from state-level financial institutions or their subsidiaries or companies promoted by them, by promoters of the target company pursuant to an agreement between such transferors and such promoter;

f) acquisition of shares in a target company from a venture capital fund or category I Alternative Investment Fund or a foreign venture capital investor registered with the Board, by promoters of the target company pursuant to an agreement between such venture capital fund or category I Alternative Investment Fund or foreign venture capital investor and such promoters.

Under Regulation 10(5), acquisitions under clause (a) of sub-regulation (1), and clauses (e) and (f) of sub-regulation (4), the acquirer shall intimate the stock exchanges where the shares of the target company are listed, the details of the proposed acquisition in such form as may be specified, at least four working days prior to the proposed acquisition, and the stock exchange shall forthwith disseminate such information to the public.

Under Regulation 10(6), any acquisition made pursuant to exemption provided for in this regulation, the acquirer shall file a report with the stock exchanges where the shares of the target company are listed, in such form as may be specified not later than four working days from the acquisition, and the stock exchange shall forthwith disseminate such information to the public.

Under Regulation 10(7), any acquisition of or increase in voting rights pursuant to exemption provided for in clause (a) of sub-regulation (1), sub-clause (iii) of clause (d) of sub- regulation (1), clause (h) of sub-regulation (1), sub-regulation (2), sub-regulation (3) and clause (c) of sub-regulation (4), clauses (a), (b) and (f) of sub-regulation (4), the acquirer shall, within twenty-one working days of the date of acquisition, submit a report in such form as may be specified along with supporting documents to the Board giving all details in respect of acquisitions, along with a non-refundable fee of rupees one lakh fifty thousand by way of direct credit in the bank account through NEFT/RTGS/IMPS or any other mode allowed by RBI or by way of a banker's cheque or demand draft payable in Mumbai in favour of the Board.

Explanation.— For the purposes of sub-regulation (5), sub-regulation (6) and sub- regulation (7) in the case of convertible securities, the date of the acquisition shall be the date of conversion of such securities.

What are the threshold limits for acquisition of shares / voting rights, beyond which an obligation to make an open offer is triggered?

Acquisition of 25% or more shares or voting rights: An acquirer, who (along with PACs, if any) holds less than 25% shares or voting rights in a target company and agrees to acquire shares or acquires shares which along with his/ PAC's existing shareholding would entitle him to exercise 25% or more shares or voting rights in a target company, will need to make an open offer before acquiring such additional shares.

Acquisition of more than 5% shares or voting rights in a financial year: An acquirer who (along with PACs, if any) holds 25% or more but less than the maximum permissible non-public shareholding in a target company, can acquire additional shares in the target company as would entitle him to exercise more than 5% of the voting rights in any financial year ending March 31, only after making an open offer.

Exemptions by the Board

According to Regulation 11(1), the Board may for reasons recorded in writing, grant exemption from the obligation to make an open offer for acquiring shares under these regulations subject to such conditions as the Board deems fit to impose in the interests of investors in securities and the securities market.

According to Regulation 11(2), the Board may for reasons recorded in writing, grant a relaxation from strict compliance with any procedural requirement under Chapter III and Chapter IV subject to such conditions as the Board deems fit to impose in the interests of investors in securities and the securities market on being satisfied that,—

a) the target company is a company in respect of which the Central Government or State Government or any other regulatory authority has superseded the board of directors of the target company and has appointed new directors under any law for the time being in force, if,—

   i. such board of directors has formulated a plan which provides for transparent, open, and competitive process for acquisition of shares or voting rights in, or control over the target company to secure the smooth and continued operation of the target company in the interests of all stakeholders of the target company and such plan does not further the interests of any particular acquirer;

   ii. the conditions and requirements of the competitive process are reasonable and fair;

   iii. the process adopted by the board of directors of the target company provides for details including the time when the open offer for acquiring shares would be made, completed and the manner in which the change in control would be effected; and

b) the provisions of Chapter III and Chapter IV are likely to act as impediment to implementation of the plan of the target company and exemption from strict compliance with one or more of such provisions is in public interest, the interests of investors in securities and the securities market.

According to Regulation 11(3), for seeking exemption under sub-regulation (1), the acquirer shall, and for seeking relaxation under sub-regulation (2) the target company shall file an application with the Board, supported by a duly sworn affidavit, giving details of the proposed acquisition and the grounds on which the exemption has been sought.

According to Regulation 11(4), the acquirer or the target company, as the case may be, shall along with the application referred to under sub-regulation (3) pay a non-refundable fee of rupees five lakh, by way of direct credit in the bank account through NEFT/RTGS/IMPS or any other mode allowed by RBI or by way of a banker's cheque or demand draft payable in Mumbai in favour of the Board.

According to Regulation 11(5), the Board may after affording reasonable opportunity of being heard to the applicant and after considering all the relevant facts and circumstances, pass a reasoned order either granting or rejecting the exemption or relaxation sought as expeditiously as possible:

Provided that the Board may constitute a panel of experts to which an application for an exemption under sub-regulation (1) may, if considered necessary, be referred to make recommendations on the application to the Board.

According to Regulation 11(6), the order passed under sub-regulation (5) shall be hosted by the Board on its official website.

OPEN OFFER PROCESS

Manager to the open offer

Regulation 12(1) states that, prior to making a public announcement, the acquirer shall appoint a merchant banker registered with the Board, who is not an associate of the acquirer, as the manager to the open offer.

Explanation.— For the purposes of this regulation the term "associate" has the same meaning as in the Securities and Exchange Board of India (Merchant Bankers) Regulations, 1992.

Regulation 12(2) states that, the public announcement of the open offer for acquiring shares required under these regulations shall be made by the acquirer through such manager to the open offer.

Timing

Regulation 13(1) states that, the public announcement referred to in regulation 3 and regulation 4 shall be made in accordance with regulation 14 and regulation 15, on the date of agreeing to acquire shares or voting rights in, or control over the target company.

Regulation 13(2) states that, such public announcement,—

a) in the case of market purchases, shall be made prior to placement of the purchase order with the stock broker to acquire the shares, that would take the entitlement to voting rights beyond the stipulated thresholds;

b) pursuant to an acquirer acquiring shares or voting rights in, or control over the target company upon converting convertible securities without a fixed date of conversion or upon conversion of depository receipts for the underlying shares of the target company shall be made on the same day as the date of exercise of the option to convert such securities into shares of the target company;

c) pursuant to an acquirer acquiring shares or voting rights in, or control over the target company upon conversion of convertible securities with a fixed date of conversion shall be made on the second working day preceding the scheduled date of conversion of such securities into shares of the target company;

d) pursuant to a disinvestment shall be made on the same day as the date of executing the agreement for acquisition of shares or voting rights in or control over the target company;

e) in the case of indirect acquisition of shares or voting rights in, or control over the target company where none of the parameters referred to in sub-regulation (2) of regulation 5 are met, may be made at any time within four working days from the earlier of, the date on which the primary acquisition is contracted, and the date on which the intention or the decision to make the primary acquisition is announced in the public domain;

f) in the case of indirect acquisition of shares or voting rights in, or control over the target company where any of the parameters referred to in sub- regulation (2) of regulation 5 are met shall be made on the earlier of, the date on which the primary acquisition is contracted, and the date on which the intention or the decision to make the primary acquisition is announced in the public domain;

g) pursuant to an acquirer acquiring shares or voting rights in, or control over the target company, under preferential issue, shall be made on the date on which the board of directors of the target company authorises such preferential issue;

h) the public announcement pursuant to an increase in voting rights consequential to a buy-back not qualifying for exemption under regulation 10, shall be made not later than the ninetieth day from the date of closure of the buy-back offer by the target company;

i) the public announcement pursuant to any acquisition of shares or voting rights in or control over the target company where the specific date on which title to such shares, voting rights or control is acquired is beyond the control of the acquirer, shall be made not later than two working days from the date of receipt of intimation of having acquired such title.

Regulation 13(2A) states that, notwithstanding anything contained in sub-regulation (2), a public announcement referred to in regulation 3 and regulation 4 for a proposed acquisition of shares or voting rights in or control over the target company through a combination of,-

i. an agreement and any one or more modes of acquisition referred to in sub- regulation (2) of regulation 13, or

ii. any one or more modes of acquisition referred in clause (a) to (i) of sub-regulation(2) of regulation 13,

shall be made on the date of first such acquisition, provided the acquirer discloses in the public announcement the details of the proposed subsequent acquisition.

Regulation 13(3) states that, the public announcement made under regulation 6 shall be made on the same day as the date on which the acquirer takes the decision to voluntarily make a public announcement of an open offer for acquiring shares of the target company.

Regulation 13(3) states that, pursuant to the public announcement made under sub-regulation (1) and sub- regulation (3), a detailed public statement shall be published by the acquirer through the manager to the open offer in accordance with regulation 14 and regulation 15, not later than five working days of the public announcement:

Provided that the detailed public statement pursuant to a public announcement made under clause (e) of sub-regulation (2) shall be made not later than five working days of the completion of the primary acquisition of shares or voting rights in, or control over the company or entity holding shares or voting rights in, or control over the target company.

Explanation.— It is clarified that in the event the acquirer does not succeed in acquiring the ability to exercise or direct the exercise of voting rights in, or control over the target company, the acquirer shall not be required to make a detailed public statement of an open offer for acquiring shares under these regulations.

Publication

Under Regulation 14(1), the public announcement shall be sent to all the stock exchanges on which the shares of the target company are listed, and the stock exchanges shall forthwith disseminate such information to the public.

Under Regulation 14(2), a copy of the public announcement shall be sent to the Board and to the target company at its registered office within one working day of the date of the public announcement.

Under Regulation 14(3), the detailed public statement pursuant to the public announcement referred to in sub-regulation (4) of regulation 13 shall be published in all editions of any one English national daily with wide circulation, any one Hindi national daily with wide circulation, and any one regional language daily with wide circulation at the place where the registered office of the target company is situated and one regional language daily at the place of the stock exchange where the maximum volume of trading in the shares of the target company are recorded during the sixty trading days preceding the date of the public announcement.

Under Regulation 14(4), simultaneously with publication of such detailed public statement in the newspapers, a copy of the same shall be sent to,—

i. the Board through the manager to the open offer,

ii. all the stock exchanges on which the shares of the target company are listed, and the stock exchanges shall forthwith disseminate such information to the public,

iii. the target company at its registered office, and the target company shall forthwith circulate it to the members of its board.

Contents

According to Regulation 15(1), the public announcement shall contain such information as may be specified, including the following,—

a) name and identity of the acquirer and persons acting in concert with him;

b) name and identity of the sellers, if any;

c) nature of the proposed acquisition such as purchase of shares or allotment of shares, or any other means of acquisition of shares or voting rights in, or control over the target company;

d) the consideration for the proposed acquisition that attracted the obligation to make an open offer for acquiring shares, and the price per share, if any;

e) the offer price, and mode of payment of consideration;

f) offer size, and conditions as to minimum level of acceptances, if any; and

g) intention of the acquirer to either delist the target company or retain the listing of the target company. In case of proposed delisting under regulation 5A, the proposed open offer price and indicative price as required under regulation 5A shall be disclosed along with an explanation setting out the rationale and basis for justifying the indicative price.

According to Regulation 15(2), the detailed public statement pursuant to the public announcement shall contain such information as may be specified in order to enable shareholders to make an informed decision with reference to the open offer.

According to Regulation 15(3), the public announcement of the open offer, the detailed public statement, and any other statement, advertisement, circular, brochure, publicity material or letter of offer issued in relation to the acquisition of shares under these regulations shall not omit any relevant information, or contain any misleading information.

Filing of letter of offer with the Board

Regulation 16(1) provides that, within five working days from the date of the detailed public statement made under sub-regulation (4) of regulation 13, the acquirer shall, through the manager to the open offer, file with the Board, a draft of the letter of offer containing such information as may be specified along with a non-refundable fee, as per the following scale, by way of direct credit in the bank account through NEFT/RTGS/IMPS or any other mode allowed by RBI or by way of a banker's cheque or demand draft payable in Mumbai in favour of the Board,—

Sl. No.	Consideration payable under the Open Offer	Fee (Rs.)
a.	Upto ten crore rupees.	Five lakh rupees (Rs. 5,00,000)
b.	More than ten crore rupees, but less than or equal to one thousand crore rupees.	0.5 per cent of the offer size
c.	More than one thousand crore rupees.	Five crore rupees (Rs. 5,00,00,000) plus 0.125 per cent of the portion of the offer size in excess of one thousand crore rupees (1000,00,00,000).

Regulation 16(2) provides that, the consideration payable under the open offer shall be calculated at the offer price, assuming full acceptance of the open offer, and in the event the open offer is subject to differential pricing, shall be computed at the highest offer price, irrespective of manner of payment of the consideration:

Provided that in the event of consideration payable under the open offer being enhanced owing to a revision to the offer price or offer size the fees payable shall stand revised accordingly, and shall be paid within five working days from the date of such revision.

Regulation 16(3) provides that, the manager to the open offer shall provide soft copies of the public announcement, the detailed public statement and the draft letter of offer in accordance with such specifications as may be specified, and the Board shall upload the same on its website.

Regulation 16(4) provides that, the Board shall give its comments on the draft letter of offer as expeditiously as possible but not later than fifteen working days of the receipt of the draft letter of offer and in the event of no comments being issued by the Board within such period, it shall be deemed that the Board does not have comments to offer:

Provided that in the event the Board has sought clarifications or additional information from the manager to the open offer, the period for issuance of comments shall be extended to the fifth working day from the date of receipt of satisfactory reply to the clarification or additional information sought.

Provided further that in the event the Board specifies any changes, the manager to the open offer and the acquirer shall carry out such changes in the letter of offer before it is dispatched to the shareholders.

Regulation 16(5) provides that, in the case of competing offers, the Board shall provide its comments on the draft letter of offer in respect of each competing offer on the same day.

Regulation 16(6) provides that, in the event the disclosures in the draft letter of offer are inadequate the Board may call for a revised letter of offer and shall deal with the revised letter of offer in accordance with sub-regulation (4).

What is a letter of offer? What are the disclosures required under the Letter of offer?

The letter of offer is a document which is dispatched to all shareholders of the target company as on identified date. This is also made available on the website of SEBI. Letter of offer contains details about the offer, background of Acquirers/PACS, financial statements of Acquirer/ PACs, escrow arrangement, background of the target company, financial statements of the target company, justification for offer price, financial arrangements, terms and conditions of the offer, procedure for acceptance and settlement of the offer. SEBI has prescribed the format for Letter of offer, which enumerates minimum disclosure requirements. The Manager to the offer/ acquirer is free to add any other disclosures which in his opinion are material for the shareholders. The format is available in the SEBI website.

Provision of escrow

Under Regulation 17(1), not later than two working days prior to the date of the detailed public statement of the open offer for acquiring shares, the acquirer shall create an escrow account towards security for performance of his obligations under these regulations, and deposit in escrow account such aggregate amount as per the following scale:

Sl. No.	Consideration payable under the Open Offer	Escrow Amount
a.	On the first five hundred crore rupees	an amount equal to twenty-five per cent of the consideration
b.	On the balance consideration	an additional amount equal to ten per cent of the balance consideration

Provided that where an open offer is made conditional upon minimum level of acceptance, hundred percent of the consideration payable in respect of minimum level of acceptance or fifty per cent of the consideration payable under the open offer, whichever is higher, shall be deposited in cash in the escrow account.

Provided further that in case of indirect acquisitions where public announcement has been made in terms of clause (e) of sub-regulation (2) of regulation 13 of these regulations, an amount equivalent to hundred per cent of the consideration payable in the open offer shall be deposited in the escrow account.

Under Regulation 17(2), the consideration payable under the open offer shall be computed as provided for in sub-regulation (2) of regulation 16 and in the event of an upward revision of the offer price or of the offer size, the value of the escrow amount shall be computed on the revised consideration calculated at such revised offer price, and the additional amount shall be brought into the escrow account prior to effecting such revision.

Under Regulation 17(3), the escrow account referred to in sub-regulation (1) may be in the form of,—

a) cash deposited with any scheduled commercial bank;

b) bank guarantee issued in favour of the manager to the open offer by any scheduled commercial bank; or

c) deposit of frequently traded and freely transferable equity shares or other freely transferable securities with appropriate margin:

Provided that securities sought to be provided towards escrow account under clause (c) shall be required to conform to the requirements set out in sub-regulation (2) of regulation 9.

Provided further that the deposit of securities shall not be permitted in respect of indirect acquisitions where public announcement has been made in terms of clause (e) of sub-regulation (2) of regulation 13 of these regulations

Explanation: The cash component of the escrow account as referred to in clause above may be maintained in an interest bearing account, subject to the merchant banker ensuring that the funds are available at the time of making payment to the shareholders.

Under Regulation 17(4), in the event of the escrow account being created by way of a bank guarantee or by deposit of securities, the acquirer shall also ensure that at least one per cent of the total consideration payable is deposited in cash with a scheduled commercial bank as a part of the escrow account.

Under Regulation 17(5), for such part of the escrow account as is in the form of a cash deposit with a scheduled commercial bank, the acquirer shall while opening the account, empower the manager to the open offer to instruct the bank to issue a banker's cheque or demand draft or to make payment of the amounts lying to the credit of the escrow account, in accordance with requirements under these regulations.

Under Regulation 17(6), for such part of the escrow account as is in the form of a bank guarantee, such bank guarantee shall be in favour of the manager to the open offer and shall be kept valid throughout the offer period and for an additional period of thirty days after completion of payment of consideration to shareholders who have tendered their shares in acceptance of the open offer.

Under Regulation 17(7), for such part of the escrow account as is in the form of securities, the acquirer shall empower the manager to the open offer to realise the value of such escrow account by sale or otherwise, and in the event there is any shortfall in the amount required to be maintained in the escrow account, the manager to the open offer shall be liable to make good such shortfall.

Under Regulation 17(8), the manager to the open offer shall not release the escrow account until the expiry of thirty days from the completion of payment of consideration to shareholders who have tendered their shares in acceptance of the open offer, save and except for transfer of funds to the special escrow account as required under regulation 21.

Under Regulation 17(9), in the event of non-fulfilment of obligations under these regulations by the acquirer the Board may direct the manager to the open offer to forfeit the escrow account or any amounts lying in the special escrow account, either in full or in part.

Under Regulation 17(10), the escrow account deposited with the bank in cash shall be released only in the following manner,—

a) the entire amount to the acquirer upon withdrawal of offer in terms of regulation 23 as certified by the manager to the open offer:

Provided that in the event the withdrawal is pursuant to clause (c) of sub-regulation (1) of regulation 23, the manager to the open offer shall release the escrow account upon receipt of confirmation of such release from the Board;

b) for transfer of an amount not exceeding ninety per cent of the escrow account, to the special escrow account in accordance with regulation 21;

c) to the acquirer, the balance of the escrow account after transfer of cash to the special escrow account, on the expiry of thirty days from the completion of payment of consideration to shareholders who have tendered their shares in acceptance of the open offer, as certified by the manager to the open offer;

d) the entire amount to the acquirer upon the expiry of thirty days from the completion of payment of consideration to shareholders who have tendered their shares in acceptance of the open offer, upon certification by the manager to the open offer, where the open offer is for exchange of shares or other secured instruments;

e) the entire amount to the manager to the open offer, in the event of forfeiture for non-fulfillment of any of the obligations under these regulations, for distribution in the following manner, after deduction of expenses, if any, of registered market intermediaries associated with the open offer,—

   i. one third of the escrow account to the target company;

   ii. one third of the escrow account to the Investor Protection and Education Fund established under the Securities and Exchange Board of India (Investor Protection and Education Fund) Regulations, 2009; and

   iii. one third of the escrow account to be distributed pro-rata among the shareholders who have accepted the open offer.

Other Procedures

Regulation 18(1) provides simultaneously with the filing of the draft letter of offer with the Board under sub-regulation (1) of regulation 16, the acquirer shall send a copy of the draft letter of offer to the target company at its registered office address and to all stock exchanges where the shares of the target company are listed.

Regulation 18(2) provides the letter of offer shall be dispatched to the shareholders whose names appear on the register of members of the target company as of the identified date, not later than seven working days from the receipt of comments from the Board or where no comments are offered by the Board, within seven working days from the expiry of the period stipulated in sub-regulation (4) of regulation 16:

Explanation:

i. Letter of offer may also be dispatched through electronic mode in accordance with the provisions of Companies Act, 2013.

ii. On receipt of a request from any shareholder to receive a copy of the letter of offer in physical format, the same shall be provided.

iii. The aforesaid shall be disclosed in the letter of offer.

Provided that where local laws or regulations of any jurisdiction outside India may expose the acquirer or the target company to material risk of civil, regulatory or criminal liabilities in the event the letter of offer in its final form were to be sent without material amendments or modifications into such jurisdiction, and the shareholders resident in such jurisdiction hold shares entitling them to less than five per cent of the voting rights of the target company, the acquirer may refrain from dispatch of the letter of offer into such jurisdiction:

Provided further that every person holding shares, regardless of whether he held shares on the identified date or has not received the letter of offer, shall be entitled to tender such shares in acceptance of the open offer.

Regulation 18(3) provides simultaneously with the dispatch of the letter of offer in terms of sub-regulation (2), the acquirer shall send the letter of offer to the custodian of shares underlying depository receipts, if any, of the target company.

Regulation 18(4) provides irrespective of whether a competing offer has been made, an acquirer may make upward revisions to the offer price, and subject to the other provisions of these regulations, to the number of shares sought to be acquired under the open offer, at any time prior to the commencement of the last one working day before the commencement of the tendering period.

Regulation 18(5) provides that in the event of any revision of the open offer, whether by way of an upward revision in offer price, or of the offer size, the acquirer shall,—

a. make corresponding increases to the amount kept in escrow account under regulation 17 prior to such revision;

b. make an announcement in respect of such revisions in all the newspapers in which the detailed public statement pursuant to the public announcement was made; and

c. simultaneously with the issue of such an announcement, inform the Board, all the stock exchanges on which the shares of the target company are listed, and the target company at its registered office.

Regulation 18(6) provides the acquirer shall disclose during the offer period every acquisition made by the acquirer or persons acting in concert with him of any shares of the target company in such form as may be specified, to each of the stock exchanges on which the shares of the target company are listed and to the target company at its registered office within twenty-four hours of such acquisition, and the stock exchanges shall forthwith disseminate such information to the public:

Provided that the acquirer and persons acting in concert with him shall not acquire or sell any shares of the target company during the period between three working days prior to the commencement of the tendering period and until the expiry of the tendering period.

Also, the acquirer shall facilitate tendering of shares by the shareholders and settlement of the same, through the stock exchange mechanism as specified by the Board.

Regulation 18(7) provides the acquirer shall issue an advertisement in such form as may be specified, one working day before the commencement of the tendering period, announcing the schedule of activities for the open offer, the status of statutory and other approvals, if any, whether for the acquisition attracting the obligation to make an open offer under these regulations or for the open offer, unfulfilled conditions, if any, and their status, the procedure for tendering acceptances and such other material detail as may be specified:

Provided that such advertisement shall be,—

a. published in all the newspapers in which the detailed public statement pursuant to the public announcement was made; and

b. simultaneously sent to the Board, all the stock exchanges on which the shares of the target company are listed, and the target company at its registered office.

Regulation 18(8) provides the tendering period shall start not later than twelve working days from date of receipt of comments from the Board under sub-regulation (4) of regulation 16 and shall remain open for ten working days.

Regulation 18(9) provides the shareholders who have tendered shares in acceptance of the open offer shall not be entitled to withdraw such acceptance during the tendering period.

Regulation 18(10) provides that, the acquirer shall, within ten working days from the last date of the tendering period, complete all requirements under these regulations and other applicable law relating to the open offer including payment of consideration to the shareholders who have accepted the open offer.

Regulation 18(11) provides that, the acquirer shall be responsible to pursue all statutory approvals required by the acquirer in order to complete the open offer without any default, neglect or delay:

Provided that where the acquirer is unable to make the payment to the shareholders who have accepted the open offer within such period owing to non- receipt of statutory approvals required by the acquirer, the Board may, where it is satisfied that such non-receipt was not attributable to any willful default, failure or neglect on the part of the acquirer to diligently pursue such approvals, grant extension of time for making payments, subject to the acquirer agreeing to pay interest to the shareholders for the delay at such rate as may be specified:

Provided further that where the statutory approval extends to some but not all shareholders, the acquirer shall have the option to make payment to such shareholders in respect of whom no statutory approvals are required in order to complete the open offer.

It also states that, without prejudice to sub-regulation 11, in case the acquirer is unable to make payment to the shareholders who have accepted the open offer within such period, the acquirer shall pay interest for the period of delay to all such shareholders whose shares have been accepted in the open offer, at the rate of ten per cent per annum:

Provided that in case the delay was not attributable to any act of omission or commission of the acquirer, or due to the reasons or circumstances beyond the control of acquirer, the Board may grant waiver from the payment of interest.

Provided further that the payment of interest would be without prejudice to the Board taking any action under regulation 32 of these regulation or under the Act.

Sub clause 12 states that, the acquirer shall issue a post offer advertisement in such form as may be specified within five working days after the offer period, giving details including aggregate number of shares tendered, accepted, date of payment of consideration.

Such advertisement shall be,—

i. published in all the newspapers in which the detailed public statement pursuant to the public announcement was made; and

ii. simultaneously sent to the Board, all the stock exchanges on which the shares of the targ1et company are listed, and the target company at its registered office.

Conditional offer

As per Regulation 19, an acquirer may make an open offer conditional as to the minimum level of acceptance:

Provided that where the open offer is pursuant to an agreement, such agreement shall contain a condition to the effect that in the event the desired level of acceptance of the open offer is not received the acquirer shall not acquire any shares under the open offer and the agreement attracting the obligation to make the open offer shall stand rescinded.

Where an open offer is made conditional upon minimum level of acceptances, the acquirer and persons acting in concert with him shall not acquire, during the offer period, any shares in the target company except under the open offer and any underlying agreement for the sale of shares of the target company pursuant to which the open offer is made.

If the minimum level of acceptance is not reached, can the acquirer acquire shares under the Share Purchase Agreement, which triggered the offer?

In a conditional offer, if the minimum level of acceptance is not reached, the acquirer shall not acquire any shares in the target company under the open offer or the Share Purchase Agreement which has triggered the open offer.

Competing offers

Under Regulation 20, upon a public announcement of an open offer for acquiring shares of a target company being made, any person, other than the acquirer who has made such public announcement, shall be entitled to make a public announcement of an open offer within fifteen working days of the date of the detailed public statement made by the acquirer who has made the first public announcement.

The open offer made under sub-regulation (1) shall be for such number of shares which, when taken together with shares held by such acquirer along with persons acting in concert with him, shall be at least equal to the holding of the acquirer who has made the first public announcement, including the number of shares proposed to be acquired by him under the offer and any underlying agreement for the sale of shares of the target company pursuant to which the open offer is made.

Notwithstanding anything contained in these regulations, an open offer made within the period referred to in sub-regulation (1) shall not be regarded as a voluntary open offer under regulation 6, and the provisions of these regulations shall apply accordingly.

Every open offer made under sub-regulation (1) and the open offer first made shall be regarded as competing offers for purposes of these regulations.

No person shall be entitled to make a public announcement of an open offer for acquiring shares, or enter into any transaction that would attract the obligation to make a public announcement of an open offer for acquiring shares under these regulations, after the period of fifteen working days referred to in sub-regulation (1 and until the expiry of the offer period for such open offer.

Unless the open offer first made is an open offer conditional as to the minimum level of acceptances, no acquirer making a competing offer may be made conditional as to the minimum level of acceptances.

No person shall be entitled to make a public announcement of an open offer for acquiring shares, or enter into any transaction that would attract the obligation to make a public announcement of an open offer under these regulations until the expiry of the offer period where,—

i. the open offer is for acquisition of shares pursuant to disinvestment, in terms of clause (d) of sub-regulation (2) of regulation 13; or

ii. the open offer is pursuant to a relaxation from strict compliance with the provisions of Chapter III or Chapter IV granted by the Board under sub- regulation (2) of regulation 11.

The schedule of activities and the tendering period for all competing offers shall be carried out with identical timelines and the last date for tendering shares in acceptance of the every competing offer shall stand revised to the last date for tendering shares in acceptance of the competing offer last made.

Upon the public announcement of a competing offer, an acquirer who had made a preceding competing offer shall be entitled to revise the terms of his open offer provided the revised terms are more favourable to the shareholders of the target company:

Provided that the acquirers making the competing offers shall be entitled to make upward revisions of the offer price at any time up to one working day prior to the commencement of the tendering period.

Except for variations made under this regulation, all the provisions of these regulations shall apply to every competing offer.

What is a competitive offer? What happens if there is a competing offer?

Competitive offer is an offer made by a person, other than the acquirer who has made the first public announcement. A competitive offer shall be made within 15 working days of the date of the Detailed Public Statement (DPS) made by the acquirer who has made the first public announcement. If there is a competitive offer, the acquirer who has made the original public announcement can revise the terms of his open offer provided the revised terms are favorable to the shareholders of the target company.

Further, the bidders are entitled to make revision in the offer price up to 3 working days prior to the opening of the offer. The schedule of activities and the offer opening and closing of all competing offers shall be carried out with identical timelines.

Payment of consideration

Regulation 21 stipulates, for the amount of consideration payable in cash, the acquirer shall open a special escrow account with a banker to an issue registered with the Board and deposit therein, such sum as would, together with cash transferred under clause (b) of sub- regulation (10) of regulation 17, make up the entire sum due and payable to the shareholders as consideration payable under the open offer, and empower the manager to the offer to operate the special escrow account on behalf of the acquirer for the purposes under these regulations.

Subject to provisos to sub-regulation (11) of regulation 18, the acquirer shall complete payment of consideration whether in the form of cash, or as the case may be, by issue, exchange or transfer of securities, to all shareholders who have tendered shares in acceptance of the open offer, within ten working days of the expiry of the tendering period.

Any unclaimed balances lying to the credit of the special escrow account referred to in sub-regulation (1) at the end of seven years from the date of deposit thereof, shall be transferred to the Investor Protection and Education Fund established under the Securities and Exchange Board of India (Investor Protection and Education Fund) Regulations, 2009.

Completion of acquisition

Under Regulation 22 (1), the acquirer shall not complete the acquisition of shares or voting rights in, or control over, the target company, whether by way of subscription to shares or a purchase of shares attracting the obligation to make an open offer for acquiring shares, until the expiry of the offer period:

Provided that in case of an offer made under sub-regulation (1) of regulation 20 of these regulations, pursuant to a preferential allotment, the offer shall be completed within the period as provided under sub-regulation (1) of regulation 170 of the Securities and Exchange Board of India (Issue of Capital and Disclosure requirements) Regulations, 2018, subject to the non-obstante clause in sub-regulation (4) of regulation 7 of these regulations.

Provided further that in case of a delisting offer made under regulation 5A, the acquirer shall complete the acquisition of shares attracting the obligation to make an offer for acquiring shares in terms of sub-regulation (1) of regulation 3, regulation 4 or regulation 5, only after making the public announcement regarding the success of the delisting proposal made in terms of sub-regulation (4) of regulation 17 of the Delisting Regulations.

Notwithstanding anything contained in sub-regulation (1), subject to the acquirer depositing in the escrow account under regulation 17, cash or providing unconditional and irrevocable bank guarantee issued in favour of the manager to the open offer by any scheduled commercial bank, subject to the approval of the Reserve Bank of India, of an amount equal to the entire consideration payable under the open offer assuming full acceptance of the open offer, the parties to such agreement may after the expiry of twenty-one working days from the date of detailed public statement, act upon the agreement and the acquirer may complete the acquisition of shares or voting rights in, or control over the target company as contemplated.

Explanation. - For the purpose of sub-regulation (2), bank guarantee shall only be issued by such scheduled commercial bank having 'AAA' rating from a credit rating agency registered with the Board, on any of its long term debt instrument.

Provided that in case of proportionate reduction of the shares or voting rights to be acquired in accordance with the relevant provision under sub-regulation (4) of regulation 7, the acquirer shall undertake the completion of the scaled down acquisition of shares or voting rights in the target company.

Under Regulation 22(2A), notwithstanding anything contained in sub-regulation (1), an acquirer may acquire shares of the target company through preferential issue or through the stock exchange settlement process, subject to,-

i. such shares being kept in an escrow account,

ii. the acquirer not exercising any voting rights over such shares kept in the escrow account:

Provided that such shares may be transferred to the account of the acquirer, subject to the acquirer complying with requirements specified in sub-regulation (2).

Under Regulation 22(3), the acquirer shall complete the acquisitions contracted under any agreement attracting the obligation to make an open offer not later than twenty-six weeks from the expiry of the offer period:

Provided that in the event of any extraordinary and supervening circumstances rendering it impossible to complete such acquisition within such period, the Board may for reasons to be published, may grant an extension of time by such period as it may deem fit in the interests of investors in securities and the securities market.

Withdrawal of open offer

An open offer for acquiring shares once made shall not be withdrawn except under any of the following circumstances,—

a. statutory approvals required for the open offer or for effecting the acquisitions attracting the obligation to make an open offer under these regulations having been finally refused, subject to such requirements for approval having been specifically disclosed in the detailed public statement and the letter of offer;

b. the acquirer, being a natural person, has died;

c. any condition stipulated in the agreement for acquisition attracting the obligation to make the open offer is not met for reasons outside the reasonable control of the acquirer, and such agreement is rescinded, subject to such conditions having been specifically disclosed in the detailed public statement and the letter of offer; or Provided that an acquirer shall not withdraw an open offer pursuant to a public announcement made under clause (g) of sub-regulation (2) of regulation 13, even if the proposed acquisition through the preferential issue is not successful.

d. such circumstances as in the opinion of the Board, merit withdrawal.

Explanation. — For the purposes of clause (d) of sub-regulation (1), the Board shall pass a reasoned order permitting withdrawal, and such order shall be hosted by the Board on its official website.

In the event of withdrawal of the open offer, the acquirer shall through the manager to the open offer, within two working days,—

a. make an announcement in the same newspapers in which the public announcement of the open offer was published, providing the grounds and reasons for withdrawal of the open offer; and

b. simultaneously with the announcement, inform in writing to,—

   i. the Board;

   ii. all the stock exchanges on which the shares of the target company are listed, and the stock exchanges shall forthwith disseminate such information to the public; and

   iii. the target company at its registered office.

OTHER OBLIGATIONS

Directors of the Target Company

Under Regulation 24, during the offer period, no person representing the acquirer or any person acting in concert with him shall be appointed as director on the board of directors of the target company, whether as an additional director or in a casual vacancy:

Provided that after an initial period of fifteen working days from the date of detailed public statement, appointment of persons representing the acquirer or persons acting in concert with him on the board of directors may be effected in the event the acquirer deposits in cash in the escrow account referred to in regulation 17, the entire consideration payable under the open offer:

Provided further that where the acquirer has specified conditions to which the open offer is subject in terms of clause (c) of sub-regulation (1) of regulation 23, no director representing the acquirer may be appointed to the board of directors of the target company during the offer period unless the acquirer has waived or attained such conditions and complies with the requirement of depositing cash in the escrow account.

Where an open offer is made conditional upon minimum level of acceptances, the acquirer and persons acting in concert shall, notwithstanding anything contained in these regulations, and regardless of the size of the cash deposited in the escrow account referred to regulation 17, not be entitled to appoint any director representing the acquirer or any person acting in concert with him on the board of directors of the target company during the offer period.

During the pendency of competing offers, notwithstanding anything contained in these regulations, and regardless of the size of the cash deposited in the escrow account referred to in regulation 17, by any acquirer or person acting in concert with him, there shall be no induction of any new director to the board of directors of the target company:

Provided that in the event of death or incapacitation of any director, the vacancy arising therefrom may be filled by any person subject to approval of such appointment by shareholders of the target company by way of a postal ballot.

In the event the acquirer or any person acting in concert is already represented by a director on the board of the target company, such director shall not participate in any deliberations of the board of directors of the target company or vote on any matter in relation to the open offer.

Obligations of the Acquirer

Prior to making the public announcement of an open offer for acquiring shares under these regulations, the acquirer shall ensure that firm financial arrangements have been made for fulfilling the payment obligations under the open offer and that the acquirer is able to implement the open offer, subject to any statutory approvals for the open offer that may be necessary.

In the event the acquirer has not declared an intention in the detailed public statement and the letter of offer to alienate any material assets of the target company or of any of its subsidiaries whether by way of sale, lease, encumbrance or otherwise outside the ordinary course of business, the acquirer, where he has acquired control over the target company, shall be debarred from causing such alienation for a period of two years after the offer period:

Provided that in the event the target company or any of its subsidiaries is required to so alienate assets despite the intention to alienate not having been expressed by the acquirer, such alienation shall require a special resolution passed by shareholders of the target company, by way of a postal ballot and the notice for such postal ballot shall *inter alia* contain reasons as to why such alienation is necessary.

The acquirer shall ensure that the contents of the public announcement, the detailed public statement, the letter of offer and the post-offer advertisement are true, fair and adequate in all material aspects and not misleading in any material particular, and are based on reliable sources, and state the source wherever necessary.

The acquirer and persons acting in concert with him shall-

i. not sell shares of the target company held by them, during the offer period.

ii. be jointly and severally responsible for fulfillment of applicable obligations under these regulations.

Obligations of the Target Company

Following are the obligations of a target company –

1. Upon a public announcement of an open offer for acquiring shares of a target company being made, the board of directors of such target company shall ensure that during the offer period, the business of the target company is conducted in the ordinary course consistent with past practice.

2. During the offer period, unless the approval of shareholders of the target company by way of a special resolution by postal ballot is obtained, the board of directors of either the target company or any of its subsidiaries shall not,—

   (a) alienate any material assets whether by way of sale, lease, encumbrance or otherwise or enter into any agreement therefor outside the ordinary course of business;

   (b) effect any material borrowings outside the ordinary course of business;

   (c) issue or allot any authorised but unissued securities entitling the holder to voting rights:

   Provided that the target company or its subsidiaries may,—

      i. issue or allot shares upon conversion of convertible securities issued prior to the public announcement of the open offer, in accordance with pre-determined terms of such conversion;

      ii. issue or allot shares pursuant to any public issue in respect of which the red herring prospectus has been filed with the Registrar of Companies prior to the public announcement of the open offer; or

      iii. issue or allot shares pursuant to any rights issue in respect of which the record date has been announced prior to the public announcement of the open offer.

   (d) implement any buy-back of shares or effect any other change to the capital structure of the target company;

   (e) enter into, amend or terminate any material contracts to which the target company or any of its subsidiaries is a party, outside the ordinary course of business, whether such contract is with a related party, within the meaning of the term under applicable accounting principles, or with any other person; and

   (f) accelerate any contingent vesting of a right of any person to whom the target company or any of its subsidiaries may have an obligation, whether such obligation is to acquire shares of the target company by way of employee stock options or otherwise.

3. In any general meeting of a subsidiary of the target company in respect of the matters referred to in sub-regulation (2), the target company and its subsidiaries, if any, shall vote in a manner consistent with the special resolution passed by the shareholders of the target company.

4. The target company shall be prohibited from fixing any record date for a corporate action on or after the third working day prior to the commencement of the tendering period and until the expiry of the tendering period.

5. The target company shall furnish to the acquirer within two working days from the identified date, a list of shareholders as per the register of members of the target company containing names, addresses, shareholding and folio number, in electronic form, wherever available, and a list of persons whose applications, if any, for registration of transfer of shares are pending with the target company:

Provided that the acquirer shall reimburse reasonable costs payable by the target company to external agencies in order to furnish such information.

6. Upon receipt of the detailed public statement, the board of directors of the target company shall constitute a committee of independent directors to provide reasoned recommendations on such open offer, and the target company shall publish such recommendations:

   Provided that such committee shall be entitled to seek external professional advice at the expense of the target company.

   Provided further that while providing reasoned recommendations on the open offer proposal, the committee shall disclose the voting pattern of the meeting in which the open offer proposal was discussed.

7. The committee of independent directors shall provide its written reasoned recommendations on the open offer to the shareholders of the target company and such recommendations shall be published in such form as may be specified, at least two working days before the commencement of the tendering period, in the same newspapers where the public announcement of the open offer was published, and simultaneously, a copy of the same shall be sent to,—

   i. the Board;

   ii. all the stock exchanges on which the shares of the target company are listed, and the stock exchanges shall forthwith disseminate such information to the public; and

   iii. to the manager to the open offer, and where there are competing offers, to the manager to the open offer for every competing offer.

8. The board of directors of the target company shall facilitate the acquirer in verification of shares tendered in acceptance of the open offer.

9. The board of directors of the target company shall make available to all acquirers making competing offers, any information and co-operation provided to any acquirer who has made a competing offer.

10. Upon fulfillment by the acquirer, of the conditions required under these regulations, the board of directors of the target company shall without any delay register the transfer of shares acquired by the acquirer in physical form, whether under the agreement or from open market purchases, or pursuant to the open offer.

What is the role of the target company in the open offer process?

- ***Once a PA is made, the board of directors of the Target Company is expected to ensure that the business of the target company is conducted in the ordinary course. Alienation of material assets, material borrowings, issue of any authorized securities, announcement of a buy- back offer etc. is not permitted, unless authorized by shareholders by way of a special resolution by postal ballot.***
- ***The target company shall furnish to the acquirer within two working days from the identified date, a list of shareholders and a list of persons whose applications, if any, for registration of transfer of shares, in case of physical shares, are pending with the target company.***
- ***After closure of the open offer, the target company is required to provide assistance to the acquirer in verification of the shares tendered for acceptance under the open offer, in case of physical shares.***
- ***Upon receipt of the detailed public statement, the board of directors of the target company shall constitute a committee of independent directors to provide reasoned recommendations on such open offer, and the target company shall publish such recommendations and such committee shall be entitled to seek external professional advice at the expense of the target company. The recommendations of the Independent Directors are published in the same newspaper where the Detailed Public Statement is published by the acquirer and are published at least 2 working days before opening of the offer. The recommendation will also be sent to SEBI, Stock Exchanges and the Manager to the offer.***

Obligations of the Manager to the Open Offer

Regulation 27 provides for obligations of the manager to the open offer. They are-

1) Prior to public announcement being made, the manager to the open offer shall ensure that,—

   a. the acquirer is able to implement the open offer; and

   b. firm arrangements for funds through verifiable means have been made by the acquirer to meet the payment obligations under the open offer.

2) The manager to the open offer shall ensure that the contents of the public announcement, the detailed public statement and the letter of offer and the post- offer advertisement are true, fair and adequate in all material aspects, not misleading in any material particular, are based on reliable sources, state the source wherever necessary, and are in compliance with the requirements under these regulations.

3) The manager to the open offer shall furnish to the Board a due diligence certificate along with the draft letter of offer filed under regulation 16.

4) The manager to the open offer shall ensure that market intermediaries engaged for the purposes of the open offer are registered with the Board.

5) The manager to the open offer shall exercise diligence, care and professional judgment to ensure compliance with these regulations.

6) The manager to the open offer shall not deal on his own account in the shares of the target company during the offer period.

7) The manager to the open offer shall file a report with the Board within fifteen working days from the expiry of the tendering period, in such form as may be specified, confirming status of completion of various open offer requirements.

DISCLOSURES OF SHAREHOLDING AND CONTROL

Disclosure-related provisions

Regulation 25 provides for Disclosure-related provisions. This regulation stipulates that, the disclosures under this Chapter shall be of the aggregated shareholding and voting rights of the acquirer or promoter of the target company or every person acting in concert with him.

For the purposes of this Chapter, the acquisition and holding of any convertible security shall also be regarded as shares, and disclosures of such acquisitions and holdings shall be made accordingly.

It may be noted that –

"*Convertible Security*" means a security which is convertible into or ex- changeable with equity shares of the issuer at a later date, with or without the option of the holder of the security, and includes convertible debt instruments and convertible preference shares. [Regulation 2(1)(f)]

For the purposes of this Chapter, the term "encumbrance" shall include,-

(a) any restriction on the free and marketable title to shares, by whatever name called, whether executed directly or indirectly;

(b) pledge, lien, negative lien, non-disposal undertaking; or

(c) any covenant, transaction, condition or arrangement in the nature of encumbrance, by whatever name called, whether executed directly or indirectly.

Upon receipt of the disclosures required under this Chapter, the stock exchange shall forthwith disseminate the information so received.

Disclosure of Acquisition and Disposal

According to Regulation 29 any acquirer, together with persons acting in concert with him acquiring shares or voting rights in a target company, which taken together aggregates to five per cent or more of the shares of such target company, shall disclose their aggregate shareholding and voting rights in such target company in such form as may be specified:

Provided that in case of listed entity which has listed its specified securities on Innovators Growth Platform, any reference to "five per cent" shall be read as "ten per cent"

Any person together with persons acting in concert with him, holds shares or voting rights entitling them to five per cent or more of the shares or voting rights in a target company, shall disclose the number of shares or voting rights held and change in shareholding or voting rights, even if such change results in shareholding falling below five per cent, if there has been change in such holdings from the last disclosure made under sub-regulation (1) or under this sub-regulation; and such change exceeds two per cent of total shareholding or voting rights in the target company, in such form as may be specified.

Provided that in case of listed entity which has listed its specified securities on Innovators Growth Platform, any reference to "five per cent" shall be read as "ten per cent" and any reference to "two per cent" shall be read as "five per cent".

The disclosures required under sub-regulation (1) and sub-regulation (2) shall be made within two working days of the receipt of intimation of allotment of shares, or the acquisition or the disposal of shares or voting rights in the target company to,—

(a) every stock exchange where the shares of the target company are listed; and

(b) the target company at its registered office.

For the purposes of this regulation, shares taken by way of encumbrance shall be treated as an acquisition, shares given upon release of encumbrance shall be treated as a disposal, and disclosures shall be made by such person accordingly in such form as may be specified:

Provided that such requirement shall not apply to a scheduled commercial bank or public financial institution or a housing finance company or a systemically important non-banking financial company as pledgee in connection with a pledge of shares for securing indebtedness in the ordinary course of business.

Explanation. - For the purpose of this sub-regulation, -

A. a "housing finance company" means a housing finance company registered with the National Housing Bank for carrying on the business of housing finance and is either deposit taking or having asset size worth rupees five hundred crores or more; and

B. a "systemically important non-banking financial company" shall have the same meaning as assigned to it in the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018.

TAKEOVER BIDS

"Takeover bid" is an offer to the shareholders of a company, who are not the promoters of the company or the sellers of the shares under an agreement, to buy their shares in the company at the offered price within the stipulated period of time. It is addressed to the shareholders with a view to acquiring sufficient number of shares to give the Offer or Company, voting control of the target company.

A takeover bid is a technique, which is adopted by a company for taking over control of the management and affairs of another company by acquiring its controlling shares.

Type of takeover bids

A takeover bid may be a "friendly takeover bid" or a "hostile takeover bid". Bids may be mandatory/competitive bids.

Mandatory Bid

The SEBI (Substantial Acquisition of Shares and Takeovers) Regulations 2011, require acquirers to make bids for acquisition of certain level of holdings subject to certain conditions. A takeover bid is required to be made by way of a public announcement issued to the stock exchanges, followed by a Detailed Public Statement in the newspapers. Such requirements arise in the following cases:

a. for acquisition of 25% or more of the shares or voting rights;

b. for acquiring additional shares or voting rights to the extent of 5% of the voting rights in any financial year beginning April 01, if such person already holds not less than 25% but not more than 75% or 90% of the shares or voting rights in a company as the case may be;

c. for acquiring control over a company.

DEFENSE STRATEGIES TO TAKEOVER BIDS

A hostile bid made directly to the shareholders of the target company with or without previous overtures to the management of the company has become a means of creating corporate combinations. Hence, there has been considerable interest in developing defense strategies by actual and potential targets. Defenses can take the form of fortifying oneself, i.e., making the company less attractive to takeover bids or more difficult to takeover and thus discourage any offers being made. Defensive actions are also resorted to in the event of perceived threat to the company ranging from early intelligence that an acquirer is accumulating shares.

FINANCIAL DEFENSE MEASURES

Adjustments in Asset and Ownership Structure

1. Firstly, consideration has to be given to developing defense structures that create barriers specific to the bidder. These include purchase of assets that may cause legal problems, purchase of controlling shares of the bidder itself, and sale to their party of assets which made the target attractive to the bidder and issuance of new securities with special provisions conflicting with the aspects of the takeover attempt.

   It must however be borne in mind that as per the Regulation 26(2) of the SEBI (SAST) Regulations, 2011, the target company cannot alienate its assets, make any material borrowings, issue any new shares with voting rights or terminate any material contract during the offering period (which commences once the public announcement is made) except with the approval of shareholders by way of a special resolution passed by Postal Ballot. Hence it would be almost impossible to bring about adjustments in Assets and Ownership structure in India.

2. A second common method is to create a consolidated vote block allied with target management. Thus securities are issued through private placements to parties friendly or in business alliance with management or to the management itself. Moreover another method can be to repurchase publicly held shares to increase an already sizeable management block in place.

   It must however be borne in mind that as per the Regulation 26(2) of the SEBI (SAST) Regulations, 2011, the target company cannot, issue any new shares with voting rights or terminate any material contract during the offering period (which commences once the public announcement is made) and can also not make a buy-back of shares from the public shareholders except with the approval of shareholders by way of a special resolution passed by Postal Ballot. Hence it would be almost impossible to bring about adjustments in Assets and Ownership structure in India. However in anticipation of a perceived threat of takeover, the management can issue shares or convertible securities beforehand so that they can be converted once the public announcement for an open offer is made.

3. A third common theme has been the dilution of the bidders vote percentage through issuance of new equity shares. However, this option will not work in India due to the strict procedures laid down in Regulation 26(2) of the SEBI (SAST) Regulations, 2011.

4. **The "Crown Jewel" Strategy**

   The central theme is this strategy is to divest the most coveted asset by the bidder, commonly known as the "crown jewel". Consequently the hostile bidder is deprived of the primary intention behind the takeover bid. A variation of the crown jewel strategy is the more radical "scorched earth approach", vide which approach, the target sells off not only the crown jewel, but also properties to diminish its worth. Such a radical step may however be self-destructive and unwise in the company's interest.

   However as per the Companies Act, 2013, selling of whole or substantially the whole of its undertaking requires the approval of the shareholders in a general meeting by way of a special resolution and Regulation 26(2) of the SEBI (SAST) Regulations, 2011, the target company cannot alienate any of its material assets during the offering period (which commences once the public announcement is made) and can also not make a buy-back of shares from the public shareholders except with the approval of shareholders by way of a special resolution passed by Postal Ballot. Hence it would be almost impossible to use the "Crown Jewel" Strategy as a defense mechanism in India.

5. **The Pacman Defence**

   This strategy although unusual attempts to purchase the shares of the raider company. This is usually the scenario if the raider company is smaller than the target company and the target company has a substantial cash flow or liquidable asset.

   Regulation 26(2) of the SEBI (SAST) Regulations, 2011, however prohibits the target company to enter into any agreement which is not in the ordinary course of business during the offering period (which commences once the public announcement is made) except with the approval of shareholders by way of a special resolution passed by Postal Ballot. Hence it would be almost impossible to use the "Pacman Defense" Strategy as a defense mechanism in India.

6. **Targeted Share Repurchase or "Buy-back"**

   This strategy is one in which the management of the target company uses up a part of the assets of the company on the one hand to increase its holding and on their hand it disposes of some of the assets that make the target company unattractive to the raider. The strategy therefore involves a creative use of buyback of shares to reinforce its control and detract a prospective raider. But "Buyback" would involve the use of the free reserves of the company and would be an expensive proposition for the target company. Further as per Regulation 26(2) of the SEBI (SAST) Regulations, 2011, the target company cannot implement a buy-back during the offer period except with the approval of shareholders by way of a special resolution passed by Postal Ballot. Hence it would be almost impossible to use this defense mechanism also in India.

7. **Golden Parachutes**

   These are separation clauses of an employment contract that compensate managers who lose their jobs under a change of management scenario. The provision usually calls for a lump-sum payment or payment over a specified period at full and partial rates of normal compensation. Target Companies invoke this provision and pay off a huge compensation to large number of employees so as to make themselves unattractive to the raider.

   However section 192 and Section 202 of the Companies Act, 2013 provide for compensation to be paid for loss of office only to a Managing Director, Whole Time Director or a Manager and not the entire senior management, as is the practice in the United States of America. Hence this defense mechanism is of no consequence in India.

ANTI TAKEOVER AMENDMENTS OR "SHARK REPELLANTS"

An increasingly used defense mechanism being used is anti-takeover amendments to the company's constitution or articles of association, popularly called as "shark repellants". This practice consists of changing the articles of associations, regulations, bye-laws, etc. to be less attractive to the raider / hostile bidder. This again may not work out in India as any change to the Articles of Association or the Memorandum of Association would require approval of the shareholders.

1. **Supermajority Amendments**

   These amendments require shareholder approval by at least 2/3rds vote and sometimes as much as 90% of the voting power of outstanding capital for all transactions involving change of control. In most existing cases, however the super majority agreements have a board out clause which provides the board with the power to determine when and if the super majority provisions will be in effect. Pure or inflexible super majority provisions would seriously limit the management's scope of options and flexibility in takeover negotiations.

2. **Classified Boards**

   Another type of anti-takeover amendments provides for a staggered or classified board of directors to delay effective transfer and control in a takeover. The much touted management rationale in proposing a classified board is to ensure continuity of policy and experience in the USA. The legal position of such classified or staggered boards is quite flexible. An example is when a 9 member board may be divided into 3 categories, with only 3 members standing for election to a three year term each, such being the modalities of the retirement by rotation. Thus a new majority shareholder would have to wait for at least 2 AGMs to gain control of the Board of Directors. Section 152 of the Companies Act, 2013 warrants that 1/3rd of the directors whose office is determinable by retirement will retire. Therefore continuing the example of 9 directors, 3 can be made permanent directors by amending the Articles and therefore the acquirer would have to wait for at least 3 AGMs to gain control over the Board. However the company may by an ordinary resolution remove a director before the expiration of his period of officer. Thus any provision in the Articles of the Company or any agreement between the company and a director by which the director is rendered irremovable from office by an ordinary resolution would be void and contrary to the Act.

3. **Authorisation of Preferred Stock**

   The Board is authorised to create a new class of securities with special voting rights. This security, typically preferred stock may be issued to a friendly party in a control context. This is referred to as issuance of Shares with Differential Voting Rights, which is subject to restrictions under the Companies Act, 2013 and SEBI (ICDR) Regulations, 2009 and hence has been rendered unattractive over a period of time.

4. **Poison Pill Defenses**

   This is a controversial but popular defense mechanism. These pills provide their holders with special rights exercisable only after a period of time following the occurrence of a triggering event. These rights take several forms but all are difficult and costly to acquire control of the issuer or the target company. Poison pills are generally adopted by the Board of Directors without shareholder approval. Usually the rights provided by the poison pill can be altered quickly by the Board or redeemed by the Company any time after they become exercisable following the occurrence of the triggering event. These provisions force the acquirer to negotiate directly with the target company's board and allow some takeover bids to go through. Many proponents of this mechanism argue that this enhances the ability of the Board of Directors to bargain for a fair price.

CROSS BORDER TAKEOVERS

Cross Border Takeover is a much sort after term in recent years. Competitiveness among the domestic firms forces many businesses to go global. There are various factors which motivate firms to go for global takeovers.

Apart from personal glory, global takeovers are often driven by market consolidation, expansion or corporate diversification motives. Also, financial, accounting and tax related matters inspire such takeovers.

Expansion and diversification are one of the primary reasons to cross the border as the domestic markets usually do not provide the desired growth opportunities. Another main reason for cross border takeovers is to attain monopoly. Acquirer company is always on the lookout for companies which are financially vulnerable but have untapped resources or intellectual capital that can be exploited by the purchaser.

Global takeovers are complex processes. Despite some harmonized rules, taxation issues are mainly dealt within national rules, and are not always fully clear or exhaustive to ascertain the tax impact of a cross-border merger or acquisition. This uncertainty on tax arrangements sometimes require seeking of special agreements or arrangements from the tax authorities on an ad hoc basis, whereas in the case of a domestic deal the process is much more deterministic.

Cross-border takeover bids are complex transactions that may involve the handling of a significant number of legal entities, listed or not, and which are often governed by local rules (company law, market regulations, self-regulations, etc.). Not only a foreign bidder might be hindered by a potential lack of information, but also some legal complexities might appear in the merger process resulting in a deadlock, even though the bid would be ‘friendly’. This legal uncertainty may result in a significant execution risk and act as a major hurdle to cross-border consolidation.

Going global is rapidly becoming Indian company’s mantra of choice. Indian companies are now looking forward to drive costs lower, innovate speedily, and increase their international presence. Companies are discovering that a global presence can help insulate them from the vagaries of domestic market and is one of the best ways to spread the risks. Indian corporate sector has witnessed several strategic acquisitions. Tata Motors acquisition of Daewoo Commercial Vehicle Company, Tata Steel’s acquisition of Singapore’s NatSteel, Reliance’s acquisition of Flag is the culmination of Indian Company’s efforts to establish a presence outside India.

It is expected that the cross borders takeovers will increase in the near future. The companies will have to keep in mind that global takeovers are not only business proposals but also a corporate bonding for which both the entities have to sit and arrive at a meaningful and deep understanding of all the issues as mentioned above.

CASE LAWS - SEBI ORDERS

SEBI Order in the matter of ***Kesar Petroproducts Limited, SEBI, 9 March 2020***

The promoter company of a listed company transferred 48.16% to two children of an individual promoter. Consequently, each child held under 25% in the target. This transfer caused no change in the overall promoter shareholding or effective control of the target. SEBI ruled that since (i) the acquirers along with PACs held over 25% in the target; and (ii) the acquisition resulted in the children’s individual shareholding crossing 5%, Regulation 3(3) read with the Creeping Acquisition Threshold was triggered.

SEBI order in the matter of ***M/s. Patels Airtemp (India) Ltd, July 25, 2018***

In this matter there was an inter-se transfer of shares of 0.30% between 2 (two) promoters. However, as a result of the inter-se transfer, the shareholding of one of the promoters (i.e. the purchaser) (“Noticee”) increased from 24.74% to 25.04%, thereby breaching the threshold limit of 25%, as provided under regulation3(1) read with 3(3) of Takeover Regulations. The total shareholding of the promoter group did not change and it remained at around 45%. The Noticee argued that the above mentioned acquisition does not trigger the applicability of either regulation 3(1) or 3(3) of the Takeover Regulations, as the said acquisition of shares by the Noticee was an inter se transfer among the promoter entities and the overall shareholding of the promoter group, of which the Noticee is a part, remained unchanged after the said acquisition. However, SEBI held that the 2 (two) promoters in this case cannot be held to be ‘persons acting in concert’ because the persons must have a common objective or purpose of acquisition of shares or voting rights. In the instant case, the acquisition in question was an inter se transfer of shares from one promoter entity to another promoter entity, which implies that the promoter entities, including the Noticee, did not have a common objective or purpose of acquisition but were rather acting in opposite directions, where one promoter entity had purchased the shares and another entity had sold the same shares. Hence, SEBI rejected the Noticee's claim that it was acting in concert with other promoter entities, while acquiring the said shares. Since the Noticee had acquired shares as a result of which its individual shareholding had increased from 24.74% to 25.04% of the total shareholding of the Target Company (even though the overall shareholding of the promoter group remain unchanged), the threshold limit provided under regulation 3(1) of the Takeover Regulations was breached. SEBI ordered the Noticee to make an open offer and also pay interest @ 10% (ten percent) per annum along with the offer price to the public shareholders.

SEBI Order in the matter of ***Praxis Home Retail Limited, 28 April 2023***

Praxis Home Retail Limited ("Praxis") equity shares aggregating to 30 lakh were allotted to one of its promoter entities Future Corporate Resources Pvt Ltd ("FCRL"), following the exercise of the conversion option of 3,180 compulsorily convertible debentures ("CCDs") by FCRL, out of the 7,500 CCDs initially allotted to it. After exercising the conversion option, the shareholding of FCRL in Praxis rose from 47.43 per cent in the quarter ended December 2019 to 53.13 per cent, an increase of 5.71 per cent in shareholding as of February 11, 2020.

SEBI noted that as the increase in shareholding of FCRL in Praxis post-allotment is 5.71 per cent, which is more than five per cent, FCRL along with the other Noticees (PACs) allegedly were required to make a public announcement of the open offer under Takeover Regulation.

SEBI order in the matter of ***Automative Axles Ltd ("AAL"), 8 May 2023***

The case relates to Cummins indirectly acquiring a 35.52 per cent share in Automotive Axles Ltd ("AAL"). The acquisition was contracted on February 21, 2022, which triggered the requirement of public announcement of making of an open offer by the applicant under the Takeover Regulations. The open offer announcement was made belatedly with a delay of 227 days. Consequently, a settlement application was filed to settle the matter.

LESSON ROUND-UP

- Takeover is a corporate device whereby one company acquires control over another company, usually by purchasing all or a majority of its shares.
- Takeovers may be classified as friendly takeover, hostile takeover and bailout takeover.
- Consideration for takeover could be in the form of cash or in the form of shares.
- The Regulations, provide certain events, on the happening of which the Acquirer is required to make a public announcement for acquiring the shares from the public shareholders of the company.
- The Regulations provide for voluntary offer, competing offer and conditional offer. Regulation 10 and 11 provide for automatic exemptions and specific exemptions.
- The regulations provide a detailed procedure once the public announcement is made.
- There are certain conditions when the open offer made can be withdrawn.
- The Regulations also provide for obligations on the part of the target company, acquirers, board of directors of the target company and the merchant banker.
- The Regulations also provide the situations in which the disclosures are to be made.
- Takeover bids may be mandatory, partial or competitive bids.
- Defense strategies to takeover bids are adopted by companies to counter takeover attempts.
- Competitiveness among the domestic firms forces many businesses to go global. There are various factors which motivate firms to go for Cross Border Takeovers.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).

1. What do you mean by the term ‘Takeover’? What are the objectives which takeover seeks to achieve?
2. “SEBI has formulated a comprehensive code for takeover of listed companies”. Do you agree?
3. Who are the persons considered to be ‘persons acting in concert’ under the SEBI (SAST) Regulations, 2011?
4. How does an acquirer make a delisting cum open offer?
5. What are the general obligations of ‘Acquirer’ and ‘Merchant Banker’ under SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011?

LIST OF FURTHER READINGS

- SEBI (SAST) Regulation 2011 Law and Practice by Abha Jaiswal, Bharat’s Publication
- The Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeover) Regulations, 2011
- The Securities and Exchange Board of India (Listing Obligations and Disclosure Requirement) Regulations, 2015
- The Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2009

OTHER REFERENCES (Including Websites / Video Links)

- https://www.sebi.gov.in/

Planning & Strategy

Lesson 3

KEY CONCEPTS

■ Mergers and Acquisitions – Primary Factors ■ Funding through financial instruments ■ Preferential allotment ■ External Commercial Borrowing (ECB)

Learning Objectives

To understand:

- Reason for Mergers and Acquisitions
- Process of Funding
- Preferential allotment
- Option is a derivative contract
- Funding through stock swaps
- Funding through ECB
- Funding through leveraged buyout (LBO)
- Protection of Minority Interest

Lesson Outline

- Planning for mergers and acquisitions
- Process of Funding
- Funding through various types of Financial Instruments
- Funding Through Equity Shares
- Preferential Allotment
- Funding through Preference Shares
- Funding through Options or Securities with
- Differential rights
- Funding through Swaps or Stock to Stock Mergers
- Funding through Financial Institutions and Banks
- Funding through Rehabilitation Finance
- Funding through Leveraged Buyouts
- Minority and 'Minority Interest' under the Companies Act, 2013
- Legal Provisions of the Companies Act, 2013
- Protection of Minority Interest
- Case Laws/ Judicial pronouncements
- Family holdings and their management
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

- The Companies Act, 2013
- The Companies (Compromises, Arrangements and Amalgamations) Rules, 2016
- SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018

PLANNING AND STRATEGY FOR MERGER AND ACQUISITIONS

Strategies play an integral role when it comes to mergers and acquisitions. A sound and effective strategic decision and procedure is very important to ensure success and fulfilling of expected desires. Every company has a different culture and follows different strategies to define their merger and acquisition appetite. There are various strategic reasons for companies to consider making an acquisition and a successful takeover can help companies achieve their strategic synergy objectives as well as increase cost effectiveness within the business.

The process of merging with another company or acquiring a company is complex. In addition to the legal ramifications, companies must be aware of the potential tax implications as well as ensuring that the terms of the deal benefit both parties. Often companies rely on strategic advisors, lawyers and professionals to negotiate on their behalf in order to obtain the best possible deal within the framework of the applicable laws.

Although many companies consider mergers and acquisitions as opportunities for growth, they can provide a viable business solution for companies attempting to downsize or companies which are looking for an effective exit strategy. By divesting company assets, the company can reduce costs and streamline its operations leading to an increase in efficiency and profitability. If companies have an underperforming subsidiary, they can rely on mergers and acquisitions to dispose of or merge the asset effectively and in to achieve overall business synergy.

> Strategic assessments of companies, industry expertise, due diligence, merger integration, and operational improvements represent areas where knowledge and skills are required for the success of a merger or acquisition.

The Indian business environment is undergoing massive change with almost all relevant corporate laws/ regulations in India having been revamped in the last few years, be it the Takeover Code, delisting guidelines, Companies Act, Accounting, Competition Law, Tax laws, Foreign Exchange Management Act (FEMA) regulations, impacting both inbound and outbound investments.

With the opening up of the economy and the government's thrust on various initiatives, such as AtmaNirbhar, Make in India and Digital India, inbound M&A activity is only going to be on the rise. Further global outlook towards India has become positive than ever before with an improved ranking in World Bank's Ease of Doing Business ranking and in the World Economic Forum's Global Competitiveness Index. India is seen as a growing economic superpower across the globe and is one of the best performing emerging markets even in the face of global financial meltdowns.

Whatever may be the reason for any M&A, the benefits are multifold, to enumerate a few:

- **Economies of scale**
- **Operational synergies and efficiencies**
- **Access to new markets, new products, new business**
- **Access to foreign capital**

Mergers and Acquisitions – Primary Factors to be considered

Merger or amalgamation is undertaken for acquiring cash resources, eliminating competition, saving on taxes or influencing the economies of large-scale operations. Therefore, there are host of factors, which require consideration before initiating a merger or amalgamation exercise. A detailed list of the primary factors requiring consideration before initiating a merger or amalgamation from the economic, commercial and legal perspective is explained as follows:

(i) Identification of Parties

Will one or more businesses be transferred to an existing firm or a newly formed entity? Consider drafting heads of terms, do you require a confidentiality agreement? Do you require an exclusivity agreement? Review financial liability of the parties - undertake appropriate searches and enquiries.

(ii) Due Diligence

Carry out legal, commercial, tax and financial due diligence on the parties entering into the transaction. This will help in identifying risk areas along with any necessary consent you will need to obtain.

(iii) Any third-party consents required?

Ascertain if any third-party consents or no objections would be required such as from banks, business contracts, partner/shareholder consents. These should emerge from due diligence. Consider also regulatory consents/licences that may be required.

(iv) Taxation

It will be necessary to ascertain the most suitable tax structure for the transaction and, in particular, the way in which the consideration should be structured, at an early stage, therefore consider consulting tax advisors.

(v) Risk

Sharing of risk – What kind of indemnities/warranties/representations be considered? Should there be a cap on such indemnities and warranties?

(vi) Will the transaction impact on existing loan/finance arrangements?

Check loan documents and constitution documents to see whether any proposed borrowing would be a breach of any existing funding. What will happen in relation to third party funding of the Seller business? Confirm that there are no restrictions on the disposal of the target business or any of its assets. How will the merged business be funded?

(vii) Existing Charges/Modifications over the assets to be acquired

Are there any mortgages, charges or debentures over any of the business assets? If yes, obtain copies and consider how they are to be satisfied/discharged. If there are floating charges, obtain certificates of non-crystallisation/release. Whether there is any pledge on shares? Obtain a Search Report from a Practicing Company Secretary.

(viii) Guarantees and indemnities (bank or other)

Has the Seller given or received any guarantees or indemnities in relation to the business? If yes, then obtain copies (including details of arrangements) and consider in particular, how to ensure the business continues to have the benefit of relevant guarantees.

(ix) Licences

Will the Buyer have all other licences which it needs to operate the business?

(x) Supply contracts

Will supply contracts be transferred or need to be terminated? How will this be done?

(xi) What IP is used in the business?

Obtain a full list of trademarks, service marks, patents, designs, domain names, copyright and other registered and unregistered intellectual property used in the business. Carry out trade mark and patent searches as may be appropriate through an IPR Attorney.

PROCESS OF FUNDING

The process of funding in the case of mergers and takeovers may be arranged by a company in a number of ways. It may be from its own funds, consisting of further issue of equity and preference share capital, through raising of borrowed funds by way of issuing various financial instruments like Non-Convertible Debentures. A company may borrow funds through the issue of debentures, bonds, external commercial borrowings, issue of securities, loans from Central or State financial institutions, banks, etc. Broadly we can divide them into three categories as described below:

Internal accruals: The retained earnings and free reserves accumulated over a period of time by well-managed companies may be utilized for the purpose of restructuring.

Borrowings: The required funds could be raised from banks and financial institutions or through external commercial borrowings or by issue of debentures.

Issue of securities: Funds may also be raised through issue of equity shares, preference shares and other securities, depending upon the quantum and urgency.

Cash deal vs. Stock deal for acquisition

In a Cash Deal, the acquiring company pays the shareholders of the target company a predetermined amount of cash per share. Here's an example:

Company A, a large tech conglomerate, decides to acquire Company B, a promising startup specializing in artificial intelligence technology, for $100 million in cash.

Company A offers to purchase all outstanding shares of Company B at $10 per share.

Company B's shareholders agree to the deal, and upon completion of the acquisition, they receive $10 in cash for each share they own.

Company A gains full control of Company B's assets, technology, intellectual property, and talent by paying cash to the shareholders.

Advantages of Cash Deals are**:**

Certainty of payment: Shareholders receive a fixed amount of cash, providing certainty and liquidity.

Simplified valuation: The valuation of the target company is straightforward based on the agreed-upon cash amount per share.

Minimal dilution: Existing shareholders of the acquiring company are not diluted by issuing additional shares.

In a Stock Deal, the acquiring company offers its own shares to the shareholders of the target company as consideration for the acquisition. Here's an example:

Company X, a growing e-commerce platform, plans to acquire Company Y, a smaller online marketplace, through a stock-for-stock transaction.

Company X proposes to exchange 1 share of its stock for every 2 shares of Company Y's stock.

Company Y's shareholders accept the offer, entitling them to receive Company X's stock in exchange for their Company Y shares.

Upon completion of the acquisition, Company Y's shareholders become shareholders of Company X, owning a portion of its equity based on the agreed exchange ratio.

Advantages of a Stock Deal are:

Tax benefits: Depending on the jurisdiction and structure, stock deals may offer tax advantages compared to cash deals.

Flexibility in valuation: Stock deals allow for flexibility in valuation, as the acquiring company's stock price can fluctuate over time.

Potential for synergies: Aligning interests through stock ownership can foster collaboration and integration between the two companies.

Considerations:

Market conditions: The choice between cash and stock deals may depend on prevailing market conditions, availability of financing, and the relative valuations of the companies involved.

Shareholder preferences: The preferences of both the acquiring company's shareholders and the target company's shareholders play a significant role in determining the structure of the deal.

Regulatory requirements: Regulatory considerations, including antitrust laws and securities regulations, may influence the choice between cash and stock transactions.

Overall, whether a cash deal or a stock deal is preferable depends on various factors, including the strategic objectives of the acquiring company, the financial position of both parties, and the prevailing market dynamics.

An all cash, all stock offer is an offer by one company to purchase all of another company's shares from its shareholders for cash. In this type of proposal, one way for the acquiring company to try to get uncertain shareholders to agree to a sale is to offer a premium over the price for which the shares are presently trading. The acquired company's shareholders may earn a capital gain if the combined entity realizes cost savings.

The prices of the shares of the company being acquired may rise, particularly if the company was bought at a premium. Premium is offered for making the deal lucrative for the seller company and is beneficial for the acquirer in the long run.

For example, the acquirer may announce cost savings from the acquisition, which typically means reducing staff count or removal of redundant technology and systems. Although layoffs are bad for the employees, for the combined company, it means enhanced profit margins through lower costs. It can also mean a higher stock for shareholders of the acquired company and perhaps the acquirer as well.

Also, if the acquired company's stock price has been low, shareholders might have the opportunity to exit and that too at a premium if the acquired company's stock surges on the news of the acquisition.

The acquiring company may not have all of the cash on its balance sheet to make an all cash, all stock acquisition. In such a situation, a company can tap into the capital markets or creditors to raise the necessary funds.

If the acquiring company was not a publicly-traded company already, it could issue an IPO whereby they would issue shares of stock to investors and receive cash in return. Existing public companies could issue additional shares (by way of preferential issue or otherwise) to raise cash for an acquisition as well.

Limitations to All Cash, All Stock Offers

Although cash transactions can appear to be an easy, straightforward way of acquiring another company, it is not always the case. All stock offer for shareholders is a taxable event. Even if they sell their shares to the acquirer at a premium, taxes may take a significant chunk of their earnings if the sale price is higher than the acquisition price investors paid when they initially purchased their shares. However, all shares of stock that are made at a price higher than the stock's cost basis constitutes a taxable event, so this particular sale is not that different from a tax standpoint from a normal sale on the secondary market.

Another possible acquisition method would be for the acquiring company to offer shareholders an exchange of all the shares they hold in the target company for shares in the acquiring company. These stock-for-stock transactions are not taxable. The acquiring firm could also offer a combination of cash and shares.

The main distinction between cash and stock transactions is that, in cash transactions, acquiring shareholders take on the entire risk that the expected synergy value embedded in the acquisition premium will not materialize. In stock transactions, that risk is shared and diversified with selling shareholders. More precisely, in stock transactions, the synergy risk is shared in proportion to the percentage of the combined company the acquiring and selling shareholders each will own.

FUNDING THROUGH VARIOUS TYPES OF FINANCIAL INSTRUMENTS

Funding may be made through various types of financial instruments. Funding may be done through any of the following modes:

- Funding through Equity Shares.
- Funding through Preferential Shares.
- Funding through Options or Securities with Differential Rights.
- Funding though Swaps or Stock to Stock Mergers.
- Funding through External Commercial Borrowings (ECBs) and Depository Receipts (DRs).
- Funding through Financial Institutions and Banks.
- Funding through Rehabilitation Finance.
- Funding through Leveraged Buyouts.

FUNDING THROUGH EQUITY SHARES

Equity share capital- It can be considered as permanent capital of the company. Equity needs no servicing as the company is not required to pay to its equity shareholders the fixed amount return in form of interest which would be the case if a company were to borrow by issue of bonds or other debt instruments.

Raising money from the public by issue of shares or bonds or debentures is a time consuming process and involves huge costs. It would require numerous things to be in place and several rounds of discussion would be required to take place between the directors and key promoters having the controlling stake, between the Board of Directors (BOD) and consultants, analysts, experts, Company Secretaries, Chartered Accountants & lawyers. Furthermore, it requires several legal compliances.

Thus, planning for an acquisition by raising funds through public issue may be complicated and long drawn process.

Issue of securities for listed companies

The Securities and Exchange Board of India (the "SEBI") is the nodal authority regulating entities that are listed and to be listed on stock exchanges in India. SEBI through SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 ("SEBI ICDR") regulates the issue of securities of such companies.

These regulations apply to:

(a) a public issue;

(b) a rights issue, where the aggregate value of specified securities offered is fifty lakh rupees or more;

(c) a preferential issue;

(d) an issue of bonus shares by a listed issuer;

(e) a qualified institutional placement by a listed issuer;

(f) an issue of Indian Depository Receipts

PREFERENTIAL ALLOTMENT

Before preferential allotment, let us first look at the various options of raising further capital for companies under Companies Act, 2013. Section 62 of the Act has listed some of the possible options.

Some of the common requirements of IPO and rights issue have been listed below:

Rights Issue Section 62(1)(a) of Companies Act 2013

- Issue where new shares are offered to existing shareholders proportionately

Preferential Offer Section 62(1)(c) of Companies Act 2013

- Issue of shares or other securities to any select person or group of persons on a preferential basis, whether or not those persons include the persons referred to in clause (a) of clause (b), either for cash or consideration other than cash.

Preferential allotment, in simple words, is an offer for allotment to a select group of identified persons, and does not include public issue, rights issue, ESOP, employee stock purchase scheme or an issue of sweat equity shares or bonus shares or depository receipts issued in a country outside India or foreign securities.

The provisions of preferential allotment are laid under section 62(1)(c) read with Rule 13 of Chapter IV- The Companies (Share Capital and Debentures) Rules, 2014. This further leads us to follow provisions of Section 42 read with Rule 14 of the Chapter III-Companies (Prospectus and Allotment of Securities) Rules, 2014, which deals with private placement. Hence, for any preferential offer, we need to compulsorily follow the provisions of private placement.

Further, listed companies have to comply with the provisions of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 for the preferential allotment. Listed companies may also raise funds by way of qualified institutional placement. Qualified institutional placement is the special type of the preferential allotment made only to the qualified institutional buyers (QIB).

Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 is applicable for preferential allotment in case of listed companies. Listed companies in addition to Companies Act, 2013 also need to follow these regulations. Some of its important features have been mentioned below:

Sl. No.	Particulars	Description
1.	Definition of preferential issue	It means an issue of specified securities by a listed issuer to any select person or group of persons on a private placement basis. It does not include an offer of specified securities made through a public issue, rights issue, bonus issue, employee stock option scheme, employee stock purchase scheme or qualified institutions placement or an issue of sweat equity shares or depository receipts issued in a country outside India or foreign securities.
2.	Preliminary conditions	A listed company can make preferential issue only if following conditions are satisfied: (a) a special resolution has been passed by its shareholders; (b) all the equity shares, if any, held by the proposed allottees in the issuer are in dematerialised form; (c) the issuer is in compliance with the conditions for continuous listing of equity shares as specified in the listing agreement with the recognised stock exchange where the equity shares of the issuer are listed; (d) the issuer has obtained the Permanent Account Number of the proposed allottees.
3.	Restriction	The issuer shall not make preferential issue of specified securities to any person who has sold any equity shares of the issuer during the six months preceding the relevant date.
4.	Allotment	Allotment pursuant to the special resolution shall be completed within a period of fifteen days from the date of passing of such resolution.

FUNDING THROUGH PREFERENCE SHARES

One more source of funding a merger or the takeover may be through the issue of preference shares, but unlike equity capital, issue of the preference share capital as purchase consideration to the shareholder of merging company mostly includes the payment of fixed preference dividend at a fixed rate.

Thus, before deciding to raise funds for this purpose, by an issue of preference shares, the Board of the company has to ensure that the merged company or Target Company would be able to yield sufficient profits for covering additional liability in respect of the payment of preference dividend. A company that is funding its merger or takeover proposal through an issue of preference shares is required to pay a dividend to such shareholders as per agreed terms.

Examples of Indian companies issuing preference shares are as under:

Tata Motors, one of India's leading automobile manufacturers, has issued preference shares to raise capital for various purposes, including expansion, working capital requirements, and debt restructuring. These preference shares often come with fixed dividend rates and priority over common shareholders in terms of dividend payments and asset distribution in the event of liquidation.

HDFC Bank, one of India's largest private sector banks, has issued preference shares as part of its capital-raising efforts. These preference shares typically offer investors a fixed dividend rate and may also come with conversion rights into common shares under certain conditions. HDFC Bank has utilized preference shares to strengthen its Tier I capital base and support its growth initiatives.

Reliance Industries Limited (RIL), a diversified conglomerate with interests in petrochemicals, refining, telecommunications, and retail, has issued preference shares in the past. These preference shares have been used to raise funds for investment in its various business segments, including the expansion of its digital services platform, Jio Platforms. RIL's preference shares may offer investors attractive dividend rates and priority in capital repayment.

ICICI Bank, one of India's leading private sector banks, has issued preference shares to strengthen its capital position and support its growth plans. These preference shares typically offer investors fixed dividend rates and may also include conversion options into common shares at predetermined terms. ICICI Bank has used preference shares as a strategic tool for optimizing its capital structure and enhancing its financial flexibility.

Adani Ports and Special Economic Zone (APSEZ), India's largest port operator, has issued preference shares to fund its expansion projects and acquisitions in the port and logistics sector. These preference shares may offer investors preferential dividend rates and priority in dividend payments. APSEZ's preference shares have been instrumental in raising capital for its ambitious growth plans and infrastructure development initiatives.

Issue and redemption of preference shares:

Section 55 of the Act read with Rule 9 and Rule 10 of the Companies (Share Capital and Debentures) Rules, 2014 deals with the procedure involved in issue and redemption of preference shares. SEBI regulations shall be followed, in case a company intends to list its preference shares on a recognized stock exchange.

Some of the features pertaining to issue and redemption of preference shares have been listed in the following table:

Sl. No.	Particulars	Description
1.	Issue of irredeemable preference shares	Not permitted, after the commencement of Companies Act, 2013.

Sl. No.	Particulars	Description
2.	Maximum period of redemption	Preference shares shall be redeemed within a period not exceeding twenty years from the date of their issue. However, a company may issue preference shares for a period exceeding twenty years but not exceeding thirty years, for infrastructure projects, subject to the redemption of a minimum ten percent of such preference shares per year from the twenty first year onwards or earlier, on proportionate basis, at the option of the preference shareholders. The term "infrastructure projects" means the infrastructure projects specified in Schedule VI. [For Schedule VI, refer to Annexure-I, at the end of this chapter]
3.	Authority to issue	Yes, authorization to issue preference shares is required in Articles of Association of Company. Further it also requires the approval of shareholders in general meeting through special resolution.
4.	Particulars of resolution	(a) the priority with respect to payment of dividend or repayment of capital vis-a-vis equity shares; (b) the participation in surplus fund; (c) the participation in surplus assets and profits, on winding-up which may remain after the entire capital has been repaid; (d) the payment of dividend on cumulative or non-cumulative basis. (e) the conversion of preference shares into equity shares. (f) the voting rights; (g) the redemption of preference shares.
5.	Explanatory statement	The explanatory statement shall provide complete material facts concerned with the issue of such shares, including- (a) the size of the issue and number of preference shares to be issued and nominal value of each share;
		(b) the nature of such shares i.e. cumulative or non - cumulative, participating or non-participating, convertible or non - convertible; (c) the objectives of the issue; (d) the manner of issue of shares; (e) the price at which such shares are proposed to be issued; (f) the basis on which the price has been arrived at; (g) the terms of issue, including terms and rate of dividend on each share, etc.; (h) the terms of redemption, including the tenure of redemption, redemption of shares at premium and if the preference shares are convertible, the terms of conversion; (i) the manner and modes of redemption; (j) the current shareholding pattern of the company; (k) the expected dilution in equity share capital upon conversion of preference shares.
6.	Preconditions for issue	Shall not have any subsisting default in the redemption of preference shares issued either before or after the commencement of the Act or in payment of dividend due on any preference shares.
7.	Preconditions for redemption	Such shares shall be fully paid, before redemption.

Sl. No.	Particulars	Description
8.	Manner of redemption	Redemption shall be done out of profits of the company which would otherwise be available for dividend or out of the proceeds of a fresh issue of shares made for the purposes of such redemption. A company may redeem its preference shares only on the terms on which they were issued or as varied after due approval of preference shareholders under section 48 of the Act. Preference shares may be redeemed: (a) at a fixed time or on the happening of a particular event; (b) any time at the company's option; or (c) any time at the shareholder's option.
9.	Inability to redeem or pay dividend	A company if is not in a position to redeem any preference shares or to pay dividend, if any, it may, with the consent of the holders of three-fourths in value of such preference shares and with the approval of the Tribunal on a petition made by it in this behalf, issue further redeemable preference shares equal to the amount due, including the dividend thereon.
10.	Transfer to Capital Redemption Reserve Account	A sum equal to the nominal amount of the shares to be redeemed shall be transferred to CRR account from profits, if such shares are proposed to be redeemed out of the profits of the company.
11.	Impact on share capital	Issue of further redeemable preference shares or the redemption of preference shares shall not be deemed to be an increase or a reduction, in the share capital of the company.
12.	Register of Members	Register of Members maintained under section 88 shall contain the particulars in respect of such preference shareholder(s).

FUNDING THROUGH OPTIONS OR SECURITIES WITH DIFFERENTIAL RIGHTS

Companies can also restructure their capital through derivatives and options as the means of raising funds. Indian companies are allowed to issue derivatives or options plus the shares and quasi-equity instruments with differential rights as to dividend and/or voting. Companies may also issue non-voting shares or the shares with differential voting rights to shareholders of Transferor Company. Such issue gives companies an additional source of fund without interest cost and without the obligation to repay, as these are other forms of the equity capital.

The promoters of the companies may be interested in such form of consideration as it does not impose any kind of obligation and there is no loss/dilution of control in case of non-voting shares.

Option is a derivative contract: An option gives the holder the right but not the obligation to buy or sell something in the future.

There are two types of Options:

1. Put option- is one which gives holder the right to sell particular number of shares (or any other commodity) at a given price and typically one buys put options, if the price of the stock is expected to decline.
2. Call option- gives the holder the right to buy the shares at a predetermined period of time and at a predetermined price. Typically, one buys call options if the price of the underlying stock is expected to rise.

Definition given by the Securities Contracts (Regulation) Act, 1956 (SCRA):

The term derivative has been defined under section 2(ac) in Securities Contracts (Regulation) Act, 1956 as follows:

(a) a security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security;

(b) a contract which derives its value from the prices, or index of prices, of underlying securities.

(c) commodity derivatives; and

(d) such other instruments as may be declared by the Central Government to be derivatives.

Further in terms of section 2(d) of the Securities Contracts (Regulation) Act, 1956 "option in securities" means a contract for the purchase or sale of a right to buy or sell, or a right to buy and sell, securities in future, and includes a *teji*, a *mandi*, a *teji mandi*, a *galli*, a put, a call or a put and call in securities.

Section 20 of the SCRA which had dealt with prohibition of options in securities had been omitted by the Securities Laws (Amendment) Act, 1995. It means that the options in securities were permitted after the omission of the Section 20 of SCRA.

Securities with Differential Rights:

Section 48 of the Companies Act, 2013 deals with the variation of shareholders' rights. This section deals with the procedure involved, when a company intends to vary rights attached with any class of shareholders. The features have been explained below:

1. **Approval of class of shareholders** - The rights attached to the shares of any class may be varied with the consent in writing of the holders of not less than three-fourths of the issued shares of that class or by means of a special resolution passed at a separate meeting of the holders of the issued shares of that class —

   (a) if provision with respect to such variation is contained in the memorandum or articles of the company; or

   (b) in the absence of any such provision in the memorandum or articles, if such variation is not prohibited by the terms of issue of the shares of that class.

2. **Impact on rights of other class** - The section provides that if variation by one class of shareholders affects the rights of any other class of shareholders, the consent of three-fourths of such other class of shareholders shall also be obtained and the provisions of this section shall apply to such variation.

3. **Cancellation of variation** - Variation may be cancelled if, holders of not less than ten per cent of the issued shares of a class did not consent to such variation or vote in favour of the special resolution for the variation. They may apply to the Tribunal to cancel the variation, and where any such application is made, the variation shall not have effect unless and until it is confirmed by the Tribunal. The decision of the Tribunal on any such application shall be binding on the shareholders. The company shall, within thirty days of the date of the order of the Tribunal, file a copy thereof with the Registrar.

Equity shares with differential rights:

Companies may issue equity shares with differential rights as to dividend, voting or otherwise in compliance with Rule 4 of the Companies (Share Capital and Debentures) Rules, 2014 Some of its important features are listed below:

Sl. No.	Particulars	Description
1.	Authority to issue	The articles of association of the company authorizes the issue ofshares with differential rights.

Sl. No.	Particulars	Description
2.	Approval of shareholders	The issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders: Provided that where the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot.
3.	Impact on post-issue capital	The shares with differential rights shall not exceed seventy-four per cent of the total post-issue paid up equity share capital including equity shares with differential rights issued at any point of time.
4.	No default in statutory filings	The company has not defaulted in filing financial statements and annual returns for three financial years immediately preceding the financial year in which it is decided to issue such shares.
5.	No default in payment of statutory dues	The company has no subsisting default in the payment of a declared dividend to its shareholders or repayment of its matured deposits or redemption of its preference shares or debentures that have become due for redemption or payment of interest on such deposits or debentures or payment of dividend.
6.	No default in repayment of borrowings	The company has not defaulted in payment of the dividend on preference shares or repayment of any term loan from a public financial institution or State level financial institution or scheduled Bank that has become repayable or interest payable thereon or dues with respect to statutory payments relating to its employees to any authority or default in crediting the amount in Investor Education and Protection Fund to the Central Government. Provided that a company may issue equity shares with differential rights upon expiry of five years from the end of the financial Year in which such default was made good.
7.	No penalization	The company has not been penalized by Court or Tribunal during the last three years of any offence under the Reserve Bank of India Act, 1934, the Securities and Exchange Board of India Act, 1992, the Securities Contracts Regulation Act, 1956, the Foreign Exchange Management Act, 1999 or any other special Act, under which such companies being regulated by sectoral regulators.
8.	No conversion	The company shall not convert its existing equity share capital with voting rights into equity share capital carrying differential voting rights and ***vice versa.***
9.	Disclosure in Board report	The holders of the equity shares with differential rights shall enjoy all other rights such as bonus shares, rights shares etc., which the holders of equity shares are entitled to, subject to the differential rights with which such shares have been issued.
10.	Register of Members	Register of Members shall contain all the relevant particulars of such shares along with details of the shareholders.

Tata Motors issued DVR shares to the public, providing shareholders with reduced voting rights compared to ordinary shares. These shares allowed Tata Group to raise funds while maintaining control over strategic decisions.

Bharti Airtel issued non-voting equity shares to investors, allowing them to participate in the company's growth and profitability without having voting rights in shareholder meetings.

Infosys issued Compulsorily Convertible Preference Shares to investors, which are convertible into equity shares of the company at a predetermined conversion price. These shares allow investors to participate in the company's growth while providing them with fixed dividends until conversion.

FUNDING THROUGH SWAPS OR STOCK TO STOCK MERGERS

Funding through stock swaps is a very common method. Under this method of funding, the holders of the target company's stock receive shares of the acquiring company's stock in lieu of the merger.

The share exchange ratio is mutually determined by the Board of Directors of both the companies on the basis of the valuation report prepared by the professionals.

Stock swap mergers might involve risk. Along with the normal risks, stock swap mergers consist of the risks associated with the fluctuations in the stock prices of two companies. The terms of deal involve an exchange of shares and are predicted on prices of the two companies' stock at the time of the announcement, drastic changes in shares prices of one or both of companies can cause an entire deal to be re-evaluated.

FUNDING THROUGH EXTERNAL COMMERCIAL BORROWINGS (ECBs) RECEIPTS

ECBs are commercial loans raised by eligible resident entities from recognised non-resident entities and should conform to parameters such as minimum maturity, permitted and non-permitted end-uses, maximum all-in-cost ceiling, etc. The parameters apply in totality and not on a standalone basis. The framework for raising loans through ECB comprises the following three tracks:

- **Track I:** Medium term foreign currency denominated ECB with minimum average maturity of 3/5 years.
- **Track II:** Long term foreign currency denominated ECB with minimum average maturity of 10 years.
- **Track III:** Indian Rupee (INR) denominated ECB with minimum average maturity of 3/5 years.

Various types of ECB: ECBs can be raised as:

1. Loans, e.g., bank loans, loans from equity holder, etc.
2. Capital market instruments, e.g.
   (a) Securitized instruments (e.g. floating rate notes/fixed rate bonds/non-convertible, optionally convertible or partially convertible preference shares/debentures)
   (b) FCCB
   (c) FCEB
4. Buyers' credit/suppliers' credit.
5. Financial lease.

However, ECB framework is not applicable in respect of the investment in non-convertible debentures (NCDs) in India made by Registered Foreign Portfolio Investors (RFPIs).

Available routes for raising ECB: Under the ECB framework, ECBs can be raised either under the automatic route or under the approval route. For the automatic route, the cases are examined by the Authorised Dealer Category-I (AD Category-I) banks. Under the approval route, the prospective borrowers are required to send their requests to the RBI through their ADs for examination. While the regulatory provisions are mostly similar, there are some differences in the form of amount of borrowing, eligibility of borrowers, permissible end-uses, etc. under the two routes. Except FCEBs which can be issued only under the approval route, all other forms of borrowings mentioned above can be raised both under automatic and approval routes.

Eligible Borrowers: The list of entities eligible to raise ECB under the three tracks is set out in the following table :

Track I	Track II	Track III
(i) Companies in manufacturing and software development sectors.	(i) All entities listed under Track I.	(i) All entities listed under Track II.

(ii) Shipping and airlines companies. (iii) Small Industries Development Bank of India (SIDBI). (iv) Units in Special Economic Zones(SEZs). (v) Export Import Bank of India (Exim Bank) (only under the approval route). (vi) Companies in infrastructure sector, Non-Banking Financial Companies - Infrastructure Finance Companies (NBFC-IFCs), NBFCs-Asset Finance Companies (N B F C - A F C s) , Holding Companies and Core Investment Companies (CICs). Also, Housing Finance Companies, regulated by the National Housing Bank, Port Trusts constituted under the Major Port Trusts Act, 1963 or Indian Ports Act, 1908.	(ii) Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (INVITs) coming under the regulatory framework of the Securities and Exchange Board of India (SEBI).	(ii) AllNon-Banking Financial Companies (NBFCs) coming under the regulatorypurview of the Reserve Bank. (iii) NBFCs-Micro Finance Institutions (NBFCs- MFIs), Not for Profit companies registered under the Companies Act, 1956/2013, Societies, trusts and cooperatives (registered under the Societies Registration Act, 1860, Indian Trust Act, 1882 and State- level Cooperative Acts/ Multi- level Cooperative Act/State-level mutually aided Cooperative Acts respectively), Non-Government Organisations (NGOs) which are engaged in micro finance activities. (iv) Companies engaged in miscellaneous services viz. research and development (R&D), training (other than educational institutes), companies supporting infrastructure, companies providing logistics services. (v) Developers of Special Economic Zones(SEZs)/ National Manufacturing andInvestment Zones (NMIZs).

ECB Framework

It has been decided, in consultation with the Government of India, to rationalise the extant framework for ECB and Rupee Denominated Bonds in light of the experience gained to improve the ease of doing business. The new framework is instrument neutral and would further strengthen the AML/CFT framework.

Salient features of the revised ECB guidelines are as under:

(i) *Merging of Tracks:* Merging of Tracks I and II as “Foreign Currency denominated ECB” and merging of Track III and Rupee Denominated Bonds framework as “Rupee Denominated ECB”.

(ii) *Eligible Borrowers:* This has been expanded to include all entities eligible to receive FDI. Additionally, Port Trusts, Units in SEZ, SIDBI, EXIM Bank, registered entities engaged in micro-finance activities, viz., registered not for profit companies, registered societies/trusts/cooperatives and non-government organisations can also borrow under this framework.

(iii) *Recognised Lender:* The lender should be resident of FATF or IOSCO compliant country. Multilateral and Regional Financial Institutions, Individuals and Foreign branches/subsidiaries of Indian banks can also be lenders.

(iv) *Minimum Average Maturity Period (MAMP):* MAMP will be 3 years for all ECBs. However, for ECB raised from foreign equity holder and utilised for specific purposes, as detailed in the Annex, the MAMP would be 5 years. Similarly, for ECB up to USD 50 million per financial year raised by manufacturing sector, which has been given a special dispensation, the MAMP would be 1 year.

(v) *Late Submission Fee (LSF) for delay in Reporting:* Any borrower, who is otherwise in compliance of ECB guidelines, except for delay in reporting drawdown of ECB proceeds before obtaining LRN or Form ECB 2 returns, can regularize the delay by payment of LSF as per the laid down procedure.

Masala Bonds: In 2017, RBI revised the norms for masala bonds. Masala bonds are rupee denominated bonds sold to offshore investors, who take the foreign exchange risk to earn higher interest rates compared with dollar- denominated overseas bond sales. After a review, the RBI declared that from October 3, 2017 masala bonds will no longer form part of the limit for Foreign Portfolio Investment (FPI) investments in corporate bonds and it will form part of ECB.

The proceeds of these bonds can be used for all purposes except for the following:

(a) Real estate activities other than for development of integrated township/affordable housing projects;

(b) Investing in capital market and using the proceeds for equity investment domestically;

(c) Activities prohibited as per the Foreign Direct Investment (FDI) guidelines;

(d) On-lending to other entities for any of the above objectives; and

(e) Purchase of land.

'Depository Receipt' means a foreign currency denominated instrument, whether listed on an international exchange or not, issued by a foreign depository in a permissible jurisdiction on the back of permissible securities issued or transferred to that foreign depository and deposited with a domestic custodian and includes 'Global Depository Receipt' as defined in section 2(44) of the Companies Act, 2013 as any instrument in the form of a depository receipt, by whatever name called, created by a foreign depository outside India and authorised by a company making an issue of such depository receipts.

The rules relating to the GDR are contained in Depository Receipts Scheme, 2014, which was issued *vide* Notification No. F. No. 9/1/2013-ECB dated 21st October, 2014.

Eligibility:

1. The following persons are eligible to issue or transfer permissible securities to a foreign depository for the purpose of issue of depository receipts:

   (a) any Indian company listed or unlisted, private or public;

   (b) any other issuer of permissible securities;

   (c) any person holding permissible securities; which has not been specifically prohibited from accessing the capital market or dealing in securities.

2. Unsponsored depository receipts on the back of listed permissible securities can be issued only if such depository receipts:

   (a) give the holder the right to issue voting instructions; and

   (b) are listed on an international exchange.

Issue: The following is the procedure for the issue of depository receipts:

- A foreign depository may issue depository receipts by way of a public offering or private placement or in any other manner prevalent in a permissible jurisdiction;
- An issuer may issue permissible securities to a foreign depository for the purpose of issue of depository receipts by any mode permissible for issue of such permissible securities to investors;

- The holders of permissible securities may transfer permissible securities to a foreign depository for the purpose of the issue of depository receipt, with or without the approval of issue of such permissible securities through transactions on a recognized stock exchange, bilateral transactions or by tendering through a public platform.

Limits: The aggregate of permissible securities which may be issued or transferred to foreign depositories for issue of depository receipts, along with permissible securities already held by persons resident outside India, shall not exceed the limit on foreign holding of such permissible securities under the Foreign Exchange Management Act, 1999.

Pricing: The permissible securities shall not be issued to a foreign depository for the purpose of issuing depository receipts at a price less than the price applicable to a corresponding mode of issue of such securities to domestic investors under the applicable laws.

FUNDING THROUGH FINANCIAL INSTITUTIONS AND BANKS

Banks and Financial Institutions may provide end-to-end advisory services to the client in mergers and acquisitions involving target search, analysis of the target and potential synergies for the client, value analysis, pricing strategy, review of the transaction documents, negotiation support, documentation and closure of the transaction.

Funding of a merger or takeover with the help of loans from financial institutions, banks, etc. has its own merits and demerits. Takeover of a company could be achieved in several ways and while deciding the takeover of a going concern, there are matters such as the capital gains tax, stamp duty on immovable properties and the facility for carrying forward of accumulated losses. With parameters playing a critical role, the takeover should be organized in such a way that best suits the facts and circumstances of the specific case and also it should meet the immediate needs and objectives of the management. While discussing modes of acquisition, certainly there would be a planning for organizing the necessary funding for the acquisition. If borrowings from domestic banks and financial institutions have been identified as the inevitable choice, all the financial and managerial information must be placed before the banks and financial institutions for the purpose of getting the necessary resources.

> The advantage of funding is that the period of such funds is definite which is fixed at the time of taking such loans. Therefore, the Board of the company is assured about continued availability of such funds for the predetermined period. On the negative side, the interest burden on such loans is quite high which must be kept in mind by the Board while deciding to use borrowed funds from financial institution. Such funding should be thought of and resorted to only when the Board is sure that the merged company or the target company will give adequate returns i.e., timely payment of periodical interest on such loans and re-payment of the loans at the end of the term for which such loans have been taken.

FUNDING THROUGH REHABILITATION FINANCE

The Insolvency and Bankruptcy Code, 2016 (IBC) seeks to consolidate the existing multiple framework by creating a single law for insolvency and bankruptcy. This law is a one stop solution for insolvency of corporates, individuals, partnerships and other entities. It received the President's assent on 28 May, 2016 and is operation from December 2016.

With the enactment of The Sick Industrial Companies (Special Provisions) Repeal Act, 2003, the Sick Industrial Companies (Special Provisions) Act, 1985 came to an end with effect from the 1st December, 2016 and with this BIFR and AIFR also stand dissolved.

Section 252 of the Insolvency and Bankruptcy Code, 2016, which has been notified w.e.f. November 1st, 2016 states that the Sick Industrial Companies (Special Provisions) Repeal Act, 2003 shall be amended in the manner specified in the Eighth Schedule. This Eighth Schedule provides that in section 4, for sub-clause (b) of the Repeal Act, the following sub-clause shall be substituted, namely—

(b) On such date as may be notified by the Central Government in this behalf, any appeal preferred to the Appellate Authority or any reference made or inquiry pending to or before the Board or any proceeding of whatever nature pending before the Appellate Authority or the Board under the Sick Industrial Companies (Special Provisions) Act, 1985 shall stand abated:

Provided that a company in respect of which such appeal or reference or inquiry stands abated under this clause may make reference to the National Company Law Tribunal under the Insolvency and Bankruptcy Code, 2016 within one hundred and eighty days from the commencement of the Insolvency and Bankruptcy Code, 2016 in accordance with the provisions of the Insolvency and Bankruptcy Code, 2016:

Provided further that no fees shall be payable for making such reference under Insolvency and Bankruptcy Code, 2016 by a company whose appeal or reference or inquiry stands abated under this clause."

Accordingly, whatever matters were pending before the BIFR/AAIFR under the SICA were also abated and could make reference to the National Company Law Tribunal under the Insolvency and Bankruptcy Code, 2016. Part II of the Code consisting of Sections 4 to 77 deals with the Insolvency Resolution and Liquidation for Corporate Persons.

The Code has become a potential generator for mergers and acquisitions as it opens up stressed asset acquisition opportunities and borrowings/internal accruals may be used as rehabilitation financing by the investors/ resolution applicants to effect the acquisition.

FUNDING THROUGH LEVERAGED BUYOUTS (LBOs)

Leverage is an investment strategy of using borrowed money, specifically, the use of various financial instruments or borrowed capital to increase the potential return of an investment. When one refers to something (a company, a property or an investment) as "highly leveraged," it means that item has more debt than equity.

A Leveraged Buyout (LBO) is the acquisition of a company in which the buyer puts up only a small amount of money and borrows the rest. The buyer can achieve this desirable result because the targeted acquisition is profitable and throws off ample cash used to repay the debt. The expectation with leveraged buyouts is that the return generated on the acquisition will more than outweigh the interest paid on the debt, hence making it a very good way to experience high returns whilst only risking a small amount of capital.

In 2000, a landmark deal was witnessed in the Indian corporate history, when Tata Tea acquired the UK brand Tetley for 271 million pounds. This deal was the largest cross border acquisition by any India Company. Apart from the size of the deal, what made it particularly special was the fact that it was the first ever leveraged buy-out by any Indian company.

Structure of the deal:

Tata Tea created a Special Purpose Vehicle (SPV)-christened Tata Tea (Great Britain) to acquire all the properties of Tetley. The SPV was capitalised at 70 mn pounds, of which Tata tea contributed 60 mn pounds; this included 45 mn pounds raised through a GDR issue. The US subsidiary of the company, Tata Tea Inc. had contributed the balance 10 mn pounds.

Tata Motors Acquisition of Jaguar Land Rover

Tata Motors acquired the UK based Jaguar and Land Rover for USD 2.3 billion from the US based Ford Motors. The deal was a part of the long term strategy of Tata Motors to increase its international presence and consolidating its position in terms of product diversification and Research and Development capabilities. The economic slowdown in Europe and American markets posed a risk to the future of the company amidst tough market conditions along with the funding risks and the currency risks associated with the deal. Tata Motors raised USD 3 billion from banks that included JP Morgan, Citibank and State Bank of India. This deal used Leveraged Buy-Out (LBO).

The purpose of a LBO is to allow an acquirer to make large acquisitions without having to commit a significant amount of capital. A typically transaction involves the setup of an acquisition vehicle that is jointly funded by a financial investor and management of the target company. Often the assets of the target company are used as collateral for the debt. Debt capital comprises of a combination of highly structured debt instruments including prepayable bank facilities and/or publicly or private placed bonds commonly referred to as high-yield debt.

This deal has provided the Leverage to Tata Group in many ways to repay the amount for the deal:

- Rs. 1.92 Billion underwriting agreement with J M financial Consultants.
- Rs.1.75 Billion was raised through a deposits scheme from the Public.
- Additional subscriptions by promoter companies such as TATA sons, TATA Capital and Investment.
- TATA was leveraged by British Government also.

Nirma – Lafarge Holcim Deal: Gujarat-based soda ash, soap and detergent manufacturing company Nirma Ltd signed an agreement to acquire Lafarge India Pvt. Ltd's assets for ₹ 9,400 crore ($1.4 billion). Of the ₹ 9,400 crore that Nirma needs to pay LafargeHolcim, nearly ₹ 7,500 crore was raised through debt. In other words, nearly 80% of the total deal value was paid through borrowed funds, making it a textbook LBO.

What Companies Make Good LBO Targets?

Considering that the buyer will put a large amount of debt on the company, it is critical that the company be stable and able to pay off its future debts otherwise it will likely default and go into bankruptcy. With that in mind, below are some types of companies that make good targets:

- Stable, strong cash flow business.
- Company with low debt levels.
- Non-cyclical businesses.
- Companies with large economic moats.
- Companies with good existing management teams.
- Companies with a large asset base that can be used for collateral.
- Distressed companies in good industries.

MINORITY AND 'MINORITY INTEREST' UNDER COMPANIES ACT, 2013

The term "minority" and "minority interest" are not clearly defined in the Companies Act, 2013 or rules made thereunder. However, in various provisions of the Act, members are given various collective statutory rights which can be exercised even if they are not in majority (i.e. holding more than 50% of the numbers/shares/voting rights). In another way, minority can be identified as those members who are not in the control or management of the affairs of the company.

The following are some of the provisions where minority interest is recognised in the Act:

1. At present as per Section 244 of the Companies Act, 2013, in case of a company having share capital, not less than 100 members or not less than 1/10th of total number of members, whichever is less or any member or members holding not less than 1/10th of issued share capital have the right to apply to NCLT in case of oppression and mismanagement. In case of companies not having share capital, not less than 1/5th of total number of members has the right to apply.

2. To reflect the interest of the "Minority", 10% criteria in case of companies having share capital and 20% criteria in the case of other companies is provided for in the Act. To help the Minority shareholders, proviso to Section 244(1) of the Companies Act, 2013 empowers NCLT to allow

application by shareholders who are not otherwise eligible (i.e. holding less than 10%-20% as aforesaid). This really opens up possibility of minority actions in deserving cases of oppression and mismanagement.

Oppression and Mismanagement

Although Companies Act, 2013 gives power to the voting decision made by the majority shareholders in general meetings but at the same time it also empowers the minority shareholders by protecting their interests and rights. Section 241 - 246 of the Act has laid down such provisions which will be discussed in detail in the following paras.

Oppression: Remedy against oppression is available in section 241(1)(a) of the Act. Oppression may be defined as conducting the company's affairs in a manner prejudicial to public interest or in a manner oppressive to any member or members or prejudicial to the interests of the company.

Mismanagement: Remedy against mismanagement is available in Section 241(1)(b) of the Act. Mismanagement may be defined as any change which takes place in the management or control of the Company, which will not be in the interests of members.

Few more points relevant in this context are:

1. If an application is made to the Tribunal, then it may waive all or any of the requirements specified in the aforementioned table for an eligible member.
2. Any share or shares held by two or more persons jointly, shall be counted only as one member.
3. Any one or more members may make the application on behalf of other members.

Powers of Tribunal

If an application is made under Section 241 of the Act to the Tribunal and it is of the opinion that the company's affairs have been or are being conducted in a manner prejudicial or oppressive to any member or members or prejudicial to public interest or in a manner prejudicial to the interests of the company and that winding-up the company would unfairly prejudice such member or members, then the Tribunal may pass relevant order to resolve the complaint. Orders may provide for the following:

- regulation of conduct of affairs of the company in future
- purchase of shares or interests of any members of the company by other members thereof or by the company
- in the case of a purchase of its shares by the company as aforesaid, the consequent reduction of its share capital
- restrictions on the transfer or allotment of the shares of the company
- the termination, setting aside or modification, of any agreement, howsoever arrived at, between the company and the managing director, any other director or manager, upon such terms and conditions as may, in the opinion of the Tribunal, be just and equitable in the circumstances of the case
- the termination, setting aside or modification of any agreement between the company and any person other than those referred to in clause (e)

In ***S.P. Jain v. Kalinga Tubes Ltd (AIR 1965 SC 1535).***, the Supreme Court expounded the principles determining the concept of oppression, i.e. that the conduct must be burdensome, harsh and wrongful, involving lack of probity or fair dealing to a member in the matter of his proprietary rights as a shareholder. Further, a mere lack of confidence between the majority and minority shareholders would not be enough, unless the lack of confidence springs from oppression of a minority by a majority in the management of the company's affairs.

In ***Needle Industries India Ltd. v. Needle Industries Newey (India) Holdings Ltd. (1981 3 SCC 333)***, the Supreme Court held that an illegal act will not in and of itself be treated as oppressive, unless it is accompanied by a mala fide intention or if otherwise such an act was harsh, burdensome and wrongful. However, where there has been a series of illegal acts directed against a person, it would be justifiable to conclude that they are a part of the same object of committing oppression.

In ***V.S. Krishnan v. Westfort Hi-Tech Hospital Ltd., (2008 3 SCC 363)***, the Supreme Court relied on the Needle Industries case,and ruled that the test to gauge whether an action is oppressive – is not whether it is illegal, but rather, whether the act of oppression entailed the absence of probity, good conduct, or an act that was mala fide, harsh burdensome and wrong or for a collateral purpose. Going further, it observed that although the ultimate objective of such an action may be in the interest of the company, the immediate purpose would result in an advantage for some shareholders vis-à-vis others.

In ***Tata Consultancy Services Ltd. v. Cyrus Investments (P) Ltd., (2021 SCC OnLine SC 272),*** Mr. Cyrus Mistry was removed from the position of Executive Chairman of Tata Sons Limited, and also removed from directorship in various companies of the Tata Group, by resolutions passed at various board and shareholder meetings. Considering the removal and the manner thereof as being oppressive to minority shareholders, viz. Cyrus Investments Pvt. Ltd. and Sterling Investment Corporation Pvt. Ltd. (shareholders of Tata Group of Companies and in which Mr. Mistry had a controlling stake), this minority group filed a complaint alleging prejudice, oppression and mismanagement before the NCLT. The NCLT ruled against the minority group. The NCLAT ruled in favour of the minority group and held that the removal of Mr. Mistry was oppressive/ prejudicial, and hence it ordered the reinstatement of Mr. Mistry as the Executive Chairman of Tata Sons and as the Director of the various companies. Tata Sons, challenged the NCLAT order before the Supreme Court, which finally held that the act of Mr. Mistry's removal as Executive Chairman of Tata Sons was not in fact, prejudicial and/ or oppressive to the interests of the minority group. Further, it noted that in the factual matrix of the case, the requisite standard to justify the winding up of the company was not met, Further and specifically in the context that the majority shareholding of Tata Sons (Private) Limited was held by philanthropic Trusts and not individuals or corporate entities, the NCLAT's decision that it was just and equitable to wind up Tata Sons was flawed as it would only result in those charitable Trusts starving to death.

CLASS ACTION

On June 1, 2016, the Ministry of Corporate Affairs, notified section 245 of the Companies Act, 2013, enlisting the provisions of class action suits in India. A class action suit is one where the shareholders or depositors of a company collectively institute a suit against the company in Tribunal.

The requirement for this provision was felt in 2009 when the Satyam scam occurred. The shareholders in Satyam Computers Services Limited ("SCSL") were unsuccessful in claiming damages (worth millions) due to the absence of the provision for filing a class action suit under the Companies Act, 1956. While the Indian shareholders suffered a loss, the American investors were able to claim their part of damages in the US courts through a class action suit against SCSL. It was felt class action suits will safeguard the interests of shareholders, whenever the company or its directors participate in any fraudulent, unlawful act, or commit an act which is against the interest of the shareholders. In fact, such suits would be the most effective remedy for raising the voice of the company's shareholders.

The legal framework for class action suits is covered in section 245 of Companies Act, 2013 as well as National Company Law Tribunal Rules, 2016.

After going through section 241 and 245 of the Act, we can question as to why a separate provision was required for class action, although both the provisions look similar.

Section 245 is much wider in scope and a major difference is the option of getting monetary compensation or damages owing to the fraudulent actions of a company.

The provisions of class action come under the head of oppression and mismanagement but there are some differences between the remedies sought under class action under Section 245 and under the general provisions of oppression and mismanagement under Section 242. While under Section 242 the NCLT can order acquisition of the company's shares, restrict transferability or allotment of shares, removal of managing director and other directors of the company, in class action, the orders will mainly be restraining orders. An added advantage of the provisions on class action suit is that they cover depositors also.

RIGHTS OF MINORITY SHAREHOLDERS DURING MERGERS/AMALGAMATIONS/ TAKEOVERS

Power to compromise or make arrangements with creditors and members –

1. Approval of Tribunal is required in case of corporate restructuring (which, *inter-alia*, includes, mergers/ amalgamations, etc.) by a company. Where a compromise or arrangement is proposed—

   (a) between a company and its creditors or any class of them; or

   (b) between a company and its members or any class of them,

   the Tribunal may, on the application of the company or of any creditor or member of the company, or in the case of a company which is being wound up, of the liquidator, appointed under this Act or under the Insolvency and Bankruptcy Code, 2016, as the case may be, order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal directs.

   The Scheme is also required to be approved by shareholders, before it is filed with the NCLT. The scheme is circulated to all shareholders along with statutory notice (Form No. CAA-2) of the Tribunal convened meetings and the explanatory statement under section 230(3) of the Act read with Rule 6 of Companies (Compromise, Arrangements and Amalgamations) Rules, 2016 for approving the scheme by shareholders.

2. As per proviso to Section 230(4) of the Act, it is provided that any objection to the compromise or arrangement shall be made by persons holding 10% or more of the shareholding or having 5% or more of the total outstanding debt as per latest audited financial statement. Thus, shareholders holding less than 10% or more of the shareholding are not entitled to object to the scheme as matter of statutory right.

   There are other built in safeguards in the matter of approval of the scheme of compromise and arrangements. The notice convening the meetings and also the notice of hearing of the petition (in Form CAA- 2) is required to be published in the newspaper as per the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016. The notice is also required to be given to various statutory authorities, sectoral regulators, etc.

   Though there may not be any express protection to any dissenting minority shareholders to file their objections as a matter of right on this issue, the Tribunal, while approving the scheme, may follow judicious approach more particularly in view of the publication of the public notices about the proposed scheme in the newspapers. Any interested person (including a minority shareholder) may appear before the NCLT. There have been, however, occasions when shareholders holding miniscule shareholdings, have made frivolous objections against the scheme, just with the objective of stalling or deferring the implementation of the scheme. The courts have, on a number of occasions, overruled their objections. In view of this, proviso to Section 230(4) of the Act has put some limit for the objectors.

3. In case of Takeovers, as per SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, SEBI has powers to appoint investigating officer to undertake investigation, in case complaints are received from the investors, intermediaries or any other person on any matter having a bearing on the allegations of substantial acquisition of shares and takeovers. SEBI may also carry out such investigation *suo moto* upon its own knowledge or information about any breach of these regulations. Under section 235 of the Act, a transferee company, which has acquired 90% shares of a transferor company through a scheme or contract, is entitled to acquire shares of remaining 10% shareholders.

Dissenting shareholders have been provided with an opportunity to approach Tribunal. For this purpose, there is no threshold applicable i.e. even a single dissentient shareholding holding one share may also approach Tribunal. In such case, further acquisition of shares by the transferee company will be subject to the outcome of the decision of the NCLT.

Section 230(12) provides that an aggrieved party may make an application to the Tribunal in the event of any grievances with respect to the takeover offer of companies other than listed companies in such manner as may be prescribed and the Tribunal may, on application, pass such order as it may deem fit.

Purchase of Minority Shareholding

Section 236 of the Companies Act, 2013 states that:

(1) In the event of an acquirer, or a person acting in concert with such acquirer, becoming registered holder of ninety per cent. or more of the issued equity share capital of a company, or in the event of any person or group of persons becoming ninety per cent. majority or holding ninety per cent. of the issued equity share capital of a company, by virtue of an amalgamation, share exchange, conversion of securities or for any other reason, such acquirer, person or group of persons, as the case may be, shall notify the company of their intention to buy the remaining equity shares.

(2) The acquirer, person or group of persons under sub-section (1) shall offer to the minority shareholders of the company for buying the equity shares held by such shareholders at a price determined on the basis of valuation by a registered valuer in accordance with such rules as may be prescribed.

(3) Without prejudice to the provisions of sub-sections (1) and (2), the minority shareholders of the company may offer to the majority shareholders to purchase the minority equity shareholding of the company at the price determined in accordance with such rules as may be prescribed under sub-section (2).

(4) The majority shareholders shall deposit an amount equal to the value of shares to be acquired by them under sub-section (2) or sub-section (3), as the case may be, in a separate bank account to be operated by company whose shares are being transferred for at least one year for payment to the minority shareholders and such amount shall be disbursed to the entitled shareholders within sixty days:

Provided that such disbursement shall continue to be made to the entitled shareholders for a period of one year, who for any reason had not been made disbursement within the said period of sixty days or if the disbursement have been made within the aforesaid period of sixty days, fail to receive or claim payment arising out of such disbursement.

(5) In the event of a purchase under this section, company whose shares are being transferred shall act as a transfer agent for receiving and paying the price to the minority shareholders and for taking delivery of the shares and delivering such shares to the majority, as the case may be.

(6) In the absence of a physical delivery of shares by the shareholders within the time specified by the company, the share certificates shall be deemed to be cancelled, and company whose shares are being transferred shall be authorised to issue shares in lieu of the cancelled shares and complete the transfer in accordance with law and make payment of the price out of deposit made under sub-section (4) by the majority in advance to the minority by despatch of such payment.

(7) In the event of a majority shareholder or shareholders requiring a full purchase and making payment of price by deposit with the company for any shareholder or shareholders who have died or ceased to exist, or whose heirs, successors, administrators or assignees have not been brought on record by transmission, the right of such shareholders to make an offer for sale of minority equity shareholding shall continue and be available for a period of three years from the date of majority acquisition or majority shareholding.

(8) Where the shares of minority shareholders have been acquired in pursuance of this section and as on or prior to the date of transfer following such acquisition, the shareholders holding seventy-five per cent. or more minority equity shareholding negotiate or reach an understanding on a higher price for any transfer, proposed or agreed upon, of the shares held by them without disclosing the fact or likelihood of transfer taking place on the basis of such negotiation, understanding or agreement, the majority shareholders shall share the additional compensation so received by them with such minority shareholders on a pro rata basis.

Explanation.—For the purposes of this section, the expressions "acquirer" and "person acting in concert" shall have the meanings respectively assigned to them in clause (b) and clause (e) of sub-regulation (1) of regulation 2 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997.

(9) When a shareholder or the majority equity shareholder fails to acquire full purchase of the shares of the minority equity shareholders, then, the provisions of this section shall continue to apply to the residual minority equity shareholders, even though,—

(a) the shares of the company of the residual minority equity shareholder had been delisted; and

(b) the period of one year or the period specified in the regulations made by the Securities and Exchange Board under the Securities and Exchange Board of India Act, 1992, had elapsed.

Purchase of minority shareholding held in demat form

Rule 26A of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 provides that:

(1) The company shall within two weeks from the date of receipt of the amount equal to the price of shares to be acquired by the acquirer, under section 236 of the Act, verify the details of the minority shareholders holding shares in dematerialised form.

(2) After verification under sub-rule (1), the company shall send notice to such minority shareholders by registered post or by speed post or by courier or by email about a cut-off abcaus.in date, which shall not be earlier than one month after the date of sending of the notice, on which the shares of minority shareholders shall be debited from their account and credited to the designated DEMAT account of the company, unless the shares are credited in the account of the acquirer, as specified in such notice, before the cut-off date.

(3) A copy of the notice served to the minority shareholders under sub-rule (2), shall also be published simultaneously in two widely circulated newspapers (one in English and one in vernacular language) in the district in which the registered office of the company is situated and also be uploaded on the website of the company, if any.

(4) The company shall inform the depository immediately after publication of the notice under sub-rule (3) regarding the cut-off date and submit the following declarations stating that:

(a) the corporate action is being effected in pursuance of the provisions of section 236 of the Act;

It may be noted that Corporate Action means any action taken by the company relating to transfer of shares and all the benefits accruing on such shares namely, bonus shares, split, consolidation, fraction shares and right issue to the acquirer.

(b) the minority shareholders whose shares are held in dematerialised form have been informed about the corporate action a copy of the notice served to such shareholders and published in the newspapers to be attached;

(c) the minority shareholders shall be paid by the company immediately after completion of corporate action;

(d) any dispute or complaints arising out of such corporate action shall be the sole responsibility of the company.

(5) For the purposes of effecting transfer of shares through corporate action, the Board shall authorise the Company Secretary, or in his absence any other person, to inform the depository under sub-rule (4), and to submit the documents as may be required under the said sub-rule.

(6) Upon receipt of information under sub-rule (4), the depository shall make the transfer of shares of the minority shareholders, who have not, on their own, transferred their shares in favour of the acquirer, into the designated DEMAT account of the company on the cut-off date and intimate the company.

(7) After receiving the intimation of successful transfer of shares from the depository under sub-rule (6), the company shall immediately disburse the price of the shares so transferred, to each of the minority shareholders after deducting the applicable stamp duty, which shall be paid by the company, on behalf of the minority shareholders, in accordance with the provisions of the Indian Stamp Act, 1899 (2 of 1899).

(8) Upon successful payment to the minority shareholders under sub-rule (7), the company shall inform the depository to transfer the shares of such shareholders, kept in the designated DEMAT account of the company, to the DEMAT account of the acquirer.

Explanation. -The company shall continue to disburse payment to the entitled shareholders, where disbursement could not be made within the specified time, and transfer the shares to the DEMAT account of acquirer after such disbursement.

(9) In case, where there is a specific order of Court or Tribunal, or statutory authority restraining any transfer of such shares and payment of dividend, or where such shares are pledged or hypothecated under the provisions of the Depositories Act, 1996 (22 of 1996), the depository shall not transfer the shares of the minority shareholders to the designated DEMAT account of the company under sub-rule (6).

Explanation. -For the purposes of this rule, if "cut-off date" falls on a holiday, the next working day shall be deemed to be the "cut-off date".

Determination of price for purchase of minority shareholding

Rule 27 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 provides that for the purposes of sub-section (2) of section 236 of the Act, the registered valuer shall determine the price (hereinafter called as offer price) to be paid by acquirer, person or group of persons referred to in sub-section (1) of section 236 of the Act for purchase of equity shares of the minority shareholders of the company, in accordance with the following rules:

(1) In case of a listed company;

(i) The offer price shall be determined in the manner as may be specified by the Securities and Exchange Board of India under the relevant regulations framed by it, as may be applicable; and

(ii) The registered valuer shall also provide a valuation report on the basis of valuation addressed to the board of directors of the company giving justification for such valuation.

(2) In the case of an unlisted company and a private company,

(i) the offer price shall be determined after taking into account the following factors:-

(a) the highest price paid by the acquirer, person or group of persons for acquisition during last twelve months;

(b) the fair price of shares of the company to be determined by the registered valuer after taking into account valuation parameters including return on net worth, book value of shares, earning per share, price earning multiple vis-à-vis the industry average, and such other parameters as are customary for valuation of shares of such companies; and

(ii) the registered valuer shall also provide a valuation report on the basis of valuation addressed to the board of directors of the company giving justification for such valuation.

LEGAL PROVISIONS OF THE COMPANIES ACT, 2013 AND DECIDED CASE LAWS

Chapter XV, comprising of sections 230 to 240 read with the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016, deals with Compromises, Arrangements and Amalgamations. The relevant sections with brief details and relevant case laws are mentioned below:

Section 230: Power to compromise or make arrangements with creditors and members.

Section 230 provides powers to Tribunal to make order on the application of the company or any creditor or member or in case of company being wound-up, of liquidator for the proposed compromise or arrangement including debt restructuring, etc., between company, its creditors and members.

The word 'arrangement' interpreted under the various judicial pronouncements is as under:

'Arrangement', as occurring in section 390(b) of the 1956 Act [corresponding to Explanation to section 230(1) of the 2013 Act] is something by which parties agree to do a certain thing notwithstanding the fact there was no dispute between the parties. ***[Navjivan Mills Co. Ltd., In re [1972] 42 Comp. Cas. 265 (Guj.)]***

The word 'arrangement' as set out in section 390(b) of the 1956 Act is an inclusive definition and contemplates all arrangements and not only reorganisation of the share capital. This is all the more clear, because the word used is 'includes'. ***[Investment Corpn. of India Ltd., In re [1987] 61 Comp. Cas. 92 (Bom.)]***

Any scheme, other than a scheme by way of compromise or reconstruction, which affects the rights of the creditors and the members of the company or any class of them, would fall within the term, 'arrangement'. ***[Bank of India Ltd. v. Ahmedabad Mfg. & Calico Printing Co. Ltd. [1972] 42 Comp. Cas. 211 (Bom.)]***

The word 'arrangement' in section 391 of the 1956 Act is of wide import. By section 390 of the 1956 Act, 'arrangement' includes reorganisation of the share capital of the company by the consolidation of shares of different classes or by the division of shares into shares of different classes or both these methods. ***[Hindusthan Commercial Bank Ltd. v. Hindusthan General Electrical Corpn. [1960] 30 Comp. Cas. 367 (Cal.)]***

The word 'class' interpreted by the Gujarat High Court in a case is as under:

Those who are offered substantially different compromises each will form a different class. Even if there are different groups within a class, the interests of which are different from the rest of the class or who are to be treated differently in the scheme, such groups must be treated as separate classes for the purpose of the scheme. The group styled as a class should ordinarily be homogeneous and must have commonality of interest and the compromise offered to them must be identical. (See section 391(1) of the 1956 Act) ***[State Bank of India v. Engg. Majdoor Sangh [2000] 27 SCL 103 (Guj.)]***

Section 231: Power of Tribunal to enforce compromise or arrangement

The section provides powers to Tribunal to enforce compromise or arrangement with creditors and members as ordered under section 230. Section also provides that, if the Tribunal is satisfied that such compromise or arrangement cannot be implemented satisfactorily with or without modifications, and the company is unable to pay its debts as per the scheme, it may make an order for winding-up of the company.

Interpretation of the words 'At time of making such order or at any time thereafter' in Section 231(1)(b) of the 2013 Act:

Clause (b) of sub-section (1) of section 392 of the 1956 Act [corresponding to section 231(1)(b) of the 2013 Act] makes it abundantly clear that the powers conferred by section 392 may be exercised 'at the time of making such order or at any time thereafter'. The provisions, therefore, envisage exercise of power at the very point of time of making the order, meaning thereby, 'before' the order is passed. The expression which follows, namely, 'at any time thereafter' lends further support to this construction, namely, that before the order is signed the power can be exercised under the earlier part of the provision and after order is signed, the power can be exercised under the second part of the provision. The expression 'or at any time thereafter' leaves no room for doubt that the preceding part contemplates exercise of power at a point of time prior to the making of the order. ***[Bhavnagar Vegetable Products Ltd., In re [1984] 55 Comp. Cas. 107 (Guj.)]***

Interpretation of the word 'Modification' used in Section 231(1)(b) of the 2013 Act: In the context of section 392(1)(b) of the 1956 Act [corresponding to section 231(1)(b) of the 2013 Act], 'modification' would mean addition to the scheme of compromise or arrangement or omission therefrom solely for the purpose of making it workable. ***[S.K. Gupta v. K.P. Jain [1979] 49 Comp. Cas. 342 (SC)]***

Section 232: Merger and amalgamation of companies

This section corresponds to section 394 of the Companies Act, 1956 and came into force with effect from 15th December, 2016.

This section provides powers to the Tribunal to order for holding meeting of the creditors or the members and to make orders on the proposed reconstruction, merger or amalgamation of companies. The section provides for manner and procedure in which the meeting so ordered by the Tribunal to be held.

For meaning of the expression "reconstruction/amalgamation", used in the section, the Calcutta High Court opined that there is no particular meaning in the word 'reconstruction' or in the word 'amalgamation'. It has to be found out from the scheme read as a whole whether it is a case of reconstruction or whether it is a case of amalgamation. See section 394 of the 1956 Act. ***[Inland Steam Navigation Workers' Union v. Rivers Steam Navigation Co. Ltd. [1968] 38 Comp. Cas. 99 (Cal.)]***

In the case of ***Sesa Industries Ltd. v. Krishna H. Baja, Civil Appeal Nos. 1430-1431 of 2011, February 7, 2011***, the Supreme Court opined that the Court before whom scheme of amalgamation is placed for sanction is not expected to put its seal of approval on scheme merely because majority of shareholders have voted in favour of scheme. Since the scheme which gets sanctioned by Court would be binding on dissenting minority shareholders or creditors, Court is obliged to examine scheme in its proper perspective together with its various manifestations and ramifications with a view to find out whether scheme is fair, just and reasonable to concerned members and is not contrary to any law or public policy.

In the case of ***Lotus Nikko Hotels Travel (P.) Ltd. v. Ashok Chopra & Co., EFA (OS) NO. 2 OF 2011, February 16, 2017***, High Court of Delhi opined that, where scheme of arrangement providing for demerger stood confirmed and was made binding, it bound creditor whether or not they might have specifically consented to such scheme.

In the case of ***Wiki Kids Ltd. v. Avantel Ltd. (21.12.2017)***, a non-listed company Wiki Kids Limited (Transferor Company), wished to amalgamate with Avantel Limited, a listed company (Transferee Company). The entities (collectively referred to as Appellants) had proposed a scheme of amalgamation and approached the Andhra Pradesh High Court. Pursuant to the directions of the High Court, the Scheme was approved by the shareholders of the Transferee Company. In the meantime, in view of constitution of NCLT vide a notification dated December 7, 2016, the case was transferred to the NCLT. The Appellants, accordingly, filed a second motion before the Hyderabad Bench of the NCLT.

The NCLT observed that the Appellants had common promoters such that the promoters of the Transferee Company held 99.90% of the shareholding of the Transferor Company. Thus, the NCLT, in light of its analysis, held that the entire scheme was designed in a manner to extend financial benefit of INR 12 crores (as per the exchange ratio the eligible number of shares to be issued by the Transferee Company to the shareholders of the Transferor Company was worked out to approximately 4 lakh shares, the market value of which is almost 12.4 Crores) only to the common promoters even though the Transferor Company had no business and little net worth/value. In view of such observations, the NCLT held the scheme to be against the public interest and refused to approve the same. The NCLAT upheld the order of the NCLT rejecting a scheme of amalgamation, as it resulted in undue advantage to the promoters of the amalgamating company.

Section 233: Merger or amalgamation of certain companies

This section came into force from 15th December, 2016. This section seeks to provide for merger or amalgamation between two small companies or between a holding company and its wholly owned subsidiary or prescribed class or class of companies by giving a notice of the proposed scheme inviting objections or suggestions by both the transferor and the transferee company from Registrar, Official Liquidator or persons affected by the scheme.

The powers of the Central Government are delegated to Regional Directors at Mumbai, Kolkata, Chennai, New Delhi, Ahmedabad, Hyderabad and Shillong.

Section 234: Merger or amalgamation of company with foreign company

This section came in force with effect from 13th April, 2017 and has no corresponding section with the Companies Act, 1956.

This is a new section and provides the mode of merger or amalgamation between companies registered under the Companies Act, 2013 and companies incorporated in the jurisdictions of such companies as may be notified from time to time by the Central Government. The Central Government may, in consultation with Reserve Bank of India make rules for the purpose of merger or amalgamation provided under this section.

Section 235: Power to acquire shares of shareholders dissenting from scheme or contract approved by majority

(1) Where a scheme or contract involving the transfer of shares or any class of shares in a company (the transferor company) to another company (the transferee company) has, within four months after making of an offer in that behalf by the transferee company, been approved by the holders of not less than nine-tenths in value of the shares whose transfer is involved, other than shares already held at the date of the offer by, or by a nominee of the transferee company or its subsidiary companies, the transferee company may, at any time within two months after the expiry of the said four months, give notice in the prescribed manner to any dissenting shareholder that it desires to acquire his shares.

The transferee company shall send a notice to the dissenting shareholder(s) of the transferor company, in **Form No.CAA.14** at the last intimated address of such shareholder for acquiring the shares of such dissenting shareholders.

(2) Where a notice under sub-section (1) is given, the transferee company shall, unless on an application made by the dissenting shareholder to the Tribunal, within one month from the date on which the notice was given and the Tribunal thinks fit to order otherwise, be entitled to and bound to acquire those shares on the terms on which, under the scheme or contract, the shares of the approving shareholders are to be transferred to the transferee company.

(3) Where a notice has been given by the transferee company under sub-section (1) and the Tribunal has not, on an application made by the dissenting shareholder, made an order to the contrary, the transferee company shall, on the expiry of one month from the date on which the notice has been given, or, if an application to the Tribunal by the dissenting shareholder is then pending, after that application has been disposed of, send a copy of the notice to the transferor company together with an instrument of transfer, to be executed on behalf of the shareholder by any person appointed by the transferor company and on its own behalf by the transferee company, and pay or transfer to the transferor company the amount or other consideration representing the price payable by the transferee company for the shares which, by virtue of this section, that company is entitled to acquire, and the transferor company shall—

(a) thereupon register the transferee company as the holder of those shares; and

(b) within one month of the date of such registration, inform the dissenting shareholders of the fact of such registration and of the receipt of the amount or other consideration representing the price payable to them by the transferee company.

(4) Any sum received by the transferor company under this section shall be paid into a separate bank account, and any such sum and any other consideration so received shall be held by that company in trust for the several persons entitled to the shares in respect of which the said sum or other

consideration were respectively received and shall be disbursed to the entitled shareholders within sixty days.

(5) In relation to an offer made by a transferee company to shareholders of a transferor company before the commencement of this Act, this section shall have effect with the following modifications, namely: —

(a) in sub-section (1), for the words "the shares whose transfer is involved other than shares already held at the date of the offer by, or by a nominee of, the transferee company or its subsidiaries,", the words "the shares affected" shall be substituted; and

(b) in sub-section (3), the words "together with an instrument of transfer, to be executed on behalf of the shareholder by any person appointed by the transferee company and on its own behalf by the transferor company" shall be omitted.

Explanation.—For the purposes of this section, "dissenting shareholder" includes a shareholder who has not assented to the scheme or contract and any shareholder who has failed or refused to transfer his shares to the transferee company in accordance with the scheme or contract.The words 'Four months' used in section 235(1) have been interpreted by the Chandigarh High Court. According to it 'Four months' is the maximum period within which the offer is to be accepted; section 395(1) of the 1956 Act [corresponding to section 235(1) of the 2013 Act] does not require that the offer must be kept open for at least four months. *Western Mfg. (Reading) Ltd., In re [1957] 27 Comp. Cas. 144 (Ch.D.)*

The words 'Four months' used in section 235(1) have been interpreted by the Chandigarh High Court. According to it 'Four months' is the maximum period within which the offer is to be accepted; section 395(1) of the 1956 Act [corresponding to section 235(1) of the 2013 Act] does not require that the offer must be kept open for at least four months. ***[Western Mfg. (Reading) Ltd., In re [1957] 27 Comp. Cas. 144 (Ch.D.)]***

In the case of ***Radhey Shyam Agarwal v. Bank of Rajasthan Ltd. Company Appeal No. 1 of 2012, September 20, 2013***, the High Court of Rajasthan observed that the prayers which has been made before the Company Law Board has been incorporated in the appeal and as regards prayer of the petitioner appellant for investigating the affairs of the respondent company i.e. Bank of Rajasthan, after the Bank of Rajasthan stood finally merged under the Scheme of Amalgamation and approved by the RBI under sub-section (4) of sec.44A of the Banking Regulation Act, 1949 and finally confirmed by the Apex Court on writ petition preferred by the petitioner, the question of investigating the affairs of the transferor, Bank of Rajasthan does not survive any further and the Company Law Board in its impugned order dt.30.9.2011 has taken note of the approval being granted by the RBI and the order of the Apex Court dated 13-9-2011 rejecting the writ petition preferred by the petitioner assailing the merger on multifarious grounds. The CLB has further noticed that apart from what is being raised in the company petition, the petitioner has also filed civil suit pending before the District Court Bhilwara and when he failed to succeed in getting interim injunction and also from the High Court on appeal being preferred his company petition on the facts brought on record has rendered infructuous. [Para 6]

After the primary grievance of the appellant being finally crystallized, investigating the affairs of transferor Bank of Rajasthan does not survive any further and the Court is also of the view that the Company Law Board has not committed any error in disposing of the company petition preferred by the appellant vide its order dated 13-9- 2011 as having been rendered infructuous and apart from it there is no question of law which emerges from the order of the Company Law Board which may be open for the Court to examine under section 10F of the 1956 Act (Corresponding to section 465 of the 2013 Act). [Para 7]

Section 236: Purchase of minority shareholding

This section came into force with effect from 15th December, 2016. This section corresponds to section 395 of the Companies Act, 1956.

This section provides the procedure and manner in which the registered holder of at least 90 per cent shares of a company shall notify the company of their intention to buy the remaining equity shares of minority shareholders, by virtue of an amalgamation, share exchange, conversion of securities, etc. This section provides the procedure to be followed for acquiring shares held by minority shareholders.

Section 237: Power of Central Government to provide for amalgamation of companies in public interest

This section corresponds to section 396 of the Companies Act, 1956 and came into force from 15th December, 2016.

This section provides power to the Central Government to provide for amalgamation of two or more companies in public interest by passing an order to be notified in the Official Gazette.

In the case of, ***Moons Technologies Ltd. v. Union of India***, the High Court of Bombay opined that final amalgamation order of NSEL with its holding company FTIL passed by Central Government under section 396 was not in violation of principles of natural justice and fair play and was a balanced as well as proportionate decision of Central Government.

Section 238: Registration of offer of schemes involving transfer of shares

This section came into force with effect from 15th December, 2016. The Prescribed fee for Appeal is Rs.2,000 under the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

This section provides mode of registration of offer of schemes or contract involving the transfer of shares. Every circular containing such offer and recommendation and containing a statement shall be accompanied by requisite information and must be registered with the ROC before issue.

Section 239: Preservation of books and papers of amalgamated companies.

Corresponds to section 396A of the Companies Act, 1956 and came into force with effect from 15th December, 2016.

This section provides that the books and papers of a company which has been amalgamated with, or whose shares have been acquired by, another company shall not be disposed of without the prior permission of the Central Government and before granting such permission, that Government may appoint a person to examine the books and papers or any of them for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion or formation, or the management of the affairs, of the transferor company or its amalgamation or the acquisition of its shares.

Section 240: Liability of officers in respect of offences committed prior to merger, amalgamation, etc.

This section came into force with effect from 15th December, 2016. No corresponding section to Companies Act, 1956.

This section provide that notwithstanding anything in any other law for the time being in force, the liability in respect of offences committed under this Act by the officers in default, of the transferor company prior to its merger, amalgamation or acquisition shall continue after such merger, amalgamation or acquisition.

PROTECTION OF MINORITY INTEREST

Section 232(3)(e) authorises the Tribunal to make provision for any person who dissent from the scheme. Thus, the Tribunal has to play a very vital role. It is not only a supervisory role but also a pragmatic role which requires the forming of an independent and informed judgment as regards the feasibility or proper working of the scheme and making suitable modifications in the scheme and issuing appropriate directions with that end in view ***[Mafatlal Industries Ltd. In re. (1995) 84 Comp. Cas. 230 (Guj.)].***

The Tribunal considers minority interest while approving the scheme of merger

As per existing provisions of the Act, approval of Tribunal is required in case of corporate restructuring (which, *inter-alia,* includes, mergers/amalgamations, etc.) by a company. The Scheme is also required to be approved by shareholders, before it is filed with the Tribunal. The scheme is circulated to all shareholders along with statutory notice of the court convened meeting and the explanatory statement under section 230(3) read with Rule 6 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 of the Act for approving the scheme by shareholders.

The notice of hearing of petition (in form CAA-2) is also required to be published in the newspaper. As per proviso to Section 230(4) of the Act, members holding 10% or more of the shareholding are entitled to file their objection before NCLT as a matter of right.

CASE STUDIES/JUDICIAL PRONOUNCEMENTS

There have been occasions when the minority shareholders have raised objections and have succeeded in preventing the implementation of a scheme of arrangement. A lone minority shareholder of ***Tainwala Polycontainers Ltd (TPL), Dinesh V Lakhani***, had apparently forced the company to call off its merger plans with *Tainwala Chemicals and Plastics (India) Ltd.* (TCPL). Lakhani had opposed the proposed merger on several grounds including allegations of willful suppression of *material facts* and *malafide* intention of promoters in floating separate companies (TPL and TCPL).

In case of Parke-Davis India Limited

In 2003, Parke-Davis India Limited and Pfizer Limited were considering implementation of a Scheme of Merger. The Minority shareholders of Parke-Davis India Ltd objected to the Scheme on the grounds that the approval from the requisite majority as prescribed under the Companies Act, 1956 had not been obtained. They filed an urgent petition before the division bench of the Bombay High Court. The division bench of the Bombay High Court by its order executed a stay order in March 2003 restraining the company from taking further steps in the implementation of the scheme of amalgamation, which was further extended till September 2003. The dissenting shareholders filed a Special Leave Petition with the Supreme Court. The turmoil came to an end when the Supreme Court dismissed the petition filed by the shareholders. Parke- Davis then proceeded to complete the implementation of the scheme of amalgamation with Pfizer.

In case of Tomco with HLL Merger

Similarly, in the case of the merger of Tomco with HLL, the minority shareholders put forward an argument that, as a result of the amalgamation, a large share of the market would be captured by HLL. However, the court turned down the argument and observed that there was nothing unlawful or illegal about it.

Fair and reasonable Scheme made in good faith

Any scheme which is fair and reasonable and made in good faith will be sanctioned if it could reasonably be supported by sensible people to be for the benefit to each class of the members or creditors concerned.

In ***Sussex Brick Co. Ltd., Re, (1960) 1 All ER 772 : (1960) 30 Com Cases 536 (Ch D)*** it was held, *inter alia*, that although it might be possible to find faults in a scheme that would not be sufficient ground to reject it. It was further held that in order to merit rejection, a scheme must be obviously unfair, patently unfair, unfair to the meanest intelligence.

It cannot be said that no scheme can be effective to bind a dissenting shareholder unless it complies with the basic requirements to the extent of 100 per cent. It is the consistent view of the Courts that no scheme can be said to be fool-proof and it is possible to find faults in a particular scheme but that by itself is not enough to warrant a dismissal of the petition for sanction of the scheme. If the court is satisfied that the scheme is fair and reasonable and in the interests of the general body of shareholders, the court will not make any provision in favour of the dissentients. For such a provision is not a *sine qua non* to sanctioning a fair and reasonable scheme, unless any special case is made out which warrants the exercise of court's discretion in favour of the dissentients. ***[Re, Kami Cement & Industrial Co. Ltd., (1937) 7 Com Cases 348, 364-65 (Bom)]***.

Minority Protection:

Majority Rule: In order to redress a wrongdoer to a company or to recover monies or damages alleged to be due to the company, the action should *prima facie* be brought by the company itself. ***[Foss v. Harbottle [1843] 2 Hare 461 (Ch.)]***

Exception to the Rule:

- Ultra vires acts: If the majority of shares are controlled by those against whom the relief is sought, the complaining shareholders may sue in their own names, but must show that the acts complained of are of a fraudulent character or beyond the powers of the company. There is no need to consult the views of the majority before instituting the suit, if from the allegations in the plaint it would appear that the act complained of was ultra vires. ***[Dhaneswari Cotton Mills Ltd. v. Nilkamal Chakravarthy [1937] 7 Comp. Cas. 417 (Cal).]***
- Fraud on Minority: Where a minority shareholder files a suit alleging fraud, suit should be tried even if majority has affirmed the transactions. ***[Cook v. Deeks [1916] 1AC 554 (PC).]***

  Wrongdoer in Control: Where majority is wrongdoer and pocket property of company, an individualshareholder has right to file a suit. ***[Menier v. Hooper's Telegraph Works [1874] 9 Ch. App. 350 (CA)]***
- A minority of shareholder in saddle of power cannot be allowed to pursue a policy of venturing into a litigation to which the majority of the shareholders were opposed. ***[Life Insurance Corp of India v. Escorts Ltd [1986] 59 Comp Cas.548 (SC).]***

Oppression:

- Mere lack of confidence between majority shareholders and minority shareholders would not be enough unless lack of confidence springs from oppression of a minority by a majority in management of company's affairs. ***[Shanti Prasad Jain v. Kainga Tubes Ltd. [1965] 35 Comp Cas. 351 (SC)]***
- A series of illegal acts can lead to conclusion that they are part of same oppressive transaction. ***[Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holdings Ltd. [1981] 51 Comp Cas. 743 (SC)]***
- When a complaint is made as regards violations of statutory or contractual right, shareholder may initiate a proceeding in a civil court but a proceeding under section 397 would be maintainable only when an extraordinary situation is bought to notice of court keeping in view wide and far-reaching power of court in relation to affairs of the company and in this situation, it is necessary that alleged illegality in conduct of majority shareholders is pleaded and proved with sufficient clarity and precision. ***[Sangramsingh P. Gaekwad v. Shantadevi P. Gaekwad [2005] 57 SCL 476 (SC).]***

FILING OF VARIOUS FORM IN THE PROCESS OF MERGER/AMALGAMATION

Various forms filed in the process of merger/amalgamation are appended below:

Form No.	Relevant Section	Rule*	Particulars
CAA 1	Section 230(2) (c)(*i*)	Rule 4	Creditor's Responsibility Statement
CAA 2	Section 230 (3)	Rule 6 and 7	Notice and Advertisement of notice of the meeting of creditors or members
CAA 3	Section 230(5)	Rule 8	Notice to Central Government and other Regulatory Authorities
CAA 4		Rule 13(2) and Rule 14	Report of result of meeting by Chairperson
CAA 5	Section 230	Rule 15(1)	Petition to sanction compromise or arrangement
CAA 6	Section 230(7)	Rule 17(3)	Order on petition

CAA 7	Section 232	Rule 20	Order under section 232
CAA 8	Section 232(7)	Rule 21	Statement to be filed with Registrar of Companies
CAA 9	Section 233(1)	Rule 25(1)	Notice of the scheme inviting objections or suggestions
CAA 10	Section 233(1) (c)	Rule 25(2)	Declaration of solvency
CAA 11	Section 233(2)	Rule 25(4)	Notice of approval of the scheme of merger
CAA 12	Section 233(5)	Rule 25(5)	Confirmation order of scheme of merger or amalgamation
CAA 13	Section 233(5)(6)	Rule 25(6)	Application by the Central Government to the Tribunal
CAA 14	Section 235(1)	Rule 26	Notice to dissenting shareholders
CAA 15	Section 238(1)	Rule 28	Information to be furnished along with circular in relation to any scheme or contract involving the transfer of sharesor any class of shares in the transferor company to the transferee company
CAA 16	Section 230	Rule 25A(4)	Declaration on compromise or arrangement or merger or demerger between an Indian company and a company or body corporated which has been incorporated in a country which shares Land border with India.

FAMILY HOLDINGS AND THEIR MANAGEMENT

For any family-owned business, transition is a crucial aspect that every founder or owner should keep in mind while pursuing the strategic business objectives of growth, diversification, expansion or sale. In the present context, passing the baton is clearly a priority for family business owners since the succession can make or break a family business and can have serious implications on the family as well. Thus, a structured approach in determining the transition plan and its communication to stakeholders is essential for managing the succession and survival of the family business and family from generation to generation.

Whether selling the business, keeping the business in the family or transitioning leadership to identified heirs or a non-family stakeholder, the issues are immense and certainly not simple. As a result, 95% of family businesses do not survive the third generation of ownership.

In terms of ownership and governance protocols for family members, typically, a trust or similar entity form becomes pivotal to the succession plan since it can provide a good balance between owners' desires, professional management, responsible business decision matrix and healthy family dynamics. The following are some of the key benefits of succession planning under a trust structure for continuing business legacy and smooth transition of the business from the hands of one generation to another:

Continuity planning: Consolidation of ownership and control under a trust allows the founder/owner and the family to set a clear vision and ensure commitment from the next generation of family members. This results in continued planning from one generation to another, resulting in harmony between goals, objectives, targets, etc., between generations, thereby reducing conflicting objectives/interests between family members.

Generational change: Family-owned firms can struggle to keep pace with global mega trends like demographic shifts and digital technology without the involvement of the new generation. At the same time, the current generation may not always have confidence in the ability of the new generation to take over the business, and may also have limitations relating to their ideas of change and growth. This calls for professionalization of the family firm by introducing external talent, leading to better governance and a more rigorous decision-making process in areas like finance, wealth management and personal expenses.

Conflict management: A trust would lay out specific protocols governing decision making and, in the case of any difference of opinion or deadlock, the process to manage the conflict. This ensures that the business does not suffer even during a phase where family members are not aligned.

Security of family/personal assets: A trust structure can also facilitate ring-fencing of family assets, protecting them from a creditor's claims as well as providing safeguards against claims from family members upon disability, divorce/ partition, etc.

Pooling and simplicity: A trust also serves as a means for pooling of assets and funds un der a common control. This can provide heirs the benefit of property without loss of control and helps to avoid the probate or court process in the event of death. It can also simplify asset holding for legal heirs in multiple jurisdictions.

A typical family-owned business, with more than one family constituent, should have a two-tier trust structure where consolidation of the family wealth and control can be achieved under a 'master trust'. The business should be tailored to incorporate an appropriate governance structure that ensures consensus of all family members and stakeholders and deals appropriately with conflict situations. This would also ensure that individual family constituents cannot unilaterally deal with common family assets and provide benefits of consolidation of control. The family and sub- trusts would typically be set up as discretionary trusts and would be customised to meet individual requirements of each family situation.

ANNEXURE I

SCHEDULE VI

(See sections 55 and 186)

INFRASTRUCTURE PROJECTS/INFRASTRUCTURAL FACILITIES

The term "infrastructural projects" or "infrastructural facilities" includes the following projects or activities:—

1. Transportation (including inter modal transportation), includes the following:—
   - (a) roads, national highways, State highways, major district roads, other district roads and village roads, including toll roads, bridges, highways, road transport providers and other road-related services;
   - (b) rail system, rail transport providers, metro rail, roads and other railway related services;
   - (c) ports (including minor ports and harbours), inland waterways, coastal shipping including shipping lines and other port related services;
   - (d) aviation, including airports, heliports, airlines and other airport related services;
   - (e) logistics services.
2. *Agriculture,* including the following, namely:—
   - (a) infrastructure related to storage facilities;
   - (b) construction relating to projects involving agro-processing and supply of inputs to agriculture;
   - (c) construction for preservation and storage of processed agro-products, perishable goods such as fruits, vegetables and flowers including testing facilities for quality.
3. *Water management,* including the following, namely:—
   - (a) water supply or distribution;
   - (b) irrigation;

(c) water treatment.

4. *Telecommunication,* including the following, namely:
   (a) basic or cellular, including radio paging;
   (b) domestic satellite service (i.e., satellite owned and operated by an Indian company for providing telecommunication service);
   (c) network of trunking, broadband network and internet services.
5. Industrial, commercial and social development and maintenance, including the following, namely: —
   (a) real estate development, including an industrial park or special economic zone;
   (b) tourism, including hotels, convention centres and entertainment centres;
   (c) public markets and buildings, trade fair, convention, exhibition, cultural centres, sports and recreation infrastructure, public gardens and parks;
   (d) construction of educational institutions and hospitals;
   (e) other urban development, including solid waste management systems, sanitation and sewerage systems.
6. *Power,* including the following: —
   (a) generation of power through thermal, hydro, nuclear, fossil fuel, wind and other renewable sources;
   (b) transmission, distribution or trading of power by laying a network of new transmission or distribution lines.
7. *Petroleum and natural gas,* including the following: —
   (a) exploration and production;
   (b) import terminals;
   (c) liquefaction and re-gasification;
   (d) storage terminals;
   (e) transmission networks and distribution networks including city gas infrastructure.
8. *Housing,* including the following: —
   (a) urban and rural housing including public/mass housing, slum rehabilitation, etc.;
   (b) other allied activities such as drainage, lighting, laying of roads, sanitation and facilities.
9. Other miscellaneous facilities/services, including the following: —
   (a) mining and related activities;
   (b) technology related infrastructure;
   (c) manufacturing of components and materials or any other utilities or facilities required by the infrastructure sector like energy saving devices and metering devices;
   (d) environment related infrastructure;
   (e) disaster management services;
   (f) preservation of monuments and icons;
   (g) emergency services (including medical, police, fire and rescue).
10. Such other facility service as may be prescribed.

LESSON ROUND-UP

- Mode of payment for mergers and acquisition to be selected from an optimum mix of available modes of payment of consideration.
- Selection of financial package depends on many considerations such as: to suit the financial structure of acquirer and acquiree, to provide a desirable gearing level, to be acceptable to vendors. Further it should prove economic to acquirer.
- Preferential offer is also a source of funding wherein shares are offered to a closed group of identified persons.
- Funding through preference share capital, unlike equity share capital, involves the payment of fixed preference dividend like interest on debentures or bonds or a fixed rate of dividend.
- Funding through shares with differential voting rights gives the companies an additional source of fund without interest cost and without an obligation to repay, as these are other form of equity capital.
- Funding can also be done through swaps and employees stock option scheme. The share capital that may be raised through the scheme of employees' stock option can only be a fraction of the entire issue.
- External commercial borrowings are permitted by the Government as a source of finance for Indian corporate for expansion of existing capacity as well as for fresh investment.
- The other modes of funding are through financial institutions and banks, rehabilitation finance and management and leveraged buy outs. All these have got its own merits and demerits.
- At present, in case of a company having share capital, not less than 100 members or not less than 1/10th of total number of members, whichever is less or any member or members holding not less than 1/10th of issued share capital have the right to apply to NCLT in case of oppression and mismanagement.
- Section 232(3)(e) authorises the Tribunal to make provision for those who dissent from the scheme.
- As per proviso to Section 230(4) of the Act, objection to compromise or arrangement shall be made only by person holding 10% or more of the shareholding or having 5% or more of the total outstanding debt as per the latest audited financial statement.

GLOSSARY

Acquirer: Acquirer means any person who, directly or indirectly, acquires or agrees to acquire whether by himself, or through, or with persons acting in concert with him, shares or voting rights in, or control over a target company.

Designated stock exchange: Recognised stock exchange in which securities of an issuer are listed or proposed to be listed and which is chosen by the issuer as a designated stock exchange for the purpose of a particular issueof specified securities.

Issuer: It means any person making an offer of specified securities.

Relevant Date: It means date of the board meeting in which the proposal for change in objects or variation in terms of a contract, referred to in the prospectus is approved, before seeking shareholders' approval.

Rights Issue: "rights issue" means an offer of specified securities by a listed issuer to the shareholders of the issuer as on the record date fixed for the said purpose.

Target Company: "target company" means a company and includes a body corporate or corporation established under a Central legislation, State legislation or Provincial legislation for the time being in force, whoseshares are listed on a stock exchange.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).

1. "Financing of mergers and acquisitions is a crucial exercise requiring utmost care." Elaborate.
2. Write short note on the various sources of funding in the case of merger/takeovers.
3. Discuss and compare the nature and procedural requirements of preferential offer and private placement and why the terms are used interchangeably.
4. Funding through Leveraged Buyouts is an innovative method of financing. Elucidate.
5. Describe remedies available to shareholders and depositors under section 241-244 and 245 of Companies Act, 2013 and why there was a need for a separate provision of class action?

LIST OF FURTHER READINGS

- Guide To Takeovers and Mergers – 4th Edition by PH Arvind Pandian and N R Sridharan
- Creating value from Mergers and Acquisitions by SudiSudarsanam, Prentice Hall
- Mergers and Acquisitions: Strategy, Value and Integration by G H Ray, PHI
- Master Guide to Mergers and Acquisitions in India - Tax & regulatory - Ernst & Young

Process of M&A Transactions

Lesson 4

KEY CONCEPTS

■ Due Diligence ■ Registered Valuer ■ Differential Pricing ■ Valuation ■ Regulatory Framework for Merger/Amalgamation

Learning Objectives

To understand:

- Process of Merger & Acquisition
- Prerequisites of Merger & Acquisition
- Due Diligence
- Type of Due Diligence
- Due Diligence Check-List
- Factors Influencing valuation
- Regulatory Framework for Merger/Amalgamation

Lesson Outline

- Approvals in a Scheme of Merger & Amalgamation
- Steps involved in Merger
- Due Diligence
- Types of Due Diligence
- Practical Guide to the Due Diligence
- Factors Influencing Valuation
- Valuation Approach
- Integration of Business & Operations
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

- Companies Act, 2013
- The Companies (Compromises, Arrangements and Amalgamations) Rules, 2016
- The National Company Law Tribunal Rules, 2016

MERGER AND ACQUISITION

Process of Merger & Acquisition involves corporate control, strategy, corporate finance and management. It involves consolidation of companies i.e. business combination, division and demerger of two or more companies. The merger and amalgamation requires various regulatory approvals and procedures as enunciated in the Companies Act, 2013.

Merger being a strategy, it has to be object oriented and it dwells upon the concept of synergy, which means value of two companies together will be more than of an individual company. Merger & Acquisition could be by way of business purchase/share purchase agreement or by way of sanction of Scheme of Arrangement through the court route.

In a sense, in the case of merger through a court route, once the scheme is sanctioned by the court/tribunal after due process of law and the scheme is filed with the Registrar of Companies, it is irreversible; it carries the stamp of final approval by a judicial authority and is acceptable to the public, shareholders, stakeholders, registering authority.

> Merger & Acquisition process is normally proceeded by formulation of strategy, identification of cost benefit analysis, carrying out due diligence, conducting valuation and considering the aspects of stamp duty and other applications. Moreover, the integration issue after the merger exercise is also to be taken care of.

Prerequisites of Merger and Acquisition

1. **Due Diligence**: It refers to the investigating effort made to gather all relevant facts and information that can influence a decision to enter into a transaction or not. Exercising due diligence is not a privilege but an unsaid duty of every party to the transaction. For instance, while purchasing a food item, a buyer must act with due diligence by checking the expiry date, the price, the packaging condition, etc. before paying for the product. It is not the duty of the seller to ask every buyer every time to check the necessary details. M&A due diligence helps to avoid legal hassles due to insufficient knowledge of important information.

2. **Business Valuation:** Business valuation or assessment is the first step of merger and acquisition. This step includes examination and evaluation of both the present and future market value of the target company. A thorough research is done on the history of the company with regards to capital gains, organizational structure, market share, distribution channel, corporate culture, specific business strengths, and credibility in the market. There are many other aspects that should be considered to ensure if a proposed company is right or not for a successful merger.

3. **Planning Exit**: When a company decides to sell its operations, it has to undergo the stage of exit planning. The company has to take firm decision as to when and how to make the exit in an organized and profitable manner. In the process the management has to evaluate all financial and other business issues like taking a decision of full sale or partial sale along with evaluating on various options of reinvestments.

4. **Structuring Business Deal**: After finalizing the merger and the exit plans, the new entity or the take-over company or target company has to take initiatives for marketing and creating innovative

strategies to enhance business and its credibility. The entire phase emphasize on structuring of the business deal.

5. **Stage of Integration**: This stage includes both the company coming together with their own parameters. It includes the entire process of preparing the document, signing the agreement, and negotiating the deal. It also defines the parameters of the future relationship between the two.

Some of key highlights of Companies Act, 2013 impacting merger and amalgamation

- Creation of treasury shares i.e. holding the share in its own name or in the name of the trust, whether on its own behalf or on behalf of any of its subsidiary or associated company is no longer permissible.
- Objections to the scheme can be raised only by shareholders holding at least 10% stake or creditors holding at least 5% of total outstanding debts as per the latest audited financial statements thereby avoiding unnecessary delays.
- Regulators to make representation within 30 days regarding scheme, else deemed 'no objections' or no representation on the proposal of such merger/amalgamation.
- No approval of Tribunal is required in case of merger between holding company and its 100% subsidiary or merger between small companies (based on prescribed capital/turnover).
- Merger of Indian company with foreign company located in certain jurisdictions is allowed subject to RBI Regulations/FDI Guidelines.
- Shareholders would have an option to vote for the scheme through postal ballot, e-voting in addition to voting physically at a meeting.

DUE DILIGENCE

Diligence: It means prudence; vigilant activity; attentiveness; or care, of which there are infinite shades, from the slightest momentary thought to the most vigilant anxiety. *People v. Hewitt, 78 Cal. App. 426, 248 P. 1021, 1024*1.

Due diligence: Such a measure of prudence, activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent man under the particular circumstances; not measured by any absolute standard, but depending on the relative facts of the special case. *Perry v. Cedar Falls*, *87 Iowa, 315, 54 N.W. 225*.

Due diligence is an investigation of a business or person prior to signing a contract, or an act with a certain standard of care. It can be a legal obligation, but the term will more commonly apply to voluntary investigations. A common example of due diligence in various industries is the process through which a potential acquirer/ investor evaluates a target company including its assets for an acquisition. The theory behind due diligence holds that performing this type of investigation contributes significantly to informed decision making by enhancing the amount and quality of information available to decision makers and by ensuring that this information is systematically used to deliberate in a reflexive manner on the decision at hand and all its costs, benefits, and risks.

Due diligence is integral to business. It is exercised in a simple over-the-counter transaction or a complicated merger and acquisition transaction. For instance, while acquiring a company, the buyer must do thorough research of the credentials of the company, its market valuation, status of accounts receivables, product and brand involved, position in the debt market, status of legal and statutory compliances, past performance, etc. It is also essential to study the previous financial reports to analyze the company's performance, to check the company background, its promoters, general reputation, and return to the existing shareholders.

Thus, a due diligence is an investigation or audit of a potential investment. It seeks to confirm all material facts in regard to a sale. It is a way of preventing unnecessary harm/hassles to either party involved in a transaction. It first came into use as a result of the US Securities Act, 1933.

TYPES OF DUE DILIGENCE

The different types of Due Diligence may be as follows:

Legal Due Diligence: Legal Due Diligence is used to ensure that there are no legal issues in buying a business or investing in it. In this, the potential purchaser will review the important legal documents of the target firm such as employment contracts, board meeting minutes, articles and memorandum of association and patents and copyrights or any other property related documents compliance status of the applicable laws etc.

Tax Due Diligence: This is aimed at ensuring that there are no past tax liabilities in the seller firm that might have materialized due to mistakes or deception and could hold the acquirer liable for it.

IP Due Diligence: IP due diligence is focused on establishing what rights the company may have in various intellectual property and where it might rely on the intellectual property of another entity. Typical areas of interest are patent, copyright and trademark filings; descriptions of the company's IP protection processes; licensing agreements, IP Assignment document, etc.

Operational Due Diligence: Operational due diligence (ODD) is the process by which a potential purchaser reviews the operational aspects of a target company during mergers and acquisitions. The ODD review looks at the main operations of the target company and attempts to confirm (or not) that the business plan that has been provided is achievable with the existing operational facilities plus the capital expenditure that is outlined in the business plan.

Commercial Due Diligence: This aims at understanding the market the target business is operating in. This looks the current market status and the forecast of the market growth in future and the target's position in the market with relation to its competitors. This also involves interaction with the significant customers of the business to understand their opinion about the business.

Information Technology (IT) Due Diligence: This aims at identifying if there are any IT issues in the target business. This involves into matters such as scalability of systems, robustness of the processes, availability of ERP, IT base and infrastructure, capacity of server, the level of documentation of processes, compliance with the legislation and ability to integrate various systems.

HR Due Diligence: This aims at understanding the impact of human capital on the proposed deal. This involves review of number and type of manpower, skills, employment records, compensation schemes, HR processes, ongoing HR litigations, effectiveness of the sales force and cultural factors.

PRACTICAL GUIDE TO DUE DILIGENCE

> Due diligence is a meaningful analysis of the collected information to arrive at some decision about the potential transaction. The due diligence exercise is a crucial task. In this process the financial and non-financial information of the target company is to be collected and analysed in order to derive profitability after acquiring the target company.

A successful due diligence depends to a large extent on the cooperation of the proposed seller. This is possible in the case of 'friendly' takeovers. Generally the buyer conducts a preliminary review of the target and after a 'provisional' offer is made by the buyer to denote interest in the acquisition, an environment is created for the target to allow access to the documents, records and most aspects of the business including the physical inspection of the undertaking.

The collection of the information relating to the target company is not an easy task specifically when the target company does not cooperate in the matter. The information may be gathered from the external as well as internal sources. External sources are available and can be extracted from the public domain; however gathering of the internal information is somewhat difficult.

Normally the due diligence process should incorporate the following areas, in order to assess the nitty-gritty of the transactions of the takeover and to opt for or opt out of the takeover deal:

1. **Industry Analysis**
   - Competition
   - Growth Rate
   - Future projections
   - Barriers to entry / exit
   - Mergers and acquisitions in industry and results
   - Brand evaluation.
2. **Management Analysis**
   - Company's HR Policies
   - Assessment of Senior Level Management, resumes of key employees their qualifications and work exposures, previous background, etc.
   - Summary Plan descriptions of qualified and non-qualified retirement plans
   - Business Experience
   - Union Contract, copies of collective bargaining agreements, description of all employees problems within last five years including the alleged wrongful termination, harassment discrimination, etc.
   - Strike History
   - Labour Relations/ Agreements, grievance procedures, labour disputes currently pending or settled within last five years.
   - Workman's' compensation claim history / unemployment claim history
   - Personnel Schemes, description of benefits of all employees' health and welfare insurance policies
   - Profile of permanent employees
   - Labour dues and settlement history
   - Status of labour law compliances.
3. **Financial Analysis**
   - Audited Financial Statements along with auditor's reports for at least past five years or since inception.
   - Auditor s letters and replies for the past five years or since inception
   - The most recent unaudited statements, with comparable statements to the prior year.
   - The company's credit report, if available
   - Analyst reports, if available
   - Budgets and forecasts and strategic plans
   - Significant ratio analysis
   - Revenue versus cost comparison.

- A description of depreciation and amortization methods and changes in accounting methods since inception Schedules of:
  - All indebtedness and contingent liabilities
  - Stock
  - Accounts receivable
  - Non-current investment
  - Cash in hand/Cash Equivalent
  - Type of ownership rights
  - Tax Liabilities
  - Accounts payable
  - Fixed Assets and its locations (including the land holdings, real estate leases, deeds, mortgages, titled deeds etc)
  - All leases of equipment
  - Sale and purchases of major capital equipments made during the last five years.
- Financial ratios
  - Return on Assets
  - Return on Net worth
  - Gross Profit to Net Profit Ratio
  - Debt Equity Ratio
  - Expense Ratio
  - Debt-Service Coverage Ratio.
- Analysis of
  - Fixed and variable expenses
  - Gross margins
- The company's general ledger
- Replacement cost data
- Valuation of Assets / Liabilities
- A description of the company's internal control procedures
- Internal audit/control reports for last five years
- Insurance coverage of all assets.

4. Intellectual Property Rights

- A list of domestic and foreign patents and patent applications
- A list of trademark and trade names
- A list of copyrights

- A description of important technical know-how
- A description of methods used to protect trade secrets and know-how
- Any work for hire agreements
- A list of and copies of all consulting agreements, agreements regarding inventions, licences, or assignments of intellectual property to or from the company
- Any patent clearance documents
- A list of and summary of any claims or threatened claims by or against the company regarding intellectual property.

5. Taxes

- Income-tax returns for the last five year or since inception
- States sales/VAT returns /GST returns
- Assessment orders
- Tax audit, where applicable
- Any tax settlement documents
- Other tax filing statements (State and Central Excise).
- Number of current tax litigations, if any.

6. Marketing Analysis

- Data on Past Sales and future trend
- Customer base and profile
- Major sales agreements, warranty agreements, distributorship/franchisee agreements, product development agreements.
- Trends
- Distribution channels
- Product Profile
- Development / Disclosure.

7. Manufacturing

- Location
- Technology
- Manufacturing process
- Quality
- Research & Development
- Sourcing of Raw Material.

8. Compliance Status of various laws as applicable

- Companies Act 2013

- Stock Exchange Compliances, SEBI/RBI Regulations
- Labour Laws
- Competition laws
- Environmental Protection laws.

9. Litigation

- A schedule of all pending litigations
- A description of any threatened litigations
- Copies of insurance policies providing coverage as to pending or threatened litigation
- Documents relating to any injunctions, consent decrees, or settlements to which the company is a party
- A list of unsatisfied judgments.

MANAGING THE DUE DILIGENCE PROCESS

As due diligence is wholesome exercise that require specialized knowledge, expertise & experience to complete the task in time bound & effective manner, therefore during the due diligence process the following points are worth consideration:

- Constitute a due diligence team comprising of technical, legal, financial and taxation experts, etc.
- Assign the task to each of the member and the co-ordination among the members be supervised by a senior level officer.
- Collect the data of the target company with reference to the:
  - Corporate records
  - Promoter's holding
  - Stockholder information
  - Important contracts including IP, Sales, Purchase, IT, etc.
  - Compliance record
  - HR record
  - Finance record including access of softwares/ERP, etc.
  - History of litigation
  - Insurance information
  - Financials and leases.
- Analyse the above information/ statistics, assess the future prospects and the benefit in acquiring with reference to the market size and cutting of the competition.
- If the proposal, found feasible, follow the regulatory requirements as mentioned in the Companies Act, 2013 and the SEBI Regulations, RBI regulations, FDI guidelines & competition laws as applicable.

CONTENTS OF THE DUE DILIGENCE REPORT

The contents of a due diligence report should more or less include certain points which would draw the attention of the intending buyer, viz:

- Comments on the management and organisation,

- Details of key managerial/ technical personnel,
- Details of marketing efforts undertaken,
- Details of financial liabilities and commitments that the intending buyer would have to meet after takeover and which are not disclosed in the audited accounts,
- Deviations from the generally accepted accounting policies/ practices,
- Analysis of major expenditure/costs, details of major/critical customers and suppliers,
- Compliance of taxation and other statutory laws as well as status and impact of all litigation in this respect,
- Benefits enjoyed by the intending seller which the intending buyer may lose on takeover and vice versa,
- List of adjustments to the latest financial statements compiled on the basis of all findings, which have an impact on the "price" of the target acquisition to be considered by the intending buyer.
- Number and type of litigations,
- Details of key assets and customers takeaways.

DUE DILIGENCE CHECK-LIST

The acquiring company is always interested in the financial aspects, human aspects, assets and liabilities of the target company. The following due diligence checks may help in carrying out the process:

Financial Aspects:

- Read the auditor's report and qualifying remarks, if any and director's responsibility statement.
- Whether the company is profit making, dividend paying company
- Calculate financial ratios and compare it with the previous year(s) figures of the company and also compare with the industry trend.
- Whether the Balance sheet have any fictitious assets?
- Whether any assets have been re-valued (particularly of real estates) in current year or in past.
- Calculate Net worth and its components and compare it with the previous year(s) figures.
- Compare the cash flow statements of current year with that of the previous year(s).
- Whether the borrowing from banks/FI is classified as Standard Assets in the books of the bank.
- Whether clear demarcation is made between the capital and revenue income and expenditure.
- Whether any penalty from Revenue Authorities, Stock Exchanges/ SEBI/ CCI/ FEMA levied in the current / past years?
- Whether any litigation against the company, is pending before any court of law?
- Amount of contingent liabilities.

Debtor's Aspects:

- Study the demographic profile of the customer.
- Study the type of customer base.
- Whether sales are made in concentration / very few buyers are available in the market.

- What is the debt realisation cycle?
- What are the terms and conditions for sales on credit?
- How the sales campaign is made in order to lead the others in the market.

Creditor's Aspects:

- Who are the suppliers?
- What are the terms and conditions for purchase on credit?
- Whether the supplier is unique or discattered or no single supplier can mis-match the supply?

Material Control Aspect:

- Make a review of all material contracts and commitments of the target company.
- Study various issues pertaining to guaranties, loans, and credit agreements.
- Study the Customer and supplier contracts, Equipment leases, Indemnification agreements, License agreements, Franchise agreements, Equity finance agreements, Distribution, dealer, sales agency, or advertising agreements, Non-competition agreements, Union contracts and collective bargaining agreements, Contracts the termination of which would result in a material adverse effect on the company.

Human Aspect:

- Study the organization chart and biographical information,
- Type of workforce and expertise involved.
- Summary of any labour disputes, information concerning any previous, pending, or threatened labour stoppage,
- Employment and consulting agreements, loan agreements, and documents relating to other transactions with officers, directors, key employees, and related parties,
- Schedule of compensation paid to officers, directors, and key employees for the three most recent fiscal years showing separately salary, bonuses, and non-cash compensation (e.g., use of cars, property, etc.)
- Employee benefits and copies of any pension, profit sharing, deferred compensation, and retirement plans, management incentive or bonus plans not included in above as well as other forms of non- cash compensation, Employment manuals and policies, involvement of key employees and officers in criminal proceedings or significant civil litigation, Actuarial reports for past three years for gratuity valuations.

Regulatory Aspects:

- Study the revenue returns filed by the company and its assessment orders.
- Whether any penalty has been imposed for contraventions of the provisions of the law and such penalty is still due.
- Whether the company is abiding with the company law compliances. Check the various returns filed with the RoC.
- Is there any specific laws applicable and compliance of such laws are regular.

REGULATORY FRAMEWORK FOR MERGER/ AMALGAMATION

The Companies Act, 2013 has brought many enabling provisions with regard to mergers, compromise or arrangements, especially with respect to cross border mergers, time bound and single window clearances, enhanced disclosures, disclosures to various regulators, simplified procedure for smaller companies, etc.

The Regulatory framework of Mergers and Amalgamations covers:

1. The Companies Act, 2013
2. National Company Law Tribunal Rules, 2016
3. Companies (Compromise, Arrangements and Amalgamations) Rules, 2016
4. Income Tax Act, 1961
5. SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015
6. Competition Act, 2002
7. Approval from industry specific regulators, wherever required.

1. Companies Act, 2013

Chapter XV of Companies Act, 2013 comprising Sections 230 to 240 contains provisions on Compromises, Arrangements and Amalgamations. The scheme of Chapter XV is as follows:

1. Section 230-231 deals with compromise or arrangements with creditors and members and power of the Tribunal to enforce such a compromise or arrangement.
2. Section 232 deals with mergers and amalgamation including demergers.
3. Section 233 is relating to the merger or amalgamation of small companies or between the holding company and its wholly owned subsidiary (also called fast track mergers)
4. Section 234 deals with amalgamation with foreign company (also called cross border mergers).
5. Section 235 deals with acquisition of shares of dissenting shareholders.
6. Section 236 deals with purchase of minority shareholding.
7. Section 237 contains provisions as to the power of the Central Government to provide for amalgamation of companies in public interest.
8. Section 238 deals with registration of offer of schemes involving transfer of shares.
9. Section 239 deals with preservation of books and papers of amalgamated companies.
10. Section 240 deals with liability of officers in respect of offences committed prior to merger, amalgamation, etc.

2. Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 (read with National Company Law Tribunal Rules, 2016)

Rules 3 to Rule 29 contain provisions dealing with the procedure for carrying out a scheme of compromise or arrangement including amalgamation or reconstruction.

3. Income Tax Act, 1961

The Income Tax Act, 1961 covers aspects such as tax relief to amalgamating/amalgamated companies, carry forward of losses, exemptions from capital gains tax, etc. For example, when a scheme of merger or demerger involves the merger of a loss making company or a hiving-off of a loss making division, it is necessary to check the relevant provisions of the Income Tax Act and the Rules for the purpose of ensuring, *inter alia* , the availability of the benefit of carrying forward the accumulated losses and setting of such losses against the profits of the Transferor Company.

4. **SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015**

SEBI has notified SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations) on September 2, 2015. Companies are required to comply with the following:

— Scheme of Arrangement (Regulation11)

— Draft scheme of arrangement & scheme of arrangement (Regulation 37)

— Minimum Public Shareholding (Regulation 38)

For details please refer to Chapter 10 of this Study.

5. **Indian Stamp Act, 1899**

It is necessary to refer to the Indian Stamp Act, 1899 to check the stamp duty payable on transfer of undertaking through a merger or demerger.

6. **Competition Act, 2002**

The provisions of Competition Act, 2002 and the Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011 are to be complied with.

Provisions of the Companies Act, 2013

Chapter XV, comprising of sections 230 to 240 read with the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016, deals with Compromises, Arrangements and Amalgamations. The relevant details are explained below:

Section 230 - Power to compromise or make arrangements with creditors and members

Section 230 lays down in detail the power of a company to make compromise or arrangements with its creditors and members. Under this section, a company can enter in to a compromise or arrangement with its creditors or its members, or any class thereof.

Scope of Section 230

Section 230 deals with the rights of a company to enter into a compromise or arrangement (i) between itself and its creditors or any class of them; and (ii) between itself and its members or any class of them. The arrangement contemplated by the section includes a re-organisation of the share capital of a company by consolidation of its shares of different classes or by sub-division of its shares into shares of different classes or by both these methods.

The section also applies to compromise or arrangement entered into by companies under winding-up. Therefore, an arrangement under this section can take a company out of winding-up.

Sub-section (1)–Application to the Tribunal for convening meetings of members/creditors

Where a company or a creditor or a member of the company proposes a compromise or arrangement between it and its creditors or between it and its members or with any class of the creditors or any class of members, the company or the creditor or member, or where the company is being wound-up, the liquidator may make an application to the Tribunal. On such application, the Tribunal may order a meeting of the creditors or members or any class of them as the case may be and such meetings shall be called, held and conducted in such manner as the Tribunal may direct.

The key words and expressions under sub-section are 'creditors', 'Tribunal', 'class of creditors or members', 'a company which is being wound-up', 'liquidator'. When a company is ordered to be wound-up, the liquidator is appointed and once winding-up commences liquidator takes charge of the company in all respects and therefore it is he who could file any application of any compromise or arrangement in the case of a company which is being wound-up. A company which is being wound-up would mean a company in respect of which the court has passed the winding-up order.

Sub-section (2)– Disclosures to the Tribunal by applicant under sub-section 1

Sub-section (2) provides that the company or any other person, who makes an application as provided under sub-section (1) shall disclose by affidavit to the Tribunal:

(a) all material facts relating to the company, such as the latest financial position of the company, the latest auditor's report on the accounts of the company and the pendency of any investigation orproceedings against the company;

(b) reduction of share capital of the company, if any, included in the compromise or arrangement;

(c) any scheme of corporate debt restructuring consented to by not less than seventy-five percent of the secured creditors in value, including—

(i) a creditor's responsibility statement in the prescribed form;

(ii) safeguards for the protection of other secured and unsecured creditors;

(iii) report by the auditor that the fund requirements of the company after the corporate debt restructuring as approved shall conform to the liquidity test based upon the estimates provided to them by the Board;

(iv) where the company proposes to adopt the corporate debt restructuring guidelines specified by the Reserve Bank of India, a statement to that effect; and

(v) a valuation report in respect of the shares and the property and all assets, tangible and intangible, movable and immovable, of the company by a registered valuer.

Sub-section (3) – Notice of the meeting

Notice of the meeting called in pursuance of the order of the tribunal shall be sent to all the creditors or class of creditors and to all the members or class of members and the debenture-holders of the company, individually at the address registered with the company which shall be accompanied by

1. a statement disclosing the details of the compromise or arrangement,
2. a copy of the valuation report, if any, and
3. explaining their effect on creditors, key managerial personnel, promoters and non-promoter members, and the debenture holders and
4. the effect of the compromise or arrangement on any material interests of the directors of the company or the debenture trustees, and
5. such other matters as may be prescribed:

Such notice and other documents shall also be placed on the website of the company, if any, and in case of a listed company, these documents shall be sent to the Securities and Exchange Board and stock exchange where the securities of the companies are listed, for placing on their website and shall also be published in newspapers in such manner as may be prescribed: When the notice for the meeting is also issued by way of an advertisement, it shall indicate the time within which copies of the compromise or arrangement shall be made available to the concerned persons free of charge from the registered office of the company.

Sub-section (4) – Notice to provide for voting by themselves or through proxy or through postal ballot

Sub-section (4) states that a notice under sub-section(3) shall provide that the persons to whom the notice is sent may vote in the meeting either themselves or through proxies or by postal ballot to the adoption of the compromise or arrangement within one month from the date of receipt of such notice.

Provided that any objection to the compromise or arrangement shall be made only by persons holding not less than ten per cent. of the shareholding or having outstanding debt amounting to not less than five per cent of the total outstanding debt as per the latest audited financial statement.

Sub-section (5) – Notice to be sent to the regulators seeking their representations

Section 230 (5) states that a notice under sub-section (3) along with all the documents in such form as may be prescribed shall also be sent to the Central Government, the income-tax authorities, the Reserve Bank of India, the Securities and Exchange Board, the Registrar, the respective stock exchanges, the Official Liquidator, the Competition Commission of India established under sub-section (1) of section 7 of the Competition Act, 2002, if necessary, and such other sectoral regulators or authorities which are likely to be affected by the compromise or arrangement and shall require that representations, if any, to be made by them shall be made within a period of thirty days from the date of receipt of such notice, failing which, it shall be presumed that they have no representations to make on the proposals.

Sub-section (6): Approval and sanction of the scheme

Section 230 (6) states that when at a meeting held in pursuance of sub-section (1), majority of persons representing three-fourths in value of the creditors, or class of creditors or members or class of members, as the case may be, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and if such compromise or arrangement is sanctioned by the Tribunal by an order, the same shall be binding on the company, all the creditors, or class of creditors or members or class of members, as the case may be, or, in case of a company being wound-up, on the liquidator appointed under this Act or under the Insolvency and Bankruptcy Code, 2016, as the case may be and the contributories of the company.

Sub-section (7): Order of the tribunal sanctioning the scheme to provide for the certain matters

An order made by the Tribunal shall provide for all or any of the following matters, namely:

(a) where the compromise or arrangement provides for conversion of preference shares into equity shares, such preference shareholders shall be given an option to either obtain arrears of dividend in cash or accept equity shares equal to the value of the dividend payable;

(b) the protection of any class of creditors;

(c) if the compromise or arrangement results in the variation of the shareholders' rights, it shall be given effect to under the provisions of section 48;

(d) if the compromise or arrangement is agreed to by the creditors under sub-section (6), any proceedings pending before the Board for Industrial and Financial Reconstruction established under section 4 of the Sick Industrial Companies (Special Provisions) Act,1985 shall abate;

(e) such other matters including exit offer to dissenting shareholders, if any, as are in the opinion of the Tribunal necessary to effectively implement the terms of the compromise or arrangement.

No compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company's auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133.

Sub-Section (8)

The order of the Tribunal shall be filed with the Registrar by the company within a period of thirty days of the receipt of the order.

Sub-section (9): The Tribunal may dispense with calling of meeting of creditors

Section 230 (9) states that the Tribunal may dispense with calling of a meeting of creditor or class of creditors where such creditors or class of creditors, having at least ninety percent value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement.

In the case of *Sabari Rubber Private Limited & other Ca(CAA)/1(KOB)/2022,* NCLT, *Kochi Bench, Order dated* 5th day of May, 2022 inter alia observed that While considering the power of the Tribunal to dispense with the meeting of shareholders, NCLT, *Kochi Bench* relied on the decision of the National Company Law Tribunal in the case of *Jupiter Alloys & Steel (India) Limited V. Jupiter Wagons Limited (2017 SCC Online NCLT14022)*, wherein it is stated that NCLT is empowered to dispense the meeting of shareholders by virtue of its inherent powers vested in NCLT by Rule 11 of the NCLT Rules, 2016. The NCLT, Kolkata Bench also made an observation that High Courts used to exercise their discretion to dispense the meeting of shareholders under the Companies Act, 2013 and such decisions cannot be ignored.

Under Section 230(9) of the Companies Act, 2013, the Tribunal may dispense with calling of a meeting of Creditors or class of Creditors where such Creditors or class of Creditors, having at least 90% value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement.

Sub-Section (10)

Compromise in respect of buy back is to be in compliance with section 68. As per Section 230 (10), no compromise or arrangement in respect of any buy-back of securities under this section shall be sanctioned by the Tribunal unless such buy-back is in accordance with the provisions of section 68.

Sub-Section (11)

Section 230(11) states that any compromise or arrangement may include takeover offer made in such manner as may be prescribed. In case of listed companies, takeover offer shall be as per the regulations framed by the Securities and Exchange Board.

Companies (Compromises, Arrangements and Amalgamations) Rules, 2016

Rule 3 provides that an application under sub-section

(1) of section 230 of the Act may be submitted in Form no. NCLT-1 (appended in the National Company Law Tribunal Rules, 2016) along with:—

- (i) a notice of admission in Form No. NCLT-2 (appended in the National Company Law Tribunal Rules, 2016);
- (ii) an affidavit in Form No. NCLT-6 (appended in the National Company Law Tribunal Rules, 2016);
- (iii) a copy of scheme of compromise or arrangement, which should include disclosures as per sub-section (2) of section 230 of the Act and certified true copies of all the enclosures; and
- (iv) fee as prescribed in the Schedule of Fees.

(2) Where more than one company is involved in a scheme in relation to which an application under sub-rule (1) is being filed, such application may, at the discretion of such companies, be filed as a joint-application.

(3) Where the company is not the applicant, a copy of the notice of admission and of the affidavit shall be served on the company, or, where the company is being wound up, on its liquidator, not less than fourteen days before the date fixed for the hearing of the notice of admission.

(4) The applicant shall also disclose to the Tribunal in the application under sub-rule (1), the basis on which each class of members or creditors has been identified for the purposes of approval of the scheme.

(5) A member of the company shall make an application for arrangement, for the purpose of takeover offer in terms of sub-section (11) of section 230, when such member along with any other member holds not less than three-fourths of the shares in the company, and such application has been filed for acquiring any part of the remaining shares of the company.

Explanation I. “shares” means the equity shares of the company carrying voting rights, and includes any securities, such as depository receipts, which entitles the holder thereof to exercise voting rights.

Explanation II. Nothing in this sub-rule shall apply to any transfer or transmission of shares through a contract, arrangement or succession, as the case may be, or any transfer made in pursuance of any statutory or regulatory requirement.

(6) An application of arrangement for takeover offer shall contain:

(a) the report of a registered valuer disclosing the details of the valuation of the shares proposed to be acquired by the member after taking into account the following factors:

(i) the highest price paid by any person or group of persons for acquisition of shares during last twelve months;

(ii) the fair price of shares of the company to be determined by the registered valuer after taking into account valuation parameters including return on net worth, book value of shares, earning per share, price earning multiple vis-d-vis the industry average, and such other parameters as are customary for valuation of shares of such companies.

(b) details of a bank account, to be opened separately, by the member wherein a sum of amount not less than one-half of total consideration of the takeover offer is deposited.

Rule 4 provides that for the purposes of sub-clause (i) of clause (c) of sub-section (2) of section 230 of the Act, the creditor's responsibility statement in Form No. CAA. 1 shall be included in the scheme of corporate debt restructuring.

Explanation:— For the purpose of this rule, it is clarified that a scheme of corporate debt restructuring as referred to in clause (c) of sub-section (2) of section 230 of the Act shall mean a scheme that restructures or varies the debt obligations of a company towards its creditors.

Rule 6 provides that

(1) Where a meeting of any class or classes of creditors or members has been directed to be convened, the notice of the meeting pursuant to the order of the Tribunal to be given in the manner provided in sub-section (3) of section 230 of the Act shall be in Form No. CAA.2 and shall be sent individually to each of the creditors or members.

(2) The notice shall be sent by the Chairperson appointed for the meeting, or, if the Tribunal so directs, by the company (or its liquidator), or any other person as the Tribunal may direct, by registered post or speed post or by courier or by e-mail or by hand delivery or any other mode as directed by the Tribunal to their last known address at least one month before the date fixed for the meeting.

Explanation: - It is hereby clarified that the service of notice of meeting shall be deemed to have been effected in case of delivery by post, at the expiration of forty eight hours after the letter containing the same is posted.

(3) The notice of the meeting to the creditors and members shall be accompanied by a copy of the scheme of compromise or arrangement and a statement disclosing the following details of the compromise or arrangement, if such details are not already included in the said scheme:—

(i) details of the order of the Tribunal directing the calling, convening and conducting of the meeting:

(a) date of the Order;

(b) date, time and venue of the meeting.

(ii) details of the company including:

(a) Corporate Identification Number (CIN) or Global Location Number (GLN) of the company;

(b) Permanent Account Number (PAN);

(c) name of the company;

(d) date of incorporation;

(e) type of the company (whether public or private or one-person company);

(f) registered office address and e-mail address;

(g) summary of main object as per the memorandum of association; and main business carried on by the company;

(h) details of change of name, registered office and objects of the company during the last five years;

(i) name of the stock exchange (s) where securities of the company are listed, if applicable;

(j) details of the capital structure of the company including authorised, issued, subscribed and paid up share capital; and

(k) names of the promoters and directors along with their addresses.

(iii) if the scheme of compromise or arrangement relates to more than one company, the fact and details of any relationship subsisting between such companies who are parties to such scheme of compromise or arrangement, including holding, subsidiary or of associate companies;

(iv) the date of the board meeting at which the scheme was approved by the board of directors including the name of the directors who voted in favour of the resolution, who voted against the resolution and who did not vote or participate on such resolution;

(v) explanatory statement disclosing details of the scheme of compromise or arrangement including: —

(a) parties involved in such compromise or arrangement;

(b) in case of amalgamation or merger, appointed date, effective date, share exchange ratio (if applicable) and other considerations, if any;

(c) summary of valuation report (if applicable) including basis of valuation and fairness opinion of the registered valuer, if any, and the declaration that the valuation report is available for inspection at the registered office of the company;

(d) details of capital or debt restructuring, if any;

(e) rationale for the compromise or arrangement;

(f) benefits of the compromise or arrangement as perceived by the Board of directors to the company, members, creditors and others (as applicable);

(g) amount due to unsecured creditors.

(vi) disclosure about the effect of the compromise or arrangement on:

(a) key managerial personnel;

(b) directors;

(c) promoters;

(d) non-promoter members;

(e) depositors;

(f) creditors;

(g) debenture holders;

(h) deposit trustee and debenture trustee;

(i) employees of the company;

(vii) Disclosure about effect of compromise or arrangement on material interests of directors, Key Managerial Personnel (KMP) and debenture trustee.

Explanation- For the purposes of these rules it is clarified that-

(a) the term 'interest' extends beyond an interest in the shares of the company, and is with reference to the proposed scheme of compromise or arrangement.

(b) the valuation report shall be made by a registered valuer, and till the registration of persons as valuers is prescribed under section 247 of the Act, the valuation report shall be made by an independent merchant banker who is registered with the Securities and Exchange Board or an independent chartered accountant in practice having a minimum experience of ten years.

(viii) investigation or proceedings, if any, pending against the company under the Act.

(ix) details of the availability of the following documents for obtaining extract from or for making or obtaining copies of or for inspection by the members and creditors, namely:

(a) latest audited financial statements of the company including consolidated financial statements;

(b) copy of the order of Tribunal in pursuance of which the meeting is to be convened or has been dispensed with;

(c) copy of scheme of compromise or arrangement;

(d) contracts or agreements material to the compromise or arrangement;

(e) the certificate issued by Auditor of the company to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the Accounting Standards prescribed under section 133 of the Companies Act, 2013; and

(f) such other information or documents as the Board or Management believes necessary and relevant for making decision for or against the scheme;

(x) details of approvals, sanctions or no-objection(s), if any, from regulatory or any other governmental authorities required, received or pending for the proposed scheme of compromise or arrangement.

(xi) a statement to the effect that the persons to whom the notice is sent may vote in the meeting either in person or by proxies, or where applicable, by voting through electronic means.

Explanation- For the purposes of this rule, disclosure required to be made by a company shall be made in respect of all the companies, which are part of the compromise or arrangement.

Rule 7 provides that the notice of the meeting under sub-section (3) of section 230 of the Act shall be advertised in Form No. CAA.2 in at least one English newspaper and in at least one vernacular newspaper having wide circulation in the State in which the registered office of the company is situated, or such newspapers as may be directed by the Tribunal and shall also be placed, not less than thirty days before the date fixed for the meeting, on the website of the company (if any) and in case of listed companies also on the website of the SEBI and the recognized stock exchange where the securities of the company are listed:

Provided that where separate meetings of classes of creditors or members are to be held, a joint advertisement for such meetings may be given.

Rule 8 provides that for the purposes of sub-section (5) of section 230 of the Act, the notice shall be in Form No. CAA.3, and shall be accompanied with a copy of the scheme of compromise or arrangement, the explanatory statement and the disclosures mentioned under rule 6, and shall be sent to.-

i. the Central Government, the Registrar of Companies, the Income-tax authorities, in all cases;

ii. the Reserve Bank of India, the Securities and Exchange Board of India, the Competition Commission of India, and the stock exchanges, as may be applicable;

iii. other sectoral regulators or authorities, as required by Tribunal.

(2) The notice to the authorities mentioned in sub-rule (1) shall be sent forthwith, after the notice is sent to the members or creditors of the company, by registered post or by speed post or by courier or by hand delivery at the office of the authority.

(3) If the authorities referred to under sub-rule (1) desire to make any representation under sub-section (5) of section 230, the same shall be sent to the Tribunal within a period of thirty days from the date of receipt of such notice and copy of such representation shall simultaneously be sent to the concerned companies and in case no representation is received within the stated period of thirty days by the Tribunal, it shall be presumed that the authorities have no representation to make on the proposed scheme of compromise or arrangement.

Section 231 – Power of the Tribunal to enforce compromise or arrangement

As per section 231(1) when the Tribunal makes an order under section 230 sanctioning a compromise or an arrangement in respect of a company, it –

(a) shall have power to supervise the implementation of the compromise or arrangement; and

(b) may, at the time of making such order or at any time thereafter, give such directions in regard to any matter or make such modifications in the compromise or arrangement as it may consider necessary for the proper implementation of the compromise or arrangement.

Sub-section (2) states that if the Tribunal is satisfied that the compromise or arrangement sanctioned under section 230 cannot be implemented satisfactorily with or without modifications, and the company is unable to pay its debts as per the scheme, it may make an order for winding-up the company and such an order shall be deemed to be an order made under section 273.

In the case of HT Mobile Solutions Ltd. & Anr.(Appellants) vs. Regional Director, Ministry of Corporate Affairs & Ors.(Respondents), Comp. App. (AT) No. 74 of 2023 judgement dated March 12, 2024, the Hon'ble National Company Law Appellate Tribunal inter alia observed that Section 231(1) (b) of the Companies Act duly empowers the Ld. NCLT to exercise discretion to "give such directions in regard to any matter or make such modifications in the compromise or arrangement as it may consider necessary for the proper implementation of the compromise or arrangement". The Ld. NCLT was thus duly vested with sufficient powers under the Companies Act, to even partly sanction the scheme.

During the argument, the reliance was also placed on 'Rama Investment Company Pvt. Ltd. vs. Ankit Mittal' wherein vide order dated 07.09.2022 in Civil Appeal Nos. 2022-2023/2022 the Hon'ble Supreme Court was pleased to set aside the order of this Tribunal and confirm the scheme of amalgamation in part as approved by the Ld. NCLT.

Section 232 – Merger and amalgamation of companies

Sub-section (1): Tribunal's power to call meeting of creditors or members, with respect to merger or amalgamation of companies

Section 232(1) states that when an application is made to the Tribunal under section 230 for the sanctioning of a compromise or an arrangement proposed between a company and any such persons as are mentioned in that section, and it is shown to the Tribunal —

(a) that the compromise or arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of the company or companies involving merger or the amalgamation of any two or more companies; and

(b) that under the scheme, the whole or any part of the undertaking, property or liabilities of any company (hereinafter referred to as the transferor company) is required to be transferred to another company (hereinafter referred to as the transferee company), or is proposed to be divided among and transferred to two or more companies, the Tribunal may on such application, order a meeting of the creditors or class of creditors or the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal may direct and the provisions of sub-sections (3) to (6) of section 230 shall apply mutatis mutandis.

Sub-section (2): Circulation of documents for members/creditors meeting

Section 232(2) states that when an order has been made by the Tribunal under sub-section (1), merging companies or the companies in respect of which a division is proposed, shall also be required to circulate the following for the meeting so ordered by the Tribunal, namely:

(a) the draft of the proposed terms of the scheme drawn up and adopted by the directors of the merging company;

(b) confirmation that a copy of the draft scheme has been filed with the Registrar;

(c) a report adopted by the directors of the merging companies explaining effect of compromise on each class of shareholders, key managerial personnel, promoters and non-promoter shareholders laying out in particular the share exchange ratio, specifying any special valuation difficulties;

(d) the report of the expert with regard to valuation, if any;

(e) a supplementary accounting statement if the last annual accounts of any of the merging company relate to a financial year ending more than six months before the first meeting of the company summoned for the purposes of approving the scheme.

Sub-section (3): Sanctioning of scheme by Tribunal

Section 232(3) states that the Tribunal, after satisfying itself that the procedure specified in sub-sections (1) and (2) has been complied with, may, by order, sanction the compromise or arrangement or by a subsequent order, make provision for the following matters, namely:—

(a) the transfer to the transferee company of the whole or any part of the undertaking, property or liabilities of the transferor company from a date to be determined by the parties unless the Tribunal, for reasons to be recorded by it in writing, decides otherwise;

(b) the allotment or appropriation by the transferee company of any shares, debentures, policies or other like instruments in the company which, under the compromise or arrangement, are to be allotted or appropriated by that company to or for any person:

No transferee company can hold shares in its own name or under any trust.

A transferee company shall not, as a result of the compromise or arrangement, hold any shares in its own name or in the name of any trust whether on its behalf or on behalf of any of its subsidiary or associate companies and any such shares shall be cancelled or extinguished;

(c) the continuation by or against the transferee company of any legal proceedings pending by or against any transferor company on the date of transfer;

(d) dissolution, without winding-up, of any transferor company;

(e) the provision to be made for any persons who, within such time and in such manner as the Tribunal directs, dissent from the compromise or arrangement;

(f) where share capital is held by any non-resident shareholder under the foreign direct investment norms or guidelines specified by the Central Government or in accordance with any law for the time being in force, the allotment of shares of the transferee company to such shareholder shall be in the manner specified in the order;

(g) the transfer of the employees of the transferor company to the transferee company;

(h) when the transferor company is a listed company and the transferee company is an unlisted company,— the transferee company shall remain an unlisted company until it becomes a listed company; if shareholders of the transferor company decide to opt out of the transferee company, provision shall be made for payment of the value of shares held by them and other benefits in accordance with a pre- determined price formula or after a valuation is made, and the arrangements under this provision may be made by the Tribunal: The amount of payment or valuation under this clause for any share shall not be less than what has been specified by the Securities and Exchange Board under any regulations framed by it;

(i) where the transferor company is dissolved, the fee, if any, paid by the transferor company on its authorised capital shall be set-off against any fees payable by the transferee company on its authorised capital subsequent to the amalgamation; and

(j) such incidental, consequential and supplemental matters as are deemed necessary to secure that the merger or amalgamation is fully and effectively carried out.

No compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company's auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133.

Sub-section (4): Transfer of property or liabilities

Sub-section (4) states that an order under this section provides for the transfer of any property or liabilities, then, by virtue of the order, that property shall be transferred to the transferee company and the liabilities shall be transferred to and become the liabilities of the transferee company and any property may, if the order so directs, be freed from any charge which shall by virtue of the compromise or arrangement, cease to have effect

Sub-section (5): Certified copy of the order to be filed with the registrar.

Section 232(5) states that every company in relation to which the order is made shall cause a certified copy of the order to be filed with the Registrar for registration within thirty days of the receipt of certified copy of the order.

Sub Section (6): Effective date of the scheme.

Section 232(6) states that the scheme under this section shall clearly indicate an appointed date from which it shall be effective and the scheme shall be deemed to be effective from such date and not at a date subsequent to the appointed date.

Clarification issued by MCA vide General Circular No. 09/2019 dated 21st August, 2019

Clarification has been sought on whether it is mandatory to indicate a specific calendar date as 'appointed date' in the schemes referred to in the section. Further, requests have also been received to confirm whether the, acquisition date' for the purpose of Ind-AS 103 (Business combinations) would be the 'appointed date' referred to in section 232(6).

In *Marshall Sons & Co. India Ltd. v. ITO 1223 [ITR 8091]*, it was held by the Hon'ble Supreme Court that every scheme of amalgamation has to necessarily provide a date with effect from which the amalgamation/transfer shall take place, and that such date may precede the date of sanctioning of the scheme by the Court, the date of filing of certified copies of the orders of the Court before the Registrar of Companies, and the date of allotment of shares, etc. It was observed therein that, the scheme, however, would be given effect from the transfer date (appointed date) itself.

In another case, in the matter of amalgamation of *Equitas Housing Finance Limited and Equitas Micro Finance Limited with Equitas Finance Limited* in C.P. Nos. 119 to 121 of 2016, the Hon'ble Madras High Court held that the provisions of section 394 (1) of the Companies Act, 1956 (corresponding to section 232 of the Companies Act, 2013) provided enough leeway to a company to delay the date on which the scheme of amalgamation shall take effect and tie the same to the occurrence of an event. Thus, the Court rejected the argument that the 'appointed date' in the scheme should necessarily be a specific calendar date.

Section 232(6) of the Act states that the scheme shall be deemed to be effective from the 'appointed date' and not a date subsequent to the 'appointed date'. This is an enabling provision to allow the companies to decide and agree upon an 'appointed date' from which the scheme shall come into force.

In view of the above, it was clarified that:

(a) The provision of section 232(6) of the Act enables the companies in question to choose and state in the scheme an 'appointed date'. This date may be a specific calendar date or may be tied to the occurrence of an event such as grant of license by a competent authority or fulfillment of any preconditions agreed upon by the parties, or meeting any other requirement as agreed upon between the parties, etc., which are relevant to the scheme.

(b) The 'appointed date' identified under the scheme shall also be deemed to be the 'acquisition date' and date of transfer of control for the purpose of conforming to accounting standards (including Ind-AS 103 Business Combinations.

(c) where the 'appointed date' is chosen as a specific calendar date, it may precede the date of filing of the application for scheme of merger/amalgamation in NCLT. However, if the 'appointed date' is significantly ante-dated beyond a year from the date of filing, the justification for the same would have to be specifically brought out in the scheme and it should not be against public interest.

(d) The scheme may identify the 'appointed date' based on the occurrence of a trigger event which is key to the proposed scheme and agreed upon by the parties to the scheme. This event would have to be indicated in the scheme itself upon occurrence of which the scheme would become effective. However in case of such event based date being a date subsequent to the date of filing the order with the Registrar under section 232(5), the company shall file an intimation of the same with the Registrar within 30 days of such scheme coming into force.

Sub-section (7): Annual statement certified by CA/CS/CWA to be filed with Registrar every year until the completion of the scheme.

Section 232(7) states that every company in relation to which the order is made shall, until the completion of the scheme, file a statement in such form and within such time as may be prescribed with the Registrar every year duly certified by a chartered accountant or a cost accountant or a company secretary in practice indicating whether the scheme is being complied with in accordance with the orders of the Tribunal or not.

Sub-section (8): Penal Provision:

If a company fails to comply with sub-section (5), the company and every officer of the company who is in default shall be liable to a penalty of twenty thousand rupees, and where the failure is a continuing one, with a further penalty of one thousand rupees for each day after the first during which such failure continues, subject to a maximum of three lakh rupees.

Section 233 –Merger or amalgamation of certain companies

Section 233 prescribes simplified procedure for Merger or amalgamation of

- two or more small companies, or

- between a holding company and its wholly-owned subsidiary company, or
- such other class or classes of companies as maybe prescribed.

As per rule 25(1)(1A) of Companies (Compromises, Arrangements and Amalgamations) Amendment Rules, 2021, a scheme of merger or amalgamation under section 233 of the Act may be entered into between any of the following class of companies, namely:-

(i) two or more start-up companies; or

(ii) one or more start-up company with one or more small company.

Explanation.- For the purposes of this sub-rule, "start-up company" means a private company incorporated under the Companies Act, 2013 or Companies Act, 1956 and recognized as such in accordance with notification number G.S.R. 127 (E), dated the 19th February, 2019 issued by the Department for Promotion of Industry and Internal Trade.

Sub-section (1)

Accordingly sub-section(1) of Section 233 states that notwithstanding the provisions of section 230 and section 232, a scheme of merger or amalgamation may be entered into between two or more small companies or between a holding company and its wholly-owned subsidiary company or such other class or classes of companies as may be prescribed, subject to the following, namely:—

(a) a notice of the proposed scheme inviting objections or suggestions, if any, from the Registrar and Official Liquidators where registered office of the respective companies are situated or persons affected by the scheme within thirty days is issued by the transferor company or companies and the transferee company;

(b) the objections and suggestions received are considered by the companies in their respective general meetings and the scheme is approved by the respective members or class of members at a general meeting holding at least ninety percent of the total number of shares;

(c) each of the companies involved in the merger files a declaration of solvency, in the prescribed form, with the Registrar of the place where the registered office of the company is situated; and

(d) the scheme is approved by majority representing nine-tenths in value of the creditors or class of creditors of respective companies indicated in a meeting convened by the company by giving a notice of twenty- one days along with the scheme to its creditors for the purpose or otherwise approved in writing.

Sub-section (2): The sub-section states that the transferee company shall file a copy of the scheme so approved in the manner as may be prescribed, with the Central Government, Registrar and the Official Liquidator where the registered office of the company is situated.

Sub-section (3): Central Government to issue confirmation order, where there are no objections or suggestions from registrar or official liquidator.

Section 233(3) states that on the receipt of the scheme, if the Registrar or the Official Liquidator has no objections or suggestions to the scheme, the Central Government shall register the same and issue a confirmation thereof to the companies.

Sub-section (4): Objections if any by the registrar or official liquidator to be communicated to the central government.

Section 233(4) If the Registrar or Official Liquidator has any objections or suggestions, he may communicate the same in writing to the Central Government within a period of thirty days. If no such communication is made, it shall be presumed that he has no objection to the scheme.

Sub-section (5): Application by Central Government to the Tribunal.

Section 233(5) states that if the Central Government after receiving the objections or suggestions or for any reason is of the opinion that such a scheme is not in public interest or in the interest of the creditors, it may file an application before the Tribunal within a period of sixty days of the receipt of the scheme under sub-section (2) stating its objections and requesting that the Tribunal may consider the scheme under section 232.

Sub-section (6): Tribunal's action to Central Government's application

Section 233(6) states that on receipt of an application from the Central Government or from any person, if the Tribunal, for reasons to be recorded in writing, is of the opinion that the scheme should be considered as per the procedure laid down in section 232, the Tribunal may direct accordingly or it may confirm the scheme by passing such order as it deems fit: If the Central Government does not have any objection to the scheme or it does not file any application under this section before the Tribunal, it shall be deemed that it has no objection to the scheme.

Sub-section (7): Registrar having jurisdiction over transferee company has to be communicated

Section 233(7) states that a copy of the order under sub-section (6) confirming the scheme shall be communicated to the Registrar having jurisdiction over the transferee company and the persons concerned and the Registrar shall register the scheme and issue a confirmation thereof to the companies and such confirmation shall be communicated to the Registrars where transferor company or companies were situated.

Sub-section (8): Effect of Registration of the scheme.

Sub-Section (8) states that the registration of the scheme under sub-section (3) or sub-section (7) shall be deemed to have the effect of dissolution of the transferor company without process of winding up.

Sub-section (9)

This sub-section states that the registration of the scheme shall have the following effects, namely:—

(a) transfer of property or liabilities of the transferor company to the transferee company so that the property becomes the property of the transferee company and the liabilities become the liabilities of the transferee company;

(b) the charges, if any, on the property of the transferor company shall be applicable and enforceable as if the charges were on the property of the transferee company;

(c) legal proceedings by or against the transferor company pending before any court of law shall be continued by or against the transferee company; and

(d) where the scheme provides for purchase of shares held by the dissenting shareholders or settlement of debt due to dissenting creditors, such amount, to the extent it is unpaid, shall become the liability of the transferee company.

Sub-section (10): Transferee Company not to hold any share in its own name or trust and all such shares are to be cancelled or extinguished

Section 233(10) states that a transferee company shall not on merger or amalgamation, hold any shares in its own name or in the name of any trust either on its behalf or on behalf of any of its subsidiary or associate company and all such shares shall be cancelled or extinguished on the merger or amalgamation.

Sub-section (11): Transferee Company to file an application with Registrar along with the scheme registered

The transferee company shall file an application with the Registrar along with the scheme registered, indicating the revised authorised capital and pay the prescribed fees due on revised capital. The fee, if any, paid by the transferor company on its authorised capital prior to its merger or amalgamation with the transferee company shall be set-off against the fees payable by the transferee company on its authorised capital enhanced by the merger or amalgamation.

Section 234: Merger or amalgamation of a company with a foreign company

Section 234(1) states that the provisions of this Chapter XV of the Companies Act, 2013 unless otherwise provided under any other law for the time being in force, shall apply *mutatis mutandis* to schemes of mergers and amalgamations between companies registered under this Act and companies incorporated in the jurisdictions of such countries as may be notified from time to time by the Central Government. The Central Government may make rules, in consultation with the Reserve Bank of India, in connection with mergers and amalgamations provided under this section.

Section 234(2) states that subject to the provisions of any other law for the time being in force, a foreign company, may with the prior approval of the Reserve Bank of India, merge into a company registered under this Act or vice versa and the terms and conditions of the scheme of merger may provide, among other things, for the payment of consideration to the share holders of the merging company in cash, or in Depository Receipts, or partly in cash and partly in Depository Receipts, as the case may be, as per the scheme to be drawn up for the purpose. For the purposes of sub-section(2), the expression "foreign company" means any company or body corporate incorporated outside India whether having a place of business in India or not.

Section235: Power to acquire shares of shareholders dissenting from scheme or contract approved by majority

Section 235 of the Companies Act, 2013 prescribes the manner of acquisition of shares of shareholders dissenting from the scheme or contract approved by the majority shareholders holding not less than nine tenth in value of the shares, whose transfer is involved. It includes notice to dissenting shareholders, application to dissenting shareholders to tribunal, deposit of consideration received by the transferor company in a separate bank account etc.

Section 236: Purchase of minority shareholding

Section 236 prescribes the manner of notification by the acquirer (majority) to the company, offer to minority for buying their shares, deposit an amount equal to the value of shares to be acquired, valuation of shares by registered valuer, etc.

Section 237: Power of Central Government to provide for amalgamation of companies in public interest

Section 237(1) states that when the Central Government is satisfied that it is essential in the public interest that two or more companies should amalgamate, the Central Government may, by order notified in the Official Gazette, provide for the amalgamation of those companies into a single company with such constitution, with such property, powers, rights, interests, authorities and privileges, and with such liabilities, duties and obligations, as may be specified in the order.

Continuation of legal proceedings

Section 237(2) states that the order under sub-section (1) may also provide for the continuation by or against the transferee company of any legal proceedings pending by or against any transfer or company and such consequential, incidental and supplemental provisions as may, in the opinion of the Central Government, be necessary to give effect to the amalgamation.

Interest or rights of members, creditors, debenture holders not to be affected.

As per Section 237(3), every member or creditor, including a debenture holder, of each of the transferor companies before the amalgamation shall have, as nearly as may be, the same interest in or rights against the transferee company as he had in the company of which he was originally a member or creditor, and in case the interest or rights of such member or creditor in or against the transferee company are less than his interest in or rights against the original company, he shall be entitled to compensation to that extent, which shall be assessed by such authority as may be prescribed and every such assessment shall be published in the Official Gazette, and the compensation so assessed shall be paid to the member or creditor concerned by the transferee company.

Sub-section 4: Appeal to Tribunal

As per Section 237(4) any person aggrieved by any assessment of compensation made by the prescribed authority under sub-section (3) may, within a period of thirty days from the date of publication of such assessment in the Official Gazette, prefer an appeal to the Tribunal and thereupon the assessment of the compensation shall be made by the Tribunal.

Sub-section 5: Conditions for order

As per Section 237 (5) No order shall be made under this section unless —

(a) a copy of the proposed order has been sent in draft to each of the companies concerned;

(b) the time for preferring an appeal under sub-section (4) has expired, or where any such appeal has been preferred, the appeal has been finally disposed off; and

(c) the Central Government has considered, and made such modifications, if any, in the draft order as it may deem fit in the light of suggestions and objections which may be received by it from any such company within such period as the Central Government may fix in that behalf, not being less than two months from the date on which the copy aforesaid is received by that company, or from any class of share holders therein, or from any creditors or any class of creditors thereof.

Sub-section 6: Copy of order before each house of Parliament

As per Section 237(6) the copies of every order made under this section shall, as soon as may be after it has been made, be laid before each House of Parliament.

Section 238: Registration of offer of schemes involving transfer of shares

Section 238(1) states that in relation to every offer of a scheme or contract involving the transfer of shares or any class of shares in the transferor company to the transferee company under section 235, — (a) every circular containing such offer and recommendation to the members of the transferor company by its directors to accept such offer shall be accompanied by such information and in such manner as may be prescribed; (b) every such offer shall contain a statement by or on behalf of the transferee company, disclosing the steps it has taken to ensure that necessary cash will be available; and (c) every such circular shall be presented to the Registrar for registration and no such circular shall be issued until it is so registered:

Provided that the Registrar may refuse, for reasons to be recorded in writing, to register any such circular which does not contain the information required to be given under clause (a) or which sets out such information in a manner likely to give a false impression, and communicate such refusal to the parties within thirty days of the application.

Section 238(2) states that an appeal shall lie to the Tribunal against an order of the Registrar refusing to register any circular under sub-section (1).

Section 238(3) states that the director who issues a circular which has not been presented for registration and registered under clause (c) of sub-section(1), shall be liable to a penalty of one lakh rupees.

Section 239: Preservation of books and papers of amalgamated companies

As per section 239, the books and papers of a company which has been amalgamated with, or whose shares have been acquired by, another company under this Chapter shall not be disposed of without the prior permission of the Central Government and before granting such permission, that Government may appoint a person to examine the books and papers or any of them for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion or formation, or the management of the affairs, of the transferor company or its amalgamation or the acquisition of its shares.

Section 240: Liability of officers in respect of offences committed prior to merger, amalgamation, etc.

As per Section 240, notwithstanding anything in any other law for the time being in force, the liability in respect of offences committed under this Act by the officers in default, of the transferor company prior to its merger, amalgamation or acquisition shall continue after such merger, amalgamation or acquisition.

APPROVALS IN SCHEME OF AMALGAMATION

Merger or amalgamation of companies involves various issues including the regulatory approvals. These regulatory approvals are to be obtained not only from the sector in which the company is operating (for example in case of merger of two banks, RBI's approval is needed) but from other departments like Income Tax, SEBI, ROC, etc.

The companies are required to obtain following approvals in respect of the scheme of amalgamation:

(i) Authorisation

- Pre-approval authorisation about appointment of intermediaries, advisors, etc.
- Approval of Valuation Report by Audit Committee.

(ii) Approval of Board of Directors

- Approval of scheme of amalgamation by the Board of both the companies.

Board resolution should, besides approving the scheme, authorise a Director/Company Secretary/ other officer to make application to Tribunal, to sign the application and other documents and to do every thing necessary or expedient in connection therewith, including changes in the scheme.

(iii) Approval of Shareholders/Creditors, etc

Members' and creditors' approval to the scheme of amalgamation is *sine qua non* for Tribunal's sanction. This approval is to be obtained at specially convened meetings held as per Tribunal's directions [Section 230(1)]. However, the Tribunal may dispense with meetings of members/creditors [Section 230(9)].

The scheme of compromise or arrangement has to be approved as directed by the Tribunal, by–

- the members of the company; or
- the members of each class, if the company has different classes of shares; and the creditors; or
- each class of creditors, if the company has different classes of creditors.

The approval of the members and creditors (or each class of them) has to be obtained at specially convened meetings as per the Tribunal directions. An application seeking directions to call, hold and conduct meetings is made to the Tribunal, which has jurisdiction having regard to the location of the registered office of the company. The steps include:

- First motion petition before the Tribunal
- Scrutinizers report about the approval by the shareholders/creditors, etc.
- Second motion petition before the Tribunal
- Notices should be sent to various stakeholders, public inviting any objections to the scheme.

(iv) Approval of the Stock Exchanges

A listed entity desirous of undertaking a scheme of arrangement or involved in a scheme of arrangement, shall file the draft scheme of arrangement, proposed to be filed before Tribunal with the stock exchange(s).

(v) Approval of Financial Institutions

The approval of the Financial Institutions, trustees to the debenture holders and banks, investment corporations would be required if the Company has borrowed funds either as term loans, working capital requirements and/ orhave issued debentures to the public and have appointed any one of them as trustees to the debenture holders.

(vi) Approval from the Land Holders

If the land on which the factory is situated is the lease-hold land and the terms of the lease deed so specifies, the approval from the lessor will be needed.

(vii) Approval of the Tribunal

- Both companies (amalgamating as well as amalgamated) involved in a scheme of compromise or arrangement or reconstruction or amalgamation is required to seek approval of the respective Tribunal for sanctioning the scheme.
- Every amalgamation, except those, which involve sick industrial companies, requires sanction of Tribunal which has jurisdiction over the State/area where the registered office of a company is situated.
- If transferor and transferee companies are under the jurisdiction of different Tribunals, separate approvals are necessary.
- The notice of every application filed with the Tribunal has to be given to the Central Government (Regional Director, having jurisdiction of the State concerned).
- After the hearing is over, the Tribunal will pass an order sanctioning the Scheme of amalgamation, with such directions in regard to any matter and with such modifications in the Scheme as the Judge may think fit to make for the proper working of the Scheme. [Section 230; Rule 5, Companies (Compromises, Arrangements and Amalgamations) Rules, 2016].

The Tribunal under Section 230-234 of the Act is also empowered to order the transfer of undertaking, property or liabilities either wholly or in part, allotment of shares or debentures and on other supplemental and incidental matters.

(viii) Approval of Reserve Bank of India

Where the scheme of amalgamation envisages issue of shares/cash option to Non-Resident Indians, the amalgamated company is required to obtain the permission of Reserve Bank of India subject to conditions prescribed under the Regulations issued by RBI.

(ix) Approvals from Competition Commission of India (CCI)

The provisions relating to regulation of combination as provided under Sections 5 and 6 of the Competition Act, 2002 would also be required to be complied with by companies, if applicable.

FILING REQUIREMENTS IN THE PROCESS OF MERGER/AMALGAMATION

The following forms, reports, returns, etc. are required to be filed with the Registrar of Companies, SEBI and Stock Exchanges at various stages of the process of merger/amalgamation:

1. (a) when the objects clause of the memorandum of association of the transferee company is altered to provide for amalgamation/merger, for which special resolution is passed;

   (b) the company's authorised share capital is increased to enable the company to issue shares to the shareholders of the transferor company in exchange for the shares held by them in that company for which a special resolution for alteration of its articles is passed;

   (c) a special resolution is passed to authorise the Company's Board of Directors to issue shares to the shareholders of the transferor company in exchange for the shares held by them in that company; and

   (d) a special resolution authorizing the transferee company to commence the business of the transferor company or companies as soon as the amalgamation/merger becomes effective; the company should file with ROC within thirty days of passing of the aforementioned special resolutions in the prescribed e-form. The following documents should be annexed to the said e-form: (i) certified true copies of all the special resolutions; (ii) certified true copy of the explanatory statement annexed to the notice for the general meeting at which the resolutions are passed, for registration of the resolution. This e-form should be digitally signed by Managing Director/Director/Manager or Secretary of the Company duly authorized by Board of Directors. This e-form should also be certified by Company Secretary or Chartered Accountant or Cost Accountant (in whole time practice) by digitally signing the e-form.

2. In compliance with the listing regulations, the transferee company is required to give notice to the stock exchanges where the securities of the company are listed, of the Board meeting called for the purpose of discussing and approving amalgamation.

3. In compliance with the listing regulations, the transferee company is required to give intimation to the stock exchanges where the securities of the company are listed, of the decision of the Board approving amalgamation and also the swap ratio, before such information is given to the shareholders and the media.

4. The transferee company is required to file with the Registrar of Companies, INC-28 along with a certified copy of the Tribunal's order on summons directing the convening and holding of meetings of equity shareholders/ creditors including debentures holders etc. as required under Section 230 of the Companies Act. This e-form should be digitally signed by the Managing Director or Director or Manager or Secretary of the Company duly authorized by the Board of Directors. However, in case of foreign company, the e-form should be digitally signed by an authorized representative of the company duly authorized by the Board of Directors.

   The original certified copy of the Tribunal order is also required to be submitted at the concerned ROC office simultaneously while filing INC-28, failing which the filing will not be considered and legal action will be taken.

5. In compliance with the listing regulations, the transferee company is required to simultaneously furnish to the stock exchanges where the securities of the company are listed, copy of every notice, explanatory statement, minutes of the meeting etc. sent to members of the company in respect of a general meeting in which the scheme of arrangement of merger/amalgamation is to be approved.

6. The transferee company is required to file with the Central Government notice of every application made to the Tribunal under Section 230 to 240 of the Companies Act, 2013. No notice need be given to the Central Government once again when the Tribunal proceeds to pass final order to dissolve the transferor company.

7. To file with the Registrar of Companies within thirty days of allotment of shares to the shareholders of the transferor company in lieu of the shares held by them in that company in accordance with the shares exchange ratio incorporated in the scheme of arrangement for merger/amalgamation, the return of allotment along with the prescribed filing fee as per requirements of the Act. This e-form should be digitally signed by Managing Director or Director or Manager or Secretary of the Company duly authorised by the Board of Directors. The e-form should also be certified by Company Secretary or Chartered Accountant or Company Secretary (in whole time practice) by digitally signing the e-form.

STEPS INVOLVED IN MERGER/AMALGAMATION

STEP – 1

Holding of Board Meeting

- To consider the proposal for Merger of the Company. It must be ensured that the companies under the consolidation must have a strong clause in the Memorandum of Association of their organization to merge although their absence will not be an obstacle, but this will make things work smoothly.

- In-Principle approval for Merger
- Decide on jurisdiction of NCLT Benches
- Appointment of Registered Valuer
- Appointment of professionals such as chartered accountant in practice, consultants, lawyers etc
- Consultants to structure the Roadmap and draft the restructuring Scheme.

STEP – 2

Holding of Independent Directors Committee Meeting

- Report from the Committee of Independent Directors recommending the draft Scheme, taking into consideration, inter alia, that the scheme is not detrimental to the shareholders of the listed entity.

Holding of Audit Committee Meeting

- Valuation Report to be placed before Audit Committee.
- Audit Committee to give its recommendation on Draft scheme/ Share Entitlement Ratio, taking into consideration the Valuation Report.
- The Audit Committee report shall also comment on the following:
  - Need for the merger/demerger/amalgamation/arrangement
  - Rationale of the scheme
  - Synergies of business of the entities involved in the scheme
  - Impact of the scheme on the shareholders
  - Cost benefit analysis of the scheme.

Holding of Second Board Meeting

- Approval of Exchange Ratio
- Approval of Valuation Report
- Approval of Scheme of Arrangement
- Public Co. to file copy of Board Resolution with ROC [Section 117(3) (g) read with Section 179(3) (i)]
- Authorisations to sign documents, make representation and enter appearances
- File copy of scheme with ROC [Section 232(2)(b)]
- In-Principle approval of Sock Exchange
- Consider the Fairness Opinion of the Merchant Banker
- Accept the recommendation of Audit Committee
- Choose one of the Stock Exchange having nation-wide trading terminals as the Designated Stock Exchange.

STEP 3 – Filings, Intimations and Website Updations

- Intimation to Stock Exchange on the decision of the Board within 24 hours of the meeting
- Filing of Form No. MGT-14 to ROC in accordance with Section 179 of the Companies Act, 2013 within 30 days
- Company to submit the Draft Scheme along with documents to Stock Exchange in accordance with Regulation 37 of SEBI (LODR) Regulations, 2015, Simultaneously, the company shall upload all the following documents filed with Stock Exchange on its website;
  - (a) Draft Scheme of arrangement/ amalgamation/ merger/ reconstruction/ reduction of capital, etc.;
  - (b) Valuation Report;
  - (c) Report from the Audit Committee recommending the Draft Scheme, taking into consideration, inter alia, the Valuation Report. The Valuation Report is required to be placed before the Audit Committee of the listed entity;
  - (d) Fairness opinion by a SEBI Registered merchant banker on valuation of assets / shares done by the valuer for the listed entity and unlisted entity;
  - (e) Pre and post amalgamation shareholding pattern of unlisted entity;
  - (f) Audited financials of last 3 years (financials not being more than 6 months old) of unlisted entity;
  - (g) Auditor's Certificate;
  - (h) Detailed Compliance Report duly certified by the Company Secretary, Chief Financial Officer and the Managing Director.
- Any complaints received by the Company (i.e. Directly or Indirectly through Stock Exchange/SEBI) shall be submitted by company as 'Complaints Reports' to the stock exchanges within 7 days of expiry of 21 days from the date of filing of Draft Scheme with Stock Exchange(s).
- In case of unpaid dues / fines / penalties, the listed entity shall submit to stock exchanges a 'Report on the Unpaid Dues' which shall contain the details of such unpaid, prior to obtaining Observation Letter from stock exchanges on the draft scheme. The report on unpaid dues, shall be submitted by listed entity to the stock exchanges along with the draft scheme.

STEP 4 – FIRST MOTION APPLICATION

Preparation and filing of first motion application:

- Consent letter of shareholders and creditors by way of affidavit.
- Certificate from Chartered Accountant certifying creditors.
- Certification from auditors to the effect that the accounting treatment is in conformity with accounting standards [proviso to sec. 230(7) read with proviso to sec. 232 (3) of CA, 2013]
- Drafting of First Motion Application (NCLT 1), Notice of Admission (NCLT 2) & Affidavit (NCLT 6) - pray for dispensation of meeting.
- No dispensation- order for individual notices to the shareholders/creditors
- Copy of the scheme of compromise or arrangement
- Creditors responsibility statement (Form CAA 1) in case a compromise or arrangement is proposed between company and its creditors or between company and its members
- Advertisement in Newspaper (Form CAA-2).

Contents of First Motion Application

- Details of the Companies.
- Jurisdiction of NCLT Bench.
- Limitation
- Fact of the case including benefit, rationale, etc.
- Relief & prayer (Dispensation) – Specific prayer regarding dispensation for each meeting (in the matter of JVA Trading Private Limited)
- Relief & payer (Meeting) - Direction for service of notice, approval of Newspaper for advertisement.

Documents/ Annexure(s) to First Motion Application

Documents/ Annexures includes:

a) Memo of parties/Brief synopsis

b) Joint application

c) Affidavit verifying application

d) Board Resolution of all the Companies

e) Certificate from Chartered Accountants

f) Certificate from Auditors

g) Audited and/or unaudited financial statement of all the Companies

h) Memorandum and Article of Association of all the Companies

i) List of shareholders of all the companies along with their consent/NOC by way affidavits.

j) List of Creditors (Secured, unsecured).

k) Scheme of Arrangement

l) Copy of valuation Report

m) List of directors

n) Memorandum of Appearance & power of Attorney / Vakalatnama

o) Notice of Admission in NCLT 2.

STEP 5 - NCLT will give order on the application of the company on the following:

(a) Date, time and venue of the meeting

(b) Appointment of the Chairman

(c) Time within which the Chairman of the meetings will give his report

(d) Dispensation of meeting for the unlisted Company

The order of the Tribunal shall be filed with the Registrar by the company within a period of 30 days of the receipt of the order.

STEP 6- Notice of First Motion Application

No dispensation – Notice of meeting of arrangement or compromise shall be given to:

- Shareholders & Creditors
- Central Government
- Income Tax Authorities
- Reserve Bank of India
- Securities and Exchange Board of India
- The Registrar
- Official Liquidator
- Competition Commission of India
- Advertisement in Newspaper (Form CAA-2).

The notice to statutory authorities shall be in Form CAA 3 and shall be accompanied with a copy of the scheme of compromise or arrangement, the explanatory statement and the prescribed disclosures

STEP 7 – Holding of Meeting

Process of Meeting

- Court appointed Chairman/ Alternate Chairman to preside over.
- Quorum, as decided by the Tribunal.
- Public shareholders consent by Postal Ballot (Listed Co.) and through e-voting (if required) as per SEBI norms
- Scrutinizer, as appointed by the Tribunal
- Report of the Scrutinizer to the Chairman
- Report of the Chairman to be filed with Tribunal within the time fixed by the tribunal, or where no time has been fixed, within three days after the conclusion of the meeting submit a report to the Tribunal on the result of the meeting in Form CAA 4

STEP 8- Filing of Second Motion application

Where the proposed compromise or arrangement is agreed to by the members or creditors or both as the case maybe with or without modification, the company (or its liquidator), shall:

- Within 7 days of receipt of certified true copy of order of NCLT and / or filing of report by the Chairperson, as the case may be, the second motion petition must be filed in Form CAA.5 for sanction of the scheme praying for appropriate orders and directions under section 230 read with section 232 of the Companies Act, 2013 [Rule 15 of the Companies (Compromise, Arrangement and Amalgamation) Rule, 2016]
- Where the company fails to present the petition for confirmation of the compromise or arrangement as aforesaid, it shall be open to any creditor or member as the case may be, with the leave of the tribunal, to present the petition and the company shall be liable for the cost thereof.

STEP 9- Hearing on admission of Second Motion

- NCLT shall fix a date of hearing of the petition, and
- Order to advertise the notice of hearing in such newspaper as the NCLT may think fit, not less than 10 days before the date of hearing of petition [Rule 16 of the Companies (Compromise, Arrangement and Amalgamation) Rule, 2016]

Publish the advertisement in Form NCLT-3A, place the same on the Website, if any and file an affidavit of compliance in relation to the same, not less than 3 days before the fixed for hearing [Rule 35 of the National Company Law Tribunal Rules, 2016].

STEP 10- Approval of Regulatory Authorities

- Filing of First motion, second motion along with notice with all the authorities.
- Report of ROC to office of Regional Director.
- Query letter and its reply to office of Regional Director
- Query letter and its reply to office of official Liquidators
- Report of RD and OL to be filed with Tribunal.

STEP 11- Final Hearing

- NCLT may, if it thinks fit, sanction the scheme and pass anOrder in Form CAA 7, with such variations as the circumstance may require.

The order shall direct that a certified copy of the same shall be filed with the registrar of companies within 30 days from the date of the receipt of copy of the order, or such other time as maybe fixed by the tribunal.

STEP 12- Filing with Scheme & other Compliance

- Board Meeting to take note of the Copy of Order, fixation of records date and board meeting of Resulting Company for allotment of shares to the members of Demerged Company
- File the certified true copy of order of NCLT with ROC in From INC-28, within 30 days from the date of the receipt of certified true copy of order [Section 232(5) of the Companies Act, 2013]
- Filing of Form PAS 3, SH. 7
- Change of Name, Conversion, Consolidation of share, reclassification of share, reduction of share, if any
- Dispatch of Share Certificates to the allottees or entering the name of allottees as beneficial owner in the records of depositories
- Apply to Stock Exchange for Listing of Shares of Resulting Company within 30 Days of Receipt of Order of the NCLT sanctioning the Scheme;
- Before commencement of Trading, advertisement is required to be given in one Hindi and one English newspaper having nationwide circulation and one regional newspaper with the wide circulation at the place where the registered office of the Resulting Company is situated
- Formalities for commencement of trading shall be completed within 45 Days of the order of NCLT

STEP 13: Certification of Compliance of Scheme

- A statement (Form CAA 8) is to be filed with Registrar in regard to compliance of scheme in accordance with the orders of the Tribunal every year until the scheme is fully implemented.
- It must be certified by a chartered accountant or a cost accountant or a company secretary in practice indicating whether the Scheme is being complied in accordance with the orders of the Tribunal or not.

REVISED ORGANIZATION CHART

One modification that has great potential to affect the new business is a change in the organizational structure. Regardless of whether the changes are large or small, planningand an intense analysis are vital to creating a decision-making and communication framework that will support post-merger objectives and help the new business grow.

Structural Change Considerations

An organizational structure refers to the levels of hierarchy, chain of command, management systems and job structures and roles. In response to a merger, duplicate departments need to be merged or eliminated, and at least some employees from both companies will either transfer to new positions or leave the company. Communication patterns will typically change as managers acquire new employees and everyone adapts to changes in policies and procedures designed to fit the new company.

Premerger Due Diligence

Review the organizational structures of both businesses to see how well each compares to the mission and long-term objectives for the new company. Analyze hierarchies and reporting relationships to see where the existing structures clash and where they're synchronized. Once an initial review is completed, appoint an integration team to speak with core employees and get their perspective on what works and what doesn't work in their respective structures. Make preliminary decisions about which features best support the new business.

Structural Change Options

Organizational structure change options include starting from scratch, eliminating one in favor of the other and combining the best features of both structures into one. Which is the best option depends on the size, complexity and objectives of the new business. For example, two small businesses with flat organizational structures may need to convert to a more hierarchical and organized structure that allows for greater internal controls and division of responsibilities. It is also useful when the owners or chief executive officer delegates some decision-making responsibilities.

The Three Phases of Change

Changing an organizational structure due to a merger involves much more than creating a new organizational chart. Although the chart will reflect decisions made about how the new business's employees will communicate with one another and make decisions, this typically occurs in multiple phases. The first phase is awareness, during which employees from both businesses come to understand the new company's direction and what it will mean to them. The goal of the second phase is acceptance, as the integration team works to build new relationships and employees at every level transition into new roles and new ways of getting work done. In the final phase, the merger is complete and the new organizational structure becomes fully adopted.

For example in merger of the associate banks of SBI with that of the State Bank of India, some of the branches of the erstwhile associate banks were allowed to shift to other places or closed down. Further the Administrative offices/ Regional offices were also reorganized since these offices of the merged bank lost their identity and the authority of the existing Regional/ Zonal Offices of the acquiring bank were expanded to have control over more branches or realigned. Similarly apart from the relocation of the branches and regional/zonal offices, the authority and responsibility of the middle level and higher level officers were also realigned and tuned with the requirement after the merger.

EMPLOYEE COMPENSATION, BENEFITS AND WELFARE ACTIVITIES

Employee's compensation in the two companies varies. For example in the case of merger between the Bank of Rajasthan Ltd. (BoR) and the ICICI Bank Ltd which was held in 2010, the BoR employees were aligned with the Indian Bank Association (IBA), while the ICICI Bank was having its own compensation and not linked with the IBA compensation policy. In order to have consistency in compensation policy the merged bank employees were forced to adopt the compensation policy of the acquiring bank.

Whatever the strategy is adopted, companies need to be sensitive with regard to terms and conditions of employment. Usually, courts would uphold terms of employment to be no less favorable than existing terms and conditions. Post-acquisition, the parent company may want the acquired company to adopt compensation structure of the parent entity. It would result in re-aligning the structure as well as pay scales of existing employees.

ALIGNING COMPANY POLICIES

After merger the merged entity is usually forced to adopt the policies of the merging company. The accounting software and policies of the amalgamating companies are to be aligned with that of the amalgamated company in a phased manner. For example in the case of the merger of the two banking companies, the acquiring bank imposes its accounting software (like Finacle) on the merged bank and also various policies like Deposit Policy, Loan Policy, Recovery & Compromise Policy, etc. in order to have uniformity in serving the customers. However if the products of the erstwhile (merged) entity is good enough, the same are allowed to be continued till the conclusion of the scheme. For example, at the time of the merger of the Bank of Rajasthan Ltd (BoR) with ICICI Bank Ltd, the customers of the BoR were charged for the same service charges for some time and allowed to continue with some of the product schemes as per the sanction terms and conditions, in order to win the customer's confidence in the acquiring bank too.

ALIGNING ACCOUNTING AND INTERNAL DATABASE MANAGEMENT SYSTEMS

Besides passing appropriate accounting entries to capture the merger/ acquisition/ financial structure, the company may need to adopt accounting policies, practices based on those followed by its new parent organization post acquisition. The company needs to understand any reporting and database requirements of acquiring company or merged entity to provide relevant data to the new management and to align existing systems with those of the parent/ merged entity. This may involve providing suitable training to concerned personnel and understanding issues, if any, to avoid incorrect reporting.

RECORD KEEPING

Preservation of books and papers of amalgamated companies: Section 239 provides that the books and papers of a company which has been amalgamated with, or whose shares have been acquired by, another company shall not be disposed of without the prior permission of the Central Government and before granting such permission, that Government may appoint a person to examine the books and papers or any of them for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion or formation, or the management of the affairs, of the transferor company or its amalgamation or the acquisition of its shares.

Maintenance of records of merging entity and making suitable entries in the records (e.g. registers under Companies Act reflecting changes in shareholding, directors etc. as applicable) of merged entity is a must. One will need to dive deep to ensure maintenance of all past records including statutory and non-statutory registers, original copies of various forms, returns, certificates, approvals, litigation and property records. Company may need to relocate the records to centralized storage maintained by the merged/new entity.

INTEGRATION OF BUSINESSES AND OPERATIONS

The integration of business and operations after merger is the crucial part and many points require attention on the issue. These may be list out as under:

- Assessment of the future cash flow generation in order to have organic growth after having gone through the process of inorganic growth.
- Integration of the accounting software, accounting policy.
- Integration of various other software.
- The customer retention of the merged entity and acquisition of more customers.
- Satisfaction of the human resources and retaining of the talent.

POST-MERGER SUCCESS AND VALUATION

Every merger is not successful. The factors which are required to measure the success of any merger are briefly discussed below:

- The earning performance of the merged company can be measured by return on total assets and return on net worth. It has been found that the probability of success or failure in economic benefits was very high among concentric mergers. Simple vertical and horizontal mergers were found successful whereas the performance of concentric mergers was in between these two extremes i.e. failure and success.
- Whether the merged company yields larger net profit than before, or a higher return on total funds employed or the merged company is able to sustain the increase in earnings.
- The capitalisation of the merged company determines its success or failure. Similarly, dividend rate and payouts also determines its success or failure.
- Whether merged company is creating a larger business organisation which survives and provides a basis for growth.
- Comparison of the performance of the merged company with the performance of similar sized company in the same business in respect of (i) Sales, (ii) assets, (iii) net profit, (iv) earning per share and (v) market price of share. In general, growth in profit, dividend payouts, company's history, and increase in size provides base for future growth and are also the factors which help in determining the success or failure of a merged company.
- Fair market value is one of the valuation criteria for measuring the success of post merger company. Fair market value is understood as the value in the hands between a willing buyer and willing seller, each having reasonable knowledge of all pertinent facts and neither being under pressure or compulsion to buy or sell. Such valuation is generally made in pre-merger cases.
- In valuing the whole enterprise, one must seek financial data of comparable companies in order to determine ratios that can be used to give an indication of the company position. The data is analyzed to estimate reasonable future earnings for the subject company. The following information must be made available and analyzed for post-merger valuation:
  - All year-end balance sheets and income statements, preferably audited, for a period of five years and the remaining period up to the valuation date.
  - All accounting control information relating to the inventory, sales, cost, and profit contribution by product line or other segment; property cost and depreciation records; executives and managerial compensation; and corporate structure.
  - All records of patents, trademarks, contracts, or other agreements.
  - A history of the company, including all subsidiaries.

Analysis of these items provides data upon which forecasts of earnings, cash flow, etc. can be made.

- Gains to shareholders have so far been measured in terms of increase or decrease in share prices of the merged company. However, share prices are influenced by many factors other than the performance results of a company. Hence, this cannot be taken in isolation as a single factor to measure the success or failure of a merged company.
- In some mergers there is not only increase in the size of the merged or amalgamated company in regard to capital base and market segments but also in its sources and resources which enable it to optimize its end earnings.
- In addition to the above factors, a more specific consideration is required to be given to factors like improved debtors realisation, reduction in non-performing assets, improvement due to economies of large scale production and application of superior management in sources and resources available relating to finance, labour and materials.

HUMAN AND CULTURAL ASPECTS

Human Aspects: The merger and acquisition in the corporate world is a common phenomenon. It may be the horizontal merger or vertical merger. A horizontal merger decreases competition in the market, while vertical merger is a merger between companies in the same industry, but at different stages of production process. However the most neglected part in the merger story is the human aspect. The employees of the amalgamated entity face secondary treatment in the amalgamating company. They are harassed, transferred recklessly and demoted one or two scale lower, which leads to frustration and are forced to take voluntary retirement. In this way the company losses the good employees too. The merger of the Bank of Rajasthan Ltd with ICICI Bank Ltd and the Associate Banks of State Bank of India with the State Bank of India are good examples, in which many of the employees of the merged entities have opted the voluntary retirement.

Cultural Aspects: Apart from the human aspects the cultural issue in the case of merger is also a crucial issue. Integration of the employees accustomed of different cultural background is a typical aspect. Implementation of structural nature may be financially and legally successful. But if cultural issues are ignored, the success may only be transient. Culture of an organisation means the sum total of things the people do and the things the people do not do. Behavioural patterns get set because of the culture. These patterns create mental blocks for the people in the organization. Pre-merger survey and summarization of varying cultures of different companies merging, needs to be carried out. People belonging to the each defined culture need to be acquainted with other cultures of other merging companies. They need to be mentally prepared to adopt the good points of other cultures and shed the blockades of their own cultures. Such an open approach will make the fusion of cultures and ethos easy and effective.

MEASURING POST-MERGER EFFICIENCY

The criterion to judge a successful merger differs in different conditions. Different factors may be considered for making value judgements such as growth in profit, dividend, company's history, increase in size, base for growth, etc. Several studies suggest different parameters to assess the success of mergers:

- Successful merger creates a larger industrial organization than before, and provides a basis for growth [Edith Perirose].
- In Arthur Dewing's study, three criteria were considered viz. (a) merger should give a larger net profit than before (b) merger should provide a higher return on total funds (c) there should be a sustained increase in earnings.
- Earnings on capitalization and dividend records determine the success of merger [Shaw L.].

During the studies in late 1960s, two types of efficiency improvements were expected to result from mergers:

(1) Improvements due to economies of large scale production

(2) Application of superior management skills to a larger organisation. Some other researches in the seventies and eighties, measure efficiency based on stock market measures, labour productivity or total factor productivity, etc. These improvements pointed towards market dominance, but for gauging efficiency, resultant profitability was accepted as a benchmark. In order to ensure progress, a conscious and concerted effort to keep track of several key elements is required, along with answers to the following questions:

1. What impact is the integration (merger/acquisition) having on key indicators of business performance? Whether synergies which were hypothesized during the valuation are being realized?
2. Are the activities and milestones developed with the integration process on target?
3. What are the major issues emerging during the integration, requiring considerable attention?
4. What important facts have emerged during the merger or acquisition that can be used to improve subsequent mergers or acquisition?

MEASURING KEY INDICATORS

The main purpose of a merger or acquisition is to deliver the expected financial results namely earnings and cash flow. However, there are certain other measures that serve as key indicators and they also need to be measured. The indicators may be grouped as:

i. Financial outcomes.

ii. Component measures of these outcomes namely revenues, costs, net working capital and capital investments.

iii. Organisational indicators such as customers, employees and operations.

All the areas being integrated and both the acquirer and target, or in a merger, both partners, should be brought within the ambit of continuous appraisal. Also, the appraisal should be based on benchmarks to ensure that merger or acquisition are yielding the financial and strategic objective so intended and are not resulting in value leakage.

There are broadly four possible reasons for business growth and expansion which is to be achieved by the merged company. These are (1) Operating economies, (2) Financial economies, (3) Growth and diversification, and (4) Managerial effectiveness.

LESSON ROUND-UP

- Chapter XV, comprising of sections 230 to 240 of the Companies Act, 2013 read with the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016, deals with Compromises, Arrangements and Amalgamations.
- Section 230 is relating to the power of the company to compromise or to make arrangement with its creditors and members.
- Section 230(2) deals with regard to information as to compromises and arrangements with creditors and members.
- Section 232 deals with facilitation of merger and amalgamation of companies.
- Sections 235-236 deal with provisions regarding the power and duty to acquire shares of shareholders dissenting from scheme or contract approved by majority shareholders.
- Section 237 contains provisions as to the power of the central government to provide for amalgamation of companies in national interest.
- Merger or amalgamation of companies involves various issues including the regulatory approvals. These regulatory approvals are to be obtained not only from the sector in which the company is operating (for example in case of merger of two banks, RBI's approval is needed) but from other departments like Income Tax, SEBI, ROC, etc.
- Due diligence is an investigation of a business or person prior to signing a contract, or an act with a certain standard of care. It can be a legal obligation, but the term will more commonly apply to voluntary investigations.
- General principles of Business Valuation are: Principle of Time Value of Money, Principle of Risk and Return, Principle of Substitution, Principle of Alternatives, Principle of Reasonableness.
- The most popular methods of valuation amongst other include Asset based valuation, Earnings based valuation and Market based valuation. Other aspects as to the Methods of Valuation are Relative Method, Super Profit Method, Contingent Claim Method, and Accounting Professionals Experts.
- 'Post-merger reorganization' is a wide term which encompasses the reorganization of each and every aspect of the company's functional areas to achieve the objectives planned and aimed at.

- There are broadly four possible reasons for business growth and expansion which is to be achieved by the merged company. These are (1) Operating economies, (2) Financial economies, (3) Growth and diversification, and (4) Managerial effectiveness.
- Human and cultural integration is central to the success of any merger.
- The earning performance of the merged company can be measured by return on total assets and return on net worth.
- In general, growth in profit, dividend pay-outs, company's history and increase in size provides the base for future growth and are also the factors which help in determining the success or failure of a merged company.

GLOSSARY

Merger : An amicable involvement of two or more companies to form one unit, and to increase overall efficiency. The shareholders of merged companies are offered equivalent holdings in the new company.

Amalgamation : The joining of one or more companies into a new entity. None of the combining companies remains; a completely new legal entity is formed.

Offer Price : The price offered per share by the acquirer.

Share Exchange Ratio : The offer price divided by the acquirer's share price.

Synergy : Cost savings and revenue enhancements that are expected to be achieved in connection with a merger/acquisition.

TEST YOURSELF

(*These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation*)

1. Write a detailed note on the merger and acquisition provisions contained in the Companies Act, 2013 and its relevant rules.
2. Describe the regulatory authorities from whom the approvals are to be taken in case of merger/amalgamation and its process.
3. Discuss the role of Tribunal in approving a scheme of reconstruction or restructuring under Sections 230-240 of the Companies Act, based on decided cases from the standpoint of shareholders and employees.
4. ABC & Co (P) Ltd. and XYZ Ltd. have finalized a scheme of arrangement. The registered offices of both the companies are located in Delhi. A joint-petition is proposed to be filed before the Tribunal for sanction of the scheme.

   Give your brief opinion in the light of the provisions of the Companies Act, 2013 and the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 whether such a joint-petition can be filed.
5. What do you understand by Due Diligence? Mention the types of due diligence and what should be the contents of the due diligence report?

LIST OF FURTHER READINGS

- Guide to Companies Act by A Ramaiya, Lexis Nexis Butterworths
- The Companies Act, 2013 with Rules and Ready Referencer by S K Kataria, Bloomsbury Publication
- Guide to Takeovers and Mergers by Sridharan and Pradhan, Wadhwa & Co.

Documentation – Merger & Amalgamation

Lesson 5

KEY CONCEPTS

■ National Company Law Tribunal ■ Documentation ■ Effective Date ■ Transferee Company ■ Transferor Company

Learning Objectives

To understand:

- Stages Involved in Mergers and Amalgamation
- Legal Provisions of Mergers and Amalgamation
- Documentation in Mergers and Amalgamation
- Drafting of Scheme of amalgamation
- Statement of compliance in Mergers and Amalgamations

Lesson Outline

- Documentation in M&A
- List of documents filed in case of a scheme of amalgamation
- Merger and Amalgamation process at National Company Law Tribunal
- Drafting of Scheme
- Drafting of Notice
- Drafting of Explanatory Statement
- Drafting of Application and Petition
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

- The Companies Act, 2013
- The Companies (Compromises, Arrangements and Amalgamations) Rules, 2016
- The National Company Law Tribunal Rules, 2016

INTRODUCTION

Documentation is an important aspect in fulfillment of legal requirements and obligations in merger and amalgamation for an effective and successful venture. The quantum of such obligations will depend upon the size of company, debt structure and profile of its creditors, compliances under the corporate laws, controlling regulations, etc. In all or in some of these cases legal documentation would be involved. If foreign collaborators are involved, their existing agreements would need a mandatory documentation to protect their interests if their terms and conditions so require. Secured debenture holders and unsecured creditors would also seek legal protection to their rights with new or changed management of the amalgamating company. Regulatory bodies like the RBI, Stock Exchanges, the SEBI, etc. would also ensure adherence to their respective guidelines, regulations or directives. In this way, while drafting the scheme of merger and amalgamation the transferor and transferee would have to ensure that they meet legal obligations in all related and requisite areas.

> Where a compromise or arrangement is proposed for the purposes of or in connection with scheme for the reconstruction of any company or companies, or for the amalgamation of any two or more companies, the petition shall pray for appropriate orders and directions under section 230, 231 and section 232 of the Companies Act 2013.

STAGES INVOLVED IN MERGERS AND AMALGAMATION UNDER THE COMPANIES ACT, 2013

In brief, it can be said that there are broadly eight stages involved in merger and amalgamation, which are listed below:

Stage 1 – Drafting of the Scheme

Stage 2 – Obtaining the approval of the Board of Directors of the companies involved

Stage 3 – Obtaining approval of the stock exchanges in case of listed companies

Stage 4 – Application / Petition for convening the meeting of members/creditors shall be filed with National Company Law Tribunal

Stage 5 – Convening meetings of the Shareholders and Creditors and obtaining their consent on

Stage 6 – Scheme Approvals or No objection from Regional Director / Official Liquidator

Stage 7 – Filing of final petition with NCLT for approving the Scheme

Stage 8 – Obtaining order for approval for scheme of merger/amalgamation from the National Company Law Tribunal.

A sample scheme of merger has been annexed to this Lesson as **Annexure A** for better understanding.

List of Documents filed in case of a scheme of amalgamation

In this case there are two companies to the amalgamation, i.e., the Transferor (1st Applicant) and the Transferee (2nd Applicant)

S. No.	Document
1.	Memorandum and Articles of Association of the First Applicant Company
2.	Audited Balance Sheet of the First Applicant Company – latest
3.	Board Resolution for approval and authorization of the scheme by the First Applicant Company
4.	List of Equity Shareholders of the First Applicant Company
5.	Consent Affidavits filed by the Equity Shareholders of the First Applicant Company
6.	Auditors Certificate stating out the no. of Secured Creditors in the First Applicant Company
7.	Auditor's Certificate listing out the no. of Unsecured Creditor in the First Applicant Company
8.	Consent Affidavit filed by no. of Unsecured Creditor of the First Applicant Company
9.	Auditors Certificate of the 1st Applicant Company in relation to the accounting treatment proposed in the Scheme of Amalgamation
10.	Memorandum and Articles of Association of the Second Applicant Company
11.	Audited Balance Sheet of the Second Applicant Company
12.	Board Resolution for approval and authorization of the Scheme by the Second Applicant Company
13.	List of Equity Shareholders of the Second Applicant Company
14.	Auditors Certificate listing out the no. of Secured Creditors in the Second Applicant Company
15.	Consent Affidavit filed by the no. of Secured Creditor of the Second Applicant Company
16.	Auditors Certificate listing out the no. of Unsecured Creditors in the Second Applicant Company
17.	Consent Affidavit filed by the no. of Unsecured Creditor of the Second Applicant Company
18.	Auditors Certificate of the 2nd Applicant Company in relation to the accounting treatment proposed in the Scheme of Amalgamation
19.	Certificate of the Chartered Accountant for Non-Applicability of obtaining a Valuation Report
20.	Fairness Opinion issued by the Merchant Banker on the Scheme of Amalgamation
21.	Undertaking regarding the Non-Applicability of paragraph I(A) 9(a) of Annexure I of SEBI Circular No. CIR/CFD/CMD/16/2015 dated 30 November 2015
22.	Observation Letter issued by the Stock Exchanges approving the Scheme of Amalgamation
23	Scheme of Amalgamation.

Merger and Amalgamation process at National Company Law Tribunal (NCLT)

It must be ensured that the companies under amalgamation have a clause in the object clause of their Memorandum of Association to undergo amalgamation though the absence may not be an impediment, but this will make matters smooth. A draft scheme of amalgamation shall be prepared for getting it approved in Board meeting of each company.

Persons eligible for filing the petition before NCLT

1. An application for merger & amalgamation shall be filed with Tribunal (NCLT) by both the transferor(s) and the transferee company in the form of petition under section 230-232 of the Companies Act, 2013 for the purpose of sanctioning the scheme of amalgamation.

2. Where more than one company is involved in a scheme, such application may, at the discretion of such companies, be filed as a joint-application.

In case, the registered office of the companies involved is in different states, there will be two Tribunals having the jurisdiction over those. Both the companies shall have to file separate petition with the respective Tribunals. However as a matter of practice and smother the process, first registered office of companies may be shifted as per section 12 of the Companies Act, 2013 to a single jurisdiction.

(1) Drafting of Scheme

The Scheme of amalgamation would comprise of various parts containing details about Transferor Company, Transferee Company. The Scheme in particular would comprise of the following in detail:

Introductory Part

1. Basic Details of the Transferor & Transferee company like date of incorporation, CIN and registered office and address for service of notice
2. Main objects in Memorandum of Association of Transferor and Transferee Company
3. Jurisdiction of the Bench
4. Limitation
5. Facts of the case - reason in brief for going into merger or amalgamation
6. Nature of business
7. Share Capital of the companies involved and shareholding relationship between the companies involved
8. Definition Clause

Operating Part – The Scheme

9. Appointed Date - The scheme shall clearly indicate an appointed date from which it shall be effective and the scheme shall be deemed to be effective from such date and not at a date subsequent to the appointed date.
10. Transfer of the undertaking of the Transferor Company or transfer of the Transferor Company *per se*
11. Transfer of assets
12. Transfer of debts and liabilities
13. Transfer of licenses, approvals / permissions
14. Transferor of Company's staff, workmen and employees
15. The transfer of undertaking or the Transferor Company not to affect the transaction / contracts of transferor Company
16. Enforcement of contracts, deeds, bonds and other instruments
17. Enforcement of Legal Proceedings
18. Issue and Allotment of Shares under the Scheme
19. Increase in Authorized Share Capital
20. Accounting Treatment

21. Conduct of business by the transferor Company till effective date
22. Dissolution of Transferor Company
23. Effect of Scheme
24. Expenses relating to the Scheme
25. Scheme conditional upon approval / sanctions
26. Effect of non-receipt of approvals
27. General terms and conditions applicable for the scheme *Prayer / Relief Part*
28. Approval of scheme
29. Particulars of Bank draft evidencing payment of fee for the Application.

In addition to the above, a clean and clear drafting of the Petition is required to be submitted to the NCLT, which would make process easier. Following are the standard guidelines for presenting an application or petition before NCLT, prescribed in National Company Law Tribunal Rules, 2016 and Companies (Compromises, Arrangements and Amalgamations) Rules, 2016:-

1. The petition / application being filed shall fall under the proper territorial jurisdiction of NCLT Bench
2. The petition / application and all enclosures shall be legibly typewritten in English language.
3. The petition / application / appeal / reply shall be printed in double line spacing on one side of the standard petition paper with an inner margin of about 4 cms width on top and with a right margin of 2.5 cm left margin of 5 cm and duly paginated, indexed and stitched together in paper book form.
4. The petition/ application shall be filed in prescribed form with stipulated fee in triplicate by duly authorised representative of the companies or by an advocate duly appointed in this behalf.
5. The petition shall also be accompanied by an index and memo of the parties.
6. The cause title of the petition/application shall be “Before the National Company Law Tribunal” and it shall also specify the Bench to which it is presented.
7. All the relevant provisions of the Companies Act, 2013 / NCLT Rules, 2016 shall be clearly mentioned in the petition / application.
8. The petition/application shall be divided into paragraphs and shall be numbered consecutively and each paragraph shall contain a separate fact or point.
9. The foot of petition / application shall have name and signature of the authorized representative.
10. The name of the petitioner / applicant along with complete address, viz, the name of the road street lane and municipal division or ward, municipal door and other number of the house, the name of the town or village; the post office; postal district and pin code shall be mentioned in the petition / application.
11. The fax number, mobile number, valid email addresses of the petitioner / applicant shall also be mentioned.
12. Every interlineations, eraser or correction or deletion in petition / application shall be initialed by the party or his authorized representative.
13. The affidavit verifying the petition in Form NCLT-6 shall be drawn on non-judicial /stamp paper of requisite value duly attested by Notary public / Oath Commissioner.

14. Full name, parentage, age, description of each party, date, address and in case a party sues or being sued in a representative character, has been set out in accordance to Rule 20(5) of the NCLT Rules, 2016.

15. Petition / application / appeal reply has been drawn in the prescribed form i.e. Form No. NCLT.1 with stipulated fee given in the Schedule of these rules. The fee is to be paid by way of demand draft / PO drawn in favour of the "The Pay & Accounts Officer, Ministry of Corporate Affairs, New Delhi" or can be paid through online at nclt.gov.in.

16. The documents attached with petition / application shall be duly certified by the authorized representative or advocate filing the petition or application.

17. The annexure to the petition / application shall be serially numbered.

18. The *Vakalatnama* shall bear court fee stamp.

19. The documents with regard to shareholding/paid-up capital/latest balance sheet of the petitioner/ applicant shall be attached.

20. Document other than in English language shall be duly translated and accordingly a translated copy duly certified shall be attached with petition/application.

(2) Submission of Application / Petition

Petition to the Tribunal for merger & amalgamation shall be submitted in Form No. NCLT-1along with following documents:

1. A notice of admission in Form No. NCLT

2 An affidavit in Form No. NCLT-6

3. A copy of Scheme of compromise and arrangement (Merger & Amalgamation)

4. The applicant shall also disclose to the Tribunal in the application, the basis on which each class of members or creditors has been identified for the purposes of approval of the scheme.

(3) Calling of Meeting by Tribunal

The Tribunal upon hearing the application may either give relevant directions / order for conducting the meeting of the creditors or class of creditors, or of the members or class of members or may dismiss the application for any appropriate reason.

Drafting of Notice of Meeting

The Notice of the meeting pursuant to the order of Tribunal shall be given in Form No. CAA-2. The table below provides basic information about Notice of Meeting:

Person entitled to receive the notice	The notice shall be sent individually to each of the Creditors or Members and the debenture-holders at the address registered with the company
Person authorized to send the notice	Chairman of the Meeting or if Tribunal so directs- by the Company or liquidator or by any other person
Modes of sending of notice	By Registered post, or by Speed post, or by courier, or By e-mail, or by and delivery, or by hand delivery, any other mode as directed by the Tribunal
Minimum time of notice	At least one month before the date fixed for meeting

The notice shall be accompanied with a copy of the scheme. Additionally, if the scheme does not include the following details, then the same shall also be sent along with the notice.

(a) Details of the order of the Tribunal directing the calling, convening and conducting of the Meeting

- Date of the Order;
- Date, time and venue of the meeting

(b) Details of the company including –

- Corporate Identification Number (CIN) or Global Location Number (GLN) of the company;
- Permanent Account Number (PAN);
- Name of the company;
- Date of incorporation;
- Type of the company (whether public or private or one-person company);
- Registered office address and e-mail address;
- Summary of main object as per the memorandum of association; and main business carried on by the company;
- Details of change of name, registered office and objects of the company during the last five years;
- Name of the stock exchange (s) where securities of the company are listed, if applicable;
- Details of the capital structure of the company including authorized, issued, subscribed and paid-up share capital;
- Names of the promoters and directors along with their addresses.

(c) Relationship between companies: if the scheme of compromise or arrangement relates to more than one company, then the fact and details of any relationship subsisting between such companies who are parties to such scheme of compromise or arrangement, including holding, subsidiary or of associate companies.

(d) Disclosure about the effect of the compromise or arrangement on:

- Key managerial personnel;
- directors;
- promoters;
- non-promoter members;
- depositors;
- creditors;
- debenture holders;
- deposit trustees and debenture trustees;
- employees of the company.

(e) Disclosure about effect of M&A on material interests of directors, Key Managerial Personnel (KMP) and debenture trustee. The term ‘interest’ extends beyond an interest in the shares of the company, and is with reference to the proposed scheme of compromise or arrangement.

(f) Details of Board Meeting: The date of the board meeting at which the scheme was approved by the board of directors, the name of the directors who voted in favor of the resolution, the names of the directors who voted against the resolution and the names of the directors who did not vote or participate on such resolution.

(g) Investigation or proceedings, if any, pending against the company under the Act.

(h) Details of the availability of the following documents for obtaining extract from or for making/obtaining copies of or for inspection by the members and creditors, namely:

- latest audited financial statements of the company including consolidated financial statements;
- copy of the order of Tribunal in pursuance of which the meeting is to be convened or has been dispensed with;
- copy of scheme of compromise or arrangement;
- contracts or agreements material to the compromise or arrangement;
- the certificate issued by auditor of the company to the effect that the accounting treatment if any proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133 of the Companies Act, 2013; and
- such other information or documents as the Board or Management believes necessary and relevant for making decision for or against the scheme.

(i) Details of approvals, sanctions or no-objection(s), if any, from regulatory or any other government authorities required, received or pending for the purpose of scheme of compromise or arrangement.

(j) A statement to the effect that the persons to whom the notice is sent may vote in the meeting either in person or by proxies, or where applicable, by voting through electronic means.

Drafting of the Explanatory Statement

Explanatory Statement disclosing details of the scheme of compromise or arrangement include the following:

(a) Parties involved in compromise or arrangement;

(b) Appointed date, effective date, share exchange ratio (if applicable) and other considerations, if any;

(c) Summary of valuation report (if applicable) including basis of valuation and fairness opinion of the registered valuer, if any, and the declaration that the valuation report is available for inspection at the registered office of the company;

(d) Details of capital or debt restructuring, if any;

(e) Rationale for the compromise or arrangement;

(f) Benefits of the compromise or arrangement as perceived by the Board of directors to the company, members, creditors and others (as applicable);

(g) Amount due to unsecured creditors.

Further details to be provided in the Notice

1. A copy of the valuation report, if any;
2. Copy of the order of Tribunal in pursuance of which the meeting is to be convened or has been dispensed with copy of scheme of Merger & Amalgamation;
3. Contracts or agreements material to the Merger & Amalgamation;

4. Such other information or documents as the Board or Management believes necessary and relevant for making decision for or against the scheme;

5. The draft of the proposed terms of the scheme drawn up and adopted by the directors of the merging company;

6. a report adopted by the directors of the merging companies explaining effect of compromise on each class of shareholders, key managerial personnel, promoters and non-promoter shareholders laying out in particular the share exchange ratio, specifying any special valuation difficulties;

7. Confirmation that a copy of the draft scheme has been filed with the Registrar;

8. The report of the expert with regard to valuation, if any;

9. A supplementary accounting statement if the last annual accounts of any of the merging company relate to a financial year ending more than six months before the first meeting of the company summoned for the purposes of approving the scheme.

The notice along with the aforementioned documents and information shall also be placed on the website of the company, if any. In case of a listed company, these documents shall be sent to Securities and Exchange Board of India (SEBI) and stock exchanges where the securities of the companies are listed, for placing on their website.

Report of the result of the meeting by the Chairperson

The Chairperson of the meeting shall within the time fixed by the Tribunal, or where no time has been fixed, within three (3) days after the conclusion of the meeting, submit a report to the Tribunal on the result of the meeting in Form no. CAA.4.

Petition for confirming compromise or arrangement

Where the proposed compromise or arrangement is agreed to by the members or creditors or both as the case may be, the company shall within seven (7) days of filing of report by the Chairperson, present a petition to the Tribunal in Form no. CAA.5.

BASIC PRINCIPLES OF DRAFTING OF APPLICATION AND PETITION

Before any professional commences drafting of Petition, Written Statement, Replication/Rejoinder or Miscellaneous application (cumulatively called pleadings), Interlocutory application it is absolutely necessary to keep in mind the provisions of Companies Act, 2013 Code of Civil Procedure (in short CPC), Limitation Act, Indian Evidence Act, National Company Law Tribunal Rules, 2016 and Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 procedural laws and certain basic and fundamental principles of drafting and pleadings must be kept in mind. Therefore, for anyone wishing to appear before NCLT or NCLAT, the professional must acquaint himself with CPC, Cr. PC, Limitation Act, Indian Evidence Act, Law of Contracts, Sale of Goods Act, etc.

Order 6 (Pleading Generally & Associates Rules of CPC)

1. As per Order 6 Rule 2 of CPC every pleading shall contain only a statement in a concise form of material facts on which the party is relying upon. However, text of documents or evidence in the form of Agreement/MOU (d) Letters (c) e-mails (d) Negotiable instruments (e) Deeds (f) written documents or well settled position of law need not be elaborated in the pleadings but only reference is required to be made. Every pleading should not contain arguments. Further, (a) every pleading shall be divided into paragraphs, numbered consecutively, each allegation should be in a separate paragraph (b) dates, sums and numbers shall be expressed in a pleading in figures as well as in words.

The Supreme Court has observed that "every pleading must state all material facts and not law. (i) *Mayar (H. K.) Ltd. and Ors. Vs. Owners and Parties , Vessel M. V . Fortune Express and Ors* [AIR 2006 SC1828] (ii) *Ramesh Kumar Agarwal Vs. Rajmala Exports Pvt. Ltd. and Ors. [AIR 2012SC 1887*]

2. However, as per Order 6 Rule 4 of CPC, in all cases, where the party alleges (a) mis-representation (b) fraud (c) breach of trust (d) willful default (e) undue influence, the party alleging any of these, must state clearly and specifically time, date month or year when any of the aforesaid happened - however, merely vague allegations are not sufficient and adequate and the court will not take cognizance.

3. Before any one proceed to commence drafting, it is absolutely necessary to gather information/ documents/ papers by having extensive discussions with the clients. The information could be gathered by asking the questions on the following points:

   - Whether all Factual Details have been taken out
   - Whether basic details of the parties have collated
   - All Evidence Necessary for Drafting
   - Appointment of Additional Directors
   - Cessation of Office of Existing Directors
   - Removal of Promoter Directors
   - Illegal Transfer of Shares / Removal of Directors
   - Information can be obtained under Right to Information Act, 2005.

4. As per Order 6 Rule 14 of CPC Every pleading shall be signed by the party and his pleader, if any, provided that where a party pleading is, by reason of absence or for other good cause; unable to sign the pleading, it may be signed by any person duly authorized by him to sign the same or to sue or defend on his behalf. The authorization to sign the pleadings could be either by way of (a) Board resolutions in case of body corporate or (b) Power of Attorney duly executed.

Forms of Pleadings

5. Generally, the rules prescribe the format of petition or application but does not prescribe the format for filing of Written Statement/Reply or Rejoinder or Replication. Therefore, the contents of petition must always be set out under various headings or sub-headings in accordance with the format prescribed – otherwise, the Registry of the NCLT or NCLAT may raise objection and your petition will not be listed for admission hearing and consequently, grant of interim relief may be delayed. The petition must adhere to the following:-

   (a) Form prescribed

   (b) Set brief description of each of the petitioner and respondents

   (c) Narrate the Facts.

Other General Points to be kept in mind while filing Application / Petition with NCLT

1. Where a particular situation is not provided in the NCLT Rules, the NCLT may for reasons to be recorded in writing, determine the procedure in a particular case in accordance with the principles of natural justice.

2. The general heading in all proceedings before the Tribunal, in all advertisement and notices shall be in Form No. NCLT-4.

3. Every petition or application or reference shall be filled in form as provided in Form No. NCLT-1 with attachments thereto accompanied by Form No. NCLT-2 and in case of an interlocutory application, the same shall be filed in Form No. NCLT-1 accompanied by such attachments thereto along with the Form No. NCLT-3.

4. Every petition or application including interlocutory application shall be verified by an affidavit in Form.

5. Notice to be issued by the NCLT to the opposite party shall be in Form No. NCLT-5.

Hearing of petition or application and production of Evidence by Affidavit.

After filing the application along with all the attachment and supporting document, the Tribunal shall notify the parties the date and place of hearing of the petition and during the hearing, where the Tribunal consider it is necessary in the interest of natural justice, it may order the parties to submit further evidence by the affidavit.

FINAL ORDER OF TRIBUNAL

On the date of final hearing, if the Tribunal is satisfied that meeting of creditors or members has been held as per the prescribed procedure and required disclosures were made to them, then the Tribunal may, by order, sanction the compromise or arrangement. The order shall be in Form No. CAA. 6. However, no compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company's auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the prescribed accounting standards.

The order may include directions in regard to any matter or such modifications in the compromise or arrangement for the proper working of the compromise or arrangement. The Tribunal also has the power to supervise the implementation of the compromise or arrangement. Moreover, if the Tribunal is satisfied that the compromise or arrangement sanctioned cannot be implemented satisfactorily with or without modifications, and the company is unable to pay its debts as per the scheme, it may make an order for winding-up the company.

Statement of compliance in mergers and amalgamations

Every company in relation to which an order has been made by the Tribunal sanctioning the scheme shall file with the Registrar of Companies a statement in Form No. CAA.8, until the scheme is fully implemented within two hundred and ten days from the end of each financial year. The statement shall be duly certified by a chartered accountant or a cost accountant or a company secretary in practice indicating whether the scheme is being complied with in accordance with the orders of the Tribunal or not.

ANNEXURE - A

SAMPLE SCHEME OF MERGER

BEFORE THE NATIONAL COMPANY LAW TRIBUNAL

IN THE MATTER OF SECTIONS 230 and 232 OF THE COMPANIES ACT, 2013

AND

IN THE MATTER OF ABC PRIVATE LIMITED

AND

IN THE MATTER OF SCHEME OF AMALGAMATION OF ABC PRIVATE LIMITED

WITH XYZ PRIVATE LIMITED AND THEIR RESPECTIVE SHAREHOLDERS AND CREDITORS

PREAMBLE

i) The Scheme of Amalgamation provides for the amalgamation of ABC Pvt. Ltd. (hereinafter referred to as 'Transferor Company') with XYZ Pvt. Ltd. (hereinafter referred to as 'Transferee Company') pursuant to Sections 230 and 232 of the Companies Act, 2013.

ii) Transferor Company was incorporated on May 23,1999 bearing CIN as U17110KA1999PTC019786 as a Private Limited Company limited by shares under the provisions of the Companies Act, 1956 with the Registrar of Companies, Karnataka at Bangalore. The main object of the Transferor Company, as per the Memorandum of Association is to carry on the business of information technology. The Transferor Company is a wholly owned subsidiary of the Transferee Company.

iii) Transferee Company is a company incorporated on August 23, 2000 bearing CIN: U72300 KA 2000 PTC 044988 as a Private Limited Company limited by shares with Registrar of Companies, Karnataka at Bangalore under the Companies Act, 1956. The Registered Office of the Company, at present, is situated at, Bangalore – 560103, Karnataka. The main objects of the Transferee Company, as per the Memorandum of Association is as follows:

(a) To provide information technology enabled services, web enabled services, business process outsourcing services and other services relating to back office operations and all kinds of business support services, including but not limited to operation support services, corporate function services, corporate support service, database services, information management services, telecom services, contact center services, consultancy services, document services, data processing services, data management services, activities for collating, accounting, managing, processing, analyzing, distributing, developing and storing documents, information and data, information technology support services, financial control support services, administration support services, professional/legal support, human resources support services, payroll support services, correspondence management services, online support services, financial and revenue accounting.

(b) To establish, maintain and run data processing/ computer centres, support and call centers, customer care and other customer service centers, providing database services including software and hardware support services, networking services, remote maintenance, testing services, network / web complex management services, digital certification services, information technology consultancy services, and other information technology and operations services.

(c) To organize, review and catalogue electronic documents, populate electronic databases and prepare reports, and conduct research including multi-jurisdictional surveys, to provide service management and business process management services in corporate, financial and general information research, financial analytics and for the purpose to act as representative, advisor, consultant, know how provider, sponsor, franchiser, licenser, job worker. To provide software development services and to produce software in connection with the above mentioned areas of expertise or otherwise."

The shares of the Transferee Company are held by XYZ Pte. Limited (99.10%) and XYZ International LLC, USA (0.10%).

iv) WHEREAS to rationalize and streamline the various functions of the entities in India, to eliminate multiple entities, to achieve administrative convenience, to achieve cost savings from more focused operational eff and to rationalize, standardize and simplify the business processes, productivity improvements and administrative expenses, it has been decided by the Board of Directors of the Transferor Company and the Transferee Company to amalgamate the Transferor Company into the Transferee Company.

v) The Scheme of Amalgamation is divided into the following parts: Part A - Definitions and Share capital Part B - Amalgamation of ABC Pvt. Ltd. with XYZ Pvt. Ltd. Part C -General Terms and Conditions

PART A – DEFINITIONS AND SHARE CAPITAL

1. Definitions

In this Scheme, unless repugnant to the context, the following expressions shall have the following meaning:

1.1 "Act" or "the Act" means the Companies Act, 2013 and shall include any statutory modifications, re-enactment or amendments thereof for the time being in force.

1.2 "Appointed Date" means April 01, 2018 or such other date as may be fixed or approved by the Hon'ble NCLT or any other appropriate authority.

1.3 "Board of Directors" or "Board" shall mean the Board of Directors of the Transferor Company and the Transferee Company as the case may be or any committee thereof duly constituted or any other person duly authorized by the Board for the purpose of this Scheme.

1.4 "Effective Date" means the latest date on which the certified copies of the order of the National Company Law Tribunal Bangalore Bench sanctioning the Scheme, as defined hereunder, are filed with the Registrar of Companies, Karnataka at Bangalore by the Transferor and the Transferee Companies.

1.5 "NCLT" means the National Company Law Tribunal, Bangalore Bench having jurisdiction in relation to the Transferor Company and the Transferee Company.

1.6 "Scheme" or "the Scheme" or "this Scheme" means this Scheme of Amalgamation of ABC Pvt. Ltd. with XYZ Pvt. Ltd. and their respective shareholders and creditors, in its present form as submitted to/ approved or directed by the NCLT or this Scheme with such modification(s), if any made, as per Clause 19 of the Scheme.

1.7 "Transferee Company" means XYZ Pvt. Ltd., a company incorporated under the Act and having its registered office at Pritech Park, Block 10, Unit 1, Sarjapur Ring Road, Bangalore – 560103, Karnataka.

1.8 "Transferor Company" means ABC Pvt. Ltd., a company incorporated under the Act and having its registered office at 40/2, Avenue Road, Ulsoor, Bangalore-560042, Karnataka.

1.9 "Undertaking" shall mean and include the whole of assets, properties, liabilities and the undertaking of the Transferor Company existing as on Appointed Date and specifically include the following (without limitation):

i) The whole of the undertaking of the Transferor Company, including all secured and unsecured debts, if any, liabilities, duties and obligations and all the assets, properties, rights, titles and benefits, whether movable or immovable, real or personal, in possession or reversion, corporeal or incorporeal, tangible or intangible, present or contingent and including but without being limited to land and building (whether owned, leased, licensed), all fixed and movable plant and machinery, vehicles, fixed assets, work in progress, current assets, investments, reserves, provisions, funds, licenses, registrations, copyrights, patents, trade names, trademarks and other rights and licenses in respect thereof, applications for copyrights, patents, trade names, trademarks, leases, licenses, tenancy rights, premises, ownership flats, hire purchase and lease arrangements, lending arrangements, benefits of security arrangements, computers, office equipment, telephones, telexes, facsimile connections, internet connections, communication facilities, equipment and installations and utilities, electricity, water and other service connections, benefits of agreements, contracts and arrangements, powers, authorities, permits, allotments, approvals, consents, privileges, liberties, advantages, easements and all the right, title, interest, goodwill, benefit and advantage, deposits, reserves, provisions, advances, receivables, deposits, funds, cash, bank balances, accounts and all other rights, benefits of all agreements, subsidies, grants, Minimum Alternate Tax, tax credits (including but not limited to credits in respect of income tax, sales tax, value added tax, turnover tax, service tax, Goods and Service tax etc), Software License, Domain

ii) Websites etc., in connection / relating to the Transferor Company and other claims and powers of whatsoever nature and wheresoever situated belonging to or in the possession of or granted in favour of or enjoyed by the Transferor Company, existing as on the Appointed Date.

iii) All staff, workmen, and employees, if any, of the Transferor Company in service on the Effective Date.

iv) All records, files, papers, information, computer programs, manuals, data, catalogues, quotations, sales advertising materials, lists of present and former customers and suppliers, customer credit information, customer pricing information and other records, whether in physical form or electronic form of the Transferor Company existing as on the Appointed Date.

1.10 Any references in the Scheme to “upon the Scheme becoming effective” or “effectiveness of the Scheme” shall mean the Effective Date.

1.11 All terms and words not defined in this Scheme shall, unless repugnant or contrary to the context or meaning thereof, have the same meaning ascribed to them under the Act, the Securities Contracts (Regulation) Act, 1956, the Depositories Act, 1996 and other applicable laws, rules, regulations, bye laws, as the case may be, including any statutory modification or re-enactment thereof from time to time.

2. Share Capital

2.1 The authorized and issued and paid up share capital of the Transferee Company as at March 31, 2018 is as under:

Authorized capital	**Amount (Rs)**
50,000,000 equity shares of Rs. 10 each	500,000,000
Issued, subscribed and paid-up capital	Amount (Rs)
15,000,000 equity shares of Rs. 10 each fully paid-up	150,000,000

2.2 The authorized and issued share capital of the Transferor Company as at March 31, 2018 is as under:

Authorized capital	**Amount (Rs)**
10,000,000 equity shares of Rs. 10 each	100,000,000
Issued, subscribed and paid-up capital	Amount (Rs)
5,000,000 equity shares of Rs. 10 each fully paid-up	5,000,000

Subsequent to March 31, 2018, there has been no change in the capital structure of Transferor Company.

PART B

AMALGAMATION OF TRANSFEROR COMPANY WITH TRANSFEREE COMPANY

3. Date of Taking Effect and Operative Date

The Scheme set out herein in its present form or with any modification(s) approved or imposed or directed by the Hon’ble NCLT or made as per Clause 19 of the Scheme, shall be effective from the Appointed Date but shall be operative from the Effective Date.

4. Amalgamation of the Transferor Company with the Transferee Company

4.1 Subject to the provisions of this Scheme as specified hereinafter and with effect from the Appointed Date, the Undertaking of the Transferor Company, as defined in clause 1.9, including all the debts, liabilities, duties and obligations of the Transferor Company of every description and also including, without limitation, all the movable and immovable properties and assets (whether tangible or intangible) of the Transferor Company comprising, amongst others, all furniture and fixtures, computers/data processing, office equipment, electrical installations, telephones, telex, facsimile and other communication facilities, deposits, reserves, provisions, advances, receivables, deposits, funds, cash, bank balances and business licenses, permits, authorizations, approvals, lease, tenancy rights, permissions, incentives, if any, and all other rights, patents, know-how, trademark, service mark, trade secret or other intellectual property rights, proprietary right, title, interest, contracts, consent, approvals and rights and powers of every kind, nature and description whatsoever, privileges, liberties, easements, advantages, benefits and approvals, if any, existing as on Appointed Date, shall, under the provisions of Sections 230 to 232 of the Act, and pursuant to the order of the Hon'ble NCLT sanctioning this Scheme and without further act, instrument or deed, but subject to the charges affecting the same as on the Effective Date, be transferred and/ or deemed to be transferred to and vested in the Transferee Company so as to become the properties, assets, rights, and undertaking(s) of the Transferee Company.

4.2 With effect from the Appointed Date, all statutory licenses, permissions, approvals or consents to carry on the operations of the Transferor Company, if any, existing as on Appointed Date shall stand vested in or transferred to the Transferee Company without any further act or deed and shall be appropriately mutated by the statutory authorities concerned in favour of the Transferee Company upon the vesting and transfer of the undertaking of the Transferor Company pursuant to this Scheme. The benefit of all statutory and regulatory permissions, licenses, approvals and consents, registrations shall vest in and become available to the Transferee Company pursuant to this Scheme.

4.3 With effect from the Appointed Date all debts, liabilities, duties and obligations of the Transferor Company existing as on the Appointed Date whether provided for or not in the books of account of the Transferor Company and all other liabilities which may accrue or arise after the Appointed Date but which relate to the period on or up to the day of the Appointed Date shall be the debts, liabilities, duties and obligations of the Transferee Company including any encumbrance on the assets of the Transferor Company or on any income earned from those assets and further that it shall not be necessary to obtain the consent of any third party or other person who is a party to any contract or arrangement by virtue of which such liabilities have arisen, in order to give effect to the provisions of this Clause.

4.4 The transfer and vesting as aforesaid shall be subject to the existing charges/ hypothecation / mortgages, if any, as may be subsisting and agreed to be created over or in respect of the said assets or any part thereof, provided however, any reference in any security documents or arrangements to which the Transferor Company is a party wherein the assets of the Transferor Company have been or are offered or agreed to be offered as security for any financial assistance or obligations shall be construed as reference only to the assets pertaining to the Transferor Company and vested in the Transferee Company by virtue of this Scheme to the end and intent that the charges shall not extend or deemed to extend to any assets of the Transferee Company.

4.5 All staff, workmen and employees, if any, engaged in the Transferor Company as on the Effective Date shall stand transferred to the Transferee Company, without any further act or deed to be done by the Transferor Company or the Transferee Company and, subject to the provisions hereof, on terms and conditions not less favorable than those on which they are engaged by the Transferor Company, without any interruption of service as a result of the amalgamation of the Transferor Company into the Transferee Company.

4.6 All items as detailed under Para 1.9 in relation to the Transferor Company shall stand transferred to or vested in the Transferee Company, without any further act or deed done by the Transferor Company or the Transferee Company.

4.7 Without prejudice to the above provisions, with effect from the Appointed Date, all inter-party transactions between the Transferor Company and the Transferee Company, if any, shall be considered as intra- party transactions for all purposes from the Appointed Date.

5. Consideration

5.1 The entire issued, subscribed and paid-up Equity Share Capital of the Transferor Company is held by the Transferee Company. Upon the Scheme becoming effective, no shares of Transferee Company shall be allotted in lieu or exchange of the holding in Transferor Company and, the whole of the investment of the Transferor Company in the share capital of the Transferee Company shall stand cancelled in the books of Transferee Company. Upon the coming into effect of this Scheme, the share certificates, if any, and/ or the shares in electronic form representing the shares held by the Transferee Company in Transferor Company shall be deemed to be cancelled without any further act or deed for cancellation thereof by Transferee Company, and shall cease to be in existence accordingly.

PART C

GENERAL TERMS AND CONDITIONS

6. Accounting Treatment in the Books of the Transferee Company

6.1 On the Scheme becoming effective, the Transferee Company shall account for the amalgamation under the Scheme in its accounts in accordance with "Pooling of Interest" method prescribed under Accounting Standard 14 "Accounting for Amalgamations" or if applicable under Appendix C of Indian Accounting Standard 103 (Business Combinations of Entities under common control) as prescribed under Companies (Accounting Standards) Rules, 2006 including any amendments thereto as may be prescribed under the Companies Act, 2013, read with rules made thereunder."

6.2 All the assets and liabilities recorded in the books of Transferor Company shall be transferred to and vested in the books of Transferee Company pursuant to the scheme and shall be recorded by Transferee Company at their respective book values as appearing in the books of Transferor Company.

6.3 The identity of the reserves of Transferor Company shall be preserved and they shall appear in the financial statements of Transferee Company in the same form and manner, in which they appeared in the financial statements of Transferor Company prior to this scheme being effective.

6.4 The investments in the equity capital of Transferor Company as appearing in the financial statements of Transferee Company shall stand cancelled.

6.5 Inter-company balances, loans and advances if any, will stand cancelled.

6.6 In case of any differences in accounting policy between Transferor Company and Transferee Company, the accounting policies followed by Transferee Company will prevail and the difference till the appointed date shall be adjusted in capital reserves of Transferee Company, to ensure that the financial statements of Transferee Company reflect the financial position on the basis of consistent accounting policy.

6.7 Subject to any corrections and adjustments as may, in the opinion of the Board of Directors of the Transferee Company, be required and except to the extent otherwise by law required, the reserves of the Transferor Company, if any, will be merged with the corresponding reserves of the Transferee Company.

7. Consequential Matters Relating to Tax and Compliance with Law

7.1 Upon the Scheme coming into effect, all taxes / cess / duties payable by or on behalf of the Transferor Company up to the Appointed Date and onwards including all or any refunds and claims, including refunds or claims pending with the revenue authorities, including the right of carry forward of accumulated losses and Minimum Alternate Tax credit under Section 115JAA of the Income-tax Act, 1961, Goods and Services tax, expenses incurred by the Transferor Company but deduction to be claimed on payment basis / on compliance with withholding tax provisions (as the case may be) under Sections 43B, 40(a) and 40(a)(ia) of the Income-tax Act, 1961, if any, shall, for all purposes, be treated as the tax / cess / duty, liabilities or refunds, claims, accumulated losses and Minimum Alternate Tax credit of the Transferee Company.

7.2 Upon the Scheme becoming effective, the Transferee Company is expressly permitted to revise its income-tax returns, sales tax returns, excise & CENVAT returns, service tax returns, Goods and Service tax return, other tax returns and to restore as input credit of service tax adjusted earlier or claim refunds / credits as required.

7.3 The Transferee Company is also expressly permitted to claim refunds, credits, including restoration of input CENVAT credit, Goods and Service tax, tax deduction in respect of nullifying of any transactions between the Transferor Company and Transferee Company.

7.4 In accordance with the Cenvat Credit Rules framed under Central Excise Act, 1944, as are prevalent on the Effective Date, the unutilized credits relating to excise duties / service tax/ Goods and Services tax paid on inputs / capital goods / input services lying in the accounts of the undertaking of the Transferor Company shall be permitted to be transferred to the credit of the Transferee Company, as if all such unutilized credits were lying to the account of the Transferee Company. The Transferee Company shall accordingly be entitled to set off all such unutilized credits against the excise duty / service tax payable by it.

7.5 Upon the Scheme becoming effective, unabsorbed tax losses and unabsorbed tax depreciation of the Transferor Company, if any, till the Appointed Date, would accrue to the Transferee Company in accordance with the provisions of the Income Tax Act, 1961.

7.6 This Scheme has been drawn up to comply with the conditions relating to "Amalgamation" as specified under the tax laws, including Section 2(1B) and other relevant sections of the Income tax Act, 1961. If any terms or provisions of the Scheme are found to be or interpreted to be inconsistent with any of the said provisions at a later date, whether as a result of any amendment of law or any judicial or executive interpretation or for any other reason whatsoever, the aforesaid provisions of the tax laws shall prevail. The Scheme shall then stand modified to the extent determined necessary to comply with the said provisions. Such modification will however not affect other parts of the Scheme. The power to make such amendments as may become necessary shall vest with the Board of Directors of the Transferor Company and the Transferee Company, which power shall be exercised reasonably in the best interests of the companies concerned.

8. Authorised Share Capital

8.1 Upon the Scheme becoming effective, the authorized share capital of the Transferor Company shall stand combined with the authorized share capital of the Transferee Company. Filing fees and stamp duty, if any, paid by the Transferor Company on its authorized share capital, shall be deemed to have been so paid by the Transferee Company on the combined authorized Share capital and accordingly, the Transferee Company shall not be required to pay any fee/ stamp duty for its increased authorized share capital.

8.2 Clause V of the Memorandum of Association and the Articles of Association of the Transferee Company shall, without any further act, instrument or deed, be and stand altered, modified and amended pursuant to Sections 61 and 64 and other applicable provisions of the Act by deleting the existing Clause and replacing it by the following:

"The Authorized Share Capital of the Company is Rs. 900,000,000/- (Rupees Ninety crore only) divided into 90,000,000 (Nine crore only) equity Shares of the face value of Rs. 10/- (Rupees ten only) each with powers to increase or reduce in accordance with the law".

8.3 The approval of this Scheme by the shareholders of the Transferee Company under sections 230 and 232 of the Act, whether at a meeting or otherwise, shall be deemed to have the approval under Sections 13, 14, 61, 64 and other applicable provisions of the Act and any other consents and approvals required in this regard.

9. Transactions Between Appointed Date and Effective Date With effect from the Appointed Date and up to the Effective Date:

9.1 The Transferor Company shall deemed to have held and stood possessed of and shall hold and stand possessed of all their properties and assets pertaining to the Undertaking of the Transferor Company for and on account of and in trust for the Transferee Company. The Transferor Company hereby undertakes to hold its said assets with utmost prudence until the scheme comes into effect.

9.2 The Transferor Company shall carry on its activities with reasonable diligence, business prudence and shall not, except in the ordinary course of business or without prior written consent of the Transferee Company alienate charge, mortgage, encumber or otherwise deal with or dispose of the Transferor Company or part thereof.

9.3 It is clarified that any advance tax paid / Tax Deduction at Source ("TDS") credits / TDS certificates received by the Transferor Company shall be deemed to be the advance tax paid by / TDS credit / TDS certificate of the Transferee Company.

9.4 All the profits or income, if any, accruing or arising to the Transferor Company or expenditure or losses, if any, arising or incurred or suffered by the Transferor Company pertaining to the undertaking of the Transferor Company shall for all purposes be treated and be deemed to be and accrue as the income or profits or losses or expenditure as the case may be of the Transferee Company.

9.5 The Transferor Company shall not vary the terms and conditions of employment of any of the employees, existing as on the Effective Date, except in the ordinary course of business or without the prior consent of the Transferee Company or pursuant to any pre-existing obligation undertaken by the Transferor Company as the case may be, prior to the Effective Date.

9.6 The Transferor Company shall not make any change in its capital structure either by any increase (by issue of equity or shares on a rights basis, bonus shares, convertible debentures or otherwise), decrease, reduction, reclassification, subdivision or consolidation, re-organization, or in any other manner which may, in any way, affect the share exchange ratio, except by mutual consent of the respective Boards of Directors of the Transferor Company and the Transferee Company or except as may be expressly permitted.

10. Employees of the Transferor Company

10.1 On the Scheme becoming effective, all staff, workmen and the employees, if any, of the Transferor Company in service on the Effective Date shall be deemed to have become staff, workmen and the employees of the Transferee Company, without any break or interruption in their services, and on the basis of continuity of service, and the terms and conditions of their employment with the Transferee Company shall not be less favourable than those applicable to them with reference to their employment with the Transferor Company on the Effective Date.

10.2 It is expressly provided that, on the Scheme becoming effective, any provident fund, gratuity fund, superannuation fund or any other special fund or trusts, if any, created or existing for the benefit of the staff, workmen and the employees of the Transferor Company in service as on the Effective Date shall become trusts/funds of the Transferee Company for all purposes whatsoever in relation to the administration or operation of such fund or funds or in relation to the obligation to make contributions to the said fund or funds in accordance with the provisions thereof as per the terms provided in the respective trust deeds, if any, to the end and intent that all rights, duties, powers and obligations of the Transferor Company in relation to such fund or funds shall become those of the Transferee Company. It is clarified that, for the purpose of the said fund or funds, the service of the staff, workmen and employees, if any, of the Transferor Company will be treated as having been continuous with the Transferee Company from the date of employment as reflected in the records of the Transferor Company.

11. Validity of Existing Resolutions

Upon the coming into effect of the Scheme, the resolutions of the Transferor Company as are considered necessary by the Board of Directors of the Transferee Company which are validly subsisting be considered as resolutions of the Transferee Company. If any such resolutions have any monetary limits approved under the provisions of the Act or of any other applicable statutory provisions, then the said limits, as are considered necessary by the Board of Directors of the Transferee Company, shall be added to the limits, if any, under the like resolutions passed by the Transferee Company.

12. Legal Proceedings

12.1 If any suit, appeal or other proceeding of whatever nature by or against the Transferor Company is pending, the same shall not abate or be discontinued or in any way be prejudicially affected by reason of or by anything contained in this Scheme, but the said suit, appeal or other legal proceedings may be continued, prosecuted and enforced by or against the Transferee Company, as the case may be, in the same manner and to the same extent as it would or might have been continued, prosecuted and enforced by or against the Transferor Company as if this Scheme had not been made.

12.2 In case of any litigation, suits, recovery proceedings which are to be initiated or may be initiated against the Transferor Company, the Transferee Company shall be made party thereto and any payment and expenses made thereto shall be the liability of the Transferee Company.

13. Contracts, Deeds, etc.

13.1 Subject to the other provisions of this Scheme, all contracts, deeds, bonds, insurance, letters of intent, undertakings, arrangements, policies, agreements and other instruments, if any, of whatsoever nature pertaining to the Transferor Company to which the Transferor Company is party and subsisting or having effect on the Effective Date, shall be in full force and effect against or in favour of the Transferee Company, as the case may be, and may be enforced by or against the Transferee Company as fully and effectually as if, instead of the Transferor Company, the Transferee Company had been a party thereto.

13.2 The Transferee Company shall enter into and/or issue and/or execute deeds, writings or confirmations or enter into any tripartite arrangements, confirmations or novations, to which the Transferor Company will, if necessary, also be party in order to give formal effect to the provisions of this Scheme, if so required or becomes necessary. The Transferee Company shall be deemed to be authorized to execute any such deeds, writings or confirmations on behalf of the Transferor Company and to implement or carry out all formalities required on the part of the Transferor Company to give effect to the provisions of this Scheme.

14. Statutory Licenses, Permissions, Approvals

With effect from the Appointed Date and upon the Scheme becoming effective, all statutory licenses, permissions, approvals, copyrights, trademarks or consents, if any, relating to the Undertaking of the Transferor Company shall stand vested in or transferred to the Transferee Company without any further act or deed and shall be appropriately mutated by the statutory authorities concerned in favour of the Transferee Company. The benefit of all statutory and regulatory permissions, environmental approvals and consents, registrations or other licenses and consents shall vest in and become available to the Transferee Company pursuant to this Scheme. In so far as the various incentives, subsidies, rehabilitation schemes, special status and other benefits or privileges enjoyed, granted by any government body, local authority or by any other person, or availed of by the Transferor Company are concerned, the same shall vest with and be available to the Transferee Company on the same terms and conditions.

15. Saving of Concluded Transactions

The transfer of Undertaking as described hereinabove and the continuance of proceedings by or against the Transferor Company, the same shall not affect any transaction or proceedings already concluded by the Transferor Company on and after the Appointed Date till the Effective Date, to the end and intent that the Transferee Company accepts and adopts all acts, deeds and things done and executed by the Transferor Company in respect thereto as done and executed on behalf of the Transferee Company.

16. Dissolution of the Transferor Company

On the Scheme becoming effective, the Transferor Company shall stand dissolved without being wound-up.

17. Conditionality of the Scheme

This Scheme is and shall be conditional upon and subject to:

17.1 The requisite, consent, approval or permission of the Central Government or any other statutory or regulatory authority, which by law may be necessary for the implementation of this Scheme.

17.2 The Scheme being approved by the requisite majorities in number and value of such classes of persons including the respective members and/or creditors of the Transferor Companies and the Transferee Company as required under the Act and as may be directed by the NCLT.

17.3 The sanction of the NCLT under Section 230 and 232 of the Act in favor of the Transferor Companies and the Transferee Company under the said provisions and the necessary orders under sections 232 of the Act being obtained.

17.4 The certified copy of the order of the Hon'ble NCLT under sections 230 and 232 of the Act sanctioning the Scheme is filed with the Registrar of Companies Karnataka at Bangalore.

17.5 Each part in Section of the Scheme shall be given effect to as per the chronology in which it has been provided for in the Scheme. The Scheme shall be effective from the Effective Date. However, failure of any one part of one Section for lack of necessary approval from the shareholders / creditors / statutory regulatory authorities shall not result in the whole Scheme failing. It shall be open to the concerned Board of Directors to consent to severing such part(s) of the Scheme and implement the rest of the Scheme as approved by the Hon'ble NCLT with such modification.

17.6 Compliance with such other conditions as may be imposed by the Hon'ble NCLT.

18. Application to Hon'ble NCLT

The Transferor Company and the Transferee Company shall, with all reasonable dispatch, make applications pursuant to Sections 230 and 232 of the Act, to the NCLT for sanction and carrying out the Scheme and for consequent dissolution of the Transferor Company without winding-up. The said companies shall also apply for and obtain such other approvals, as may be necessary in law, if any, for bringing the Scheme into effect and be entitled to take such other steps and proceedings as may be necessary or expedient to give full and formal effect to the provisions of this Scheme.

19. Modification or Amendments to the Scheme

Subject to approval of the Hon'ble NCLT, the Transferor Company and the Transferee Company by their respective Boards of Directors, may assent to/make and/or consent to any modifications/ amendments to the Scheme or to any conditions or limitations that the Hon'ble NCLT and/or any other Authority under law may deem fit to direct or impose, or which may otherwise be considered necessary, desirable or appropriate as a result of subsequent events or otherwise by them (i.e. the Board). The Transferor Company and the Transferee Company by their respective Board are authorised to take all such steps as may be necessary, desirable or proper to resolve any doubts, difficulties or questions whatsoever for carrying the Scheme into effect, whether by reason of any directive or Order of any other authorities or otherwise howsoever, arising out of or under or by virtue of the Scheme and/or any matter concerned or connected therewith.

20. Effect of Non-Receipt of Approvals

In the event of any approvals or conditions enumerated in the Scheme not being obtained or complied with, or for any other reason, the Scheme cannot be implemented, the Board of Directors of the Transferee Company and the Transferor Company shall mutually waive such conditions as they consider appropriate to give effect, as far as possible, to this Scheme and failing such mutual agreement, or in case the Scheme not being sanctioned by the Hon'ble NCLT, the Scheme shall become null and void and each party shall bear and pay their respective costs, charges and expenses in connection with the Scheme.

21. Costs, Charges & Expenses

In the event of the Scheme being sanctioned by the Hon'ble NCLT, the Transferee Company shall bear and pay all costs, charges, expenses, taxes including duties, levies in connection with the Scheme.

Authorised Representative

ABC Pvt. Ltd.

Place:

Date:

ANNEXURE -B

SAMPLE OF SCHEME OF AMALGAMATION

Under Sections 230 To 232 of the Company Act, 2013

Of

ABC LIMITED

(THE "TRANSFEROR COMPANY")

And

XYZ LIMITED

(THE "TRANSFEREE COMPANY")

And

THEIR RESPECTIVE SHAREHOLDERS

GENERAL

A. Description of Company and Background

I. ABC Limited, (CIN: U27104CT1999PLC013744) is a unlisted public limited Company incorporated under the Company Act, 1956 having its registered office at ____________________ (hereinafter referred to as the "Transferor Company"). The Transferor Company is engaged in the business of generation of power and has set up a 25MW Captive Power Plant at ____________________.

II. XYZ Limited, (CIN: L27106CT1999PLC013756) is a listed public limited Company incorporated under the Company Act, 1956 having its registered office at ____________________ (hereinafter referred to as the "Transferee Company"). The Transferee Company is engaged in the business of Iron & Steel with captive power generation and having an Integrated Steel Plant.

III. The Transferor Company is an Associate Company of the Transferee Company. The Transferee Company's equity shares are listed on BSE Limited and National Stock Exchange of India Limited.

IV. This Scheme of Amalgamation provides for the amalgamation of the Transferor Company with the Transferee Company pursuant to Sections 230 to 232 and other relevant provisions of the Company Act, 2013.

B. Rationale for the Scheme

a. The amalgamation of the Transferor Company with the Transferee Company would inter alia have the following benefits: a. With the proposed amalgamation of Transferor Company into Transferee Company and completion of integration of the Power Plant of the Transferor Company with Steel Plant of Transferee Company, the captive power generation capacity of the Transferee Company will stand enhanced to 98 MW and thereby availability of much needed additional 25MW of power capacity, to meet the shortfall of electricity requirement of Transferee Company, assuring uninterrupted power supply to its steel making units at competitive cost, leading to increase in capacity utilization of its steel melting plant and cost savings through operating leverage. It is pertinent to mention that no fresh capacity addition is allowed in the plant location of Transferee Company on account of environmental and pollution reasons and therefore the Power Plant of Transferor Company is critical for operations of Transferee Company.

b. The consolidation of operations of the Transferor Company and the Transferee Company by way of amalgamation will lead to a more efficient utilization of capital, administrative and operational rationalization and promote organizational efficiencies. It will prevent cost duplication that can erode financial efficiencies of the holding structure and the resultant operations will be more cost-efficient with the achievement of greater economies of scale, reduction in overheads and improvement in various other operating parameters.

c. The amalgamation will result in the formation of a stronger company with a larger capital and asset base and enable the combined business to be pursued more conveniently and advantageously. The amalgamation will have beneficial results for the amalgamating companies, their stakeholders and all concerned.

d. Greater integration and greater financial strength and flexibility for the amalgamated entity, which would result in maximising overall shareholder value, and will improve the competitive position of the combined entity.

e. Improved organizational capability and leadership, arising from the pooling of human capital who have the diverse skills, talent and vast experience to compete successfully in an increasingly competitive industry.

f. Cost savings are expected to flow from more focused operational efforts, rationalization, standardisation and simplification of business processes, and the elimination of duplication, and rationalization of administrative expenses.

In view of the aforesaid, the Board of Directors of the Transferor Company and the Transferee Company have considered and proposed the amalgamation of the entire undertaking and business of the Transferor Company with the Transferee Company in order to benefit the stakeholders of both the companies. Accordingly, the Board of Directors of the Transferor Company and the Transferee Company have formulated this Scheme of Amalgamation for the transfer and vesting of the entire Undertaking (herein after defined)and business of the Transferor Company with and into the Transferee Company pursuant to the provisions of Section 230 to Section 232 and other relevant provisions of the Act.

C. Parts of the Scheme:

This Scheme of Amalgamation is divided into the following parts:

(i) **Part I** deals with definitions of the terms used in this Scheme of Amalgamation and sets out the share capital of the Transferor Company and the Transferee Company;

(ii) **Part II** deals with the transfer and vesting of the Undertaking (as hereinafter defined) of the Transferor Company to and in the Transferee Company;

(iii) **Part II**I deals with the Consideration i.e. issue of new equity shares by the Transferee Company to the eligible shareholders of the Transferor Companies, as applicable and cancellation shares held by Transferee Company in the Transferor Company;

(iv) **Part IV** deals with the accounting treatment for the amalgamation in the books of the Transferee Company and dividends;

(v) **Part V** deals with the dissolution of the Transferor Company and the general terms and conditions applicable to this Scheme of Amalgamation and other matters consequential and integrally connected thereto.

D. The amalgamation of the Transferor Company with the Transferee Company, pursuant to and in accordance with this Scheme, shall take place with effect from the Appointed Date and shall be in accordance with the relevant provisions of the Income Tax Act, 1961 including but not limited to Section 2(1B) and Section 47 thereof.

PART I

DEFINITIONS AND SHARE CAPITAL

1. Definitions

In this Scheme, unless repugnant to the meaning or context thereof, the following expressions shall have the following meaning:

1.1. “Act” means the Companies Act, 2013, the rules and regulations made thereunder and will include any statutory re-enactment or amendment(s) thereto, from time to time;

1.2. “Appointed Date” For the purpose of this Scheme and for Income Tax Act, 1961, the “Appointed Date” means the open of business hours on 1st April 2017;

1.3 “Board of Directors” or “Board” means the board of directors of the Transferor Company or the Transferee Company, as the case may be, and shall include a duly constituted committee thereof;

1.4 “Effective Date” means the last of the dates on which the certified or authenticated copies of the order of the National Company Law Tribunal sanctioning the Scheme are filed with the Registrar of Companies by the Transferor Company and by the Transferee Company. Any references in this Scheme to the date of "coming into effect of this Scheme "or "effectiveness of this Scheme "or "Scheme taking effect "shall mean the Effective Date;

1.5. "Equity Shares" means equity shares of the Transferee Company, having face value of Rs 10/- (Ten only), per share fully paid;

1.6 "Governmental Authority" means any applicable central, state or local government, legislative body, regulatory or administrative authority, agency or commission or any court, tribunal, board, bureau or instrumentality thereof or arbitration or arbitral body having jurisdiction over the territory of India including but not limited to Securities and Exchange of India, Stock Exchanges, Registrar of Companies, competition Commission of India and National Company Law Tribunal;

1.7 " New Equity Shares" means Equity Shares of Transferee Company, to be issued to shareholders of the Transferor Company pursuant to this scheme, upon approval of NCLT in exchange of equity shares held in Transferor Company;

1.6 "NCLT" means the National Company Law Tribunal, Mumbai Bench, Mumbai;

1.7 "Registrar of Companies" means the Registrar of Companies, Chhattisgarh.

1.8 "Scheme" means this Scheme of Amalgamation between the Transferor Company and the Transferee Company and their respective shareholders as submitted to the NCLT together with any modification(s) approved or directed by the NCLT Mumbai Bench;

1.9 "Stock Exchanges" means BSE Limited and National Stock Exchange of India Limited where the shares of Transferee Company are listed;

1.10 "Transferor Company" means ABC Limited, Transferor Company (CIN: U27104CT1999PLC013744) is a unlisted public limited company incorporated under the Companies Act, 1956 having its registered office at ____________________;

1.11 "Transferee Company" means XYZ Limited, Transferee Company (CIN: L27106CT1999PLC013756) is a listed public limited company incorporated under the Companies Act, 1956 having its registered office at ____________________;

1.12 "Undertaking" means the whole of the undertaking and entire business of the Transferor Company as a going concern, including (without limitation):

I. All the assets and properties (whether movable or immovable, tangible or intangible, real or personal, corporeal or incorporeal, present, future or contingent) of the Transferor Company, including but not limited to, plant and machinery, equipment, buildings and structures, offices, residential and other premises, sundry debtors, furniture, fixtures, office equipment, appliances, accessories, depots, deposits, all stocks, assets, investments of all kinds (including shares, scrips, stocks, bonds, debenture stocks, units), and interests in its subsidiaries, cash balances or deposits with banks, loans, advances, disbursements, contingent rights or benefits, book debts, receivables, actionable claims, earnest moneys, advances or deposits paid by the Transferor Company, financial assets, leases (including lease rights), hire purchase contracts and assets, lending contracts, rights and benefits under any agreement, benefit of any security arrangements or under any guarantees, reversions, powers, municipal permissions, tenancies in relation to the office and/or residential properties for the employees or other persons, guest houses, godowns, warehouses, licenses, fixed and other assets, trade and service names and marks, patents, copyrights, and other intellectual property rights of any nature whatsoever, know how, good will, rights to use and avail of telephones, telexes, facsimile, email, internet, leased line connections and installations, utilities, electricity and other services, reserves, provisions, funds, benefits of assets or properties or other interest held in trust, registrations, contracts, engagements, arrangements of all kind, privileges and all other rights including, title, interests, other benefits (including tax benefits), easements, privileges, liberties, mortgages, hypothecations, pledges or other security interests created in favour of the Transferor Company and advantages of whatsoever nature and wheresoever situated in India or abroad, belonging to or in the ownership, power or possession and in the control of or vested in or granted in favour of or enjoyed by the Transferor Company or in connection with or relating to the Transferor Company and all other interests of whatsoever nature belonging to or in the ownership, power, possession or the control of or vested in or granted in favour of or held for the benefit of or enjoyed by the Transferor Company, whether in India or abroad;

II. All liabilities including, without being limited to, secured and unsecured debts (whether in Indian rupees or foreign currency),sundry creditors, liabilities (including contingent liabilities),duties and obligations of the Transferor Company, of every kind, nature and description whatsoever and howsoever arising, raised or incurred or utilised;

III. All agreements, rights, contracts, entitlements, permits, licenses, approvals, authorizations, concessions, consents, quota rights, engagements, arrangements, authorities, allotments, security arrangements (to the extent provided herein), benefits of any guarantees, reversions, powers and all other approvals of every kind, nature and description whatsoever relating to the

Business activities and operations of the Transferor Company;

IV. All records, files, papers, computer programs, manuals, data, catalogues, sales material, lists of customers and suppliers, other customer information and all other records and documents relating to the business activities and operations of the Transferor Company;

V. All permanent employees engaged by the Transferor Company as on the Effective Date;

VI. All rights, entitlements, export/import incentives and benefits including advance licenses, bids, tenders (at any stage as it may be), letters of intent, expressions of interest, development rights (whatever vested or potential and whether under agreements or otherwise), subsidies, tenancies in relation to office, benefit of any deposits privileges, all other rights, receivables, powers and facilities of every kind, nature and description whatsoever, rights to use and avail of telephones, telexes, facsimile connections and installations, utilities, electricity and other services, provisions and benefits of all agreements, contracts and arrangements, including technological licensing agreements, and all other interests in connection with or relating thereto;

VII. All intellectual property rights created, developed or invented by employees concentrated on the research, development or marketing of products (including process development or enhancement) in connection with the Transferor Company;

VIII. all benefits and privileges under letters of permission and letters, of approvals, all tax credits, including CENVAT and other Input credits, refunds; reimbursements, claims, exemptions, benefits under service tax laws, value added tax, purchase tax, sales tax or any other duty or tax or cess or imposts under central or state law including sales tax deferrals, advance taxes, tax deducted at source, right to carry forward and set-off unabsorbed losses, if any and depreciation, deductions and benefits under the Income-tax Act, 1961.

1.13. All capitalized terms not defined but used in this Scheme shall, unless repugnant or contrary to the context or meaning thereof, have the same meaning ascribed to them under the Act, the Securities Contracts (Regulation) Act, 1956, the Depositories Act, 1996 and other applicable laws, rules, regulations and byelaws, as the case may be, or any statutory amendment(s) or re-enactment thereof, for the time being in force.

2. Share Capital

***2.1. Transferor Company*:**

The Authorised, Issued, Subscribed and Paid-up share capital of the Transferor Company as on March 31, 2017and subsequent changes are as under:

Particulars	Rs. In Lacs
AUTHORISED SHARE CAPITAL:	
1,00,00,000 Equity Shares of Rs.10/- each	1,000.00
TOTAL	**1,000.00**
ISSUED, SUBSCRIBED AND PAID UP CAPITAL:	
99,95,700 Equity Shares of Rs.10/- each	999.57
TOTAL AS ON 31.03.2017	**999.57**
Less 23,26,000 Equity Shares of Rs.10/- each bought back on 31.01.2018.	232.60
TOTAL AFTER BUY BACK	**766.97**

Subsequent to the above balance sheet date there is no change in the Capital Structure of Transferor Company except buy back of 23, 26,000 equity shares of Rs.10 each fully paid as shown in the above table. The Transferor Company shall not make any alteration in its' paid up share capital from the date of approval of this scheme by the Board of Directors of the both the Companies, either by issuance of fresh equity shares or bonus issue or any other from, till Effective Date.

***2.2. Transferee Company*:**

The Authorised, Issued, subscribed and paid-up share capital of the Transferee Company as on March 31, 2017 was as under:

Particulars	Amount (Rs. In lacs)
AUTHORISED SHARE CAPITAL:	
4,98,00,000 Equity Shares of Rs.10/- each	4,980.00
32,00,000 Preference Shares of Rs.10/- each	320.00
TOTAL	**5,300.00**
ISSUED, SUBSCRIBED AND PAID UP CAPITAL:	
3,52,36,247 Equity Shares of Rs.10/- each	3411.12
TOTAL	**3411.12**

[*Note: The issued, subscribed and paid up share capital of the Transferee Company is Rs. 35,23,62,470/- divided into 3,52,36,247 Equity Shares of Rs. 10/- each fully paid up. Out of these 3,52,36,247 Equity Shares 11,25,000 Equity Shares have been held by the Transferee Company itself in the name of its Trustee as Trust Shares. As per the Indian Accounting Standards, the amount of share capital pertaining these 11,25,000 Equity Shares of Rs. 10/- each has been reduced from the issued, subscribed and paid up share capital on the liabilities side and from the investments on the asset side of the balance sheet. Hence the amount of issued, subscribed and paid up share capital in point 2.2 of the Scheme is Rs. 3411.12 Lacs (i.e. Rs. 3523.62 Lacs - Rs. 112.50 Lacs).]

Subsequent to the above balance sheet date there is no change in the capital structure of Transferee Company. It is hereby clarified that the Transferee Company will be free to make further issue of Equity Shares as per provisions of the Companies Act, 2013 and Rules and Regulations made thereunder and other applicable laws, rules and regulations including SEBI regulations. However, the Transferee Company shall be not be entitled to make bonus issue of Equity Shares by capitalisation of its free reserves & surplus till the Effective Date.

The equity shares of Transferee Company are, at present, listed on the National Stock Exchange of India Limited and the BSE Limited.

3. Date of Taking Effect and Operative Date

The Scheme set out herein in its present form or with any modifications approved or imposed or directed by NCLT shall be effective from the Appointed Date but shall be operative from the Effective Date.

PART II

TRANSFER AND VESTING OF UNDERTAKING

4. Transfer of Undertaking

4.1 Upon the coming into effect of this Scheme and with effect from the Appointed Date, the Undertaking, pursuant to the sanction of this Scheme by the NCLT under and in accordance with the provisions of Sections 230 to 232 and other applicable provisions, if any, of the Act, shall stand transferred to and be vested in or be deemed to have been transferred to and vested in the Transferee Company, as a going concern without any further act, instrument, deed, matter or thing to be made, done or executed so as to become, as and from the Appointed Date, the Undertaking of the Transferee Company by virtue of and in the manner provided in this Scheme.

4.2 Subject to the provisions of this Scheme as specified hereinafter and with effect from the Appointed Date, the entire Undertaking(s) of the Transferor Company, including all the debts, liabilities, losses, duties and obligations, including those arising on account of taxation laws and other allied laws of the Transferor Company of every description and also including, without limitation, all the movable and immovable properties and assets, tangible or Intangible assets (whether or not recorded in the books of account of the Transferor Company) of the Transferor Company comprising, amongst others, all freehold land, leasehold land, building, plants, motor vehicles, manufacturing facilities, laboratories receivables, actionable claims, furniture and fixtures, computers, office equipment, electrical installations, generators, containers, telephones, telex, facsimile and other communication facilities and business licenses, licenses under Factories Act, manufacturing licenses, permits, deposits, authorisations, approvals, recognitions and registrations granted by the Department of Scientific & Industrial Research to the in-house research and development units established, insurance cover of every description, lease, tenancy rights, permissions, incentives, if any, and all other rights, patents, know-how, trademark, service mark, trade secret, brands, registrations, licenses including other intellectual property rights, proprietary rights, title, interest, contracts, no objection certificates, deeds, bonds, consents, approvals and rights and powers of every kind, nature and description whatsoever, privileges, liberties, easements, advantages and benefits, approvals, filings, dossiers, copyrights, industrial designs, trade secrets, know-how, data, formulations, technology, methodology, manufacturing procedures and techniques, test procedures, brand names, trade names and domain names, and all other interests in connection with or relating to and product registrations, applications and authorisations for product registrations, and all other interests exclusively relating to the goods or services, shall, under the provisions of Sections 230to 232 of the Act, and pursuant to the orders of the NCLT sanctioning this Scheme and without further act, instrument or deed, but subject to the charges affecting the same as on the Effective Date, be transferred and/or deemed to be transferred to and vested in the Transferee Company, so as to become the properties, assets, rights, business and Undertaking(s) of the Transferee Company.

4.3 Transfer of Assets:

4.3.1 Without prejudice to the generality of Clause 4.1 above, upon the coming into effect of this Scheme and with effect from the Appointed Date.

4.3.1.1 All the assets and properties comprised in the Transferor Company of whatsoever nature and wheresoever situated, shall, under the provisions of Sections 230 to 232 and all other applicable provisions, if any, of the Act, without any further act or deed, be and stand transferred to and vested in the Transferee Company or be deemed to be transferred to and vested in the Transferee Company as a going concern so as to become the assets and properties of the Transferee Company.

4.3.1.2 Without prejudice to the provisions of Clause 4.3.1.1 above, in respect of such of the assets and properties of the Transferor Company as are movable in nature or incorporeal property or are otherwise capable of transfer by manual delivery or by endorsement and/or delivery, the same shall be so transferred by the Transferor Company and shall, upon such transfer, become the assets and properties of the Transferee Company as an integral part of the Undertaking, without requiring any separate deed or instrument or conveyance for the same.

4.3.1.3 In respect of movables other than those dealt with in Clause4.3.1.2 above including sundry debts, receivables, bills, credits, loans and advances of the Transferor Company, if any, whether recoverable in cash or in kind or for value to be received, bank balances, investments, earnest money and deposits with any Governmental Authority or with any Company or other person, the same shall on and from the Appointed Date stand transferred to and vested in the Transferee Company.

4.3.1.4 All interests of the Transferor Company in their respective subsidiaries and associates as on the Appointed Date will become the interests, subsidiaries and associates of the Transferee Company.

4.3.1.5 All the licenses, permits, approvals, permissions, registrations, incentives, tax deferrals and benefits, subsidies, concessions, grants, rights, claims, leases, tenancy rights, liberties, special status and other benefits or privileges enjoyed or conferred upon or held or availed of by the Transferor Company and all rights and benefits that have accrued or which may accrue to the Transferor Company, whether before or after the Appointed Date, shall, under the provisions of Sections 230 to 232 and all other applicable provisions, if any, of the Act, without any further act, instrument or deed, cost or charge be and stand transferred to and vest in or be deemed to be transferred to and vested in and be available to the Transferee Company so as to become as and from the Appointed Date licenses, permits,, approvals, permissions, registrations, incentives, tax deferrals and benefits, subsidies, concessions, grants, rights, claims, leases, tenancy rights, liberties, special status and other benefits or privileges of the Transferee Company and shall remain valid, effective and enforceable on the same terms and conditions.

4.3.2 The Transferor Company shall, if so required, also give notice in such form as it may deem fit and proper to the debtors, that pursuant to the sanction of this Scheme by NCLT under and in accordance with Sections 230 and 232 and all other applicable provisions, if any, of the Act, the said debtors should pay to the Transferee Company the debt, loan or advance or make the same on account of the Transferor Company and the right of the Transferor Company to recover or realize the same stands extinguished.

4.3.3 All assets and properties of the Transferor Company as on the Appointed Date, whether or not included in the books of the respective Transferor Company, and all assets and properties which are acquired by the Transferor Company on or after the Appointed Date but prior to the Effective Date, shall be deemed to be and shall become the assets and properties of the Transferee Company, and shall under the provisions of Sections 230 to 232 and all other applicable provisions, if any, of the Act, without any further act, instrument or deed, be and stand transferred to and vested in and be deemed to have been transferred to and vested in the Transferee Company upon the coming into effect of this Scheme. Provided, however, that no onerous assets shall have been acquired by the Transferor Company after the Appointed Date without the consent of the Transferee Company as provided for in this Scheme.

4.4 Transfer of Liabilities:

4.4.1 Upon the coming into effect of this Scheme and with effect from the Appointed Date all liabilities relating to and comprised in the Transferor Company including all secured and unsecured debts (whether in Indian rupees or foreign currency), sundry creditors, liabilities(including contingent liabilities), duties and obligations and undertakings of the Transferor Company of every kind, nature and description whatsoever and howsoever arising, raised or incurred or utilised for its business activities and operations (herein referred to as the "Liabilities"), shall, pursuant to the sanction of this Scheme by the NCLT under and in accordance with the provisions of Sections 230 to232 and other applicable provisions, if any, of the Act, without any further act, instrument, deed, matter or thing, be transferred to and vested in or be deemed to have been transferred to and vested in the Transferee Company, along with any charge, encumbrance, lien or security thereon, and the same shall be assumed by the Transferee Company to the extent they are outstanding as on the Effective Date so as to become as and from the Appointed Date the liabilities of the Transferee Company on the same terms and conditions as were applicable to the Transferor Company, and the Transferee Company shall meet, discharge and satisfy the same and further it shall not be necessary to obtain the consent of any third party or other person who is a party to any contract or arrangement by virtue of which such Liabilities have arisen in order to give effect to the provisions of this Clause.

4.4.2 All debts, liabilities, duties and obligations of the Transferor Company as on the Appointed Date, whether or not provided in the books of the respective Transferor Company, and all debts and loans raised, and duties, liabilities and obligations incurred or which arise or accrue to the Transferor Company on or after the Appointed Date till the Effective Date, shall be deemed to be and shall become the debts, loans raised, duties, liabilities and obligations incurred by the Transferee Company by virtue of this Scheme.

4.4.3 Where any such debts, loans raised, liabilities, duties and obligations of the Transferor Company as on the Appointed Date have been discharged or satisfied by the Transferor Company after the Appointed Date and prior to the Effective Date, such discharge or satisfaction shall be deemed to be for and on account of the Transferee Company.

4.4.4 Loans, advances and other obligations (including any guarantees, letters of credit, letters of comfort or any other instrument or arrangement which may give rise to a contingent liability in whatever form), if any, due or which may at any time in future become due between the Transferor Company and the Transferee Company shall, ipso facto, stand discharged and come to an end and there shall be no liability in that behalf on any party and appropriate effect shall be given in the books of accounts and records of the Transferee Company.

4.5 Encumbrances:

4.5.1 The transfer and vesting of the assets comprised in the Transferor Company to and in the Transferee Company under Clauses 4.1 and 4.3 of this Scheme shall be subject to the mortgages and charges, if any, affecting the same, as and to the extent hereinafter provided.

4.5.2 All the existing securities, mortgages, charges, encumbrances or liens(the "Encumbrances"), if any, as on the Appointed Date and created by the Transferor Company after the Appointed Date, over the assets comprised in the Undertaking or any part thereof transferred to the Transferee Company by virtue of this Scheme and in so far as such Encumbrances secure or relate to liabilities of the Transferor Company, the same shall, after the Effective Date, continue to relate and attach to such assets or any part thereof to which they are related or attached prior to the Effective Date and as are transferred to the Transferee Company, and such Encumbrances shall not relate or attach to any of the other assets of the Transferee Company, provided however that no Encumbrances shall have been created by the Transferor Company over its assets after the Appointed Date without the consent of the Transferee Company as provided for in this Scheme.

4.5.3 The existing Encumbrances over the assets and properties of the Transferee Company or any part thereof which relate to the liabilities and obligations of the Transferee Company prior to the Effective Date shall continue to relate only to such assets and properties and shall not extend or attach to any of the assets and properties of the Undertaking transferred to and vested in the Transferee Company by virtue of this Scheme.

4.5.4 Any reference in any security documents or arrangements (to which the Transferor Company are a party) to the Transferor Company and its assets and properties, shall be construed as a reference to the Transferee Company and the assets and properties of the Transferor Company transferred to the Transferee Company by virtue of this Scheme. Without prejudice to the foregoing provisions, the Transferor Company and the Transferee Company may execute any instruments or documents or do all the acts and deeds as may be considered appropriate, including the filing of necessary particulars and/or modification(s) of charge(s), with the Registrar of Company to give formal effect to the above provisions, if required.

4.5.5 Upon the coming into effect of this Scheme, the Transferee Company alone shall be liable to perform all obligations in respect of the Liabilities, which have been transferred to it in terms of the Scheme.

4.5.6 It is expressly provided that, no other term or condition of the Liabilities transferred to the Transferee Company is modified by virtue of this Scheme except to the extent that such amendment is required statutorily or by necessary implication.

4.5.7 The provisions of this Clause 4.5 shall operate in accordance with the terms of the Scheme, notwithstanding anything to the contrary contained in any instrument, deed or writing or the terms of sanction or issue or any security document; all of which instruments, deeds or writings shall be deemed to stand modified and/or superseded by the foregoing provisions.

4.6 Inter - se Transactions:

Without prejudice to the provisions of Clauses 4.1 to 4.5, with effect from theAppointed Date, all inter-party transactions between the Transferor Companyand the Transferee Company shall be considered as intra-party transactions forall purposes.

5. Contracts, Deeds, etc.

5.1 Upon the coming into effect of this Scheme and subject to the provisions of this Scheme, all contracts, deeds, bonds, agreements, schemes, arrangements, assurances and other instruments of whatsoever nature to which the Transferor Company are a party or to the benefit of which the Transferor Company may be eligible, and which are subsisting or have effect immediately before the Effective Date, shall continue in full force and effect by, for or against or in favour of, as the case may be, the Transferee Company and may be enforced as fully and effectually as if, instead of the Transferor Company, the Transferee Company had been a party or beneficiary or obligee or obligor thereto or thereunder.

5.2 Without prejudice to the other provisions of this Scheme and notwithstanding the fact that vesting of the Undertaking occurs by virtue of this Scheme itself, the Transferee Company may, at any time after the coming into effect of this Scheme in accordance with the provisions hereof, if so required under any law or otherwise, take such actions and execute such deeds (including deeds of adherence), confirmations or other writings or arrangements with any party to any contract or arrangement to which the Transferor Company are a party or any writings as may be necessary in order to give formal effect to the provisions of this Scheme. The Transferee Company shall, under the provisions of this Scheme, be deemed to be authorised to execute any such writings on behalf of the Transferor Company and to carry out or perform all such formalities or compliances referred to above on the part of the Transferor Company.

5.3 For the avoidance of doubt and without prejudice to the generality of the foregoing, it is clarified that upon the coming into effect of this Scheme, all consents, permissions, licenses, certificates, clearances, authorities, powers of attorney given by, issued to or executed in favour of the Transferor Company shall without any further act or deed, stand transferred to the Transferee Company, as if the same were originally given by, issued to or executed in favour of the Transferee Company, and the Transferee Company shall be bound by the terms thereof, the obligations and duties thereunder, and the rights and benefits under the same shall be available to the Transferee Company.

6. Legal Proceedings

6.1 On and from the Appointed Date, all suits, actions, claims and legal proceedings by or against the Transferor Company pending and/or arising on or before the Effective Date shall be continued and / or enforced as desired by the Transferee Company and on and from the Effective Date, shall be continued and / or enforced by or against the Transferee Company as effectually and in the same manner and to the same extent as if the same had been originally instituted and/or pending and/or arising by or against the Transferee Company. On and from the Effective Date, the Transferee Company shall have the right to initiate, defend, compromise or otherwise deal with any legal proceedings relating to the Undertaking, in the same manner and to the same extent as would or might have been initiated by the Transferor Company as the case may be, had the Scheme not be made; If any suit, appeal or other proceedings relating to the Undertaking, of whatever nature by or against the Transferor Company be pending, the same shall not abate or be discontinued or in any way be prejudicially affected by reason of the amalgamation of the Undertaking or by anything contained in this Scheme but the proceedings maybe continued, prosecuted and enforced by or against the Transferee Company in the same manner and to the same extent as it would or might have been continued, prosecuted and enforced by or against the Transferor Company as if this Scheme had not been made.

7. Conduct of Business

7.1 With effect from the Appointed Date and up to and including the Effective Date:

7.1.1 The Transferor Company shall carry on and shall be deemed to have carried on all its business and activities as hitherto and shall hold and stand possessed of and shall be deemed to have held and stood possessed of the Undertaking on account of, and for the benefit of and in trust for, the Transferee Company.

7.1.2 All the profits or income accruing or arising to the Transferor Company and all expenditure or losses arising or incurred (including all taxes, if any, paid or accruing in respect of any profits and income) by the Transferor Company shall, for all purposes, be treated and be deemed to be and accrue as the profits or income or as the case may be, expenditure or losses (including taxes) of the Transferee Company.

7.1.3 Any of the rights, powers, authorities and privileges attached or related or pertaining to and exercised by or available to the Transferor Company shall be deemed to have been exercised by the Transferor Company for and on behalf of and as agent for the Transferee Company. Similarly, any of the obligations, duties and commitments attached, related or pertaining to the Undertaking that have been undertaken or discharged by the Transferor Company shall be deemed to have been undertaken or discharged for and on behalf of and as agent for the Transferee Company.

7.2 With effect from the first of the date of filing of this Scheme with the NCLT and up to and including the Effective Date:

7.2.1 The Transferor Company shall preserve and carry on their business and activities with reasonable diligence and business prudence and shall not undertake any additional financial commitments of any nature whatsoever, borrow any amounts nor incur any other liabilities or expenditure, issue any additional guarantees, indemnities, letters of comfort or commitments either for itself or on behalf of its group Company or any third party or sell, transfer, alienate, charge, mortgage or encumber or deal with the Undertaking or any part thereof save and except in each case in the following circumstances:

7.2.1.1 if the same is in its ordinary course of business as carried on by itas on the date of filing this Scheme with NCLT; or

7.2.1.2 if the same is permitted by this Scheme; or

7.2.1.3 if consent of the Board of Directors of the Transferee Company has been obtained.

7.2.2 The Transferor Company shall not take, enter into, perform or undertake, as applicable

(i) any material decision in relation to its business and operations other than decisions already taken prior to approval of the Scheme by the respective Board of Directors (ii) any agreement or transaction; and (iii) any new business, or discontinue any existing business or change the capacity of facilities.: (iv) such other matters as the Transferee Company may notify from time to time save and except in each case in the following circumstances:

7.2.2.1 if the same is in its ordinary course of business as carried on by it as on the date of filing this Scheme with NCLT; or

7.2.2.2 if the same is permitted by this Scheme; or

7.2.2.3 if consent of the Board of Directors of the Transferee Company has been obtained.

7.3 Treatment of Taxes

7.3.1 Any tax liabilities under the Income-tax Act, 1961, Wealth Tax Act, 1957,Customs Act, 1962, Central Excise Act, 1944, Central Sales Tax Act, 1956 , any other state Sales Tax /Value Added Tax laws, service tax, luxury tax, stamp laws, Goods and Service Tax (GST) or other applicable laws/ regulations (hereinafter in this Clause referred to as "Tax Laws") dealing with taxes/ duties/ levies allocable or related to the business of the Transferor Company to the extent not provided for or covered by tax provision in the accounts made as on the date immediately preceding the Appointed Date shall be transferred to Transferee Company.

7.3.2 All taxes (including income tax, wealth tax, sales tax, excise duty, customs duty, service tax, luxury tax, VAT, GST etc.) paid or payable by the Transferor Company in respect of the operations and/or the profits of the business on and from the Appointed Date, shall be on account of the Transferee Company and, insofar as it relates to the tax payment(including without limitation income tax, wealth tax, sales tax, excise duty, customs duty, service tax, luxury tax, VAT, GST etc.), whether by way of deduction at source, advance tax or otherwise howsoever, by the Transferor Company in respect of the profits or activities or operation of the business on and from the Appointed Date, the same shall be deemed to be the corresponding item paid by the Transferee Company, and shall, in all proceedings, be dealt with accordingly.

7.3.3 Any refund under the Tax Laws due to Transferor Company consequent to the assessments made on Transferor Company and for which no credit is taken in the accounts as on the date immediately preceding the Appointed Date shall also belong to and be received by the Transferee Company.

7.3.4 Without prejudice to the generality of the above, all benefits including under the income tax, sales tax, excise duty, customs duty, service tax, luxury tax, VAT, GST etc., to which the Transferor Company are entitled to in terms of the applicable Tax Laws of the Union and State Governments, shall be available to and vest in the Transferee Company.

8. Staff Workmen and Employees

8.1 Upon the coming into effect of this Scheme:

8.1.1 All the permanent employees of the Transferor Company who are in its employment as on the Effective Date shall become the permanent employees of the Transferee Company with effect from the Effective Date without any break or interruption in service and on terms and conditions as to employment and remuneration not less favourable than those on which they are engaged or employed by the Transferor Company. It is clarified that the employees of the Transferor Company who become employees of the Transferee Company by virtue of this Scheme, shall not be entitled to the employment policies and shall not be entitled to avail of any schemes and benefits that may be applicable and available to any of the employees of the Transferee Company(including the benefits of or under any employee stock option schemes applicable to or covering all or any of the employees of the Transferee Company), unless otherwise determined by the Board of Directors of the Transferee Company. The Transferee Company undertakes to continue to abide by any agreement/ settlement, if any, validly entered into by the Transferor Company with any union/employee of the Transferor Company (as may be recognized by the Transferor Company). After the Effective Date, the Transferee Company shall be entitled to vary the terms and conditions as to employment and remuneration of the employees of the Transferor Company on the same basis as it may do for the employees of the Transferee Company.

8.1.2 The existing provident fund, gratuity fund and pension and/or superannuation fund or trusts or retirement funds or benefits created by the Transferor Company or any other special funds created or existing for the benefit of the concerned permanent employees of the Transferor Company (collectively referred to as the "Funds") and the investments made out of such Funds shall, at an appropriate stage, be transferred to the Transferee Company to be held for the benefit of the concerned employees. The Funds shall, subject to the necessary approvals and permission and at the discretion of the Transferee Company, either be continued as separate funds of the Transferee Company for the benefit of the employees of the Transferor Company or be transferred to and merged with other similar funds of the Transferee Company. In the event that the Transferee Company does not have its own fund with respect to any such Funds, the Transferee Company may, subject to necessary approvals and permissions, continue to maintain the existing Funds separately and contribute thereto, until such time as the Transferee Company creates its own funds at which time the Funds and the investments and contributions pertaining to the employees of the Transferor Company shall be transferred to such funds of the Transferee Company.

9. Saving of Concluded Transactions

Subject to the terms of this Scheme, the transfer and vesting of the Undertaking of the Transferor Company under Clause 4 of this Scheme shall not affect any transactions or proceedings already concluded by the Transferor Company on or before the Appointed Date or concluded after the Appointed Date till the Effective Date, to the end and intent that the Transferee Company accepts and adopts all acts, deeds and things made, done and executed by the Transferor Company as acts, deeds and things made, done and executed by or on behalf of the Transferee Company.

PART III

CONSIDERATION

10. Issue of Shares by the Transferee Company

10.1 Upon the Scheme coming into effect and without any further application, act or deed, the Transferee Company shall, in consideration of the amalgamation of the Transferor Company with the Transferee Company, the 26,05,000 (Twenty Six Lacs Five Thousand) equity shares of Transferor Company held by Transferee Company, will be cancelled without any act, deeds or instrument and the Transferee Company will issue and allot, to every equity shareholder of the Transferor Company, holding fully paid-up equity shares in the Transferor Company and whose names appear in the register of members of the Transferor Company on the Record Date to be announced by the Board of the Transferor Company, 45 (Forty Five)Equity Shares of of the Transferee Company, credited as fully paid-up with rights attached thereto as hereinafter mentioned (hereinafter referred to as the "New Equity Shares") for every 100 (One Hundred) Equity Shares of Rs.10 each fully paid-up, held by such shareholder in the capital of the Transferor Company ("Share Exchange Ratio").

10.2 In respect of the equity shares in the Transferor Company already held in dematerialized form, the New Equity Shares to be issued by the Transferee Company in lieu thereof shall also be issued in dematerialized form with the New Equity Shares being credited to the existing depository accounts of the members of the Transferor Company entitled thereto. Members of the Transferor Company desirous of receiving the New Equity Shares in the Transferee Company in dematerialized form should have their shareholding in the Transferor Company dematerialized on or before the Record Date.

10.3 Pursuant to the Scheme, the shares of the Transferor Company held by its equity shareholders (both in physical and dematerialized form), shall, without any further application, act, instrument or deed, be deemed to have been automatically cancelled. The said equity shares of Transferor Company held in physical form shall be deemed to have been automatically cancelled without any requirement to surrender the certificates for shares held by the shareholders of the Transferor Company.

10.4 No fractional share shall be issued by the Transferee Company in respect of the fractional entitlements, if any, to which the equity shareholders of the Transferor Company may be entitled on issue and allotment of New Equity Shares in the Transferee Company as above. The Board of Directors of the Transferee Company shall consolidate all such fractional entitlements and thereupon, issue and allot New Equity Shares in lieu thereof to the Trustee nominated by the Transferee Company for the purpose who shall hold the New Equity Shares in trust for and on behalf of the members entitled to such fractional entitlements with the express understanding that such Trustee shall sell the same at such time or times and at such price or prices to such person or persons, as it deems fit. The said Trustee shall distribute such net sale proceeds to the shareholders of the Transferor Company in the same proportion, as their respective fractional entitlements bear to the consolidated fractional entitlements. The Trustee shall be appointed by the Board of Directors of the Transferee Company.

10.5 The New Equity Shares in the Transferee Company to be issued to the shareholders of the Transferor Company shall be subject to the Memorandum and Articles of Association of the Transferee Company and the New Equity Shares so issued shall rank pari-passu in all respects with the existing Equity Shares of the Transferee Company.

10.6 The New Equity Shares of the Transferee Company issued in terms of the Scheme shall, subject to applicable regulations, be listed and/or admitted to trading on the relevant stock exchange(s) where the existing Equity Shares of the Transferee Company are listed and/or admitted to trading.

10.7 Consequent to and as part of the amalgamation of the Transferor Company with the Transferee Company herein, the Authorised Share Capital of the Transferor Company shall stand merged into and combined with the Authorised Share Capital of the Transferee Company pursuant to the Scheme, without any further act of deed, and without payment of any registration or filing fee on such combined Authorised Share Capital, the Transferor Company and the Transferee Company having already paid such fees. Accordingly, the Authorised Share Capital of the Transferee Company resulting from the amalgamation of the Transferor Company with the Transferee Company shall be a sum of Rs. 59,80,00,000/- divided into 5,98,00,000 Equity Shares of Rs.10/- each and Clause V of the Memorandum of Association of the Transferee Company shall stand altered accordingly.

It further clarified that the approval of the members of the Transferee Company to the Scheme shall be deemed to be their consent / approval also to the alteration of the Memorandum and Articles of Association of the Transferee Company as maybe required under the Act. Clause 'V' of the Memorandum of Association of the Transferee Company shall stand substituted by virtue of the Scheme to read as follows:

Clause 'V' of the Memorandum of Association

The authorised Share Capital of the Company is Rs.63,00,00,000 (Rupees Sixty Three Crores Only) divided into 5,98,00,000 (Five Crores Ninety Eight Lacs) Equity Shares of Rs. 10/- (Rupees Ten) each and 32,00,000 (Thirty Two Lacs) Preference Shares of Rs.10/- (Rupees Ten) each.

10.8 The equity shares of the Transferee Company allotted pursuant to the scheme shall remain frozen in the depositories system till listing / trading permission is given by the designated stock exchanges.

10.9 Till the listing of the New Equity Shares of the Transferee Company, there will be no change in the pre-arrangement capital structure and shareholding pattern or controls in the Transferee Company, which may affect status of the approval of the stock exchanges to this scheme.

10.10 Approval of the Scheme by the shareholders of Transferee Company shall be deemed to be due compliance of the provisions of section 42, 62 if any and other relevant or applicable provisions of the Companies Act, 2013 and Rules made thereunder for the issue and allotment of the Equity shares by Transferee Company to the shareholders of Transferor Company as provided hereinabove.

11. No Allotment of Shares to the Transferee Company

Upon the Scheme coming into effect, all equity shares which the Transferee Company holds in the Transferor Company (either directly or through nominees) shall stand cancelled without any issue or allotment of New Equity Shares or payment whatsoever by the Transferee Company in lieu of such Equity Shares of the Transferor Company.

PART IV

ACCOUNTING TREATMENT AND DIVIDENDS

12. Accounting Treatment

12.1 Upon the coming into effect of this Scheme and with effect from the Appointed Date, for the purpose of accounting for and dealing with the value of the assets and liabilities in the books of the Transferee Company, all assets and liabilities shall be recorded at Fair Value and adjust differences in Goodwill/ Capital Reserve/Gain from bargain purchase price.

12.2 In case of any difference in accounting policy between the Transferor Company and the Transferee Company, the impact of the same till the Appointed Date will be quantified and adjusted in accordance with 'Indian Accounting Standard Ind AS-8Áccounting Policies, Change in Accounting Estimates and Errors', in the books of the Transferee Company to ensure that the financial statements of the Transferee Company reflect the financial position on the basis of consistent accounting policy.

12.3 The difference between the value of respective investments carried in the books of the Transferee Company and the "Fair Value" of the assets of the respective Transferor Company, shall be debited/ credited to Goodwill/ Other Comprehensive Income respectively as the case may be, in the books of the Transferee Company, and dealt with in accordance with the Indian Accounting Standard Ind AS-103 issued by the Institute of Chartered Accountants of India.

12.4 Subject to provisions of this Scheme, the Transferee Company shall abide by Indian Accounting Standard Ind AS-103issued by the Institute of Chartered Accountants of India.

12.5 The amalgamation of Transferor Company with the Transferee Company in terms of this Scheme shall take place with effect from the Appointed Date and shall be in accordance with the provisions of Section 2(1B) of the Income Tax Act, 1961.

12.6 All inter-corporate deposits, loans and advances, outstanding balances or other obligations between Transferee Company and Transferor Company shall be cancelled and there shall be no obligation/ outstanding in that behalf.

12.7 Notwithstanding the above, the Transferee Company, in consultation with their statutory auditors, are authorized to account for this Scheme and effect thereof in any manner whatsoever as may be deemed fit in accordance with the applicable accounting standards.

13. Declaration of Dividend

13.1 During the period between the Appointed Date and up to and including the Effective Date, the Transferor Company shall not declare any dividend without the prior written consent of the Board of Directors of the Transferee Company.

13.2 For the avoidance of doubt, it is hereby declared that nothing in the Scheme shall prevent the Transferee Company from declaring and paying dividends, whether interim or final, to its equity shareholders as on the Record Date for the purpose of dividend and the shareholders of the Transferor Company shall not be entitled to dividend, if any, declared by the Transferee Company prior to the Effective Date.

14. Power to Give Effect to this Part

14.1. The Transferee Company shall enter into and/ or issue and/ or execute deeds, writings or confirmations or enter into any tripartite arrangements, confirmations or novations, to which the Transferor Company will, if necessary, also be party in order to give formal effect to the provisions of this Scheme, if so required. Further, the Transferee Company shall be deemed to be authorised to execute any such deeds, writings or confirmations on behalf of the Transferor Company and to implement or carry out all formalities required on the part of the Transferor Company to give effect to the provisions of this Scheme.

14.2. Upon coming into effect of the Scheme, the Transferee Company and/or the Transferor Company shall, with reasonable dispatch apply for transition of all licenses and statutory registrations of the Transferee Company including but not limited to product registrations (including applications and authorizations for product registrations), manufacturing licenses, product permissions, certificates, market authorizations, filings, (including experience and prequalification submissions), industrial licences, municipal permissions, approvals, consent, permits, incentives and subsidies. The period between the Effective Date and the last date on which the transfer of all such aforementioned licenses and statutory registrations have occurred is hereinafter referred to as "Transitory Period".

PART V

DISSOLUTION OF TRANSFEROR COMPANY AND GENERAL TERMS AND CONDITIONS

15. Dissolution of Transferor Company

On the coming into effect of this Scheme, the Transferor Company shall stand dissolved without winding-up, and the Board of Directors and any committees thereof of the Transferor Company shall without any further act, instrument or deed be and stand dissolved.

16. Validity of Existing Resolutions, etc.

Upon the coming into effect of this Scheme the resolutions, if any, of the Transferor Company, which are valid and subsisting on the Effective Date, shall continue to be valid and subsisting and be considered as resolutions of the Transferee Company and if any such resolutions have any monetary limits approved under the provisions of the Act, or any other applicable statutory provisions, then the said limits shall be added to the limits, if any, under like resolutions passed by the Transferee Company and shall constitute the aggregate of the said limits in the Transferee Company.

17. Modification of Scheme

17.1 Subject to approval of NCLT, the Transferor Company and the Transferee Company by their respective Board of Directors or any director/executives or any committee authorised in that behalf (hereinafter referred to as the "Delegate") may assent to, or make, from time to time, any modification(s) or addition(s) to this Scheme which NCLT or any authorities under law may deem fit to approve of or may impose and which the Board of Directors of the Transferor Company and the Transferee Company may in their discretion accept, or such modification(s) or addition(s) as the Board of Directors of the Transferor Company and the Transferee Company or as the case may be, their respective Delegate may deem fit, or required for the purpose of resolving any doubts or difficulties that may arise in carrying out this Scheme. The Transferor Company and the Transferee Company by their respective Boards of Directors or Delegates are authorised to do and execute all acts, deeds, matters and things necessary for bringing this Scheme into effect, or review the position relating to the satisfaction of the conditions of this Scheme and if necessary, waive any of such conditions (to the extent permissible under law) for bringing this

Scheme into effect, and/or give such consents as may be required in terms of this Scheme. In the event that any conditions are imposed by NCLT or any Governmental Authorities, which the Board of Directors of the Transferor Company or the Transferee Company find unacceptable for any reason, then the Transferor Company and the Transferee Company shall be at liberty to withdraw the Scheme.

17.2 For the purpose of giving effect to this Scheme or to any modification(s) thereof or addition(s) thereto, the Delegates (acting jointly) of the Transferor Company and Transferee Company may give and are authorised to determine and give all such directions as are necessary for settling or removing any question of doubt or difficulty that may arise under this Scheme or in regard to the meaning or interpretation of any provision of this Scheme or implementation thereof or in any matter whatsoever connected therewith (including any question or difficulty arising in connection with any deceased or insolvent shareholders or depositors, if any of the Transferor Company) or to review the position relating to the satisfaction of various conditions of this Scheme and if necessary, to waive any such conditions (to the extent permissible in law) and such determination or directions or waiver, as the case may be, shall be binding on all parties, in the same manner as if the same were specifically incorporated in this Scheme. For the avoidance of doubt it is clarified that where this Scheme requires the approval of the Board of Directors of the Transferor Company or the Transferee Company to be obtained for any matter, the same may be given through their Delegates.

18. Severability

If any part of this Scheme is found to be unworkable for any reason whatsoever, the same shall not, subject to the decision of the Board of Directors of the Transferor Company and the Transferee Company, affect the validity or implementation of the other parts and/or provisions of this Scheme.

19. Miscellanious – SEBI Observations

XYZ Ltd, a Transferee Company, its directors and one of Subsidiary Company, namely Ardent Steel Limited, were classified as defaulters for non-payment of the principle amount and interest on the debts availed from the banks and financial institutions in the year 2016-17. The debts of the said Companies were restructured vide Master Restructure Agreements dated 30th March, 2017. Since then the Transferee Company and its Subsidiary are regular in repayment of dues to the banks and financial institutions and there are no over dues as on the date, which is confirmed by the Canara Bank, vide their e-mail dated 07th August, 2018, however, the names of the Company, its subsidiary and their directors are still appearing in the CIBIL's list of defaulters in the category of Non filing suits above Rs. 100 Lakhs.

20. Filing of Applications

The Transferor Company and the Transferee Company shall use their best efforts to make and file all applications and petitions under Sections 230 to 232and other applicable provisions of the Act, before the respective NCLT for sanction of this Scheme under the provisions of law, and shall apply for such approvals as may be required under law.

21. Approvals

The Transferee Company shall be entitled, pending the sanction of the Scheme, to apply to any Governmental Authority, if required, under any law for such consents and approvals which the Transferee Company may require to own the Undertaking and to carry on the business of the Transferor Company.

22. Scheme Conditional upon Sanctions, etc.

22.1 This Scheme is conditional upon and subject to:

22.1.1 The Scheme being agreed to by the requisite majority of the respective members and/or creditors of the Transferor Company and of the Transferee Company as required under the Act and the requisite orders of the NCLT being obtained;

22.1.2 The Transferee Company will provide for voting by the public shareholders through e-voting and will disclose all material facts in the explanatory statement to be sent to the shareholders in relation to the Resolution Sanctioning the Scheme of Amalgamation; and

22.1.3 The certified copies of the orders of the NCLT sanctioning this Scheme being filed with the Registrar of Companies, Chhattisgarh.

23. Costs, Charges, Expenses and Stamp Duty

All costs, charges and expenses (including any taxes and duties) incurred or payable by the Transferor Company and Transferee Company in relation to or in connection with this Scheme and incidental to the completion of the amalgamation of the Transferor Company with the Transferee Company in pursuance of this Scheme, including stamp duty on the orders of NCLT, if any and to the extent applicable and payable, shall be borne and paid by the Transferee Company.

(Source : Reference taken from Scheme of Amalgamation of Godawari Power and Ispat Limited & Jagdamba Power and Alloys Limited.)

FORMAT-
REPORT OF THE AUDIT COMMITTEE FOR RECOMMENDING THE SCHEME OF AMALGAMATION BETWEEN ABC LTD. AND XYZ LTD. AND THEIR RESPECTIVE SHAREHOLDERS AND CREDITORS

The following members were present in the Meeting of the Audit Committee of the Board of Directors of the Company held on (Day), (Date) at (Time) at (Address)

Members present:

In attendance:

By Invitation:

1. Background

1.1 A meeting of the Audit Committee of ABC Ltd. ("Company") was held on _________ to consider and recommend the proposed scheme of amalgamation between XYZ Ltd. and the Company ("Scheme"), involving

(i) the amalgamation of XYZ Ltd. with the Company, and dissolution of XYZ without winding up and consequent issuance of equity shares of the Company to the shareholders of XYZ Ltd., in accordance with the Scheme **("Amalgamation")**;

(ii) various other matters incidental, consequential or otherwise integrally connected therewith, including the increase in the share capital of the Company, in accordance with the provisions of, inter alia, Sections 230 to 232 of the Companies Act, 2013.

1.2 In terms of the SEBI Scheme Circular CFD/DIL1/CIR/P/2020/249 dated December 22, 2020 ("SEBI Scheme Circular"), a report from the Audit Committee is required recommending the Draft Scheme, taking into consideration, inter alia, the Valuation Report. This report of the Audit Committee is made in order to comply with the requirements of the SEBI Scheme Circular.

1.3 In this regard, the Audit Committee considered, inter alia, the following documents:

(i) The draft Scheme;

(ii) Valuation report issued by Independent Chartered Accountant appointed by the Company, for the purposes of determining the share exchange ratio ("Valuation Report");

(iii) Fairness opinion issued by, a SEBI Registered Merchant Banker, on the equity shares to be issued by the Company to the shareholders of XYZ pursuant to the amalgamation ("Fairness Opinion");

(iv) Certificates obtained from the Statutory Auditors of the Company on the accounting treatment prescribed in the Scheme.

2. Salient features of the Draft Scheme

3. Recommendation of the Audit Committee

The Audit Committee, having considered the aforementioned documents as placed before the Committee, including the Valuation Report and the Fairness Opinion, does hereby recommend the draft Scheme for favourable consideration by the Board of Directors of the Company, BSE Limited and the National Stock Exchange of India Limited and the Securities and Exchange Board of India.

By order of the Audit Committee

For and on behalf of

Format for Auditor's Certificate

To,

The Board of Directors,

....

(Name and address of the Company)

We, the statutory auditors of .... (name of the listed entity),(hereinafter referred to as "the Company"), have examined the proposed accounting treatment specified in clause .... (specify clause number) of the Draft Scheme of .... (specify the type of Scheme) between .... (names of the companies/entities involved) in terms of the provisions of section(s) .... (specify the relevant section(s)) of the Companies Act, 1956/ Companies Act, 2013 with reference to its compliance with the applicable Accounting Standards notified under the Companies Act, 1956/ Companies Act, 2013 and Other Generally Accepted Accounting Principles.

The responsibility for the preparation of the Draft Scheme and its compliance with the relevant laws and regulations, including the applicable Accounting Standards as aforesaid, is that of the Board of Directors of the Companies involved. Our responsibility is to examine and report whether the Draft Scheme complies with the applicable Accounting Standards and Other Generally Accepted Accounting Principles. Nothing contained in this Certificate, nor anything said or done in the course of, or in connection with the services that are subject to this Certificate, will extend any duty of care that we may have in our capacity of the statutory auditors of any financial statements of the Company. We carried out our examination in accordance with the Guidance Note on Audit Reports and Certificates for Special Purposes, issued by the Institute of Chartered Accountants of India.

Based on our examination and according to the information and explanations given to us, we confirm that the accounting treatment contained in the aforesaid scheme is in compliance with SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 and circulars issued thereunder and all the applicable Accounting Standards notified by the Central Government under the Companies Act, 1956/ Companies Act, 2013 and/or the accounting treatment in respect of .... (specify the financial statement item(s)) as prescribed by .... (name of the regulator) vide its Notification .... (details of the Notification) which prevail over the accounting treatment for the same as prescribed under the aforesaid Accounting Standards (wherever applicable), except the following:

....

....

This Certificate is issued at the request of the .... (name of the Company) pursuant to the requirements of circulars issued under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 for onward submission to the .... (name of the Stock Exchange(s)). This Certificate should not be used for any other purpose without our prior written consent.

For

....

(name of the Firm)

Chartered Accountants

Firm Registration No.:

Signature

(Name of the member)

Designation (Partner or proprietor, as may be applicable):

Membership Number:

Place:

Date:

Format for Report on Complaints

Part A

Sr. No.	Particulars	Number
1.	Number of complaints received directly	
2.	Number of complaints forwarded by Stock Exchanges / SEBI	
3.	Total Number of complaints/comments received (1+2)	
4.	Number of complaints resolved	
5.	Number of complaints pending	

Part B

Sr. No.	Name of complainant	Date of Complaint	Status (Resolved/pending)
1.			
2.			
3.			

Format of the Compliance Report to be submitted along with the draft scheme

It is hereby certified that the draft scheme of arrangement involving (Name of the entities) does not, in any way violate, override or limit the provisions of securities laws or requirements of the Stock Exchange(s) and the same is in compliance with the applicable provisions of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 and this circular, including the following:

Sl.	Reference	Particulars
1.	Regulations 17 to 27 of LODR Regulations	Corporate governance requirements
2.	Regulation 11 of LODR Regulations	Compliance with securities laws
Requirements of this circular		
(a)	Para (I)(A)(2)	Submission of documents to Stock Exchanges
(b)	Para (I)(A)(2)	Conditions for schemes of arrangement involving unlisted entities

(c)	Para (I)(A)(4) (a)	Submission of Valuation Report
(d)	Para (I)(A)(5)	Auditors certificate regarding compliance with Accounting Standards
(e)	Para (I)(A)(9)	Provision of approval of public shareholders through e-voting

Company Secretary **Managing Director**

Certified that the transactions / accounting treatment provided in the draft scheme of arrangement involving (Name of the entities) are in compliance with all the Accounting Standards applicable to a listed entity.

Chief Financial Officer **Managing Director**

Format for report on unpaid dues

Sr. No.	Particulars	Details of dues/fine	Amount	Reason for non-payment
1.	Pending Dues of SEBI			
2.	Pending Dues of Stock Exchanges			
3.	Pending Dues of Depositories			

Computation of Fair Share Exchange Ratio

Valuation Approach	XYZ Ltd		PQR Ltd	
	Value per Share	Weight	Value per Share	Weight
Asset Approach	x	a	y	d
Income Approach	x	b	y	e
Market Approach	x	c	y	f
Relative Value per Share	**X**		**Y**	
Exchange Ratio (rounded off)			**xx**	

Specimen Resolution

Consider and approve the Scheme of Amalgamation between the _______ (Transferee Company) and ___________ (Transferor Company) and their respective members and creditors under Section 233 of the Companies Act, 2013.

To consider, and if thought fit, to pass with or without modifications, the following Special Resolution:

"RESOLVED THAT pursuant to the provisions of Sections 230 to 232 read with Section 234 and other applicable provisions, if any, of the Companies Act, 2013 including rules, circulars, notifications, if any, made thereunder (including any statutory modification(s) or re-enactment thereof for the time being in force), the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 and other applicable provisions of the regulations and guidelines issued by the Securities and Exchange Board of India (SEBI) and Reserve Bank of India (RBI) from time to time, and the applicable provisions of the Memorandum and Articles of Association of the Company and subject to the approval of the Hon'ble National Company Law Tribunal, ________ Bench and subject to such other approvals, permissions and sanctions of regulatory and other authorities, as may be necessary and subject to such conditions and modifications as may be prescribed or imposed by the Hon'ble National Company Law Tribunal, _________ Bench or by any regulatory or other authorities, while granting such consents, approvals and permissions, which may be agreed to by the Board of Directors of the Company (hereinafter referred to as the ("Board"), which term shall be deemed to mean and include one or more Committee(s) constituted/to be constituted by the Board or any person(s) authorized by the Board to exercise its powers including the powers conferred by this resolution), the Scheme of Amalgamation for merger of the businesses of the industrial undertakings of ____________ and ______________ ("Scheme'), be and is hereby approved.

RESOLVED FURTHER THAT the Board be and is hereby authorized to do all such acts, deeds, matters and things, as it may, in its absolute discretion deem requisite, desirable, appropriate or necessary to give effect to this resolution and effectively implement the amalgamation/merger embodied in the Scheme and to accept such modifications, amendments, limitations and/or conditions, if any, which may be required and/or imposed by the Hon'ble National Company Law Tribunal, __________Bench or such other regulatory/statutory authorities while sanctioning the amalgamation/merger embodied in the Scheme or as may be required for the purpose of resolving any doubts or difficulties that may arise in giving effect to the Scheme or for any other such reason, as the Board may deem fit and proper."

TAKE FURTHER NOTICE that in compliance with the provisions of (i) Sections 230, 232, 234 read with Sections 108 and 110 of the Companies Act, 2013; (ii) Rule 6 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016; (iii) Rule 20, 22 and other applicable provisions of the Companies (Management and Administration) Rules, 2014; (iv) Regulation 44 and other applicable provisions of the SEBI Listing Regulations; and (v) Secretarial Standards on General Meetings, the Transferee Company has also provided the facility of voting prior to the meeting through Postal Ballot and e-voting, so as to enable the Shareholders, to consider and approve the Scheme by way of the aforesaid resolution. Accordingly, voting by Shareholders of the Transferee Company to the Scheme shall be carried out through (i) Postal Ballot (ii) remote e-voting and (iii) e-voting at the venue of the meeting to be held on _________ at ________.

Place: **For and on behalf of the Board of Directors of**

________ (Name of Company)

Date: __________Chairman and Managing Director

DIN: _________

Chairperson appointed for the meeting

Specimen Resolution

CERTIFIED TRUE COPY OF THE RESOLUTION PASSED AT THE MEETING OF THE BOARD OF DIRECTORS OF ______________ HELD ON ________ AT THE REGISTERED OFFICE OF THE COMPANY SITUATED AT ______________.

Consideration and approval of draft Scheme of Amalgamation under section 230-232 and other applicable provisions, if any, of the Companies Act, 2013.

"RESOLVED THAT pursuant to the provisions of Sections 230-232 of Companies Act, 2013 read with Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 and other applicable rules and regulations made thereunder (including any statutory modification(s) or re-enactment(s) or amendment(s) thereof for the time being in force), relevant provisions of Memorandum of Association and Articles of Association of the Company, and subject to the approval of the shareholders of the Company, the Hon'ble National Company Tribunal, ________ Bench **("NCLT")** and any other statutory authorities, as may be applicable, on the basis of Audit Committee recommendations the consent of the Board of Directors (hereinafter referred to as "the Board") be and is hereby accorded to the draft Scheme **("Scheme")** of Amalgamation along with Share Exchange Ratio between ________ **("Transferee Company")** and ______________ **("Transferor Company")** and their respective shareholders.

RESOLVED FURTHER THAT Certificate of ___________, Chartered Accountants, the Statutory Auditors of the Transferee Company confirming that the accounting treatment outlined in the Scheme is in compliance with the applicable Indian Accounting Standards (Ind AS) notified under Section 133 and Companies (India Accounting Standards) Rules 2015 and other generally accepted accounting principles.

RESOLVED FURTHER THAT the report of the Audit Committee, considering inter alia the Valuation Report dated ________ of ____________, Chartered Accountants and Fairness opinion dated ________ given by ________ SEBI authorized Cat 1 Merchant Banker, be and is hereby taken on record.

RESOLVED FURTHER THAT in compliance with the SEBI Circular, for the purpose of approval under Regulation 37 of the Listing Regulations, 2015 and coordinating with SEBI, the Board of Directors of the company hereby designate "BSE Limited" as the Designated Stock Exchange.

RESOLVED FURTHER THAT any Director of the Transferee Company or Mr ______ or Mr _______, Authorised Signatories of Transferee Company, be and are hereby severally authorized to give effect to the Scheme and to do such acts, deeds, matters and things and also to execute such documents, writings etc. as may be necessary and to settle any questions or difficulties which may arise and give any directions necessary for obtaining approval of and giving effect to the Scheme, as and when required including to take all necessary steps.

CERTIFIED TRUE COPY

FOR ________________ (Company Name)

_______ (Name of the Director)

(Designation ________)

Address:

Date:

Place:

LESSON ROUND-UP

- There are various stages in the process of merger and amalgamations under the Companies Act, 2013.
- It is necessary to understand the key terms used in the process of mergers and amalgamations for better documentation.
- Documentation is a very important aspect for filing the scheme along with proper enclosures before the NCLT for seeking approval of the scheme.
- The Scheme of amalgamation would comprise of various parts containing details about Transferor Company, Transferee Company and further details about these two companies.
- Legal provisions of the mergers and amalgamations are contained in Section 230 to 240 of the Companies Act, 2013.
- Detailed care should be taken while drafting the Scheme of amalgamation, notice and explanatory statement.
- There are various forms prescribed under the National Company Law Tribunal Rules, 2016 and the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 for various applications/ petitions to be submitted before NCLT.
- Various documents are to be attached with Petition / Application to be submitted for merger and amalgamation and due care has to be taken to ensure that all such documents are duly enclosed.

GLOSSARY

Documentation: The process of classifying and annotating texts that provides official information or that serves as a record.

Drafting: In legal sense, means an act of preparing the legal documents like agreements, contracts, deeds, etc.

Petition: Petition and application are interchangeable terms normally used to indicate formal applications for seeking a remedy provided by law.

Rejoinder: A written statement/reply of the plaintiff/petitioner by way of defense to pleas' raised in the counter affidavit/written statement from the defendant/respondent.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).

1. What are the steps involved in the merger and amalgamation?
2. Who are the persons eligible for filing petition before the National Company Law Tribunal?
3. What are the various forms prescribed under the NCLT Rules and Companies (Compromises, Arrangements and Amalgamations) Rules, 2016?
4. What are the various documents to be enclosed along with various types of petitions / applications to be made before the NCLT?
5. Discuss briefly the points to be considered while drafting a scheme of merger and amalgamation.

LIST OF FURTHER READINGS

- Drafting of Contracts by Ravi Singhania, Bloomsbury Publications
- Legal writing and Contract Drafting by Madhavan & Ryder, Bloomsbury Publications
- National Company Law Tribunal and National Company Law Appellate Tribunal: Law Practice and Procedure by Prachi Manekar Wazalwar
- Practical Approach to deeds & documents by MC Bhandari

Accounting in Corporate Restructuring: Concept and Accounting Treatment

Lesson 6

KEY CONCEPTS

■ Accounting Standard ■ Ind AS ■ Business Combination ■ Demerger ■ Internal Reconstruction ■ Consideration

Learning Objectives

To understand:

- Accounting for Corporate Restructuring
- Accounting Standard (AS)-14
- Ind AS-103
- Consideration for Amalgamation
- Estimating the useful life of goodwill

Lesson Outline

- Introduction
- Applicability
- Accounting Standard
- Accounting for Amalgamations
- Methods of accounting for Amalgamations
- Consideration for Amalgamation
- Treatment of Reserves on Amalgamation
- Goodwill on Amalgamation
- Disclosure Requirements
- Amalgamation after Balance sheet date
- Ind AS-103 Business Combination
- Business and Business Combination
- Accounting for Business Combination
- Recognising goodwill or bargain purchase
- IFRS-3 Business combination
- Demerger
- Internal Reconstruction
- Lesson Round Up
- Glossary
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

To understand:

- Companies Act, 2013
- Accounting Standards
- IFRS/Ind AS

INTRODUCTION

Corporate restructuring implies a process by which the legal, ownership or operational or other structures of the company is reorganised to make it more profitable or to make corporate more agile to meet the competition and operational requirements. Restructuring may also happen as a response to major events like buyout, bankruptcy, demerger or due to financial restructuring.

In simple words, Corporate Restructuring is re-arranging business of a company so as to increasing its efficiency and profitability. Restructuring is a method of changing the organizational structure in order to achieve the strategic goals of the organization. It involves dramatic changes in an organization.

The most common forms of corporate restructuring are mergers/amalgamations, acquisitions/takeovers, financial restructuring, divestures/demergers and buy-outs. It is essentially the process of re-designing one or more aspects of the Company.

Accounting for corporate restructuring is dealt with in the following accounting standards:

(a) Accounting for Amalgamation (AS-14) - Applicable to those who have to comply with Companies (Accounting Standards) Amendent Rules, 2016

(b) Business Combinations (IND AS-103) - Applicable to those who have to comply with Companies (Indian Accounting Standards) Rules, 2015

Accounting Standard-14 (AS-14) deals with accounting for amalgamations. According to AS-14 amalgamation may be either in the nature of merger or in the nature of purchase. It prescribes certain conditions to be fulfilled for consideration of amalgamation in the nature of merger. It includes aspects relating to transfer of assets, and liabilities, shareholders of transferor companies becoming shareholders of transferee company, consideration for amalgamation, continuity of business of transferor company (ies).

AS-14 further prescribes that amalgamation in the nature of merger should be accounted for under pooling of Interest method and amalgamation in the nature of purchase should be accounted for under the purchase method. It also covers aspects such as treatment of reserves/goodwill in a scheme of amalgamation, amalgamation after the balance sheet date, etc.

Indian Accounting Standard - 103 (IND AS-103) lays down the accounting principles for business combination and not for asset combination. IND AS-103 is substantially different from Accounting for Amalgamation (AS-14). To apply the IND AS-103, there should be transaction which meets the definition of business combination.

APPLICABILITY

Accounting Standard-14 ‘Accounting for Amalgamations’ lays down the accounting and disclosure requirements in respect of amalgamations of companies and the treatment of any resultant goodwill or reserves.

Business Combinations (IND AS-103) applies to a transaction or other event that meets the definition of a business combination.

Exception

This standard does not deal with cases of acquisitions which arise when there is a purchase by one company (acquiring company) of the whole or part of the shares, or the whole or part of the assets, of another company (acquired company) in consideration by payment in cash or by issue of shares or other securities in the acquiring company or partly in one form and partly in the other. The distinguishing feature of an acquisition is that the acquired company is not dissolved and its separate entity continues to exist.

Business Combinations (IND AS-103) does not apply to the following:

(a) The formation of a joint venture.

(b) The acquisition of an asset or a group of assets that does not constitute a business. In such cases the acquirer shall identify and recognise the individual identifiable assets acquired (including those assets that meet the definition of, and recognition criteria for, intangible assets in Ind AS 38 Intangible Assets) and liabilities assumed. The cost of the group shall be allocated to the individual assets and liabilities on the basis of their relative fair values at the date of purchase. Such a transaction or event does not give rise to goodwill.

(c) Accounting for combination of entities or business under common control.

Further, in corporate restructuring, for proper and accurate accounting one also need to know and understand following standards:

Under Indian Accounting Standards (IND AS)

Ind AS 110 Consolidated Financial Statements

Ind AS 111 Joint Arrangements

Ind AS 112 Disclosure of Interest in other Entity

Ind AS 28 Investments in Associates and Joint Ventures

Under Accounting Standards

AS 13 Accounting for Investments

AS 21 Consolidated Financial Statements

AS 23 Accounting for Investments in Associates in Consolidated Financial Statements

AS 27 Financial Reporting of Interests in Joint Ventures

ACCOUNTING STANDARD-14 ACCOUNTING FOR AMALGAMATIONS

Types of Amalgamation

Accounting Standard (AS)-14 recognizes two types of amalgamation:

(a) Amalgamation in the nature of merger.

(b) Amalgamation in the nature of purchase.

An amalgamation should be considered to be an amalgamation in the nature of merger when all the following conditions are satisfied:

(i) All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.

(ii) Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.

(iii) The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.

(iv) The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.

(v) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

An amalgamation should be considered to be an amalgamation in the nature of purchase, when any one or more of the conditions specified above is not satisfied. These amalgamations are in effect a mode by which one company acquires another company and hence, the equity shareholders of the combining entities do not continue to have a proportionate share in the equity of the combined entity or the business of the acquired company is not intended to be continued after amalgamation.

Example:

X Ltd. acquire Y Ltd. under the scheme of merger sanctioned by the Tribunal. Y Ltd. ceases to exist. Consideration is discharged by way of issue of equity shares of X Ltd. to the shareholders of Y Ltd. in the ratio 1:1. X Ltd. already held 5% in Y Ltd. as an investment prior to the effective date of merger i.e. 1st October 2022. 86% of the shareholders (by face value) of Y Ltd. excluding X Ltd. agreed to become shareholders of X Ltd. Whether the above case will qualify to be classified as merger as per AS-14.

Solution:

Even if we exclude the shares of Y Ltd. already held by X Ltd., consequent to the allotment of shares pursuant to merger, 90% criteria for amalgamation to be classified as merger is being met. Since 90% of the remaining shares i.e. 95% comes out to 85.5% shareholders. Thus the threshold is being met. Hence the above case will qualify as merger.

METHODS OF ACCOUNTING FOR AMALGAMATION

There are two main methods of accounting for amalgamations:

(a) the pooling of interests method; and

(b) the purchase method.

The pooling of interests method is used in case of amalgamation in the nature of merger. The purchase method is used in accounting for amalgamations in the nature of purchase.

The Pooling of Interests Method

Since merger is a combination of two or more separate business, there is no reason to restate carrying amounts of assets and liabilities. Accordingly, only minimal changes are made in aggregating the individual financial statements of the amalgamating companies.

In preparing the transferee company's financial statements, the assets, liabilities and reserves (whether capital or revenue or arising on revaluation) of the transferor company should be recorded at their existing carrying amounts and in the same form as at the date of the amalgamation. The balance of the Profit and Loss Account of the transferor company should be aggregated with the corresponding balance of the transferee company or transferred to the General Reserve, if any.

If, at the time of the amalgamation, the transferor and the transferee company have conflicting accounting policies, a uniform set of accounting policies should be adopted following the amalgamation. The effects on the financial statements of any changes in accounting policies should be reported in accordance with Accounting Standard (AS-5), Net Profit or Loss for the Period 'Prior Period Items and Changes in Accounting Policies'.

The difference between the amount recorded as share capital issued (plus any additional consideration in the form of cash or other assets) and the amount of share capital of the transferor company should be adjusted in reserves. It has been clarified that the difference between the issued share capital of the transferee company and share capital of the transferor company should be treated as capital reserve. The reason given is that this difference is a kin to share premium. Furthermore, reserve created on amalgamation is not available for the purpose of distribution to shareholders as dividend and/or bonus shares. It means that if consideration exceeds the share capital of the transferor company (or companies), the unadjusted amount is a capital loss and adjustment must be made, first of all in the capital reserves and in case capital reserves are insufficient, in the revenue reserves. However, if capital reserves and revenue reserves are insufficient, the unadjusted difference may be adjusted against revenue reserves by making addition thereto by appropriation from profit and loss account. There should not be direct debit to the profit and loss account. If there is insufficient balance in the profit and loss account also, the difference should be reflected on the assets side of the balance sheet in a separate heading.

The Purchase Method

In preparing the transferee company's financial statements, the assets and liabilities of the transferor company should be incorporated at their fair value or, alternatively, the consideration should be allocated to individual identifiable assets and liabilities on the basis of their fair values at the date of amalgamation. The reserves (whether capital or revenue or arising on revaluation) of the transferor company, other than the statutory reserves, should not be included in the financial statements of the transferee company except as in case of statutory reserve.

Any excess of the amount of the consideration over the fair value of the net assets of the transferor company acquired by the transferee company should be recognized in the transferee company's financial statements as goodwill arising on amalgamation in the nature of purchase. If the amount of the consideration is lower than the negotiated value of the net assets acquired, the difference should be treated as Capital Reserve.

The goodwill arising on amalgamation should be amortised to income on a systematic basis over its useful life.

The amortization period should not exceed five years unless a somewhat longer period can be justified.

The reserves of the transferor company, other than statutory reserve should not be included in the financial statements of the transferee company. The statutory reserves refer to those reserves which are required to be maintained for legal compliance. The statute under which a statutory reserve is created may require the identity of such reserve to be maintained for a specific period.

Where the requirements of the relevant statute for recording the statutory reserves in the books of the transferee company are complied with, such statutory reserves of the transferor company should be recorded in the financial statements of the transferee company by crediting the relevant statutory reserve account. The corresponding debit should be given to a suitable account head (e.g., 'Amalgamation Adjustment Account) which should be disclosed as a part of "miscellaneous expenditure" or other similar category in the balance sheet as a separate line item. When the identity of the statutory reserves is no longer required to be maintained, both the reserve and the aforesaid account should be reversed.

Differences between Pooling of Interest Method and Purchase Method

Particulars	Pooling of Interest Method	Purchase Method
Purchase consideration	Consideration will be in the form of shares only.	Consideration may be in the form of equity shares/ other securities / cash/ other assets.
Recording of assets and Liabilities	Under this method assets and liabilities of transferor companies are recorded at Book Value only.	Under this method assets and liabilities of transferor companies are recorded at Fair Value.
Difference in consideration and Net assets taken over	Difference in consideration and Net assets taken over is adjusted in Reserve and surplus.	Difference in consideration and Net assets taken over is recorded in Goodwill or capital reserve.
Reserve	All reserve are incorporated in the books of Transferee company at the same value at which they appeared in the books of transferor.	No reserve are incorporated in the books of Transferee company except statutory reserve.

Let us recapitulate

There are two types of amalgamation and two methods of accounting for amalgamations under AS 14. The types of amalgamation are amalgamation in the nature of merger and amalgamation in the nature of purchase. There are two main methods of accounting for amalgamations viz. the pooling of interests method and the purchase method. The pooling of interests method is used in case of amalgamation in the nature of merger. The purchase method is used in accounting for amalgamations in the nature of purchase.

CONSIDERATION FOR AMALGAMATION

The consideration for amalgamation means the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company. In determining the value of the consideration, assessment is made of the agreed value or negotiated value of its various elements.

The consideration for the amalgamation should include any non-cash element at fair value. The fair value may be determined by a number of methods. For example, in case of issue of securities, the value fixed by the statutory authorities may be taken to be the fair value. In case of other assets, the fair value may be determined by reference to the market value of the assets given up, and where the market value of the assets given up cannot be reliably assessed, such assets may be valued at their respective net book values.

While the scheme of amalgamation provides for an adjustment to the consideration contingent on one or more future events, the amount of the additional payment should be included in the consideration if payment is probable and areas on able estimate of the amount can be made. In all other cases, the adjustment should be recognized as soon as the amount is determinable.

Example:

A Ltd. acquire B Ltd., on 1st April, 2022 and discharges consideration for the business as follows:

(a) Issued 42,000 fully paid equity shares of Rs.10 each at par to the equity shareholders of B Ltd.

(b) Issued fully paid up 15% preference shares of Rs.100 each to discharge the preference shareholders (Rs.1,70,000) of B Ltd. at a premium of 10%

(c) It is agreed that the debentures of B Ltd. (Rs.50,000) will be converted into equal number and amount of 13% debentures of A Ltd.

Calculate the amount of purchase consideration.

Solution:

Calculation of purchase consideration:

(a)	42,000 equity shares `Rs. 10 each issued at Rs. 10	= 4,20,000
(b)	15% preference shares of Rs. 1,70,000*110%	= 1,87,000
	Total	= 6,07,000
(c)	Not to be included in purchase considered as it is payment to debenture holders.	

TREATMENT OF RESERVES ON AMALGAMATION

If the amalgamation is an 'amalgamation in the nature of merger'

If the amalgamation is an 'amalgamation in the nature of merger', the identity of the reserves is preserved and they appear in the financial statements of the transferee company in the same form in which they appeared in the financial statements of the transferor company. Thus, for example, the General Reserve of the transferor company becomes the General Reserve of the transferee company, the Capital Reserve of the transferor company becomes the Capital Reserve of the transferee company and the Revaluation Reserve of the transferor company becomes the Revaluation Reserve of the transferee company. As a result of preserving the identity, reserves which are available for distribution as dividend before the amalgamation would also be available for distribution as dividend after the amalgamation. The difference between the amount recorded as share capital issued (plus any additional consideration in the form of cash or other assets) and the amount of share capital of the transferor company is adjusted in reserves in the financial statements of the transferee company.

Example:

X Ltd. having a share capital of Rs. 20 lakhs and Y Ltd. having a share capital of Rs. 30 lakhs. Z Ltd. was formed to take over the business of X Ltd and Y Ltd. at a purchase consideration of Rs. 25 lakhs and Rs. 28 lakhs, payable in shares of Z Ltd. The assets and liabilities were taken at their carrying amounts. Compute the Goodwill or Capital Reserve.

Solution:

Since the purchase consideration is payable in shares of the transferee company and all the assets and liabilities are taken over at their carrying amounts, the amalgamation is in the nature of merger, i.e. pooling of interests method.

For X Ltd. Purchase consideration	= Rs. 25 lakhs
Less: Share capital of X Ltd	= Rs. 20 lakhs
Excess of purchase consideration	= Rs. 5 lakhs.

This shall have to be adjusted against the Reserves of Z Ltd.

For Y Ltd. Purchase Consideration	= Rs. 28 lakhs
Less: Share Capital of Y Ltd	= Rs. 30 lakhs

Since purchase consideration is less than share capital of the transferor company, Rs. 2 lakhs shall be treated as Capital Reserve.

If the amalgamation is an 'amalgamation in the nature of purchase'

If the amalgamation is an 'amalgamation in the nature of purchase', the identity of the reserves, other than the statutory reserves is not preserved, dealt within the certain circumstances mentioned below.

Certain reserves may have been created by the transferor company pursuant to the requirements of, or to avail of the benefits under, the Income-tax Act, 1961; for example, Development Allowance Reserve, or

Investment Allowance Reserve. The Act requires that the identity of the reserves should be preserved for a specified period. Likewise, certain other reserves may have been created in the financial statements of the transferor company in terms of the requirements of other statutes. Though, normally, in an amalgamation in the nature of purchase, the identity of reserves is not preserved, an exception is made in respect of reserves of the afore said nature (referred to herein after as 'statutory reserves') and such reserves retain their identity in the financial statements of the transferee company in the same form in which they appeared in the financial statements of the transferor company, so long as their identity is required to be maintained to comply with the relevant statute. This exception is made only in those amalgamations where the requirements of the relevant statute for recording the statutory reserves in the books of the transferee company are complied with. In such cases the statutory reserves are recorded in the financial statements of the transferee company by a corresponding debit to a suitable account head (e.g., 'Amalgamation Adjustment Account') which is disclosed as a part of 'miscellaneous expenditure' or other similar category in the balance sheet. When the identity of the statutory reserves is no longer required to be maintained, both the reserves and the aforesaid account are reversed.

The amount of the consideration is deducted from the value of the net assets of the transferor company acquired by the transferee company. If the result of the computation is negative, the difference is debited to goodwill arising on amalgamation and dealt with in the manner stated below undertreatment of goodwill on amalgamation. If the result of the computation is positive, the difference is credited to Capital Reserve.

GOODWILL ON AMALGAMATION

Goodwill arising on amalgamation represents a payment made in anticipation of future income and it is appropriate to treat it as an asset to be amortised to income on a systematic basis over its useful life. Due to nature of goodwill, it is difficult to estimate its useful life, but estimation is done on a prudent basis. Accordingly, it should be appropriate to amortise goodwill over a period not exceeding five years unless a somewhat longer period can be justified.

The following factors are to be taken into account in estimating the useful life of goodwill:

(i) the foreseeable life of the business or industry;

(ii) the effects of product obsolescence, changes in demand and other economic factors;

(iii) the service life expectancies of key individuals or groups of employees;

(iv) expected actions by competitors or potential competitors; and

(v) legal, regulatory or contractual provisions affecting the useful life.

Example:

What is goodwill and capital reserve as per AS-14?

Solution:

Goodwill is the excess of the price paid in a purchase over the fair value of the net identifiable assets acquired. Capital reserve is the excess of the fair value (agreed value) of the net identifiable assets acquired over the purchase price.

Balance of Profit and Loss Account

In the case of an 'amalgamation in the nature of merger', the balance of the Profit and Loss Account appearing in the financial statements of the transferor company is aggregated with the corresponding balance appearing in the financial statements of the transferee company. Alternatively, it is transferred to the General Reserve, if any.

In the case of an 'amalgamation in the nature of purchase', the balance of the Profit and Loss Account appearing in the financial statements of the transferor company, whether debit or credit, loses its identity.

DISCLOSURE REQUIREMENTS

(a) For ***amalgamations of every type following disclosures*** should be made in the:

(i) first financial statements after the amalgamation;

(ii) names and general nature of business of the amalgamating companies;

(iii) effective date of amalgamation for accounting purposes;

(iv) the method of accounting used to reflect the amalgamation; and

(v) particulars of the scheme sanctioned under a statute.

(b) In case of ***amalgamations accounted for under the pooling of interests method, the following additional disclosures*** are required to be made in the first financial statements following the amalgamation:

(i) description and number of shares issued, together with the percentage of each company's equity shares exchanged to effect the amalgamation;

(ii) the amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof.

(c) In case of ***amalgamations accounted for under the purchase method the following additional disclosures*** are required to be made in the first financial statements following the amalgamations:

(i) consideration for the amalgamation and a description of the consideration paid or contingently payable, and

(ii) the amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof including the period of amortization of any goodwill arising on amalgamation.

Amalgamation after the Balance Sheet Date

While an amalgamation is effected after the balance sheet date but before the issuance of the financial statements of either party to the amalgamation, disclosure should be made as per the provisions of AS-4, 'Contingencies and Events Occurring after the Balance Sheet Date', but the amalgamation should not be incorporated in that financial statements. In certain circumstances, the amalgamation may also provide additional information affecting the financial statements themselves, for instance, by allowing the going concern assumption to be maintained.

INDIAN ACCOUNTING STANDARD 103- BUSINESS COMBINATIONS

Ind AS 103 defines business combination which has a wider scope when compared to AS-14 which deals only with amalgamation. Business combination is the process under which two or more business organisations or their net assets are brought under common control in a single business entity.

Business and Business Combination as per IND AS 103

Business: A business consists of inputs and process applied to those inputs that have the ability to create outputs. Thus, a business has three elements:

(a) *Input:* An economic resource that creates or has the ability to create outputs when one or more processes are applied to it. Example Non-current assets.

(b) *Process:* Any system, standard, protocol, convention or rule that when applied to an input or inputs, creates or has the ability to create outputs. Example: Strategic management processes.

(c) *Output:* The results of inputs and processes applied to those inputs that provide or have the ability to provide a return in the form of dividend, lower costs or other economic benefits directly to investors or other owners, members or participants.

Business Combination

A transaction or other event in which an acquirer obtains control of one or more business. Transactions sometimes referred to as true mergers or mergers of equals are also business combinations as that term is used in this IND AS.

A business combination is an act of bringing together of separate entities or business into one reporting unit. The result of business combination is one entity obtains control of one or more businesses. If an entity obtains control over other entities which are not business, the act is not a business combination. In such a case the reporting entity will account it as asset acquisition.

From the definition of Business Combination, it is clear that for business combination, control by one entity of another is sufficient and both the entities can continue to exist.

For example, if X Ltd., acquires 70% shares of Y Ltd., then it is a case of business combination even if X Ltd. and Y Ltd. will continue to exist. X Ltd. becomes a holding company of Y Ltd. and therefore, they become one reporting entity by reporting consolidated financial statements.

Difference between Ind AS-103 Business Combinations and Ind AS-110 Consolidated Financial statements

It may seem that Ind AS-110 Consolidated Financial statements and Ind AS-103 Business Combinations deal with the same thing which is not accurate. Ind AS 110 deals with accounting aspect of consolidation of businesses whereas Ind AS 103 deals with scope of business combinations.

While Ind AS-110 defines a control and prescribes specific consolidation procedures, Ind AS-103 is more about the measurement of the items in the consolidated financial statements, such as goodwill, non-controlling interest, etc.

While preparing consolidated financial statements, first you have to apply Ind AS-103 for measurement of assets and liabilities acquired, non-controlling interest and goodwill/bargain purchase then the consolidation procedure as per Ind AS-110.

Acquisition Method of Business Combination as per IND AS 103

An entity shall account for each business combination by applying the acquisition method. Applying the acquisition method requires the following:

(a) Identifying the acquirer

(b) Determining the acquisition date

(c) Identification and measurement of consideration transferred

(d) Recognising and measuring the identifiable assets acquired, liabilities assumed and any non-controlling interest in the acquiree; and

(e) Recognising and measuring goodwill or a gain from a bargain purchase.

(a) Identifying the acquirer

- For each Business Combination one of the combining entities shall be identified as the acquirer.

- Acquirer is the entity that obtains control of business.
- The guidance in Ind AS 110 shall be used to identify the acquirer — the entity that obtains control of another entity, i.e., the acquiree.

As per Ind AS 110 'Consolidated Financial Statements', an investor controls an investee if and only if the investor has all the following:

(a) power over the investee;

(b) exposure, or rights, to variable returns from its involvement with the investee; and

(c) the ability to use its power over the investee to affect the amount of the investor's returns.

The above definition is very wide and control assessment does not depend only on voting rights instead it depends on the following as well:

- Potential voting rights;
- Rights of non-controlling shareholders; and
- Other contractual right of the investor if those are substantive in nature.

When it is not clear from Ind AS 110, the following factors should be considered under Ind AS 103:

- In a business combination effected primarily by transferring cash or other assets or by incurring liabilities, the acquirer is usually the entity that transfers the cash or other assets or incurs the liabilities.
- In a business combination effected primarily by exchanging equity interests, the acquirer is usually the entity that issues its equity interests.
- The acquirer is usually the combining entity whose owners have the ability to elect or appoint or to remove a majority of the members of the governing body of the combined entity.
- The acquirer is usually the combining entity whose (former) management dominates the management of the combined entity.
- The acquirer is usually the combining entity that pays a premium over the pre-combination fair value of the equity interests of the other combining entity or entities.
- The acquirer is usually the combining entity whose relative size (measured in, for example, assets, revenues or profit) is significantly greater than that of the other combining entity or entities.

(b) Determining the acquisition date

The acquirer shall identify the acquisition date, which is the date on which it obtains control of the acquiree.

The date on which the acquirer obtains control of the acquiree is generally the date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree—the closing date. However, the acquirer might obtain control on a date that is either earlier or later than the closing date.

For example, the acquisition date precedes the closing date if a written agreement provides that the acquirer obtains control of the acquiree on a date before the closing date. An acquirer shall consider all pertinent facts and circumstances in identifying the acquisition date.

The acquisition date is a very important step in the business combination accounting because it determines when the acquirer recognises and measures the consideration, the assets acquired and liabilities assumed. The acquiree's results are consolidated from this date. The acquisition date materially impacts the overall acquisition accounting, including post-combination earnings.

The acquisition date is often readily apparent from the structure of the business combinations and the terms of the sale and purchase agreement (if applicable) but this is not always the case.

Example

Company ABC purchased 51% equity interest in Company XYZ. The consideration is paid in cash. The relevant dates are as under:

Date of agreement with shareholders -1st June, 2022

Appointed date as per agreement -1st April, 2022

Date of obtaining control over the Board -1st July, 2022

Date of payment of consideration -15th July, 2022

In this case, as the control over financial and operating policies are acquired through obtaining control over Board on 1st July, 2022, it is this date that is considered as the acquisition date. It may be noted that the appointed date as per the agreement is not considered as the acquisition date, as the Company ABC did not have control over Company XYZ as at that date.

Example

Sony Ltd. and Zee Ltd. are production of films and TV serials. Sony Ltd. makes a bid for Sony Ltd.'s business and the Competition Commission of India (CCI) announces that the proposed transaction is to be scrutinised to ensure that competition laws are not breached. Even though the contracts are made subject to the approval of the CCI, Sony Ltd. and Zee Ltd. mutually agree the terms of the acquisition and the purchase price before competition authority clearance is obtained. Can the acquisition date in this situation be the date on which Sony Ltd. and Zee Ltd. agree the terms even though the approval of CCI is awaited?

Paragraph 8 of Ind AS 103 provides that acquisition date is the date on which the acquirer obtains control of the acquiree.

Further, paragraph 9 of Ind AS 103 clarifies that the date on which the acquirer obtains control of the acquiree is generally the date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree—the closing date. However, the acquirer might obtain control on a date that is either earlier or later than the closing date.

For example, the acquisition date precedes the closing date if a written agreement provides that the acquirer obtains control of the acquiree on a date before the closing date. An acquirer shall consider all pertinent facts and circumstances in identifying the acquisition date. Since CCI approval is a substantive approval for Sony Ltd. to acquire control of Zee Ltd.'s operations, the date of acquisition cannot be earlier than the date on which approval is obtained from CCI. This is pertinent given that the approval from CCI is considered to be a substantive process and accordingly, the acquisition is considered to be completed only on receipt of such approval.

(c) Identification and measurement of consideration transferred

The consideration transferred in a business combination is the sum of the fair values of assets transferred, liabilities incurred, and equity issued by the acquirer.

The consideration transferred in a business combination shall be measured at fair value, which shall be calculated as the sum of the acquisition-date fair values of the assets transferred by the acquirer, the liabilities incurred by the acquirer to former owners of the acquiree and the equity interests issued by the acquirer.

- The consideration transferred may include assets or liabilities of the acquirer that have carrying amounts that differ from their fair values at the acquisition date (for example, non-monetary assets or a business of the acquirer). If so, the acquirer shall remeasure the transferred assets or liabilities to their fair values as of the acquisition date and recognize the resulting gains or losses, if any, in profit or loss.

Note: If acquirer has transferred a land as a part of the business combination arrangement to the owners of the acquiree then the fair value of the land will be considered in determining the fair value of the consideration. Consequently, the land will be de-recognised in the financial statements of the acquirer and the difference between the carrying amount of the land and the fair value considered for purchase consideration will be recorded in profit and loss.

- Further, any items that are not part of the business combination be accounted separately from business combination (example: acquisition related costs)
- Contingent consideration (Obligation by the acquirer to transfer additional assets or equity interest, if specified future events occur or conditions are met), if any, should also be measured at fair value at acquisition date. The acquirer shall classify an obligation to pay contingent consideration as a liability or as equity on the basis of the definitions of an equity instrument and a financial liability in accordance with the requirement of Ind AS 32 Financial Instruments: Presentation, or other applicable Indian Accounting Standards.

Company A acquires Company B in April, 2022. The acquisition agreement further states that an additional 20 Crore cash will be paid to B's former shareholders if profits of B after acquisition exceeds Rs. 100 crore for the next two years. The 20 Crore further payable depends upon profit generated by B, hence it is a contingent consideration.

A has to determines the fair value of the contingent consideration and a liability to be recognised at acquisition date.

Further, since the consideration is to be settled in cash, such consideration would be in the nature of financial liability rather than equity.

As at the acquisition date, the acquirer should consider the acquisition date fair value of contingent consideration as part of business combination. Accordingly, such recognition would increase goodwill (or reduce gain on bargain purchase, as the case may be).

(d) Recognising and measuring the identifiable assets acquired, liabilities assumed and any non-controlling Interest in the acquiree

As of the acquisition date, the acquirer shall recognise, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. The identifiable assets acquired and liabilities assumed must meet the definitions of assets and liabilities in the Framework for the Preparation and Presentation of Financial Statements in accordance with Indian Accounting Standards issued by the Institute of Chartered Accountants of India at the acquisition date. For example, costs the acquirer expects but is not obliged to incur in the future to effect its plan to exit an activity of an acquiree or to terminate the employment of or relocate an acquiree's employees are not liabilities at the acquisition date. Therefore, the acquirer does not recognise those costs as part of applying the acquisition method. Instead, the acquirer recognises those costs in its post combination financial statements in accordance with other Ind AS.

The acquirer's application of the recognition principle and conditions may result in recognising some assets and liabilities that the acquiree had not previously recognised as assets and liabilities in its financial statements. For example, the acquirer recognises the 80 acquired identifiable intangible assets, such as a brand name, a patent or a customer relationship, that the acquiree did not recognise as assets in its financial statements because it developed them internally and charged the related costs to expense.

(e) Recognising and measuring goodwill or a gain from a bargain purchase;

The acquirer shall recognise goodwill as of the acquisition date measured as the excess of (a) over (b) below:

(a) the aggregate of:

(i) the consideration transferred;

(ii) the amount of any non-controlling interest in the acquiree; and

(iii) in a business combination achieved in stages, the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree.

(b) the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed measured in accordance with this Ind AS.

In extremely rare circumstances, an acquirer will make a bargain purchase in a business combination in which the amount in (b) exceeds the aggregate of the amounts specified in (a). If that excess remains, the acquirer shall recognise the resulting gain (as bargain purchase) in other comprehensive income on the acquisition date and accumulate the same in equity as capital reserve. The gain shall be attributed to the acquirer.

Measurement of Non-Controlling Interest (NCI)

Non-Controlling Interest (NCI) is the portion of equity ownership in a subsidiary not attributable to the parent company, who has a controlling interest (greater than 50% but less than 100%) and consolidates the subsidiary's financial results with its own.

Ind AS 103 allows the acquirer to measure a non-controlling interest in the acquiree at its fair value at the acquisition date. Sometimes an acquirer will be able to measure the acquisition-date fair value of a non-controlling interest on the basis of a quoted price in an active market for the equity shares (ie those not held by the acquirer). In other situations, however, a quoted price in an active market for the equity shares will not be available. In those situations, the acquirer would measure the fair value of the non-controlling interest using other valuation techniques. The fair values of the acquirer's interest in the acquiree and the non-controlling interest on a pershare basis might differ. The main difference is likely to be the inclusion of a control premium in the per-share fair value of the acquirer's interest in the acquiree or, conversely, the inclusion of a discount for lack of control (also referred to as a non-controlling interest discount) in the per-share fair value of the non-controlling interest if market participants would take into account such a premium or discount when pricing the non-controlling interest.

Example

Amber Ltd. acquires 60% of the equity shares of Natural Ltd. a private entity, for Rs. 150 crore. The fair value of its identifiable net assets is Rs. 120 crore. How will the non-controlling interest be measured?

Solution

(a) Fair value method

Fair value of 40% of the equity shares owned by non-controlling shareholders = 150/60% *40% = 100 crore.

(b) Proportionate Net Asset value method

Net asset value of 40% of the equity shares owned by non-controlling shareholders = 120*40%=48 crore.

(f) Disclosures

Ind AS 103 requires detailed disclosures on Business Combination. The acquirer shall disclose the following information for each business combination that occurs during the reporting period:

a. the name and a description of the acquiree.

b. the acquisition date.

c. the percentage of voting equity interests acquired.

d. the primary reasons for the business combination and a description of how the acquirer obtained control of the acquiree.

e. a qualitative description of the factors that make up the goodwill recognised, such as expected synergies from combining operations of the acquiree and the acquirer, intangible assets that do not qualify for separate recognition or other factors.

f. the acquisition-date fair value of the total consideration transferred and the acquisition-date fair value of each major class of consideration, such as:

   I. cash;

   II. other tangible or intangible assets, including a business or subsidiary of the acquirer;

   III. liabilities incurred, for example, a liability for contingent consideration; and

   IV. equity interests of the acquirer, including the number of instruments or interests issued or issuable and the method of measuring the fair value of those instruments or interests.

g. for contingent consideration arrangements and indemnification assets:

   i. the amount recognised as of the acquisition date;

   ii. a description of the arrangement and the basis for determining the amount of the payment; and

   iii. an estimate of the range of outcomes (undiscounted) or, if a range cannot be estimated, that fact and the reasons why a range cannot be estimated. If the maximum amount of the payment is unlimited, the acquirer shall disclose that fact.

h. for acquired receivables:

   i. the fair value of the receivables;

   ii. the gross contractual amounts receivable; and

   iii. the best estimate at the acquisition date of the contractual cash flows not expected to be collected. The disclosures shall be provided by major class of receivable, such as loans, direct finance leases and any other class of receivables.

i. the amounts recognised as of the acquisition date for each major class of assets acquired and liabilities assumed.

j. for each contingent liability recognised, the information required as per Ind AS 37, Provisions, Contingent Liabilities and Contingent Assets.

   If a contingent liability is not recognised because its fair value cannot be measured reliably, the acquirer shall disclose:

   i. the information required by paragraph 86 of Ind AS 37; and

   ii. the reasons why the liability cannot be measured reliably.

k. the total amount of goodwill that is expected to be deductible for tax purposes.

l. for transactions that are recognised separately from the acquisition of assets and assumption of liabilities in the business combination:

   i. a description of each transaction;

   ii. how the acquirer accounted for each transaction;

   iii. the amounts recognised for each transaction and the line item in the financial statements in which each amount is recognised; and

   iv. if the transaction is the effective settlement of a pre-existing relationship, the method used to determine the settlement amount.

m. the disclosure of separately recognised transactions shall include the amount of acquisition-related costs and, separately, the amount of those costs recognised as an expense and the line item or items in the statement of profit and loss in which those expenses are recognised. The amount of any issue costs not recognised as an expense and how they were recognised shall also be disclosed.

n. in a bargain purchase (see paragraphs 34–36A):

   i. the amount of any gain recognised in other comprehensive income in accordance with paragraph 34;

   ii. the amount of any gain directly recognised in equity in accordance with paragraph 36A; and

   iii. a description of the reasons why the transaction resulted in a gain in case of (i) above.

o. for each business combination in which the acquirer holds less than 100 per cent of the equity interests in the acquiree at the acquisition date: i. the amount of the non-controlling interest in the acquiree recognised at the acquisition date and the measurement basis for that amount; and ii. for each non-controlling interest in an acquiree measured at fair value, the valuation technique(s) and significant inputs used to measure that value.

p. in a business combination achieved in stages:

   i. the acquisition-date fair value of the equity interest in the acquiree held by the acquirer immediately before the acquisition date; and

   ii. the amount of any gain or loss recognised as a result of remeasuring to fair value the equity interest in the acquiree held by the acquirer before the business combination (see paragraph 42) and the line item in the statement of profit and loss in which that gain or loss is recognised.

q. Following additional information:

   i. the amounts of revenue and profit or loss of the acquiree since the acquisition date included in the consolidated statement of profit and loss for the reporting period; and

   ii. the revenue and profit or loss of the combined entity for the current reporting period as though the acquisition date for all business combinations that occurred during the year had been as of the beginning of the annual reporting period. If disclosure of any of the information required by this subparagraph is impracticable, the acquirer shall disclose that fact and explain why the disclosure is impracticable.

Step Acquisitions

In the case an entity acquires an entity step by step through series of purchase then the acquisition date will be the date on which the acquirer obtains control. Till the time the control is obtained the Investment will be accounted as per the requirements of other Ind AS 109, if the investments are covered under that standard or as per Ind AS 28, if the investments are in Associates or Joint Ventures.

If a business combination achieved in stages, the acquirer shall remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss or other comprehensive income, as appropriate.

In prior reporting periods, the acquirer may have recognised changes in the value of its equity interest in the acquiree in other comprehensive income. If so, the amount that was recognised in other comprehensive income shall be recognised on the same basis as would be required if the acquirer had disposed directly of the previously held equity interest.

Accounting Treatment:

Initial Acquisition: When the acquiring entity first obtains control over the target, it accounts for the transaction using the applicable accounting standards for business combinations (e.g., IFRS 3 or ASC 805).

Subsequent Acquisitions: For each subsequent increase in ownership interest, the acquiring entity reassesses its control or significant influence over the target to determine whether consolidation is required.

Fair Value Adjustments: Any changes in the fair value of previously held equity interests due to subsequent acquisitions are recognized in the acquirer's profit or loss unless they represent transactions with non-controlling interests.

Consolidation Considerations:

Control Assessment: The acquiring entity reassesses its control over the target at each step acquisition. Control is generally indicated by the ability to direct the relevant activities of the target to generate returns.

Significant Influence: If control is not achieved, the acquiring entity assesses whether it has significant influence over the target. This assessment is based on factors such as representation on the target's board of directors, participation in policy-making decisions, and material transactions between the entities.

Consolidation Methods: If control or significant influence is established, the acquiring entity consolidates the target's financial statements using either the acquisition method (for control) or the equity method (for significant influence).

Financial Reporting:

Disclosures: Acquiring entities are required to provide comprehensive disclosures about step acquisitions in their financial statements. This includes information about the nature and terms of each transaction, the fair value of assets acquired and liabilities assumed, and the impact on the acquirer's financial position, results of operations, and cash flows.

Segment Reporting: Step acquisitions may result in changes to the acquirer's reportable segments, which need to be disclosed in accordance with relevant accounting standards (e.g., IFRS 8 or ASC 280).

Tax Implications:

Tax Planning: Step acquisitions may have significant tax implications for both the acquiring entity and the target, including considerations related to tax basis step-ups, tax attributes utilization, and potential tax liabilities.

Transfer Pricing: Transactions between related parties as part of step acquisitions are subject to transfer pricing rules and regulations to ensure compliance with tax laws and regulations.

Business Combination of Entities under Common Control

Common control business combination means a business combination involving entities or businesses in which all the combining entities or businesses are ultimately controlled by the same party or parties both before and after the business combination, and that control is not transitory.

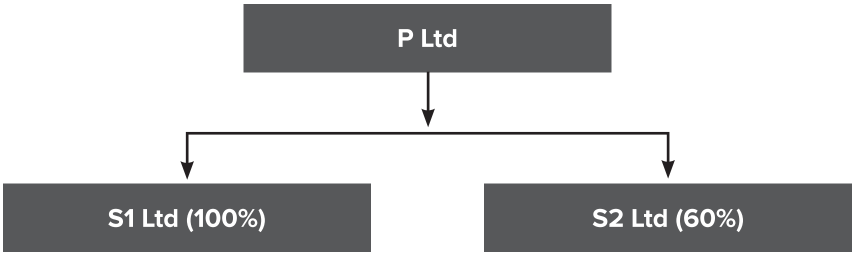
Common control business combinations will include transactions, such as transfer of subsidiaries or businesses, between entities within a group.

The extent of non-controlling interests in each of the combining entities before and after the business combination is not relevant to determining whether the combination is not relevant to determining whether the combination involves entities under common control. This is because of partially-owned subsidiary in nevertheless under the control of the parent entity.

Example:

Consider the following two groups:

P Ltd. acquires from S1 Ltd., its 60% stake in S2 Ltd. for Rs.10 Crores. After that the position of the group will be as below:



METHOD OF ACCOUNTING FOR COMMON CONTROL BUSINESS COMBINATIONS

Business combinations involving entities or businesses under common control shall be accounted for using the pooling of interest method.

The pooling of interest method is considered to involve the following:

(a) The assets and liabilities of the combining entities are reflected at their carrying amounts.

(b) No adjustments are made to reflect fair values or recognise any new assets or liabilities. The only adjustments that are made are to harmonise accounting policies.

(c) The financial information in the financial statements in respect of prior periods should be restated as if the business combination had occurred from the beginning of the earliest period presented in the financial statements, irrespective of the actual date of the combination. However, if business combination had occurred after that date, prior period information shall be restated only from that date.

The consideration for the business combination may consist of securities, cash or other assets. Securities shall be recorded at nominal value. In determining the value of the consideration, assets other than cash shall be considered at their fair values.

The balance of the retained earnings appearing in the financial statements of the transferor is aggregated with the corresponding balance appearing in the financial statements of the transferee. Alternatively, it is transferred to General Reserve, if any.

The identity of the reserves shall be preserved and shall appear in the financial statements of the transferee in the same form in which they appeared in the financial statements of the transferor.

The excess, if any, between the amount recorded as share capital issued plus any additional consideration in the form of cash or other assets and the amount of share capital of the transferor is recognised as goodwill in the financial statements of the transferee entity; in case of any deficiency, the same shall be treated as capital reserve.

Disclosures

The following disclosures shall be made in the first financial statements following the business combination:

(a) Names and general nature of business of the combining entities;

(b) The date on which the transferor obtains control of the transferee;

(c) Description and number of shares issued, together with the percentage of each entity's equity shares exchanged to effect the business combination; and

(d) The amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof.

Reverse Acquisition

A reverse acquisition occurs when the entity that issues securities (the legal acquirer) is identified as the acquiree for accounting purposes. The entity whose equity interests are acquired (the legal acquiree) must be the acquirer for accounting purposes for the transaction to be considered a reverse acquisition. For example, reverse acquisitions sometimes occur when a private operating entity wants to become a public entity but does not want to register its equity shares. To accomplish that, the private entity will arrange for a public entity to acquire its equity interests in exchange for the equity interests of the public entity. In this example, the public entity is the legal acquirer because it issued its equity interests, and the private entity is the legal acquiree because its equity interests were acquired. However, application of the guidance in paragraphs B13–B18 of Ind AS 103 results in identifying:

(a) the public entity as the acquiree for accounting purposes (the accounting acquiree); and

(b) the private entity as the acquirer for accounting purposes (the accounting acquirer).

The accounting acquiree must meet the definition of a business for the transaction to be accounted for as a reverse acquisition, and all of the recognition and measurement principles in Ind AS103, including the requirement to recognise goodwill, apply.

Reverse Acquisitions are often pursued for several reasons:

Quicker Access to Public Markets: It provides a faster and less costly route to becoming a publicly traded company compared to an IPO.

Less Regulatory Scrutiny: Reverse acquisitions typically involve less regulatory scrutiny and disclosure requirements compared to traditional IPOs.

Enhanced Credibility: Being publicly traded can enhance the credibility and visibility of the private company, making it easier to raise capital and attract investors.

Tax Benefits: Depending on the structure and jurisdiction, there may be potential tax benefits associated with a reverse acquisition.

However, Reverse Acquisitions also come with potential challenges and risks, including:

Due Diligence: It's crucial to conduct thorough due diligence on the target company to assess its financial condition, liabilities, and potential risks.

Integration: Integrating the operations and cultures of the two companies can be complex and challenging.

Market Perception: Reverse acquisitions may be viewed sceptically by investors, leading to volatility in the company's stock price.

Regulatory Compliance: The combined entity must comply with ongoing regulatory requirements and reporting obligations associated with being a public company.

Examples

1. In 1994 Godrej Soaps, a consumer product manufacturing business did a reverse merger with its loss-making subsidiary unit 'Gujarat Godrej Innovative chemical' and named it 'Godrej Soaps Ltd'.
2. In 2002, ICICI became the first firm to choose a reverse merger when it merged with its arm company, ICICI Bank, and renamed the combined entity ICICI Bank.

Business Combination after the balance sheet date

When a business combination is effected after the balance sheet but before the approval of the financial statements for issue by either party to the business combination, disclosure is made in accordance with Ind AS 10 Events after the reporting period, but the business combination is not incorporated in the financial statements. In certain circumstances, the business combination may also provide additional information affecting the financial statements themselves, for instance, by allowing the going concern assumption to be maintained.

Detailed explanation of how such situations are typically handled:

Disclosure According to Ind AS 10: Events after the Reporting Period: Ind AS 10 provides guidance on how to treat events that occur after the balance sheet date but before the financial statements are approved for issue. In the case of a business combination, disclosure is made in the financial statements in accordance with this standard. This typically involves disclosing the nature of the business combination, including the entities involved, the acquisition date, and any other pertinent details.

Non-Incorporation of the Business Combination in Financial Statements: Despite the occurrence of the business combination, if the financial statements have not been adjusted to reflect the transaction, the assets acquired and liabilities assumed are not recognized in the financial statements. This is because the transaction took place after the balance sheet date, and thus the financial statements reflect the financial position of the entity as of that date.

Additional Information Affecting Financial Statements: In certain circumstances, the business combination may provide additional information that impacts the financial statements themselves. For example, if the business combination strengthens the financial position of the entity or provides access to resources that allow the entity to continue operating as a going concern, this information may affect the assessment of the entity's ability to continue its operations for the foreseeable future. In such cases, the going concern assumption may be maintained, which is crucial for preparing the financial statements.

Management's Responsibility: It's the responsibility of management to evaluate the impact of the business combination on the financial statements and ensure that appropriate disclosures are made in accordance with accounting standards. Management should assess the materiality of the business combination and its effect on the financial position, results of operations, and cash flows of the entity.

Subsequent Adjustment and Restatement: If the business combination is significant and occurs before the financial statements are approved for issue, but after the balance sheet date, adjustments to the financial statements may be necessary. This could involve restating comparative information for prior periods to reflect the impact of the business combination on the entity's financial position and performance.

RECENT DEVELOPMENT'S IN M&A ACCOUNTING

AS-14 Accounting for amalgamations did not provide guidance in many situations such as demerger, reverse acquisition. In the absence of specific accounting guideline companies were using various alternative accounting alternatives for achieving tax efficiencies.

In the cases court approved mergers and acquisition, the accounting treatment was prescribed by the courts which sometimes used to be contrary to the accounting standard.

With the introduction of IND-AS 103 – Business combination and Companies Act, 2013 accounting treatment of Mergers and Acquisitions have undergone a drastic change.

Section 232 of the Companies Act 2013 provides that accounting treatment prescribed in the court approved scheme for merger, demerger, amalgamation or group restructuring should be in accordance with the notified accounting standards prescribed in the Companies Act, 2013.

Certain other developments in M&A accounting are as below:

(a) Method of Accounting for business combination

Under AS-14 many companies were able to account for business combination between commonly controlled enterprises using purchase method. As a result of this, tax benefits for goodwill amortisation was available while computing book profit for MAT purpose.

Under IND AS-103 it is mandatory to use pooling of interest method for business combination between commonly controlled enterprises.

As a result of this accounting alternatives gets restricted and the consequent tax benefits will also be not available.

(b) *Appointed date v. Effective date*

The date from which the scheme of amalgamation comes into force (and is usually specified in the scheme of amalgamation). It also denotes the date on which the amalgamation takes place or, in other words, the property, assets, and liabilities of the Transferor-Company vest in and are transferred to the Transferee Company. In court approved merger, demerger and other restructuring accounting was done from the appointed date once the court order became effective.

The effective date is the date when the amalgamation/merger is completed in all respects after having gone through the formalities involved and the transferor company having been liquidated by the Registrar of Companies, based on the approval of the NCLT and filing the necessary documents thereof with the Registrar of Companies.

With the implementation of IND-AS 103 Business combination this is going to change. As per IND-AS 103 accounting for business combination should be done on the date on which the acquirer obtains control.

(c) Accounting for goodwill

AS-14 provided an accounting choice to compute the goodwill at the fair value of the assets taken over or at the net asset value of the assets taken over. However, this choice is not available in IND AS 103 Business combination, as the goodwill has to be computed using the fair value of the net assets taken over.

AS-14 provides for amortisation of goodwill over a period of five years. IND-AS 103 Business combination prohibits amortisation of goodwill and is required to test goodwill for impairment annually. This will result in a volatile profit and loss account.

Goodwill amortisation was available as tax deductible item while computing MAT liability. This will not be available in the IND-AS regime.

(d) Common control business combinations

IND AS prescribes specific accounting principles for common control business combinations. It mandates the use of the pooling of interest method with restatement of the comparative period presented for the period the entities were in common control. The requirement to restate comparative may not be fully in sync with the tax treatment of considering the merger or amalgamation only from the appointed date.

(e) Income Taxes

As per the requirement of Ind AS 12, no deferred tax consequence should be recorded on initial recognition of deferred tax except assets and liabilities acquired during business combination. Accordingly, the acquirer shall recognise and measure a deferred tax asset or liability arising from the assets acquired and liabilities assumed in a business combination in accordance with Ind AS 12, Income Taxes.

The acquirer shall account for the potential tax effects of temporary differences and carry forwards of an acquiree that exist at the acquisition date or arise as a result of the acquisition in accordance with Ind AS 12.

(f) Indemnification assets

The seller in a business combination may contractually indemnify the acquirer for the outcome of a contingency or uncertainty related to all or part of a specific asset or liability. For example, the seller may indemnify the acquirer against losses above a specified amount on a liability arising from a particular contingency; in other words, the seller will guarantee that the acquirer's liability will not exceed a specified amount. As a result, the acquirer obtains an indemnification asset. The acquirer shall recognise an indemnification asset at the same time that it recognises the indemnified item measured on the same basis as the indemnified item, subject to the need for a valuation allowance for uncollectible amounts.

Example

Sun Pharma Limited acquires Ranbaxy Limited in a business combination on 1st April, 2021. Ranbaxy Limited is being sued by one of its customers for side effects of medicines for Rs. 25,00,000. The sellers of Ranbaxy Limited provide an indemnification to Sun Pharma for the reimbursement of any losses greater than Rs. Rs. 10,00,000. At the acquisition date, Sun Pharma determined recognises the fair value of the contingent liability of Rs. 25,00,000 in the acquisition accounting.

In the acquisition accounting Sun Pharma also recognises an indemnification asset of Rs. ` 15,00,000 (Rs. ` 25,00,000 – Rs. 10,00,000).

(g) Intangible assets

The acquirer shall record separately from Goodwill, the identifiable intangible acquired in a business combination. An intangible asset is identifiable if it meets either the separability criterion or the contractual-legal criterion.

(h) Share based payment transactions

The acquirer shall measure a liability or an equity instrument related to share-based payment transactions of the acquiree or the replacement of an acquiree's share-based payment transactions with share-based payment transactions of the acquirer in accordance with the method in Ind AS 102, Share-based Payment, at the acquisition date.

(i) Assets held for sale

The acquirer shall measure an acquired non-current asset (or disposal group) that is classified as held for sale at the acquisition date in accordance with Ind AS 105, Non-current Assets Held for Sale and Discontinued Operations, at fair value less costs to sell in accordance with that Ind AS.

Difference between Ind AS 103 and AS 14

- ***Scope:*** Ind AS 103 has a wider scope than AS 14.
- ***Method of accounting:*** Ind AS 103 prescribe only acquisition method for every business combination whereas AS 14 states two method of accounting: Pooling of interest method and Purchase method.
- ***Recognition and measurement:*** Ind AS 103 recognises acquired identifiable assets liabilities and non-controlling interest at fair value. AS 14 allows choice of Book value or Fair Value.
- ***Goodwill:*** Under Ind AS 103, Goodwill is not amortised but tested for annual impairment where as AS 14 require goodwill to be amortised over a period not exceeding 5 years.
- ***Non Controlling Interest (NCI):*** Ind AS 103 provide for accounting of NCI, AS 14 do not.
- ***Recording for consolidated financial statements:*** It is provided in Ind AS 103, not in AS 14.

- ***Common control transactions:*** Appendix C deals with accounting for common control transactions, which prescribes Pooling of interest method of accounting. AS14 do not prescribe any different accounting for such transactions.
- ***Contingent Consideration:*** Ind AS 103 recognise contingent consideration, AS 14 do not.
- ***Reverse acquisitions:*** Ind AS 103 deal with reverse acquisitions, AS 14 do not.

IFRS 3- BUSINESS COMBINATION

The principles of IND- AS 103 Business combination and IFRS 3 are same to a very great extent.

There are only few carve out in IND-AS 103 when compared to IFRS 3. They are as follows:

IFRS-3 excludes from its scope business combinations of entities under common control. Ind AS 103 (Appendix C) gives the guidance in this regard.

IFRS-3 requires bargain purchase gain arising on business combination to be recognised in profit or loss account. IND-AS 103 requires that the bargain purchase gain to be recognised in other comprehensive income and accumulated in equity as capital reserve, unless there is no clear evidence for the underlying reason for classification of the business combination as a bargain purchase, in which case, it shall be recognised directly in equity as capital reserve.

The main reason for this carve out is, the recognition of such gains in profit or loss would result into recognition of unrealised gains as the value of net assets is determined on the basis of fair value of net assets acquired.

DEMERGER

Demerger is a method of corporate restructuring by which a business unit or subsidiary of a company becomes an independent entity from its parent's entity. The parent firm distributes shares of subsidiary to its shareholders through a stock dividend. In most cases demerger unlocks hidden shareholder value. For the parent company, it sharpens the management focus. For the new entity, it gets independence to make decisions, explore new opportunities based on its strength.

The word demerger has got statutory recognition in the Income Tax Act, 1961. As per Income Tax Act, 1961 demerger in relation to companies, means the transfer, pursuant to a scheme of arrangement under Companies Act, 2013 by a demerged company of its one or more undertakings to any resulting company subject to conditions specified. As per various court decisions AS-14 -Accounting for Amalgamations is not applicable to demergers.

Types of Demergers

Spin-off: A company creates a new, independent entity and distributes its shares to existing shareholders.

Split-off: Existing shareholders exchange their shares in the parent company for shares in the newly formed entity.

Equity Carve-out: A parent company sells a portion of its subsidiary's shares through an initial public offering (IPO) while retaining control.

Asset Divestiture: The parent company sells specific assets or divisions to another entity.

Motivations for Demergers:

Focus on Core Business: Allows the parent company to concentrate on its core operations, enhancing operational efficiency and strategic focus.

Unlocking Shareholder Value: Shareholders may benefit from increased transparency, improved valuation multiples, and enhanced growth prospects in separate entities.

Regulatory Compliance: Demergers can be a response to regulatory requirements or antitrust concerns to ensure compliance with competition laws.

Tax Efficiency: Demergers may offer tax advantages, such as realizing tax losses, optimizing capital structures, or achieving tax-free status in certain jurisdictions.

Process of Demergers:

Strategic Planning: The parent company assesses its portfolio and identifies non-core assets or divisions for potential separation.

Structuring: Deciding on the type of demerger, determining the ownership structure of the new entity, and establishing governance mechanisms.

Legal and Regulatory Compliance: Ensuring compliance with applicable laws, regulations, and corporate governance requirements.

Financial and Tax Considerations: Evaluating the financial impact of the demerger, including tax implications, allocation of assets and liabilities, and potential restructuring costs.

Communication: Effectively communicating the rationale, benefits, and implications of the demerger to stakeholders, including shareholders, employees, customers, and regulators.

Implementation: Executing the demerger plan, which may involve legal filings, shareholder approvals, transfer of assets and liabilities, and listing of shares on stock exchanges.

Impact of Demergers:

Financial Reporting: Demergers result in changes to the financial statements of the parent company and the newly formed entity, including adjustments to assets, liabilities, equity, and related disclosures.

Employee Relations: Demergers can affect employee morale, job security, and organizational culture. Companies need to manage employee transitions effectively.

Market Reaction: The stock prices of the parent company and the new entity may be impacted by market perceptions of the demerger's strategic rationale, expected synergies, and future prospects.

Operational Integration: After the demerger, both entities may need to reorganize their operations, systems, and processes to operate independently and achieve their strategic objectives.

Challenges and Risks:

Execution Risks: Demergers involve complex legal, financial, and operational processes, and failure to execute effectively can result in disruptions, delays, or cost overruns.

Regulatory Hurdles: Obtaining regulatory approvals and managing compliance with antitrust, tax, and other regulatory requirements can pose challenges.

Value Leakage: The value created through the demerger may be eroded by transaction costs, tax liabilities, or adverse market reactions.

Integration Challenges: Separating shared services, IT systems, and other interdependencies between the parent company and the demerged entity can be challenging and costly.

Case 1 – Scheme of arrangement between Sony India Private Limited (Sony India) and Sony Software Centre Private Limited (Sony Software) with reference to transfer of software undertaking of Sony India to Sony Software

The Delhi High Court, while approving scheme of arrangement between Sony India and Sony Software in 2012 has clarified that AS-14 (i.e., accounting standards issued by the Institute of Chartered Accountants of India) is applicable only to amalgamations and not to demerger. As per the scheme of arrangement, 'Software Undertaking' of Sony India is proposed to be transferred to Sony Software under Sections 391 to 394 of the Companies Act, 1956. One of the conditions of the scheme was that any excess in the value of net assets of software undertaking transferred to the resulting company shall be applicable for distribution to the shareholders of the resulting company.

Regional Director of Northern Region, Ministry of Corporate has raised objection in his affidavit filed with the High Court stating that excess, if any, in the value of the net assets of the software undertaking should be adjusted to the capital reserve as prescribed in AS-14 and not to the general reserve as proposed in the scheme of arrangement.

The petitioners contended that AS-14 is applicable only to amalgamations and not to demerger. It was clarified that AS-14 is applicable only to amalgamations and not to demerger. On a plain reading of the accounting standard under reference, it is clear that the same is applicable only in case of an amalgamation and not in case of demergers. This has also been held by the Gujarat High Court in the case of 2010 1CLJ 351 tiled *Gallops Realty* (P) Ltd. v. *State of Gujarat.*

Case 2- *Gallops Realty* (P) Ltd. v. *State of Gujarat*

High Court of Gujarat in the case of ***Gallops Realty (P) Ltd., In re v. K.A. PUJ, J.(2010),*** under Section 391, read with sections 394 and 100, of the Companies Act, 1956 Petitioner-companies, i.e., demerged company and resulting company, sought for sanction of composite scheme of arrangement in nature of purchase of shares and demerger of hotel business of demerged company to resulting company and consequent reconstruction of share capital of demerged company under section 391, read with sections 394, 78 and 100 consisting of reduction of paid-up share capital as well as utilization of share premium account. Regional Director stated that as per scheme, capital profit on demerger would be transferred to general reserve in books of resulting company which was not in consonance with generally accepted accounting principles as also Accounting Standard-14 which provide that any profit arising out of a capital transaction ought to be treated as capital profit and, hence, would be transferred to capital reserve and not to general reserve. It was held that the observation of Regional Director was not in consonance with accounting principles in general and Accounting Standard-14 in particular, as Accounting Standard-14 is applicable only in case of amalgamation and not in case of demerger, as envisaged in instant scheme.

Applicability of IND-AS 103 for Demerger Transactions

As discussed above the concept of demerger is recognised in the Income Tax Act, 1961. However, tax benefits are available only if the conditions of demerger provided in section 2(19AA) are met. One such condition is that assets and liabilities are to be recorded by the transferee company at the book value of the transferor company.

The requirement to record assets and liabilities at fair value in case of non-common control business combination under IND-AS 103 may create problem in achieving a most tax efficient demerger.

INTERNAL RECONSTRUCTION

When a company incurs loss for number of years, the balance sheet does not reflect the true position of the business, as a higher net worth is depicted, than that of the real one. In such a company the assets are overvalued and it has many intangible assets and fictitious assets. Such a situation does not depict a true picture of financial statements. Such a situation requires reconstruction. Such a reconstruction may be carried out internally.

In an internal reconstruction, the assets are revalued, liabilities are negotiated, and losses suffered are written-off by reducing the paid-up value of shares and/or varying the rights attached to different classes of shares. Existing company is not liquidated.

Internal reconstruction may be done in the following ways:

(a) Cost reduction through closure of units.

(b) Redundancy programmes.

(c) Management or organisational restructuring involving decentralization.

Internal Reconstruction may be done by ways of:

(a) Cost Reduction through Closure of Units:

Assessment of Underperforming Units: The company evaluates its business units or operations to identify those that are underperforming or no longer aligned with its strategic objectives.

Closure or Rationalization: Underperforming units or operations may be closed down entirely or rationalized to reduce costs. This could involve shutting down unprofitable facilities, discontinuing unproductive product lines, or exiting unprofitable markets.

Impact Analysis: The company assesses the financial and operational impact of closure or rationalization, considering factors such as employee layoffs, asset write-offs, lease terminations, and potential restructuring costs.

Communication and Stakeholder Management: Transparent communication with employees, suppliers, customers, and other stakeholders is essential to manage the impact of closures effectively. The company may provide support to affected employees and establish a transition plan for suppliers and customers.

Optimization of Resources: By closing underperforming units, the company can reallocate resources, including capital, personnel, and management attention, to focus on core businesses or areas with higher growth potential.

(b) Redundancy Programs:

Identification of Redundancies: The company identifies areas of duplication, inefficiency, or overlap in its operations, such as redundant processes, roles, functions, or departments.

Voluntary or Involuntary Redundancy Programs: Redundancy programs may involve offering voluntary retirement packages, early retirement incentives, or severance packages to employees. In some cases, involuntary layoffs or job eliminations may be necessary to streamline operations.

Skills Assessment and Retention: The company assesses the skills and capabilities of its workforce to retain critical talent and ensure that the right people are in the right roles post-restructuring.

Legal and Regulatory Compliance: Redundancy programs must comply with applicable labor laws, regulations, and collective bargaining agreements. The company may need to consult with employee representatives or unions and provide adequate notice and compensation to affected employees.

Reorganization and Workforce Planning: Following redundancy programs, the company may reorganize its workforce and realign roles and responsibilities to optimize efficiency and productivity. Workforce planning ensures that the company has the necessary talent and skills to support its strategic objectives.

(c) Management or Organizational Restructuring involving Decentralization:

Evaluation of Organizational Structure: The company assesses its existing organizational structure to determine whether it is conducive to agility, innovation, and effective decision-making.

Decentralization: Management restructuring may involve decentralizing decision-making authority and empowering lower-level managers or teams to make more autonomous decisions. This could lead to faster responses to market changes, improved customer service, and increased accountability.

Clarification of Roles and Responsibilities: Clear delineation of roles, responsibilities, and accountability is essential in decentralized structures to avoid confusion and ensure alignment with organizational goals.

Communication and Training: Effective communication is critical to ensure that employees understand the rationale behind decentralization and their roles in the new structure. Training programs may be provided to equip managers and employees with the necessary skills to thrive in a decentralized environment.

Performance Monitoring and Feedback: The company establishes performance metrics and feedback mechanisms to evaluate the effectiveness of decentralization and make adjustments as needed. Regular monitoring helps identify bottlenecks, address challenges, and capitalize on opportunities for improvement.

Process of Internal Reconstruction:

Identify the Objective: Determine the purpose of the internal reconstruction, whether it's to eliminate accumulated losses, to change the capital structure, or for any other reason.

Assess the Current Capital Structure: Review the company's balance sheet to understand the existing capital structure, including share capital, reserves, and surplus.

Propose Changes: Decide on the changes to be made to the capital structure to achieve the desired objective. This could involve the conversion of reserves into share capital, the cancellation of accumulated losses against reserves, or other adjustments.

Journal Entries: Prepare the necessary journal entries to reflect the changes in the capital structure. Ensure that the total capital remains unchanged throughout the process.

Disclosure: Provide adequate disclosure in the financial statements regarding the internal reconstruction, including any notes explaining the changes made and their impact on the company's financial position.

LESSON ROUND-UP

- Accounting Standard-14 'Accounting for Amalgamations' lays down the accounting and disclosure requirements in respect of amalgamations of companies and the treatment of any resultant goodwill or reserves. AS14 is not applicable to demergers.AS 14 provides for two types of amalgamations viz. amalgamation in the nature of merger and amalgamation in the nature of purchase.
- There are two main methods of accounting for amalgamations viz. the pooling of interests method; and the purchase method. The pooling of interests method is used in case of amalgamation in the nature of merger. The purchase method is used in accounting for amalgamations in the nature of purchase.
- The consideration for amalgamation means the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company.
- If the amalgamation is an 'amalgamation in the nature of merger', the identity of the reserves is preserved and they appear in the financial statements of the transferee company in the same form in which they appeared in the financial statements of the transferor company.
- If the amalgamation is an 'amalgamation in the nature of purchase', the identity of the reserves, other than the statutory reserves is not preserved, dealt within the certain circumstances specified.
- Good will arising on amalgamation represents a payment made in anticipation of future income and it is appropriate to treat it as an asset to be amortised to income on a systematic basis over its useful life.
- When an amalgamation is effected after the balance sheet date but before the issuance of the financial statements of either party to the amalgamation, disclosure should be made as per the provisions of AS-4, contingencies and events occurring after the Balance Sheet Date, but the amalgamation should not be incorporated in the financial statements.

- While filing for approval of any draft Scheme of amalgamation/merger/reconstruction, etc. with the stock exchange under the listing agreement, the company is also required to file an auditors' certificate to the effect that the accounting treatment contained in the scheme is in compliance with all the Accounting Standards.
- A business combination is an act of bringing together of separate entities or business into one reporting unit. The result of business combination is one entity obtains control of one or more businesses. If an entity obtains control over other entities which are not business, the act is not a business combination. In such a case the reporting entity will account it as asset acquisition.
- For each business combination, one of the combining entities shall be identified as the acquirer. Most of the time, it is straightforward - the acquirer is usually the investor who acquires an investment or a subsidiary. The acquiree is the business that the acquirer obtains control of in business combination.
- The acquirer shall identify the acquisition date, which is the date on which it obtains control of the acquire. The acquirer shall measure the identifiable assets acquired and liabilities assumed at their acquisition date fair values.
- On the acquisition date, the acquirer shall recognise separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. The acquirer shall recognize goodwill as of the acquisition date measured based on the principles discussed above.
- Business combinations involving entities or businesses under common control shall be accounted for using the pooling of interest method. In a business combination achieved in stages, the acquirer shall remeasure its previously held equity interest in the acquiree at its acquisition date fair value and recognise the resulting gain or loss, if any, in profit or loss.
- The acquirer shall disclose information that enables users of its financial statements to evaluate the nature and financial effect of a business combination that occurs either: During the current reporting period; or after the end of the reporting period but before the financial statements are approved for issue.
- Section 232 of the Companies Act 2013 provides that accounting treatment prescribed in the court approved scheme for merger, demerger, amalgamation or group restructuring should be in accordance with the notified accounting standards prescribed in the Companies Act, 2013.
- The consideration for which the acquirer transfers in exchange for the acquiree includes any asset or liability resulting from a contingent consideration arrangement.

GLOSSARY

Acquiree: An acquiree is a target company that is subject to an acquisition attempt by an acquirer.

Acquirer: An acquirer is a person or company that purchases all or a portion of an asset or company. Acquisition Date: The acquisition date is the date on which the acquirer obtains control of the acquire.

Appointed date: Appointed date is the date which is chosen by the management for effecting the Scheme and its accounting entries.

Business combination: A business combination is a transaction in which the acquirer obtains control of another business (the acquiree).

Common control business combination: Common control business combination means a business combination involving entities or business in which all the combining entities or business are ultimately controlled by the same party or parties both before and after the business combination.

Effective date: Effective date is the date from which the Scheme becomes effective in terms of law and the date on which all the necessary approvals have been obtained.

Goodwill: Goodwill is an intangible asset which represents non-physical items that add to a company's value but cannot be easily identified or valued.

Measurement period: The measurement period is the period after the acquisition date during which the parent may adjust the provisional amounts recognised in respect of the acquisition of the subsidiary.

Transferee Company: A company into which a transferor company is amalgamated. The company buying the other company is known as "Transferee Company".

Transferor Company: A company which is amalgamated into another company. The company selling its business is known as "Transferor Company".

TEST YOURSELF

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. Does AS-14 apply to demerger? Explain.
2. What are the types of amalgamation provided under AS-14?
3. What are the methods of accounting provided under AS-14?
4. What is business as per IND-AS 103?
5. What is the meaning of Business Combination as per IND-AS 103?

LIST OF FURTHER READINGS

- Financial Management, 2nd Edition by P C Tulsian, S. Chand Publications
- Master Guide to Merger and Acquisition in India – Tax and Regulatory, 4th Edition, CCH India
- Mergers & Acquisitions and Corporate Valuation, Dr. Manu Sharma, Wiley Publication
- Accounting for Amalgamation -AS-14 (Revised) issued by the Ministry of Corporate Affairs. 5. Business Combination (Ind AS -103) issued by the Ministry of Corporate Affairs
- Students Guide to Ind AS Converged IFRS by Dr D.S. Rawat

Taxation & Stamp Duty aspects of Corporate Restructuring

Lesson 7

KEY CONCEPTS

■ Capital Gain Tax ■ Conveyance ■ Stamp Duty ■ Slump Sale ■ Instrument ■ Demerger

Learning Objectives

To understand:

- Merger/ Demerger
- Slump Sale
- Carrying forward and set-off of accumulated business loss
- Unabsorbed Depreciation Allowance
- Capital Gains Tax
- Levy of stamp duty on
- Amalgamation and Mergers

Lesson Outline

- Taxation aspects of mergers and amalgamations
- Taxation aspects of slump sale
- Taxation aspects of demerger
- Deemed Dividend
- Constitutional background on levy of stamp duty
- Stamp duty payable on High Court order sanctioning amalgamation
- Amalgamation of holding and subsidiary companies – exemption from payment of stamp duty
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Futher Readings

REGULATORY FRAMEWORK

- Companies Act, 2013
- Income Tax Act, 1961
- Indian Stamp Act, 1899

INTRODUCTION

In any merger or amalgamation, financial aspects of the transaction are of prime importance as the same are expected to accrue financial benefits. While framing a scheme of merger or amalgamation, a company has to fulfil the conditions prescribed under the Company Law as already discussed in previous lessons, but it has also to look after two very important aspects, i.e., taxation and stamp duty.

Tax considerations predominate and inevitably direct the manner in which the entire scheme has to be designed. Tax planning in cases of amalgamation of companies is perhaps the most vital aspect of decision-making involved in framing of the scheme of amalgamation. A company planning a merger or a takeover, need to do intensive tax planning before finalising the deal to get the maximum tax concession and benefits in the deal. In India, law provides for ample benefits in the form of various provisions to companies going in for amalgamation.

Since a merger or demerger inevitably entails some transfer of property, movable or immovable, it attracts the imposition of stamp duty which is essentially a form of revenue for the government arising out of taxation of various transactions governed under the Indian Stamp Act, 1899. The exposition of stamp duty is a vital aspect because it could substantially increase the costs of a merger deal.

In corporate restructuring through amalgamation and merger, stamp duty planning assumes a significant role and all efforts are made to pay as less a duty on such amalgamations as possible and yet proceed with the acquisitions through mergers and amalgamations. The incidence of stamp duty is an important consideration in the planning of any merger.

Since the stamp duty levied on amalgamations or mergers differ from one State to another, there is disadvantage of amalgamations in one State compared to another and therefore professional time and attention is devoted to work out the best method which can afford stamp duty savings on such amalgamations or mergers.

TAXATION ASPECTS OF MERGERS AND AMALGAMATIONS

The Companies Act, 2013 without strictly defining the term Amalgamation or Demerger, explains the concept. A 'merger' is a combination of two or more entities into one; the desired effect being not just the accumulation of assets and liabilities of the distinct entities, but organization of such entity into one business. Section 2(1B) of the Income Tax Act, 1961 defines the term 'amalgamation' as follows:

"Amalgamation" in relation to companies, means the merger of one or more companies with another company or the merger of two or more companies to form one company (the company or companies which so merge being referred to as the amalgamating company or companies and the company with which they merge or which is formed as a result of the merger, as the amalgamated company), in such a manner that –

(i) all the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation;

(ii) all the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation;

(iii) shareholders holding not less than three-fourths in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee for, the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of the amalgamation, otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first mentioned company.

Example:

Company "A" merges with another Company "B" in a scheme of amalgamation, and immediately before the amalgamation, company "B" held 20% of the shares in Company "A", the abovementioned condition will be satisfied if shareholders holding not less than 3/4th in value of the remaining 80% of share in company "A" i.e. 60% thereof (3/4th of 80), become shareholders of company "B" by virtue of the amalgamation.

Thus, for a merger to be qualified as an 'amalgamation' for the purpose of the Income Tax Act, 1961, the above three conditions have to be satisfied.

CARRY FORWARD AND SET OFF OF ACCUMULATED LOSS AND UNABSORBED DEPRECIATION ALLOWANCE

Under Section 72A of Income Tax Act, 1961, a special provision is made which relaxes the provision relating to carrying forward and set-off of accumulated business loss and unabsorbed depreciation allowance in certain cases of amalgamation.

(A) Amalgamation

(1) Where there has been an amalgamation of—

(a) a company owning an industrial undertaking or a ship or a hotel with another company; or

(b) a banking company referred to in clause (c) of section 5 of the Banking Regulation Act, 1949 with a specified bank; or

(c) one or more public sector company or companies with one or more public sector company or companies; or

(d) an erstwhile public sector company with one or more company or companies, if the share purchase agreement entered into under strategic disinvestment restricted immediate amalgamation of the said public sector company and the amalgamation is carried out within five years from the end of the previous year in which the restriction on amalgamation in the share purchase agreement ends,

then, notwithstanding anything contained in any other provision of this Act, the accumulated loss and the unabsorbed depreciation of the amalgamating company shall be deemed to be the loss or, as the case may be, allowance for unabsorbed depreciation of the amalgamated company for the previous year in which the amalgamation was effected, and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly:

Provided that the accumulated loss and the unabsorbed depreciation of the amalgamating company, in case of an amalgamation referred to in clause (d), which is deemed to be the loss or, as the case may be, the allowance for un-absorbed depreciation of the amalgamated company, shall not be more than the accumulated loss and unabsorbed depreciation of the public sector company as on the date on which the public sector company ceases to be a public sector company as a result of strategic disinvestment.

Explanation.— For the purposes of clause (d), —

(i) "control" shall have the same meaning as assigned to in clause (27) of section 2 of the Companies Act, 2013;

(ii) "erstwhile public sector company" means a company which was a public sector company in earlier previous years and ceases to be a public sector company by way of strategic disinvestment by the Government;

(iii) "strategic disinvestment" means sale of shareholding by the Central Government or any State Government or a public sector company, in a public sector company or in a company, which results in—

(a) reduction of its shareholding to below fifty-one per cent; and

(b) transfer of control to the buyer:

Provided that the condition laid down in sub-clause (a) shall apply only in a case where shareholding of the Central Government or the State Government or the public sector company was above fifty-one per cent before such sale of shareholding:

Provided further that requirement of transfer of control referred to in sub-clause (b) may be carried out by the Central Government or the State Government or the public sector company or any two of them or all of them.

(2) Notwithstanding anything contained in sub-section (1), the accumulated loss shall not be set off or carried forward and the unabsorbed depreciation shall not be allowed in the assessment of the amalgamated company unless—

(a) the amalgamating company—

(i) has been engaged in the business, in which the accumulated loss occurred or depreciation remains unabsorbed, for three or more years;

(ii) has held continuously as on the date of the amalgamation at least three-fourths of the book value of fixed assets held by it two years prior to the date of amalgamation.

(b) the amalgamated company—

(i) holds continuously for a minimum period of five years from the date of amalgamation at least three-fourths of the book value of fixed assets of the amalgamating company acquired in a scheme of amalgamation;

(ii) continues the business of the amalgamating company for a minimum period of five years from the date of amalgamation.

(iii) fulfils such other conditions as may be prescribed to ensure the revival of the business of the amalgamating company or to ensure that the amalgamation is for genuine business purpose.

(3) In a case where any of the conditions laid down in sub-section (2) are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the amalgamated company shall be deemed to be the income of the amalgamated company chargeable to tax for the year in which such conditions are not complied with.

(B) Demerger

(4) Notwithstanding anything contained in any other provisions of this Act, in the case of a demerger, the accumulated loss and the allowance for unabsorbed depreciation of the demerged company shall—

(a) where such loss or unabsorbed depreciation is directly relatable to the undertakings transferred to the resulting company, be allowed to be carried forward and set off in the hands of the resulting company;

(b) where such loss or unabsorbed depreciation is not directly relatable to the undertakings transferred to the resulting company, be apportioned between the demerged company and the resulting company in the same proportion in which the assets of the undertakings have been retained by the demerged company and transferred to the resulting company, and be allowed to be carried forward and set off in the hands of the demerged company or the resulting company, as the case may be.

(5) The Central Government may, for the purposes of this Act, by notification in the Official Gazette, specify such conditions as it considers necessary to ensure that the demerger is for genuine business purposes.

(C) Reorganisation of Business

(6) Where there has been reorganisation of business, whereby, a firm is succeeded by a company fulfilling the conditions laid down in clause (xiii) of section 47 or a proprietary concern is succeeded by a company fulfilling the conditions laid down in clause (xiv) of section 47, then, notwithstanding anything contained in any other provision of this Act, the accumulated loss and the unabsorbed depreciation of the predecessor firm or the proprietary concern, as the case may be, shall be deemed to be the loss or allowance for depreciation of the successor company for the purpose of previous year in which business reorganisation was effected and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly:

Provided that if any of the conditions laid down in the proviso to clause (xiii) or the proviso to clause (xiv) to section 47 are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the successor company, shall be deemed to be the income of the company chargeable to tax in the year in which such conditions are not complied with.

Conversion of Company into LLP [Section 72A(6A)]

(6A) Where there has been reorganisation of business whereby a private company or unlisted public company is succeeded by a limited liability partnership fulfilling the conditions laid down in the proviso to clause *(xiiib*) of section 47, then, notwithstanding anything contained in any other provision of this Act, the accumulated loss and the unabsorbed depreciation of the predecessor company, shall be deemed to be the loss or allowance for depreciation of the successor limited liability partnership for the purpose of the previous year in which business reorganisation was effected and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly:

Provided that if any of the conditions laid down in the proviso to clause *(xiiib)* of section 47 are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the successor limited liability partnership, shall be deemed to be the income of the limited liability partnership chargeable to tax in the year in which such conditions are not complied with.

(7) For the purposes of Section 72A—

(a) "accumulated loss" means so much of the loss of the predecessor firm or the proprietary concern or the private company or unlisted public company before conversion into limited liability partnership or the amalgamating company or the demerged company, as the case may be, under the head "Profits and gains of business or profession" (not being a loss sustained in a speculation business) which such predecessor firm or the proprietary concern or the company or amalgamating company or demerged company, would have been entitled to carry forward and set off under the provisions of section 72 if the reorganisation of business or conversion or amalgamation or demerger had not taken place;

(aa) "industrial undertaking" means any undertaking which is engaged in—

(i) the manufacture or processing of goods; or

(ii) the manufacture of computer software; or

(iii) the business of generation or distribution of electricity or any other form of power; or (iiia) the business of providing telecommunication services, whether basic or cellular, including radio paging, domestic satellite service, network of trunking, broadband network and internet services; or

(iv) mining; or

(v) the construction of ships, aircrafts or rail systems;

(b) ***"unabsorbed depreciation"*** means so much of the allowance for depreciation of the predecessor firm or the proprietary concern or the private company or unlisted public company before conversion into limited liability partnership or the amalgamating company or the demerged company, as the case may be, which remains to be allowed and which would have been allowed to the predecessor firm or the proprietary concern or the company or amalgamating company or demerged company, as the case may be, under the provisions of this Act, if the reorganisation of business or conversion or amalgamation or demerger had not taken place;

(c) ***"specified bank"*** means the State Bank of India constituted under the State Bank of India Act, 1955 or a subsidiary bank as defined in the State Bank of India (Subsidiary Banks) Act, 1959 or a corresponding new bank constituted under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 or under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980.

CARRY FORWARD AND SET OFF OF ACCUMULATED BUSINESS LOSSES AND UNABSORBED DEPRECIATION IN A SCHEME OF AMALGAMATION IN CERTAIN CASES [SECTION 72AA]

(1) Applicability: This section provides for carry forward and set off of accumulated loss and unabsorbed depreciation allowance where there has been an amalgamation of –

(i) one or more banking company with—

(a) any other banking institution under a scheme sanctioned and brought into force by the Central Government under sub-section (7) of section 45 of the Banking Regulation Act, 1949; or

(b) any other banking institution or a company subsequent to a strategic disinvestment, wherein the amalgamation is carried out within a period of five years from the end of the previous year during which such strategic disinvestment is carried out; or

(ii) one or more corresponding new bank or banks with any other corresponding new bank under a scheme brought into force by the Central Government under section 9 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 or under section 9 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 or both, as the case may be; or

(iii) one or more Government company or companies with any other Government company under a scheme sanctioned and brought into force by the Central Government under section 16 of the General Insurance Business (Nationalisation) Act, 1972.

(2) Allowability of carry forward and set-off of accumulated loss and unabsorbed depreciation in case of amalgamation:

The accumulated loss and the unabsorbed depreciation of such banking company or companies or amalgamating corresponding new bank or banks or amalgamating Government company or companies shall be deemed to be the loss or, as the case may be, allowance for depreciation of such banking institution or company or amalgamated corresponding new bank or amalgamated Government company for the previous year in which the scheme of amalgamation was brought into force and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly.

For the purposes of Section72AA —

(i) "accumulated loss" means so much of the loss of the amalgamating banking company or companies or amalgamating corresponding new bank or banks or amalgamating Government company or companies under the head "Profits and gains of business or profession" (not being a loss sustained in a speculation business) which such amalgamating banking company or companies or amalgamating corresponding new bank or banks or amalgamating Government company or companies, would have been entitled to carry forward and set off under the provisions of section 72, if the amalgamation had not taken place;

(ii) "banking company" shall have the meaning assigned to it in clause (c) of section 5 of the Banking Regulation Act, 1949;

(iii) "banking institution" shall have the meaning assigned to it in sub-section (15) of section 45 of the Banking Regulation Act, 1949;

(iv) "corresponding new bank" shall have the meaning assigned to it in clause (d) of section 2 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 or, as the case may be, clause (b) of section 2 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980;

(v) "general insurance business" shall have the meaning assigned to it in clause (g) of section 3 of the General Insurance Business (Nationalisation) Act, 1972;

(vi) "Government company" means a Government company as defined in clause (45) of section 2 of the Companies Act, 2013, which is engaged in the general insurance business and which has come into existence by operation of section 4 or section 5 or section 16 of the General Insurance Business (Nationalisation) Act, 1972;

(via) "strategic disinvestment" shall have the meaning assigned to it in clause (iii) of the Explanation to clause (d) of sub-section (1) of section 72A;

(vii) "unabsorbed depreciation" means so much of the allowance for depreciation of the amalgamating banking company or companies or amalgamating corresponding new bank or banks or amalgamating Government company or companies which remains to be allowed and which would have been allowed to such banking company or companies or amalgamating corresponding new bank or banks or amalgamating Government company or companies, if the amalgamation had not taken place.

Capital Gains Tax

Capital gains tax is leviable if there arises capital gain due to transfer of capital assets. The word 'transfer' under section 2(47) of the Income Tax Act, 1961 includes the sale, exchange or relinquishment of the asset or the extinguishment of any rights therein or the compulsory acquisition thereof under any law or in a case where the asset is converted by the owner thereof into, or is treated by him as, stock-in-trade of a business carried on by him, such conversion or treatment or any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in Section 53A of the Transfer of Property Act,1882 or any transaction (whether by way of becoming a member of, or acquiring shares in, a co-operative society, company or other association of persons or by way of any agreement or any arrangement or in any other manner whatsoever) which has the effect of transferring or enabling the enjoyment of any immovable property.

Capital gain arises only when a capital asset is transferred. If the asset transferred is not a capital asset, it will not be taxed as capital gain. Section 2(14) of the Income Tax Act, 1961 defines capital assets as below:

For the purposes of this subject, Capital asset means,

(a) Property of any kind held by an assessee, whether or not connected with his business or profession.

(b) Any securities held by a Foreign Institutional Investor which has invested in such securities in accordance with the regulations made under Securities and Exchange Board of India Act, 1992.

(c) any unit linked insurance policy (ULIP) issued on or after 1.2.2021, to which exemption under section 10(10D) does not apply on account of –

(i) premium payable exceeding Rs, 2,50,000 for any of the previous years during the term of such policy; or

(ii) the aggregate amount of premium exceeding Rs. 2,50,000 in any of the previous years during the term of any such ULIP(s), in a case where premium is payable by a person for more than one ULIP issued on or after 1.2.2021.

But does not include the following:

1. Any stock in trade (Other than the securities referred to in sub-clause (b)), consumables stores or raw materials held for the purpose of his business or profession.

2. Personal effects (movable property including wearing apparel and furniture for personal use).

   Exclusions: (a) jewellery; (b) archaeological collections; (c) drawings; (d) paintings; (e) sculptures; or (f) any work of art.

3. Rural Agricultural land in India, which is not an urban agricultural land. In other words, it must be rural agricultural land.

   Explanation: For the removal of doubts, it is hereby clarified that "property" includes and shall be deemed to have always included any rights in or in relation to an Indian Company, including rights of management or control or any other rights whatsoever.

In an amalgamation, capital gain arises if there is a transfer of capital asset. However, section 47 of the Income Tax Act, 1961 treats certain transactions from amalgamation as not transfer and hence capital gains tax will not be applicable. They are as under:

(vi) any transfer in a scheme of amalgamation of a capital asset by the amalgamating company to the amalgamated company, if the amalgamated company is an Indian company.

(via) any transfer, in a scheme of amalgamation, of a capital asset being a share or shares held in an Indian company, by the amalgamating foreign company to the amalgamated foreign company, if–

(a) at least twenty-five per cent of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and

(b) such transfer does not attract tax on capital gains in the country, in which the amalgamating company is incorporated;

(viaa) any transfer, in a scheme of amalgamation of a banking company with a banking institution sanctioned and brought into force by the Central Government under sub-section (7) of section 45 of the Banking Regulation Act, 1949, of a capital asset by the banking company to the banking institution.

Explanation: For the purposes of this clause:

(i) "banking company" shall have the same meaning assigned to it in clause (c) of section 5 of the Banking Regulation Act, 1949;

(ii) "banking institution" shall have the same meaning assigned to it in sub-section (15) of section 45 of the Banking Regulation Act, 1949.

(viab) any transfer, in a scheme of amalgamation, of a capital asset, being a share of a foreign company, referred to in the Explanation 5 to clause (i) of sub-section (1) of section 9, which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the amalgamating foreign company to the amalgamated foreign company, if–

(A) at least twenty-five per cent of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and

(B) such transfer does not attract tax on capital gains in the country in which the amalgamating company is incorporated;

(vib) any transfer, in a demerger, of a capital asset by the demerged company to the resulting company, if the resulting company is an Indian company.

(vic) any transfer in a demerger, of a capital asset, being a share or shares held in an Indian company, by the demerged foreign company to the resulting foreign company, if–

(a) the shareholders holding not less than three-fourths in value of the shares of the demerged foreign company continue to remain shareholders of the resulting foreign company; and

(b) such transfer does not attract tax on capital gains in the country, in which the demerged foreign company is incorporated:

Provided that the provisions of sections 230 to 232 of the Companies Act, 2013 shall not apply in case of demergers referred to in this clause.

(vica) any transfer in a business reorganisation, of a capital asset by the predecessor co-operative bank to the successor co-operative bank or to the converted banking company;

(vicb) any transfer by a shareholder, in a business reorganisation, of a capital asset being a share or shares held by him in the predecessor co-operative bank if the transfer is made in consideration of the allotment to him of any share or shares in the successor co-operative bank or to the converted banking company.

Explanation: For the purposes of clauses (vica) and (vicb), the expressions "business reorganisation", "converted banking company", "predecessor co-operative bank" and "successor co-operative bank" shall have the meanings respectively assigned to them in section 44DB.

(vicc) any transfer in a demerger, of a capital asset, being a share of a foreign company, referred to in the Explanation 5 to clause (i) of sub-section (1) of section 9, which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the demerged foreign company to the resulting foreign company, if–

(a) the shareholders, holding not less than three-fourths in value of the shares of the demerged foreign company, continue to remain shareholders of the resulting foreign company; and

(b) such transfer does not attract tax on capital gains in the country in which the demerged foreign company is incorporated:

Provided that the provisions of sections 230 to 232 of the Companies Act, 2013 shall not apply in case of demergers referred to in this clause.

(vid) any transfer or issue of shares by the resulting company, in a scheme of demerger to the shareholders of the demerged company if the transfer or issue is made in consideration of demerger of the undertaking

(vii) any transfer by a shareholder, in a scheme of amalgamation, of a capital asset being a share or shares held by him in the amalgamating company, if–

(a) the transfer is made in consideration of the allotment to him of any share or shares in the amalgamated company except where the shareholder itself is the amalgamated company, and

(b) the amalgamated company is an Indian company.

Even in the absence of Section 47(vii) of the Act, a shareholder is not liable to pay any capital gains tax since an amalgamation does not include exchange or relinquishment of the assets. Amalgamation does not involve an exchange or relinquishment of shares by amalgamating company as held in *CIT v. Rasik Lal Manek Lal (1975) 95I TR 656).* However, no benefit will be available under Section 47(vii) if the shareholders of amalgamating company are allotted something more than share in the amalgamated company viz. bonds or debentures ***[CIT v. Gautam Sarabhai Trust (1988)173 ITR 216(Guj.)]***.

When a proprietary concern is sold as a going concern for a consideration to a Company and the proprietor receives consideration as shares in the company and proprietor has held more than 51% shares for five years the capital gains will be exempt under section 47 (xiv) and is not liable to be taxed under section 50B of the Income Tax Act, 1961. ***ACIT v. Madan Mohan Chandak (2011).***

For Example, Mr. "X" held 2000 shares in a company XYZ Ltd. This company amalgamated with another company during the previous year ending 31-3-2022. Under the scheme of amalgamation, Mr. "X" was allotted 1500 shares in the new company. The market value of shares allotted is higher by Rs. 150,000 than the value of holding in XYZ Ltd. The Assessing Officer proposes to treat the transaction as an exchange and to tax Rs. 1,50,000 as capital gain. Is he justified?

In the above case the transaction is squarely covered by the exemption under section 47(vii) and the proposal of the Assessing Officer to treat the transaction as an exchange is not justified.

Amortisation of Preliminary Expenses

The benefit of amortization of preliminary expenses under section 35D of the Income-tax Act, 1961 are ordinarily available only to the assessee who incurred the expenditure. However, the benefit will not be lost in case the undertaking of an Indian company which is entitled to the amortization is transferred to another Indian company in a scheme of amalgamation within the 5 years period of amortisation. In that event, the deduction in respect of previous year in which the amalgamation takes place and the following previous year within the 5 years period will be allowed to the amalgamated company and not to the amalgamating company.

Capital Expenditure on Scientific Research

In the case of an amalgamation, if the amalgamating company transfers to the amalgamated company, which is an Indian company, any asset representing capital expenditure on scientific research, provision of section 35 of the Income-tax Act, 1961 would apply to the amalgamated company as they would have applied to amalgamating company if the latter had not transferred the asset.

Expenditure on Amalgamation

Section 35DD of the Income-tax Act, 1961 provides that where an assessee being an Indian company incurs any expenditure, on or after the 1st day of April, 1999, wholly and exclusively for the purposes of amalgamation or demerger of an undertaking, the assessee shall be allowed a deduction of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the previous year in which the amalgamation or demerger takes place.

Expenditure for obtaining Licence to Operate Telecommunication Services (Section 35 ABB)

The provisions of the section 35ABB of the Income Tax Act, 1961 relating to deduction of expenditure, incurred for obtaining licence to operate communication services shall, as far as may be, apply to the amalgamated company as they would have applied to the amalgamating company if the latter had not transferred the licence.

Expenditure for obtaining Spectrum (Section 35 ABA)

The provisions of the section 35ABA of the Income Tax Act, 1961 relating to deduction of expenditure, incurred for obtaining spectrum to operate communication services shall, as far as may be, apply to the amalgamated company as they would have applied to the amalgamating company if the latter had not transferred the spectrum.

Deduction for expenditure on prospecting, etc., for certain minerals (Section 35E)

The provisions of section 35E of the Income Tax Act, 1961 relating to expenditure on prospecting, etc., for certain minerals shall, as far as may be, apply to the amalgamated company as they would have applied to the amalgamating company as if the amalgamation has not happened.

TAX ASPECTS ON SLUMP SALE

Section 180(1) of the Companies Act, 2013 empowers the Board of Directors of a company, after obtaining the consent of the company by a special resolution to sell, lease or otherwise dispose off the whole or substantially the whole of the undertaking(s) of a company.

Explanation-

(i) "undertaking" shall mean an undertaking in which the investment of the company exceeds twenty per cent. of its net worth as per the audited balance sheet of the preceding financial year or an undertaking which generates twenty per cent of the total income of the company during the previous financial year;

(ii) the expression "substantially the whole of the undertaking" in any financial year shall mean twenty per cent. or more of the value of the undertaking as per the audited balance sheet of the preceding financial year.

The transaction in this case, is normally of either of the following type:

(a) Sale of a running concern.

(b) Sale of a concern which is being wound-up.

(a) Sale of a Running Concern

This type of sale as a going concern provides for the continuation of the running of the undertaking without any interruption. But there is always a problem of fixing a value in the case of a running concern for all tangible and intangible assets including fixing a value for the infrastructure and other environmental facilities available. In view of all this, the seller normally fixes a lump sum price called 'slump price'.

The noun 'slump' means 'a gross amount, a lump'. Similarly, 'slump sum' means a 'lump sum' [Chambers Twentieth Century Dictionary, 1983 Edn., p1220). A slump sale or a slump transaction would, therefore, mean a sale or a transaction which has a lump sum price for consideration.

(b) Sale of a concern which is being wound-up

On the other hand, a sale in the course of winding up, is nothing but a realization sale aimed at collecting the maximum price for distributing to the creditors and the balance to the contributories (the shareholders). By the very nature of the transaction, this is a piecemeal sale and not a slump sale. In this case, there will be liability to tax as per the various provisions of the Income Tax Act and the criteria which is applicable to a slump sale is not applicable here.

Normally, any sale of a capital asset will give rise to a capital receipt and any profit derived may give rise to capital gains in certain cases. This is true in the case of sale of an undertaking also.

> Section 2(42C) of the Income Tax Act, 1961 defines slump sale as a means of transfer of one or more undertakings by *any means* for a lump sum consideration without values being assigned to the Individual assets and liabilities in such transfer.

The word any means now allows the transfer of a business undertaking not only 'by way of sale' but also 'by way of an exchange' or any other transfer structure defined in Section 2(47) of the Act to be included within its scope.

Determination of the value of an asset or liability (for sole purpose of payment of stamp duty, registration fees or other similar taxes or fee) shall not be regarded as assignment of values to individual assets or liabilities.

As per section 50B of the Income Tax Act, 1961 any profits or gains arising from the slump sale effected in the previous year shall be chargeable to income-tax as capital gains from the transfer of long-term capital asset and shall be deemed to be the income of the previous year in which the transfer took place.

The gain or loss resulting out of a slump sale shall be a Capital Gain/Loss under the Income Tax Act. The computation has been prescribed as follows:

Particulars	Amount
Full Value of Consideration	XXXX
(-) Expenses in relation to transfer	XXXX
Net Consideration	Xxxx
Cost of Acquisition / net worth	Xxxx
Capital Gain or (Loss)	xxxx

Sale consideration to be calculated as per the Fair Market Value computation which includes monetary as well as non-monetary considerations.

The capital gain or loss as computed above will be either long term or short-term depending upon the period for which the undertaking is held.

If the undertaking is held for more than 36 months, the resulting capital gain or loss shall be long-term and if it is held for less than 36 months, the resulting capital gain or loss shall be short term.

Further, there will be no indexation benefit available in the computation of the capital gains.

In computing the net worth of the entity, the following points need to be considered:

1. The value of net worth should not take into account any change in the value of the asset or liability resulting from revaluation of such asset or liability.
2. In case of depreciable assets under the Income Tax Act, the Written Down Value of Block of assets as per the Act shall be considered.
3. In case of assets on which 100% deduction has been allowed u/s 35AD (specified business), the value of such assets will not be considered.
4. In case of any other asset, value as appearing in the books of accounts shall be considered.
5. After considering the above points, if the resulting net worth is negative, then the cost of acquisition shall be taken as nil for the purpose of computation of capital gains.
6. Value of goodwill while computing the 'net worth' of the undertaking while computing the 'net worth' of an undertaking which is then deemed 'cost of acquisition' under Section 50B, the insertion of Explanation 2(aa) of Section 50B clarifies that the value of any goodwill of business or profession (other than goodwill acquired by purchase from a previous owner) would need to be taken as NIL.

   Tax rates: The rates of tax applicable to the capital gain in a slump sale are as follows:

   Short Term Capital Gain: Normal Rates of taxation

   Long Term Capital Gain: 20%

In ***Doughty v. Commissioner of Taxes,*** the Privy Council laid down the following principles: The sale of a whole concern engaged in production process, e.g. dairy farming or sheep rearing, does not give rise to a revenue profit. The same might be said of a manufacturing business which is sold with the lease holds and plant, even if there are added to the sale piece goods in stock and even if these piece goods form a very substantial part of the aggregate sold. Where, however, business consists entirely in buying and selling, it is difficult to distinguish for income tax purposes between an ordinary and realisation sale, the object in either case being to dispose of the goods at a profit. The fact that the stock is sold out in one sale does not render the profit obtained any different in kind from the profit obtained by a series of gradual and smaller sales. In the case of such a realization sale, if there is an item which can be traced as representing the stock-in-trade sold, the profit obtained by the sale of the stock-in-trade, though it is in conjunction with the sale of the whole concern, may be treated as taxable income. But where there is a sale of the whole concern and a transfer of all the assets for a single unapportioned consideration, there cannot be said to be any revenue profit realised on the sale of the stock-in-trade which is sold with all the other assets, although the business of the concern may consist entirely in buying and selling.

The Supreme Court, based on the above decision held in the following two cases that the price received on the sale of industrial undertaking is a capital receipt.

CIT v. West Coast Chemicals and Industries Ltd.– 46 ITR135 – Where a slump price is paid and no portion is attributable to the stock-in-trade, it may not be possible to say that there is a profit other than what results from the appreciation of capital. The essence of the matter, however, is not that an extra amount has been gained by the selling out or the exchange but whether it can fairly be said that there was a trading, from which alone profit can arise in business.

CIT v. Mugneeram Bangur and Co. – 57 ITR 299 – In the case of a concern carrying on the business of buying land, developing it and then selling it, it is easy to distinguish a realization sale from an ordinary sale, and it is very difficult to attribute part of the slump price to the cost of land sold in the realization sale. The mere fact that in the schedule, the price of land was stated does not lead to the conclusion that part of the slump price is necessarily attributable to the land sold.

The same view was also reiterated by the Gujarat High Court in the following cases:

1. ***Sarabhai M. Chemicals Pvt. Ltd. v. P.M. Mittal, Competent Authority–126 ITR1.***
2. ***Artex Manufacturing Co. v. CIT–131 ITR 559.***

At the same time, the Gujarat High Court also recognized that when an undertaking as a whole is sold as a going concern there will be liability under the head Capital Gains. In 126 ITR 1 the Gujarat High Court stated as follows:

It is well settled that business is property and the undertaking of a business is a capital asset of the owner of the undertaking. When an undertaking as a whole is transferred as a going concern together with its goodwill and all other assets, what is sold is not the individual itemised property but what is sold is the capital asset consisting of the business of the undertaking and any tax that can be attracted to such a transaction for a slump price at book value would be merely capital gains tax and nothing else but capital gains tax. Plant or machinery or any fixture or

furniture is not being sold as such. What is sold is the business of undertaking for a slump price. If the capital asset, namely, the business of the undertaking, has a greater value than its original cost of acquisition, then, capital gains may be attracted in the ordinary case of a sale of an undertaking.

The Bombay High Court also recognized that there will be a capital gains tax when a sale of business as a whole occurs (Refer ***Killick Nixon and Co .v. CIT 49 ITR 244***).

Where assessee company had sold its entire running business with all assets and liabilities in one go, the Supreme Court held it was a slump sale of a long term capital asset and be taxed under section 50B and not under section 50(2). Section 50(2) applies to a case where any block of assets are transferred by assesse ***CIT Vs Equinox solution (P) Ltd. 2017.***

TAX ASPECTS OF DEMERGER

Tax concession/incentives in case of demerger

Section 2(19AA) of the Income Tax Act, 1961 defines the term demerger as follows:

"demerger", in relation to companies, means the transfer, pursuant to a scheme of arrangement under sections 231 to 232 of the Companies Act, 2013, by a demerged company of its one or more undertakings to any resulting company in such a manner that–

(i) all the property of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the property of the resulting company by virtue of the demerger;

(ii) all the liabilities relatable to the undertaking, being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger;

(iii) the property and the liabilities of the undertaking or undertakings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger;

Provided *that the provisions of this sub-clause shall not apply where the resulting company records the value of the property and the liabilities of the undertaking or undertakings at a value different from the value appearing in the books of account of the demerged company, immediately before the demerger, in compliance to the Indian Accounting Standards specified in Annexure to the Companies (Indian Accounting Standards) Rules, 2015.*

(iv) the resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis except where the resulting company itself is a shareholder of the demerged company;

(v) the shareholders holding not less than three-fourths in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or, its subsidiary) become shareholders of the resulting company or companies by virtue of the demerger, otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company;

(vi) the transfer of the undertaking is on a going concern basis;

(vii) the demerger is in accordance with the conditions, if any, notified under sub-section (5) of section (viii) 72A by the Central Government in this behalf.

Explanation 1.–For the purposes of this clause, "undertaking" shall include any part of an undertaking, or a unit or division of an undertaking or a business activity taken as a whole, but does not include individual assets or liabilities or any combination thereof not constituting a business activity.

Explanation 2.–For the purposes of this clause, the liabilities referred to in sub-clause (ii), shall include–

(a) the liabilities which arise out of the activities or operations of the undertaking;

(b) the specific loans or borrowings (including debentures) raised, incurred and utilised solely for the activities or operations of the undertaking; and

(c) in cases, other than those referred to in clause (a) or clause (b), so much of the amounts of general or multipurpose borrowings, if any, of the demerged company as stand in the same proportion which the value of the assets transferred in a demerger bears to the total value of the assets of such demerged company immediately before the demerger.

Explanation 3.–For determining the value of the property referred to in sub-clause (iii), any change in the value of assets consequent to their revaluation shall be ignored.

Explanation 4.–For the purposes of this clause, the splitting up or the reconstruction of any authority or a body constituted or established under a Central, State or Provincial Act, or a local authority or a public sector company, into separate authorities or bodies or local authorities or companies, as the case may be, shall be deemed to be a demerger if such split up or reconstruction fulfils such conditions as may be notified in the Official Gazette, by the Central Government.

Explanation 5.–For the purposes of this clause, the reconstruction or splitting up of a company, which ceased to be a public sector company as a result of transfer of its shares by the Central Government, into separate companies, shall be deemed to be a demerger, if such reconstruction or splitting up has been made to give effect to any condition attached to the said transfer of shares and also fulfils such other conditions as may be notified by the Central Government in the Official Gazette.

Explanation 6. —For the purposes of this clause, the reconstruction or splitting up of a public sector company into separate companies shall be deemed to be a demerger, if such reconstruction or splitting up has been made to transfer any asset of the demerged company to the resulting company and the resulting company—

(i) is a public sector company on the appointed day indicated in such scheme, as may be approved by the Central Government or any other body authorised under the provisions of the Companies Act, 2013 or any other law for the time being in force governing such public sector companies in this behalf; and

(ii) fulfils such other conditions as may be notified by the Central Government in the Official Gazette in this behalf;

It should also be noted that in such cases, the reconstruction or splitting should, be made to transfer any asset of the demerged company to the resulting company and the resulting company is a public sector company on the appointed date indicated in such scheme as may be approved by the Central Government or any other authorised body and fulfils such other conditions as the Central Government may prescribe.

If any demerger takes place within the meaning of section 2(19AA) of the Income-tax Act, 1961 the tax concessions shall be available to:

1. Demerged company.
2. Shareholders of demerged company.
3. Resulting company.

These concessions are on similar lines as are available in case of amalgamation. However, some concessions available in case of amalgamation are not available in case of demerger.

1. Tax concession to demerged company

(i) Capital gains tax not attracted [Section 47(vib)]

According to section 47(vib), where there is a transfer of any capital asset in case of a demerger by the demerged company to the resulting company, such transfer will not be regarded as a transfer for the purpose of capital gain provided the resulting company is an Indian company.

(ii) Tax concession to a foreign demerged company [Section 47(vic)]

Where a foreign company holds any shares in an Indian company and transfers the same, in case of a demerger, to another resulting foreign company, such transaction will not be regarded as transfer for the purpose of capital gain under section 45 if the following conditions are satisfied:

(a) the shareholders holding not less than three-fourths in value of the shares of the demerged foreign company continue to remain shareholders of the resulting foreign company; and

(b) such transfer does not attract tax on capital gains in the country, in which the demerged foreign company is incorporated:

Provided that the provisions of Sections 391 to 394 of the Companies Act, 1956 (1 of 1956) (Now Sections 230 to 232 of Companies Act, 2013) shall not apply in case of demergers referred to in this clause;

(iii) any transfer in a demerger, of a capital asset, being a share of a foreign company, referred to in Explanation 5 to clause (i) of subs-section (1) of section 9, which derives directly or indirectly its values substantially from the share or shares of an Indian Company, held by the demerged foreign company to the resulting foreign company will not be regarded as transfer for the purpose of capital gains if the following conditions are satisfied: [Section 47(vicc)]

(a) Shareholders holding not less than three-fourths in value of the shares of the demerged foreign company, continue to remain shareholders of the resulting foreign company; and

(b) Such transfer does not attract tax on capital gains in the country in which the demerged foreign company is incorporated.

(iv) Reserves for shipping business: Where a ship acquired out of the reserve is transferred in a scheme of demerger, even within the period of eight years of acquisition there will be no deemed profits to the demerged company.

2. Tax concessions to the shareholders of the demerged company [Section 47(vid)]

Any transfer or issue of shares by the resulting company, in a scheme of demerger to the shareholders of the demerged company shall not be regarded as a transfer if the transfer or issue is made in consideration of demerger of the undertaking.

In the case of demerger, the existing shareholders of the demerged company will hold after demerger:

(a) shares in resulting company; and

(b) shares in demerged company.

And in case the shareholder transfers any of the above shares subsequent to the demerger, the cost of such shares shall be calculated as under: –

Cost of acquisition of shares in the resulting company [Section 49(2C)]

The cost of acquisition of the shares in the resulting company shall be the amount which bears to the cost of acquisition of shares held by the assessee in the demerged company the same proportion as the net book value of the assets transferred in a demerger bears to the net worth of the demerged company immediately before such demerger.

Cost of acquisition of shares in the demerged company [Section 49(2D)]

The cost of acquisition of the original shares held by the shareholder in the demerged company shall be deemed to have been reduced by the amount as so arrived at under sub-section (2C).

For the above purpose, net worth shall mean the aggregate of the paid-up share capital and general reserves as appearing in the books of account of the demerged company immediately before the demerger.

Period of holding of shares of the resulting company [Section 2(42A)(g)]

In the case of a capital asset, being a share or shares in an Indian company, which becomes the property of the assessee in consideration of a demerger, there shall be included the period for which the share or shares held in the demerged company were held by the assessee.

3. Tax concessions to the resulting company

The resulting company shall be eligible for tax concessions only if the following two conditions are satisfied:

(i) The demerger satisfies all the conditions laid down in section 2 (19AA); and

(ii) The resulting company is an Indian company.

The following concessions are available to the resulting company pursuant to a scheme of demerger:

(a) Expenditure for obtaining licence to operate telecommunication services [Section 35ABB]

The provisions of the section 35ABB of the Income Tax Act, 1961 relating to deduction of expenditure, incurred for obtaining licence to operate communication services shall, as far as may be, apply to the resulting company as they would have applied to the demerged company, if the latter had not transferred the licence.

(b) Expenditure for obtaining Spectrum to operate telecommunication services [Section 35ABA]

The provisions of the section 35ABA of the Income Tax Act, 1961 relating to deduction of expenditure, incurred for obtaining spectrum to operate communication services shall, as far as may be, apply to the resulting company as they would have applied to the demerged company if the latter had not transferred the spectrum.

(c) Amortisation of certain preliminary expenses [Section 35D]

The benefit of amortization of preliminary expenses under section 35D of the Income-tax Act, 1961 are ordinarily available only to the assessee who incurred the expenditure. However, the benefit will not be lost in case the undertaking of an Indian company which is entitled to the amortization is transferred to another Indian company in a scheme of demerger within the 5 years period of amortisation. In that event the deduction in respect of previous year in which the demerger takes place and the following previous year within the 5 years period will be allowed to the resulting company and not to the demerged company.

(d) Treatment of expenditure on prospecting, etc. of certain minerals [Section 35E(7A)]

The provisions of section 35E of the Income Tax Act, 1961 relating to expenditure on prospecting, etc., for certain minerals shall, as far as may be, apply to the resulting company as they would have applied to the demerged company as if the demerger has not happened.

(e) Treatment of bad debts [Section 36(1)(vii)]

Where due to demerger ,the debts of the demerged company have been taken over by the resulting company and subsequently by such debt or part of debt becomes bad such bad debt will be allowed as a deduction to the resulting company. This is based upon the decision of the Supreme Court in the case of ***CIT v. Veerabhadra Rao (T.), K. Koteswara Rao & Co.(1985) 155 ITR 152 (SC)*** which was decided in the case of amalgamation of companies.

Section 36(1) provides that the deductions provided in the clauses contained therein shall be allowed in respect of the matters dealt with therein, in computing the income referred to in section 28. Clause (vii) provides that;

Subject to the provisions of sub-section (2), the amount of any bad debt or part thereof which is written off as irrecoverable in the accounts of the assessee for the previous year shall be allowed as deduction.

Provided that in the case of an assessee to which clause (viia) applies, the amount of the deduction relating to any such debt or part thereof shall be limited to the amount by which such debt or part thereof exceeds the credit balance in the provision for bad and doubtful debts account made under that clause:

Provided further that where the amount of such debt or part thereof has been taken into account in computing the income of the assessee of the previous year in which the amount of such debt or part thereof becomes irrecoverable or of an earlier previous year on the basis of income computation and disclosure standards notified under sub-section (2) of section 145 without recording the same in the accounts, then, such debt or part thereof shall be allowed in the previous year in which such debt or part thereof becomes irrecoverable and it shall be deemed that such debt or part thereof has been written off as irrecoverable in the accounts for the purposes of this clause.

Explanation 1.–For the purposes of this clause, any bad debt or part thereof written off as irrecoverable in the accounts of the assessee shall not include any provision for bad and doubtful debts made in the accounts of the assessee;

Explanation 2.–For the removal of doubts, it is hereby clarified that for the purposes of the proviso to clause (vii) of this sub-section and clause (v) of sub-section(2), the account referred to therein shall be only one account in respect of provision for bad and doubtful debts under clause (viia) and such account shall relate to all types of advances, including advances made by rural branches.

(f) Amortisation of expenditure in case of amalgamation or demerger [Section 35DD]

Where an assessee, being an Indian company, incurs any expenditure wholly and exclusively for the purposes of demerger of an undertaking, the assessee shall be allowed a deduction of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the previous year in which the demerger takes place.

(g) Carry forward and set off of business losses and unabsorbed depreciation of the demerged company [Section 72A (4)&(5)]

Section 72A(4): Notwithstanding anything contained in any other provisions of this Act, in the case of a demerger, the accumulated loss and the allowance for unabsorbed depreciation of the demerged company shall–

(a) where such loss or unabsorbed depreciation is directly relatable to the undertakings transferred to the resulting company, be allowed to be carried forward and set off in the hands of the resulting company;

(b) where such loss or unabsorbed depreciation is not directly relatable to the undertakings transferred to the resulting company, be apportioned between the demerged company and the resulting company in the same proportion in which the assets of the undertakings have been retained by the demerged company and transferred to the resulting company, and be allowed to be carried forward and set off in the hands of the demerged company or the resulting company, as the case may be.

Section 72A(5): The Central Government may, for the purposes of this Act, by notification in the Official Gazette, specify such conditions as it considers necessary to ensure that the demerger is for genuine business purposes.

(h) Deduction available under section 80 - IA (12) or 80 - IB (12)

Deductions in respect of profits and gains from industrial undertakings or enterprises engaged in infrastructure development, etc.:

Section 80-IA(12): Where any undertaking of an Indian company which is entitled to the deduction under this section is transferred, before the expiry of the period specified in this section, to another Indian company in a scheme of amalgamation or demerger–

(a) no deduction shall be admissible under this section to the amalgamating or the demerged company for the previous year in which the amalgamation or the demerger takes place; and

(b) the provisions of this section shall, as far as may be, apply to the amalgamated or the resulting company as they would have applied to the amalgamating or the demerged company if the amalgamation or demerger had not taken place.

However, nothing contained in sub-section (12) of sec 80IA shall apply to any enterprise or undertaking which is transferred in a scheme of amalgamation or demerger on or after the 1st day of April, 2007.

Deduction in respect of profits and gains from certain industrial undertakings other than infrastructure development undertakings:

Section 80-IB(12): Where any undertaking of an Indian company which is entitled to the deduction under this section is transferred, before the expiry of the period specified in this section, to another Indian company in a scheme of amalgamation or demerger–

(a) no deduction shall be admissible under this section to the amalgamating or the demerged company for the previous year in which the amalgamation or the demerger takes place; and

(b) the provisions of this section shall, as far as may be, apply to the amalgamated or the resulting company as they would have applied to the amalgamating or the demerged company if the amalgamation or demerger had not taken place.

Dividend & Deemed Dividend

Section 2(22) of the Income Tax Act, 1961 defines the term dividend. Dividend includes—

(a) any distribution by a company of accumulated profits, whether capitalised or not, if such distribution entails the release by the company to its shareholders of all or any part of the assets of the company;

(b) any distribution to its shareholders by a company of debentures, debenture-stock, or deposit certificates in any form, whether with or without interest, and any distribution to its preference shareholders of shares by way of bonus, to the extent to which the company possesses accumulated profits, whether capitalised or not;

(c) any distribution made to the shareholders of a company on its liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before its liquidation, whether capitalised or not;

(d) any distribution to its shareholders by a company on the reduction of its capital, to the extent to which the company possesses accumulated profits which arose after the end of the previous year ending next before the 1st day of April, 1933, whether such accumulated profits have been capitalised or not;

(e) any payment by a company, not being a company in which the public are substantially interested, of any sum (whether as representing a part of the assets of the company or otherwise) made after the 31st day of May, 1987, by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than ten per cent of the voting power, or to any concern in which such shareholder is a member or a partner and in which he has a substantial interest (hereafter in this clause referred to as the said concern) or any payment by any such company on behalf, or for the individual benefit, of any such shareholder, to the extent to which the company in either case possesses accumulated profits ;

but "dividend" does not include—

(i) a distribution made in accordance with sub-clause (c) or sub-clause (d) in respect of any share issued for full cash consideration, where the holder of the share is not entitled in the event of liquidation to participate in the surplus assets;

(ia) a distribution made in accordance with sub-clause (c) or sub-clause (d) in so far as such distribution is attributable to the capitalised profits of the company representing bonus shares allotted to its equity shareholders after the 31st day of March, 1964, and before the 1st day of April, 1965;

(ii) any advance or loan made to a shareholder or the said concern by a company in the ordinary course of its business, where the lending of money is a substantial part of the business of the company;

(iii) any dividend paid by a company which is set off by the company against the whole or any part of any sum previously paid by it and treated as a dividend within the meaning of sub-clause (e), to the extent to which it is so set off;

(iv) any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of the Companies Act,;

(v) any distribution of shares pursuant to a demerger by the resulting company to the shareholders of the demerged company (whether or not there is a reduction of capital in the demerged company).

Explanation 1.—The expression "accumulated profits", wherever it occurs in this clause, shall not include capital gains arising before the 1st day of April, 1946, or after the 31st day of March, 1948, and before the 1st day of April, 1956.

Explanation 2.—The expression "accumulated profits" in sub-clauses (a), (b), (d) and (e), shall include all profits of the company up to the date of distribution or payment referred to in those sub-clauses, and in sub-clause (c) shall include all profits of the company up to the date of liquidation, but shall not, where the liquidation is consequent on the compulsory acquisition of its undertaking by the Government or a corporation owned or controlled by the Government under any law for the time being in force, include any profits of the company prior to three successive previous years immediately preceding the previous year in which such acquisition took place.

Explanation 2A.—In the case of an amalgamated company, the accumulated profits, whether capitalised or not, or loss, as the case may be, shall be increased by the accumulated profits, whether capitalised or not, of the amalgamating company on the date of amalgamation.

Explanation 3. —For the purposes of this clause, —

(a) "concern" means a Hindu undivided family, or a firm or an association of persons or a body of individuals or a company;

(b) a person shall be deemed to have a substantial interest in a concern, other than a company, if he is, at any time during the previous year, beneficially entitled to not less than twenty per cent of the income of such concern.

Taxability

Finance Act, 2018 has bought the deemed dividend within the ambit of dividend distribution tax under section 115-O, at the rate of 30% in the hands of the closely held companies.

As per the provisions of Section 10(34), dividend income under section 2(24)(e) is 100% exempt in the hands of the shareholders as it is charged to Dividend Distribution Tax under section 115-O of the Income Tax Act, 1961.

In Budget 2021, the burden of paying tax on dividend is transferred to the shareholders. Now the companies are not liable to pay Dividend Distribution Tax (DDT) while distributing dividends to the shareholders, i.e. DDT is abolished. These amendment has put all this to rest.

STAMP DUTY ASPECTS OF MERGER AND AMALGAMATIONS

The incidence of stamp duty is an important consideration in the planning of any merger. In fact, in some cases, the whole form in which the merger is sought to take place is selected taking into account the savings in stamp duty. The incidence of stamp duty, more particularly on transfer of immovable property is fairly high to merit serious consideration. The fact that, in India, stamp duty is substantially levied by the States has given considerable scope for savings in stamp duty.

CONSTITUTIONAL BACKGROUND ON LEVY OF STAMP DUTY ON AMALGAMATION AND MERGERS

Article 265

Article 265 of the Constitution prohibits levy or collection of tax except by authority of law.

Article 246, read with the Seventh Schedule of the Constitution provides legislative powers to be exercised by the Parliament and the State Legislatures.

The Seventh Schedule consists of three lists viz., List I-Union List, List II-State List and List III-Concurrent List. List I is the exclusive domain of the Parliament to make laws in relation to that matter and it becomes a prohibited field for the State Legislature. List II is within the exclusive competence of the State Legislature and Parliament is prohibited to make any law with regard to the same except in certain circumstances. In List III, both Parliament and State Legislature can make laws subject to certain conditions. Matters not mentioned in any of the three lists fall within the exclusive domain of the Parliament.

Article 372

All the laws in force immediately before the commencement of the Constitution continue to be in force until altered or repealed or amended by a competent Legislature or other competent authority. Accordingly, the Indian Stamp Act, 1899 is continuing to this extent.

The relevant entries in the Seventh Schedule regarding stamp duty are as follows:

List I Entry 91

> "91. Rates of stamp duty in respect of bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, transfer of shares, debentures, proxies and receipts."

List II Entry 63

> "63. Rates of stamp duty in respect of documents other than those specified in the provisions of List I with regard to rates of stamp duty."

List III Entry 44

> "44. Stamp duties other than duties or fees collected by means of judicial stamps, but not including rates of stamp duty."

In exercise of power conferred by Entry 63, List II, the State Legislature can make amendment in the Indian Stamp Act, 1899 under article 372, in regard to the rates of stamp duty in respect of documents other than those specified in provisions of List I.

Stamp duty is levied in India on almost all, except a few documents, by the States and hence the rate and incidence of stamp in different states vary. The State Legislature has jurisdiction to levy stamp duty under entry 44, List III of the Seventh Schedule of the Constitution of India and prescribe rates of stamp duty under entry 63, List II.

Under the provisions of the Companies Act, 1956 it has been decided that by sanctioning of amalgamation scheme, the property including the liabilities are transferred as provided in sub-section (2) of section 394 of the Companies Act and on that transfer instrument, stamp duty is levied.

Therefore, it cannot be said that the State Legislature has no jurisdiction to levy such duty on an order of the High Court sanctioning a scheme of compromise or arrangement under section 394 of the Companies Act, 1956. *[Li Taka Pharmaceuticals Ltd. and another v. State of Maharashtra and others ibid].*

Stamp Duty Payable on a Tribunal Order Sanctioning Amalgamation

Section 232 of the Companies Act, 2013 is the corresponding section to the Section 394 of the Companies Act, 1956 and for understanding the payment of Stamp duty on Tribunal Order sanctioning Amalgamation, it is necessary to take reference of the judicial pronouncement under the Companies Act, 1956, which is as under:

1. In amalgamation the undertaking comprising property, assets and liabilities, of one (or more) company (amalgamating or Transferor Company) are absorbed by the transferee company and transferor company merges into or integrates with the Transferee Company. The former loses its entity and is dissolved (without winding-up).
2. The transfer and vesting of Transferor Company's property, assets, etc. into Transferee Company takes place "by virtue of" the High Court's order [Section 394(2)]. Thus, the vesting of the property occurs on the strength of the order of the High Court sanctioning the scheme of amalgamation, without any further document or deed. Property includes every kind of property, rights and powers of every description [Section 394(4)(d)].
3. For the purpose of conveying to the transferee company the title to the immovable property of the transferor company, necessary registration in the lands records in the concerned office of the State in which the property is situated, will be done on the basis of the High Court order sanctioning the amalgamation. If any stamp duty is payable under the Stamp Act of the State in which the property is situated, it will be paid on the copy of the High Court order.
4. An order of the High Court under section 394 is founded and based on the compromise or arrangement between the two companies for transferring assets and liabilities of the transferor company to the transferee company and that order is an instrument as defined in Section 2(1) of the Bombay Stamp Act, 1958 which included every document by which any right or liability is transferred *[Li Taka Pharmaceuticals Ltd. v. State of Maharashtra (1996)22 CLA154: AIR 1997 Bom 7].*
5. Thus, an order of the High Court sanctioning a scheme of amalgamation under Section 394 of the companies Act, 1956 is liable to stamp duty only in those States where the states stamp law provides.

In ***Hindustan Lever Ltd. v. State of Maharashtra (2003) 117 Comp Cas SC 758*** the Supreme Court considered this issue. Tata Oil Mills Company Ltd. (TOMCO) was merged with the *Hindustan Lever Ltd (HLL).* The State imposed stamp duty on the order sanctioning the scheme of merger. The demand was challenged by the company on two grounds that State Legislature is not competent to impose stamp duty on the order of amalgamation passed by a court and such order of the court is neither instrument nor document (transferring properties from transferor company to transferee company) liable to stamp duty.

The Supreme Court dismissed the appeal of the company on following reasons:

Transfer of property has been defined to mean an act by which a living person conveys property, in present or in future, to one or more living persons. Companies or associations or bodies of individuals, whether incorporated or not, have been included amongst living persons. It clearly brings out that a company can affect transfer of property. The word inter vivos in the context of section 394 of the Companies Act, 1956 would include, within its meaning, also a transfer between two juristic persons or a transfer to which a juristic person is one of the parties. The company would be a juristic person created artificially in the eyes of law capable of owning and transferring the property. The method of transfer is provided in law. One of the methods prescribed is dissolution of the transferee company along with all its assets and liabilities. Where any property passes by conveyance, the transaction is said to be *inter vivos* as distinguished from a case of succession..

The State Legislature would have the jurisdiction to levy stamp duty under Entry 44 List III of the Seventh Schedule of the constitution and prescribes rate of stamp duty under Entry 63, List II. It does not in any way impinge upon any Entry in List I. Entry 44 of List III empowers the State Legislature to prescribe rates of stamp duty in respect of documents other than those specified in List I. By sanctioning a scheme of amalgamation, the property including the liabilities are transferred as provided in Section 394 of the Companies Act, 1956 and on that transfer instrument, stamp duty is levied. Therefore, it cannot be said that the State Legislature has no jurisdiction to levy such duty. Under the scheme of amalgamation, the whole or any part of the undertaking, properties or liability of any company concerned in the scheme are to be transferred to the other company. The intended transfer is a voluntary act of the contracting parties. The transfer has all trappings of a sale. While exercising its power in sanctioning a scheme of arrangement, the court has to examine as to whether the provisions of the statute have been complied with. Once the court finds that the parameters set out in section 394 of the Companies Act, 1956 have been met then the court would have no further jurisdiction to sit in appeal over the commercial wisdom of the class of persons who with their eyes open give their approval, even if, in the view of the court a better scheme could have been framed. Two broad principles underlying a scheme of amalgamation are that the order passed by the court amalgamating the company is based on a compromise or arrangement arrived at between the parties; and that the jurisdiction of the company court while sanctioning the scheme is supervisory only. Both these principles indicate that there is no adjudication by the court on merits as such.

The order of the court under sub-section (2) of section 391 has to be presented before the Registrar of Companies within 30 days for registration and shall not have effect till a certified copy of the order has been filed with the Registrar and the Registrar of Companies certifies that the transferor company stands amalgamated with the transferee company along with all its assets and liabilities. Thus, the amalgamation scheme sanctioned by the court would be an instrument within the meaning of section 2(i) of the Bombay Stamp Act, 1958. By the said instrument, the properties are transferred from the transferor company to the transferee company, the basis of which is the compromise or arrangement arrived at between the two companies. A document creating or transferring a right is an instrument. An order effectuating the transfer is also a document.

6. The company will provide to the Collector of Stamps–

- application for adjudication of the High Court order for determination of stamp duty payable;
- proof of the market value of equity shares of the transferor company (Stock Exchange quotation or a certificate from Stock Exchange) as of the appointed day;

- certificate from an approved valuer or valuation of the immovable property being transferred to the transferee company.

7. The Collector thereafter will adjudicate the order and determine stamp duty.

8. The stamp duty will be paid in the manner prescribed under the Stamp Rules. The duty-paid Order will be registered with the Sub-Registrar of Assurances where the lands and buildings are located.

Incidence of Levy of Stamp Duty

Stamp duty is levied on "Instruments". Section 3 of the Bombay Stamp Act, 1958 specifies the following essentials for the levy of stamp duty:

1. There must be an instrument
2. Such instrument is one of the instruments specified in Schedule I
3. Such instrument must be executed
4. Such instrument must have either–

   (a) not having been previously executed by any person in the 'State' or

   (b) having been executed outside the State, relates to any property situated in the State or any matter or thing done or to be done in the State and is received in the State.

Instrument

The term 'instrument' is defined in Section 2(i) of the Bombay Stamp Act, 1958 as follows:

> "Instrument" includes every document by which any right or liability is or purports to be created, transferred, limited, extended, extinguished or recorded but does not include a bill of exchange, cheque, promissory note, bill of lading, letter of credit, policy of insurance, transfer of shares, debentures, proxy and receipt."

An award is an instrument within the meaning of the Stamp Act and the same is required to be stamped as was decided in the case ***Hindustan Steel Ltd. v. Dilip Construction Co., AIR 1969 SC 1238.***

The scheme of amalgamation sanctioned by the court would be an instrument within the meaning of Section 2(1) whereby the properties are transferred from the transferor company to the transferee company based on compromise arrived at between the two companies. The State legislature would have the jurisdiction to levy stamp duty under Entry 44, List II of the Seventh Schedule of the Constitution on the order of the court sanctioning scheme of amalgamation vide the case of ***Hindustan Lever v. State of Maharashtra, AIR 2004.***

This definition is an inclusive definition and includes any document which purports to transfer assets or liabilities considered as an instrument.

Order of Court under Section 394 of Companies Act, 1956 - A Transfer

It was earlier held that when transfer takes place by virtue of a court order to a scheme of amalgamation, stamp duty is leviable. By virtue of Section 2(g), the order of the Court ordering the transfer of assets and liabilities of the transferor company to the transferee company is deemed to be a conveyance. The definition of conveyance is given below:

As per Section 2(g) of the Bombay Stamp Act, 1958, "Conveyance" includes–

(i) a conveyance on sale,

(ii) every instrument,

(iii) every decree or final order of any Civil Court,

(iv) every order made by the High Court under Section 394 of the Companies Act, 1956 in respect of amalgamation of companies;

By which property, whether moveable or immovable, or any estate or interest in any property is transferred to, or vested in, any other person, *inter vivos,* and which is not otherwise specifically provided for by Schedule I.

The amended definition of term 'conveyance' under section 2(g) of the Bombay Stamp Act, 1958 (amended in 1985) *inter-alia* includes every order made by the High Court under section 394 of the Companies Act, 1956 in respect of amalgamation of companies by which property, whether moveable or immovable, or any estate or interest in any property of transferor is transferred to, or vested in the transferee company.

Transfer of the property of a partnership firm to a limited company on its conversion was held to be treated as a conveyance and, hence, chargeable to stamp duty, irrespective of the fact that the partners of the firm were the shareholders of the Company [In re ***The Kandoli Tea Company 13 Cal 43; Foster v. Commissioners, (1894)1QB516].***

The landmark decision of Bombay High Court in ***[Li Taka Pharmaceuticals v. State of Maharashtra (1996) 8 SC 102 (Bom.)]*** has serious implications for mergers covered not just by the Bombay Stamp Act, 1958 but also mergers covered by Acts of other States. The following are the major conclusions of the Court:

1. An amalgamation under an order of Court under Section 394 of the Companies Act,1956 is an instrument under the Bombay Stamp Act, 1958.
2. States are well within their jurisdiction when they levy stamp duty on instrument of amalgamation.
3. Stamp duty would be levied not on the gross assets transferred but on the "undertaking", when the transfer is on a going concern basis, i.e. on the assets less liabilities. The value for this purpose would thus be the value of shares allotted. This decision has been accepted in the Act and now stamp duty is leviable on the value of shares allotted plus other consideration paid.

The Calcutta High Court in the case of *Emami Biotech Ltd.* (2012) held that a Court order sanctioning a scheme of amalgamation or demerger under section 391 to 394 of the Companies Act, 1956 is an instrument and conveyance within the meaning of the Stamp Act applicable to the State of West Bengal and is accordingly, subject to stamp duty.

This case is related to a scheme sanctioned by the Calcutta High Court in West Bengal.

Stamp Duty on Other Documents

Usually, in a merger, several other documents, agreements, indemnity bonds, etc. are executed, depending on the facts of each case and requirements of the parties. Stamp duty would also be leviable as per the nature of the instrument and its contents.

Amalgamation between Holding and Subsidiary Companies–Exemption from payment of Stamp Duty

The Central Government has exempted the payment of stamp duty on instrument evidencing transfer of property between companies limited by shares as defined in the Indian Companies Act, 1913, in a case:

(i) where at least 90 percent of the issued share capital of the transferee company is in the beneficial ownership of the transferor company, or

(ii) where the transfer takes place between a parent company and a subsidiary company one of which is the beneficial owner of not less than 90 percent of the issued share capital of the other, or

(iii) where the transfer takes place between two subsidiary companies each of which having not less than 90 percent of the share capital is in the beneficial ownership of a common parent company:

Provided that in each case a certificate is obtained by the parties from the officer appointed in this behalf by the local Government concerned that the conditions above prescribed are fulfilled.

Therefore, if property is transferred by way of order of the High Court in respect of the Scheme of Arrangement/ Amalgamation between companies which fulfil any of the above mentioned three conditions, then no stamp duty would be levied provided a certificate certifying the relation between companies is obtained from the officer appointed in this behalf by the local Government (generally this officer is the Registrar of Companies).

A circular was issued in the year 1937 vide which exemption was granted on payment of Stamp Duty when there is an amalgamation/merger between holding and subsidiary company. Delhi High Court in the case of ***Delhi Towers Ltd. Vs. GNCT of Delhi*** made reference to this circular.

However, stamp duty being a state subject, the above would only be applicable in those States where the State Government follows the above stated notification of the Central Government otherwise stamp duty would be applicable irrespective of the relations mentioned in the said notification.

LESSON ROUND-UP

- Financial aspects of mergers denote financial benefits in terms of stamp duty and taxation related aspects.
- Under Section 72A, a special provision is made which relaxes the provision relating to carrying forward and set-off of accumulated business loss and unabsorbed depreciation allowance in certain cases of amalgamation.
- Capital gains tax is leviable if there arises capital gain due to transfer of capital assets.
- The incidence of stamp duty is an important consideration in the planning of any merger. In fact, in some cases, the whole form in which the merger is sought to take place is selected taking into account the savings in stamp duty. The incidence of stamp duty, more particularly on transfer of immovable property is fairly high to merit serious consideration. The fact that, in India, stamp duty is substantially levied by the States has given considerable scope for savings in stamp duty.
- Usually, in a merger, several other documents, agreements, indemnity bonds, etc. are executed, depending on the facts of each case and requirements of the parties. Stamp duty would also be leviable as per the nature of the instrument and its contents.

GLOSSARY

Deemed Dividend: Deemed dividend is the amount paid in such a manner and to such persons as specified in section 2(22)(e) of the Income Tax Act, 1961.

Slump Sale: Slump sale means of transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the Individual assets and liabilities in such sales.

Stamp duty: Stamp duty is levied in India on almost all, except a few documents, by the States. The State Legislature has jurisdiction to levy stamp duty under Entry 44, List III of the Seventh Schedule of the Constitution of India. Hence, the rate of duty varies from one state to another state. Under the provisions of the Companies Act, by sanctioning of amalgamation scheme, the property including the liabilities is transferred and on that transfer instrument, stamp duty is levied.

Conveyance: Conveyance means a conveyance on sale, every instrument, every decree or final order of any civil court, every order made by the High Court in respect of amalgamation of companies by which property, whether moveable or immovable or any estate or interest in any property is transferred to or vested in, any other person.

Instrument: Instrument includes every document by which any right or liability is or purports to be created, transferred, limited, extended, extinguished or recorded but does not include a bill of exchange, cheque, promissory note, bill of lading, letter of credit, policy of insurance, transfer of shares, debentures, proxy and receipt.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Describe the financial benefits that would arise out of merger.
2. What are the tax advantages of mergers? Discuss provisions related to capital gains.
3. Discuss the taxation aspects of slump sale.
4. What are provisions related to taxation aspects of demerger?
5. What is deemed dividend under section 2(22)(e) of the Income-tax Act, 1961? Discuss its taxability.
6. Explain the constitutional background of Indian Stamp Act, 1899 with respect to merger.
7. Is the order of Tribunal an instrument? Is stamp duty compulsory on the Tribunal order?

LIST OF FURTHER READINGS

- Master Guide to Mergers and Acquisition in India – Tax and Regulatory, 4th Edition, CCH
- Income Tax Act, 1961
- Indian Stamp Act, 1899
- State Stamp Acts

Regulation of Combinations

Lesson 8

KEY CONCEPTS

■ Competition Commission of India ■ Combination ■ Relevant Geographic Market ■ Relevant Product Market

Learning Objectives

To understand:

- Combination under Competition Law
- Competition Commission of India
- Classification of Combination
- Combination Regulations
- Appreciable Adverse Effect on Competition (AAEC)

Lesson Outline

- Competition aspects of combinations
- Kind of combinations
- Combination thresholds
- Regulation of combinations
- Relevant market
- Filing Process
- Role of CCI
- Inquiry into combination by the Commission
- Orders of Commission
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

- The Competition Act, 2002
- The Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011
- The Competition Commission of India (General) Regulations, 2009

INTRODUCTION

The Sherman Anti-Trust Act of 1890 (Sherman Anti-Trust Act) can be said to be the origin of anti-trust/competition law. This legislation was the result of intense public opposition to the concentration of economic power in large corporations and in combinations of business concerns that had been taking place in the U.S. in the decades following the Civil War.

The Sherman Antitrust Act was the first measure enacted by the U.S. Congress. The Sherman Antitrust Act was based on the constitutional power of Congress to regulate interstate commerce. In 1914, US Congress passed two measures that provided additional support for the Sherman Antitrust Act. One was the Clayton Antitrust Act, which elaborated on the general provisions of the Sherman Act and specified a number of illegal practices that either contributed to or resulted from monopolization. It explicitly outlawed commercial practices such as price discrimination (i.e., charging different prices to different customers), the buying out of competitors and interlocking boards of directors. The other was the establishment of the Federal Trade Commission, an agency with the power to investigate possible violations of antitrust laws and to issue orders forbidding unfair competitive practices. Gradually, competition law came to be recognized as one of the key pillars of a market economy. This recognition led to enactment of competition law in many countries including developing countries.

Limiting Competition

It would be wrong to conclude that mergers limit or restrict competition from the consumers' point of view. In mergers business enterprises achieve what could be termed as a buy-out of the competitor's market shares or stake. The purpose of such acquisition could be to consolidate or to eliminate the competition posed by the acquired enterprise. It does not mean new competitive forces cannot emerge or survive. Mergers may enable a dynamic functioning of the product / service market resulting in benefit to the customers. It is only natural for business enterprises and the people who drive such enterprises to look at opportunities for acquiring more and more market stake. Mergers therefore are tools in the hands of the entrepreneurial community to keep a watch on the competition and take appropriate action. Mergers are looked at as inorganic mechanisms for diversification and growth.

Following statutory provisions apply to mergers, amalgamations and acquisitions from competition law perspective:

- The Competition Act, 2002
- The Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011
- The Competition Commission of India (General) Regulations, 2009
- Notifications issued by Competition Commission of India from time to time.

COMPETITION ACT, 2002

At the behest of the Directive Principles of State Policy, the first Indian competition law was enacted in 1969 and was named the Monopolies and Restrictive Trade Practices Act, 1969 ("**MRTP Act**").

In the wake of economic reforms since 1991, i.e. the liberalization/privatization/globalization reforms, it was felt that the MRTP Act has become obsolete in the light of international economic developments which relate more particularly to competition laws and thus there was a need to shift the focus from curbing monopolies to promoting competition. Therefore, a 'High Level Committee on Competition Policy and Law' was constituted by the Central Government which submitted its Report on May 23, 2002. In accordance with the recommendations of this Committee, the Competition Act, 2002 was passed by both Houses of Parliament in 2002 and received the assent of President in January 2003. It provided for setting-up of a quasi-judicial body, *i.e.,* the CCI, comprising of a Chairperson and two to ten other Members, to prevent practices having adverse effect on competition, to promote and sustain competition in markets, to protect the interests of consumers and to ensure freedom of trade carried on by other participants in markets in India and for matters connected therewith or incidental thereto.

In exercise of these powers, the sections 3 and 4 were brought into force from 20th May 2009 and section 5 and 6 were brought into force with effect from 1st June 2011.

An Act to provide for, keeping in view of the economic development of the country, the establishment of a Commission to prevent practices having adverse effect on competition, to promote and sustain competition in markets, to protect the interest of consumers and to ensure freedom of trade carried on by other participants in market, in India, and for matters connected therewith or incidental thereto.

Key Provisions

Key provisions of the Act are contained in section 3, 4, 5 and 6. Through these sections, the Act declares anti-competitive agreements as *void;* prohibits abuse of dominant position, and regulates large combinations.

Section 5 and 6 provides for regulation of the combinations beyond the prescribed threshold. A combination includes the acquisition of control, shares, voting rights, assets as well as the cases of merger or amalgamation. Section 6 provides that no person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be *void*.

Competition Commission of India (CCI / Commission)

Section 7 of the Act provides for the establishment of the Competition Commission of India ("Commission"). The Commission is a statutory body, established under the Act with the legislative mandate inter alia to prevent practices having adverse effect on competition, to promote and sustain competition in the markets, to protect the interests of consumers and to ensure freedom of trade carried on by other participants in the markets, in India. To perform the above-mentioned functions, under the scheme of the Act, the Commission is vested with inquisitorial, investigative, regulatory, adjudicatory and advisory jurisdiction. As such, the purpose of filing information before the Commission is only to set the ball rolling as per the provisions of the Act. The Commission works as the overarching supervisory and regulatory framework for competition related matters in India.

National Company Law Appellate Tribunal (NCLAT)

The Act also provided for the establishment of Competition Appellate Tribunal ("COMPAT") which was in operation till 25th May 2017. With effect from 26th May 2017, COMPAT has been merged with the National Company Law Appellate Tribunal ("NCLAT") constituted under the Companies Act, 2013 and the NCLAT has been designated as the Appellate Authority under the Act.

Combinations and the Competition Act, 2002 (Act)

Section 5 defines the combination as (i) acquisition of control, shares, voting rights or assets; or (ii) acquiring of control by a person over an enterprise when such person has already direct or indirect control over another enterprise engaged in production, distribution or trading of a similar or identical or substitutable goods or provision of a similar or identical or substitutable service; or (iii) merger or amalgamation.

A combination beyond the prescribed thresholds is regulated under the Act. Section 6 declares a combination as *void* if it causes or is likely to cause an adverse effect on competition within the relevant market in India.

Kinds of combinations

Based on the economic activities being carried out by the parties, combinations may be classified into three categories:

Horizontal combinations

Horizontal combinations involve the joining together of two or more enterprises engaged in producing the same goods, or rendering the same services. They may be termed as competitors to each other. They result in reduction in the number of competing firms in an industry and may create a dominant enterprise.

Vertical combinations

Vertical combinations involve the joining together of two or more enterprises where one of them is an actual or potential supplier of goods or services to the other. They involve enterprises operating at different levels of the production chain. The object of these combinations may be to ensure a source of supply or an outlet for products or to enhance the efficiency.

Conglomerate combinations

Conglomerate combinations involve the combination of enterprises not having horizontal or vertical connection. These enterprises are engaged in unrelated activities and may be affected with an objective to diversify into new areas by the acquiring enterprise.

Based on the geographical location of the enterprises, the combination may be classified into two categories:

Domestic Combinations

Domestic combinations involve the joining together of two or more enterprises located in India only.

Cross-border Combinations

Cross-border combinations involve the joining together of two or more enterprises where one or more of them are operating from other countries. In such combinations, the combination needs to be approved by the Commission only if the overseas enterprises satisfy the local nexus test, as stated in section 5 of the Act.

In essence, only if the enterprises exceed the *de minimis* exemption thresholds and the thresholds under Section 5 of the Competition Act, will they be considered to have local nexus. This aligns the position in India more with the international standards.

Section 5 of the Competition Act, 2002 provides that the acquisition of one or more enterprises by one or more persons or merger or amalgamation of enterprises shall be a combination of such enterprises and persons or enterprises, if—

a. any acquisition where—

i. the parties to the acquisition, being the acquirer and the enterprise, whose control, shares, voting rights or assets have been acquired or are being acquired jointly have,—

A. either, in India, the assets of the value of more than rupees one thousand crores or turnover more than rupees three thousand crores; or

B. in India or outside India, in aggregate, the assets of the value of more than five hundred million US dollars, including at least rupees five hundred crores in India, or turnover more than fifteen hundred million US dollars, including at least rupees fifteen hundred crores in India; or

ii. the group, to which the enterprise whose control, shares, assets or voting rights have been acquired or are being acquired, would belong after the acquisition, jointly have or would jointly have,—

A. either in India, the assets of the value of more than rupees four thousand crores or turnover more than rupees twelve thousand crores; or

B. in India or outside India, in aggregate, the assets of the value of more than two billion US dollars or turnover more than six billion US dollars; or

b. acquiring of control by a person over an enterprise when such person has already direct or indirect control over another enterprise engaged in production, distribution or trading of a similar or identical or substitutable goods or provision of a similar or identical or substitutable service, if—

i. the enterprise over which control has been acquired along with the enterprise over which the acquirer already has direct or indirect control jointly have, —

A. either in India, the assets of the value of more than rupees one thousand crores or turnover more than rupees three thousand crores; or

B. in India or outside India, in aggregate, the assets of the value of more than five hundred million US dollars, including at least rupees five hundred crores in India, or turnover more than fifteen hundred million US dollars, including at least rupees fifteen hundred crores in India; or

ii. the group, to which enterprise whose control has been acquired, or is being acquired, would belong after the acquisition, jointly have or would jointly have, —

A. either in India, the assets of the value of more than rupees four thousand crores or turnover more than rupees twelve thousand crores; or

B. in India or outside India, in aggregate, the assets of the value of more than two billion US dollars, including at least rupees five hundred crores in India, or turnover more than six billion US dollars, including at least rupees fifteen hundred crores in India; or

c. any merger or amalgamation in which—

i. the enterprise remaining after merger or the enterprise created as a result of the amalgamation, as the case may be, have, —

A. either in India, the assets of the value of more than rupees one thousand crores or turnover more than rupees three thousand crores; or

B. in India or outside India, in aggregate, the assets of the value of more than five hundred million US dollars, including at least rupees five hundred crores in India, or turnover more than fifteen hundred million US dollars, including at least rupees fifteen hundred crores in India; or

ii. the group, to which the enterprise remaining after the merger or the enterprise created as a result of the amalgamation, would belong after the merger or the amalgamation, as the case may be, have or would have, —

A. either in India, the assets of the value of more than rupees four-thousand crores or turnover more than rupees twelve thousand crores; or

B. in India or outside India, in aggregate, the assets of the value of more than two billion US dollars, including at least rupees five hundred crores in India, or turnover more than six billion US dollars, including at least rupees fifteen hundred crores in India.

d. value of any transaction, in connection with acquisition of any control, shares, voting rights or assets of an enterprise, merger or amalgamation exceeds rupees two thousand crore:

Provided that the enterprise which is being acquired, taken control of, merged or amalgamated has such substantial business operations in India as may be specified by regulations.

e. notwithstanding anything contained in clause (*a*) or clause (*b*) or clause (*c*), where either the value of assets or turnover of the enterprise being acquired, taken control of, merged or amalgamated in India is not more than such value as may be prescribed, such acquisition, control, merger or amalgamation, shall not constitute a combination under section 5.

Explanation. —For the purposes of section 5 —

a. ***"Control"*** means the ability to exercise material influence, in any manner whatsoever, over the management or affairs or strategic commercial decisions by—

  i. one or more enterprises, either jointly or singly, over another enterprise or group; or

  ii. one or more groups, either jointly or singly, over another group or enterprise;

b. ***"Group"*** means two or more enterprises where one enterprise is directly or indirectly, in a position to—

  i. exercise twenty-six per cent. or such other higher percentage as may be prescribed, of the voting rights in the other enterprise; or

  ii. appoint more than fifty per cent. of the members of the board of directors in the other enterprise; or

  iii. control the management or affairs of the other enterprise;

c. ***"Turnover"*** means the turnover certified by the statutory auditor on the basis of the last available audited accounts of the company in the financial year immediately preceding the financial year in which the notice is filed under sub-section (*2*) or sub-section (*4*) of section 6 and such turnover in India shall be determined by excluding intra-group sales, indirect taxes, trade discounts and all amounts generated through assets or business from customers outside India, as certified by the statutory auditor on the basis of the last available audited accounts of the company in the financial year immediately preceding the financial year in which the notice is filed under sub-section (*2*) or sub-section (*4*) of section 6;

d. ***"Value of Transaction"*** includes every valuable consideration, whether direct or indirect, or deferred for any acquisition, merger or amalgamation;

e. ***the Value of Assets*** shall be determined by taking the book value of the assets as shown, in the audited books of account of the enterprise, in the financial year immediately preceding the financial year in which the date of proposed combination falls and if such financial statement has not yet become due to be filed with the Registrar under the Companies Act, 2013 then as per the statutory auditor's report made on the basis of the last available audited accounts of the company in the financial year immediately preceding the financial year in which the notice is filed under sub-section (*2*) or sub-section (*4*) of section 6, as reduced by any depreciation, and the value of assets shall include the brand value, value of goodwill, or 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 under the laws provided in sub-section (*5*) of section 3;

f. where a portion of an enterprise or division or business is being acquired, taken control of, merged or amalgamated with another enterprise, the value of assets or turnover or value of transaction as may be applicable, of the said portion or division or business or attributable to it, shall be the relevant assets or turnover or relevant value of transaction for the purpose of applicability of the thresholds under section 5.

Combination Regulations

Competition Act, 2002 requires mandatory notification of combination. Assets and turnover thresholds for such mandate are prescribed by the Act, and are modifiable by the Government as prescribed under section 20(3) of the Act. The basic concern is with the existence or likelihood of the proposed combination causing appreciable adverse effect on competition ("AAEC") in the relevant market in India.

The process of combination analysis undertaken by the Commission is therefore broken down into:

(a) delineation of the relevant market (product and geographic);

(b) identification of overlap in the relevant market; and finally,

(c) subjecting the combination to competition analysis under section 20(4) of the Act to ensure that there is no appreciable adverse effect on competition in the relevant market. The test under section 20(4) of the Act involves balancing of the benefits and the adverse effects on competition, due to the proposed combination.

To aid and assist the parties to the combination in relation to certain procedural and substantive provisions, the CCI has provided for informal non-binding pre-merger consultative process and has also provided for couple of guidance notes i.e., Introductory Note1 and Notes to Form I in order to assist the notifying parties in drafting the merger notification form(s) to be submitted to the Commission.

The Section 5 and 6 of the Competition Act are the operative and substantive provisions dealing with the combinations and Section 29 to 31 along with the CCI (Procedure in regard to the transaction of business relating to combinations) Amendment Regulations, 2011 (**Combination Regulations**) set-up the procedural provisions in relation to the combinations. In addition to Combination Regulations, the applicable provisions in relation to confidentiality under Section 57 of the Competition Act and CCI (General) Regulation 2009 are applicable. Further, a transaction will be construed as a combination for the purposes of Competition Act, if the transaction crosses certain minimum thresholds in terms of the assets and/ or turnover of the enterprises affected by the transaction.

What is a Combination?

Section 5 provides the financial thresholds and all combinations exceeding these financial thresholds are required to be mandatorily approved by the Commission.

Combination

Combinations as envisaged under section 5(a), 5(b) and 5(c) were explained by the Supreme Court in ***Competition Commission of India v. Thomas Cook (India) Ltd. & Anr. (Civil Appeal No.13578 of 2015)*** in the following manner:

Under section 5(a), a combination is formed if the acquisition by one person or enterprise of control, shares, voting rights or assets of another person or enterprise subject to certain threshold requirement that is minimum asset valuation or turn over within or outside India.

Under Section 5(b) of the Act the combination is formed if the acquisition of control by a person over enterprise when such person has already acquired direct or indirect control over another enterprise engaged in the production, distribution or payment of a similar or identical or substitutable good provided that the exigencies provided in section 5(b) in terms of asset or turnover are met.

Under section 5(c) merger and amalgamation are also within the ambit of combination. The enterprise remaining after merger or amalgamation subject to a minimum threshold requirement in terms of assets or turnover is covered within the purview of section 5(c).

Thresholds

In exercise of the powers conferred by sub-section (3) of Section 20 of the Competition Act, 2002, the Central Government vide its Notification dated March 07, 2024 and in consultation with the Competition Commission of India, enhanced, on the basis of the wholesale price index and exchange rate of rupee, the value of assets and the value of turnover, by One hundred and fifty percent for the purposes of section 5 of the Competition Act. The value of assets and turnover after revision is as under:

THRESHOLDS FOR FILING NOTICE				
Enterprise level		**Assets**		**Turnover**
	India	***> 2500 INR Crore***	**Or**	***> 7500 INR Crore***
	In India or Outside India	***> USD 1.25 bn with at least > 1250 INR Crore in India***		***> USD 3.75 bn with at least > 3750 INR Crore in India***
OR				
Group Level		**Assets**		**Turnover**
	India	***> 10000 INR Crore***	**Or**	***> 30000 INR Crore***
	In India or Outside India	***> USD 5 bn with at least > 1250 INR Crore in India***		***> USD 15 bn with at least > 3750 INR Crore in India***

De-Minimis Thresholds: In exercise of the powers conferred by clause (a) of section 54 of the Competition Act, 2002 it has also been decided with regards to de-minimis thresholds that the value of assets and turnover be enhanced from INR 350 crore (rupees three hundred fifty crore) to INR 450 crore (rupees four hundred fifty crore) for assets and from INR 1000 crore (rupees one thousand crore) to INR 1250 crore (rupees one thousand two hundred fifty crore) for turnover.

THRESHOLDS FOR AVALING OF DE-MINIMIS EXEMPTION				
		Assets		**Turnover**
Target Enterprise	**In India**	< Rs.450 Crore	**Or**	< Rs.1250 Crore

In exercise of the powers conferred by clause (a) of section 54 of the Competition Act, 2002, the Central Government vide Notification S.O. 1131(E) dated March 07, 2024 and in public interest exempted the enterprises being parties to ––

(a) any acquisition referred to in clause (a) of section 5 of the Competition Act;

(b) acquiring of control by a person over an enterprise when such person has already direct or indirect control over another enterprise engaged in production, distribution or trading of a similar or identical or substitutable goods or provision of a similar or identical or substitutable service, referred to in clause (b)of section 5 of the Competition Act; and

(c) any merger or amalgamation, referred to in clause (c) of section 5 of the Competition Act,

where the value of assets being acquired, taken control of, merged or amalgamated is not more than rupees Four hundred and fifty crore in India or turnover of not more than rupees One thousand two hundred and fifty crore in India, from the provisions of section 5 of the said Act for a period of two years from the date of publication of this notification in the Official Gazette.

Where a portion of an enterprise or division or business is being acquired, taken control of, merged or amalgamated with another enterprise, the value of assets of the said portion or division or business and or attributable to it, shall be the relevant assets and turnover to be taken into account for the purpose of calculating the thresholds under section 5 of the Act. The value of the said portion or division or business shall be determined 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 have 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, as reduced by any depreciation, and the value of assets shall include the brand value, value of goodwill, or value of copyright, patent, permitted use, collective mark, registered proprietor, registered trade mark, registered user, homonymous geographical indications, geographical indications, design or layout- design or similar other commercial rights, if any, referred to in sub-section (5) of section 3. The turnover of the said portion or division or business shall be as certified by the statutory auditor on the basis of the last available audited accounts of the company.

Anti-Competitive Agreements

Section 3 of the Competition Act provides for the prohibition of certain anti-competitive agreements. Under the Act, anti-competitive agreements include any agreement related to the production, supply, storage, or control of goods or services, that can cause an appreciable adverse effect on competition in India. Any agreement between enterprises or persons engaged in identical or similar businesses will have such adverse effect on competition if it meets certain criteria. These include: (a) directly or indirectly determining purchase or sale prices, (b) controlling production, supply, markets, or provision of services, or (c) directly or indirectly leading to collusive bidding.

As per Competition (Amendment) Act, 2023, if an enterprise or association of enterprises or a person or association of persons though not engaged in identical or similar trade shall also be presumed to be part of the agreement under this sub-section if it participates or intends to participate in the furtherance of such agreement. The amendment introduces an additional provision stating that an enterprise or association of enterprises or a person or association of persons though not engaged in identical or similar trade shall also be presumed to be part of such anti-competitive agreements if they participate or intends to participate in the furtherance of such agreements.

Group & Turnover

As per Section 5 of the Competition Act, 2002 as amended in 2023 "Group" means two or more enterprises where one enterprise is directly or indirectly, in a position to——

(i) exercise fifty per cent or more of the voting rights in the other enterprise; or

(ii) appoint more than fifty per cent of the members of the board of directors in the other enterprise; or

(iii) control the management or affairs of the other enterprise.

Further, "Turnover" means the turnover certified by the statutory auditor on the basis of the last available audited accounts of the company in the financial year immediately preceding the financial year in which the notice is filed under sub-section (*2*) or sub-section (*4*) of section 6 and such turnover in India shall be determined by excluding intra-group sales, indirect taxes, trade discounts and all amounts generated through assets or business from customers outside India, as certified by the statutory auditor on the basis of the last available audited accounts of the company in the financial year immediately preceding the financial year in which the notice is filed under sub-section (*2*) or sub-section (*4*) of section 6.

Regulation of Combinations

Section 6 of the Competition Act, 2002 prohibits any person or enterprise from entering into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and if such a combination is formed, it shall be *void*. Section 6 read as under:

Regulation of combinations

(1.) No person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be void.

(2.) Subject to the provisions contained in sub-section (1), any person or enterprise, who or which proposes to enter into a combination, shall give notice to the Commission, in the form as may be specified, and the fee which may be determined, by regulations, disclosing the details of the proposed combination, after any of the following, but before consummation of the combination—

(a) approval of the proposal relating to merger or amalgamation, referred to in clause (d) of section 5, by the board of directors of the enterprises concerned with such merger or amalgamation, as the case may be;

(b) execution of any agreement or other document for acquisition referred to in clause (d) of section 5 or acquiring of control referred to in clause (b) of that section.

It may be noted that "other document" means any document, by whatever name called, conveying an agreement or decision to acquire control, shares, voting rights or assets or if the acquisition is without the consent of the enterprise being acquired, any document executed by the acquiring enterprise, by whatever name called, conveying a decision to acquire control, shares or voting rights or where a public announcement has been made in accordance with the provisions of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 made under the Securities and Exchange Board of India Act, 1992 for acquisition of shares, voting rights or control such public document.

(2A) No combination shall come into effect until one hundred and fifty days have passed from the day on which the notice has been given to the Commission under sub-section (2) or the Commission has passed orders under section 31, whichever is earlier.

(3) The Commission shall, after receipt of notice under sub-section (2), deal with such notice in accordance with the provisions contained in sections 29, 29A, 30 and 31.

(4) Notwithstanding anything contained in sub-sections (2A) and (3) and section 43A, if a combination fulfils such criteria as may be prescribed and is not otherwise exempted under this Act from the requirement to give notice to the Commission under sub-section (2), then notice for such combination may be given to the Commission in such form and on payment of such fee as may be specified by regulations, disclosing the details of the proposed combination and thereupon a separate notice under sub-section (2) shall not be required to be given for such combination.

(5) Upon filing of a notice under sub-section (4) and acknowledgement thereof by the Commission, the proposed combination shall be deemed to have been approved by the Commission under sub-section (*1*) of section 31 and no other approval shall be required under sub-section (2) or sub-section (2A).

(6) If within the period referred to in sub-section (1) of section 20, the Commission finds that the combination notified under sub-section (4) does not fulfil the requirements specified under that sub-section or the information or declarations provided are materially incorrect or incomplete, the approval under sub-section (5) shall be void *ab initio* and the Commission may pass such order as it may deem fit:

Provided that no such order shall be passed unless the parties to the combination have been given an opportunity of being heard.

(7) Notwithstanding anything contained in this section and section 43A, upon fulfilment of such criteria as may be prescribed, certain categories of combinations shall be exempted from the requirement to comply with sub-sections (2), (2A) and (4).

(8) Notwithstanding anything contained in sub-sections (4), (5), (6) and (7)—

(*i*) the rules and regulations made under this Act on the matters referred to in these sub-sections as they stood immediately before the commencement of the Competition (Amendment) Act, 2023 and in force at such commencement, shall continue to be in force, till such time as the rules or regulations, as the case may be, made under this Act; and

(*ii*) any order passed or any fee imposed or combination consummated or resolution passed or direction given or instrument executed or issued or thing done under or in pursuance of any rules and regulations made under this Act shall, if in force at the commencement of the Competition (Amendment) Act, 2023, continue to be in force, and shall have effect as if such order passed or such fee imposed or such combination consummated or such resolution passed or such direction given or such instrument executed or issued or done under or in pursuance of this Act.

(9) The provisions of this section shall not apply to share subscription or financing facility or any acquisition, by a public financial institution, foreign portfolio investor, bank or Category I alternative investment fund, pursuant to any covenant of a loan agreement or investment agreement.

Explanation.—For the purposes of this section, the expression—

(*a*) "Category I alternative investment fund" has the same meaning as assigned to it under the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012 made under the Securities and Exchange Board of India Act, 1992;

(*b*) "foreign portfolio investor" has the same meaning as assigned to it under the Securities and Exchange Board of India (Foreign Portfolio Investors) Regulations, 2019 made under the Securities and Exchange Board of India Act, 1992.

Open Offers

Section 6A of the Act provides that nothing contained in sub-section (*2A*) of section 6 and section 43A shall prevent the implementation of an open offer or an acquisition of shares or securities convertible into other securities from various sellers, through a series of transactions on a regulated stock exchange from coming into effect, if—

(*a*) the notice of the acquisition is filed with the Commission within such time and in such manner as may be specified by regulations; and

(*b*) the acquirer does not exercise any ownership or beneficial rights or interest in such shares or convertible securities including voting rights and receipt of dividends or any other distributions, except as may be specified by regulations, till the Commission approves such acquisition in accordance with the provisions of sub-section (*2A*) of section 6 of the Act.

Explanation. —For the purposes of this section, "open offer" means an open offer made in accordance with the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulation, 2011 made under the Securities and Exchange Board of India Act, 1992.

Exemptions to Banking Sector and Oil and Gas Sector

Section 54(a) of the Act empowers the Central Government to grant exemption to any class of enterprises from all or any provisions of the Act if such exemption is necessary in the interest of security of the State or public interest. To exercise the said power, the Central Government has to issue a notification giving details about the extent of exemption and the duration of such exemption. With regard to the combinations relating to banking sector and oil and gas sectors, the Central Government has issued the following notifications.

(i) *Regional Rural Banks:* Regional Rural Banks in respect of which the Central Government has issued a notification under sub-section (1) of section 23A of the Regional Rural Banks Act, 1976 are exempted from complying with the provisions of the application sections 5 and 6 of the Competition Act, 2002 for a period of five years. - S.O. 2561(E). 10th August 2017 issued by the Ministry of Corporate Affairs.

(ii) *Nationalized banks:* All cases of reconstitution, transfer of the whole or any part thereof and amalgamation of nationalized banks, under the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 and the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980, are exempted from complying with the provisions of the application of sections 5 and 6 of the Competition Act, 2002 for a period of five years. - S.O. 2828(E). 30th August 2017 issued by the Ministry of Corporate Affairs.

(iii) *Oil and Gas Sectors:* All cases of combinations under section 5 of the Act involving the Central Public Sector Enterprises (CPSEs) operating in the Oil and Gas Sectors under the Petroleum Act, 1934 and the rules made thereunder or under the Oilfields (Regulation and Development) Act, 1948 and the rules made thereunder, along with their wholly or partly owned subsidiaries operating in the Oil and Gas Sectors, are exempted from complying with the provisions of the application of sections 5 and 6 of the Competition Act, 2002 for a period of five years. - S.O. 3714(E). 22nd November 2017 issued by the Ministry of Corporate Affairs.

Ordinarily exempt transactions under Combination Regulations

The Combinations Regulations, 2011 provide for the procedural framework on regulation of the combinations. Schedule I to the Regulations provides a list of transactions which are ordinarily not likely to raise competition concerns and hence normally exempt from approval requirements. They are known as 'ordinarily exempt' transactions. However, such ordinarily exempt transactions also need prior approval of the Commission if the same is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination. In other words, the parties will have to approach the Commission, before giving effect to the proposed combination.

The Commission has highlighted this fact in in the matter of ***SCM Soilfert Limited / Deepak Fertilizers*** (order under section 43A relating to Combination Registration No. C-2014/05/175), in the following words:

"*It is observed that the categories of combinations listed in Schedule I to the Combination Regulations must be interpreted in light of the Commission's objectives (listed in Section 18 of the Act) and the intent of Schedule I (expressed in Regulation 4 of the Combination Regulations). This means that the categories of combinations listed in Schedule I as normally not notifiable ought not to include combinations which envisage or are likely to cause a change in control or are of the nature of strategic combinations including those between competing enterprises or enterprises active in vertical markets*."

Control

One of the most important facets of the Indian merger control regime is the element of 'control'. Control over an enterprise has the ability to change the competitive dynamics of any market, and the CCI, like all other competition regulators, gives due importance to changes in control.

Apart from the 'positive control' over an enterprise which comes from owning more than 50%of the voting rights of a company or control over more than 50% of the board of directors of a company, the CCI also considered 'negative control', i.e. control exercised contractually by way of Affi Voting Rights (AVRs) / veto rights over the strategic business decisions of the company. This is concurrent with the practice in other advanced jurisdictions such as the EU, which also follow the test of decisive control4. The CCI judges each case on its merits and circumstances, and seeks to distinguish between rights that are purely investment protection rights, and those that enable the holder to control the key strategic business decisions of the company.

As per Section 5 of the Competition Act, 2002 as amended in 2023 "Control" means the ability to exercise material influence, in any manner whatsoever, over the management or affairs or strategic commercial decisions by—

(i) one or more enterprises, either jointly or singly, over another enterprise or group;

(ii) one or more groups, either jointly or singly, over another group or enterprise.

Further, "group" means two or more enterprises where one enterprise is directly or indirectly, in a position to—

(*i*) exercise twenty-six per cent. or such other higher percentage as may be prescribed, of the voting rights in the other enterprise; or

(*ii*) appoint more than fifty per cent. of the members of the board of directors in the other enterprise; or

(*iii*) control the management or affairs of the other enterprise.

From the control perspective, a combination may involve acquisition of control; acquisition of joint control; transfer from joint control to sole control; or continuation of joint control even after acquisition has taken place. Based on the Regulations and the interpretation by the CCI in numerous cases, the term control can have different dimensions such as joint control, indirect control, common control, negative control, strategic control etc.

Notice to the Commission disclosing details of the proposed combination

As stated earlier, section 6(2) envisages that any person or enterprise, who or which proposes to enter into any combination, shall give a notice to the Commission disclosing details of the proposed combination, in the form prescribed and submit the form together with the fee prescribed by Regulations. Contravention of this provision would attract the result into the imposition of penalty under section 43A of the Act.

Inquiry into combination by the Commission

The Commission under section 20 of the Competition Act may inquire into the appreciable adverse effect caused or likely to be caused on competition in India as a result of combination in the following circumstances:

(i) upon its own knowledge or information (*suo moto*); or

(ii) upon receipt of notice under section 6(2) relating to acquisition referred to in section 5(a); or acquiring of control referred to in section 5(b); or merger or amalgamation referred to in section 5(c) of the Act.

It has also been provided that a *suo moto* enquiry shall be initiated by the Commission within one year from the date on which such combination has taken effect. Thus, the Act has provided a time limit within which *suo moto* inquiry into combinations can be initiated. This provision dispels the fear of enquiry into combination between merging entities after the expiry of stipulated period.

On receipt of the notice under section 6(2) from the person or an enterprise which proposes to enter into a combination, it is mandatory for the Commission to inquire whether the combination referred to in that notice, has caused or is likely to cause an appreciable adverse effect on competition (AAEC) within the relevant market in India.

Appreciable Adverse Effect on Combination (AAEC)

The Commission shall have due regard to all or any of the following factors listed under section 20(4) for the purposes of determining whether the combination causes or is likely to cause an AAEC in the relevant market:

(a) actual and potential level of competition through imports in the market;

(b) extent of barriers to entry into the market;

(c) level of concentration in the market;

(d) degree of countervailing power in the market;

(e) likelihood that the combination would result in the parties to the combination being able to significantly and sustainably increase prices or profit margins;

(f) extent of effective competition likely to sustain in a market;

(g) extent to which substitutes are available or likely to be available in the market;

(h) market share, in the relevant market, of the persons or enterprise in a combination, individually and as a combination;

(i) likelihood that the combination would result in the removal of a vigorous and effective competition or competitors in the market;

(j) nature and extent of vertical integration in the market;

(k) possibility of a failing business;

(l) nature and extent of innovation;

(m) relative advantage, by way of the contribution to the economic development, by any combination having or likely to have appreciable adverse effect on competition;

(n) whether the benefits of the combination outweigh the adverse impact of the combination, if any.

The above yardsticks are to be taken into account irrespective of the fact whether an inquiry is instituted, on receipt of notice under section 6(2) or upon its own knowledge. The scope of assessment of adverse effect on competition will be confined to the "relevant market". Most of the facts enumerated in section 20(4) are external to an enterprise. It is noteworthy that sub clause (n) of Section 20(4) requires to invoke principles of a "balancing". It requires the Commission to evaluate whether the benefits of the combination outweigh the adverse impact of the combination, if any. In other words if the benefits of the combination outweigh the adverse effect of the combination, the Commission will approve the combination. Conversely, the Commission may declare such a combination as *void*.

Relevant market

Relevant market is the mix of relevant geographic market and relevant product market. Sub-section (r) of section 2 defines relevant market to mean the market which may be determined by the Commission with reference to the relevant product market or the relevant geographic market or with reference to both the markets.

Relevant geographic market

Sub-section (s) of section 2 defines the relevant geographic market to mean a market comprising the area in which the conditions of competition for supply of goods or provision of services or demand of goods or services are distinctly homogenous and can be distinguished from the conditions prevailing in the neighboring areas.

Relevant product market

Sub-section (t) of section 2 defines the relevant product market to mean a market comprising all those products or services which are regarded as interchangeable or substitutable by the consumer, by reason of characteristics of the products or services, their prices and intended use.

Competition (Amendment) Act, 2023 expands the definition of relevant product market to include the perspective of suppliers. As per revised definition "relevant product market" means a market comprising of all those products or services—

(*i*) which are regarded as inter-changeable or substitutable by the consumer, by reason of characteristics of the products or services, their prices and intended use; or

(*ii*) the production or supply of, which are regarded as interchangeable or substitutable by the supplier, by reason of the ease of switching production between such products and services and marketing them in the short term without incurring significant additional costs or risks in response to small and permanent changes in relative prices.

Filing of notice (Form)

For seeking approval to the proposed combination, parties to the combination are required to give notice to the Commission by filing Form I or Form II. Format of these forms are given in Schedule II to the Combination Regulations.

Form of Notice for the Proposed Combination (Regulation 5)

(1) Any enterprise which proposes to enter into a combination shall give notice of such combination to the Commission in accordance with sub-section (2) of section 6 of the Act and these regulations.

(2) The notice under sub-section (2) of section 6 of the Act, shall ordinarily be filed in Form I as specified in schedule II to these regulations, duly filled in and accompanied by evidence of payment of requisite fee by the parties to the combination.

(3) Notwithstanding anything contained in sub-regulation (2) and without prejudice to the provisions of sub-regulation (5), the parties to the combination may, at their option, give notice in Form II, as specified in schedule II to these regulations, preferably in the instances where-

(a) the parties to the combination are engaged in production, supply, distribution, storage, sale or trade of similar or identical or substitutable goods or provision of similar or identical or substitutable services and the combined market share of the parties to the combination after such combination is more than fifteen percent (15%) in the relevant market;

(b) the parties to the combination are engaged at different stages or levels of the production chain in different markets, in respect of production, supply, distribution, storage, sale or trade in goods or provision of services, and their individual or combined market share is more than twenty five percent (25%) in the relevant market.

(3A) The parties to the combination shall give notice in Form I or Form II, as the case may be, in accordance with the notes to Form I and Form II issued by the Commission and published on its official website, from time to time.

(4) Where in the course of inquiry, it is found by the Commission that it requires additional information, the Commission may direct the parties to the combination to file such additional information: Provided that the time taken by the parties to the combination in filing such additional information shall be excluded from the period provided in sub-section (2A) of section 6 of the Act; sub-section (11) of section 31 of the Act and sub-regulation (1) of regulation 19 of these regulations.

(5) Having due regard to the provisions of sub-regulations (2) and (4), in cases where the parties to the combination have filed notice in Form I and the Commission requires information in Form II to form its prima facie opinion whether the combination is likely to cause or has caused appreciable adverse effect on competition within the relevant market, it shall direct the parties to the combination to file notice in Form II as specified in schedule II to these regulations.

Provided that the fee already paid by the parties to the combination while filing notice in Form I shall be reduced from the fee payable for filing notice in Form II:

Provided further that the time period mentioned in sub-section (2A) of section 6 of the Act, sub-section (11) of section 31 of the Act and sub-regulation (1) of regulation 19 of these regulations shall commence from the date of receipt of notice in Form II.

(6) If the requisite details are not available for any of the columns in Form I or Form II, the date on which they may be submitted should be clearly indicated against those columns, by the parties to the combination.

Provided that the time taken by the parties to the combination to submit the requisite details shall be excluded from the period provided in sub-section (2A) of section 6 of the Act; sub-section (11) of section 31 of the Act and sub-regulation (1) of regulation 19 of these regulations.

Notice for Approval of Combinations under Green Channel (Regulation 5A)

(1) For the category of combination mentioned in Schedule III, the parties to such combination may, at their option, give notice in Form I pursuant to regulation 5 along with the declaration specified in Schedule IV.

(2) Upon filing of a notice under sub-regulation (1) and acknowledgement thereof, the proposed combination shall be deemed to have been approved by the Commission under sub-section (1) of section 31 of the Act: Provided that where the Commission finds that the combination does not fall under Schedule III and/or the declaration filed pursuant to sub-regulation (1) is incorrect, the notice given and the approval granted under this regulation shall be void ab initio and the Commission shall deal with the combination in accordance with the provisions contained in the Act.

Provided further that the Commission shall give to the parties to the combination an opportunity of being heard before arriving at a finding that the combination does not fall under Schedule III and/or the declaration filed pursuant to sub-regulation (1) is incorrect.

Filing of details of Acquisition under section 6(5) of the Act (Regulation 6)

(1) The details of acquisition by a public financial institution, foreign institutional investor, bank or venture capital fund, pursuant to any covenant of a loan or investment agreement, shall be filed without any fee in Form III, along with a certified copy of the loan agreement or investment agreement referred to in sub- section (5) of section 6 of the Act.

(2) The duly filled in Form III, along with one copy and electronic version thereof, shall be delivered to the Commission at the address published on its official website.

(3) Without prejudice to the provisions of the Act, where details of acquisition filed in Form III under sub-regulation (1) are received in the Commission beyond the time limit mentioned in subsection (5) of section 6 of the Act, the Commission may admit such details of acquisition in Form III.

Obligation to File the Notice (Regulation 9)

(1) In case of an acquisition or acquiring of control of enterprise(s), the acquirer shall file the notice in Form I or Form II, as the case may be, which shall be duly signed by the person(s) as specified under regulation 11 of the Competition Commission of India (General) Regulations, 2009.

Provided that in case of a company, apart from the persons specified under clause (c) of sub-regulation (1) of regulation 11 of the Competition Commission of India (General) Regulations, 2009, Form I or Form II may also be signed by any person duly authorised by the company.

(2) In case the enterprise is being acquired without its consent, the acquirer shall furnish such information as is available to him, in Form I or Form II, as the case may be, relating to the enterprise being acquired.

Provided that all information required to be filed, relating to the enterprise being acquired shall be filed with the Commission within fifteen days from filing of the notice and in case the acquirer is not in a position to furnish all the required information in Form I or Form II, as the case may be, relating to the enterprise being acquired, the Commission may direct the enterprise being acquired to furnish such information as it deems fit and the time taken by the parties to the combination or the acquired enterprise, as the case may be, in furnishing the required information including document(s) shall be excluded from the period provided in sub-section (2A) of section 6 of the Act; sub-section (11) of section 31 of the Act and sub-regulation (1) of regulation 19 of Combination Regulations.

(3) In case of a merger or an amalgamation, parties to the combination shall jointly file the notice in Form I or Form II, as the case may be, duly signed by the person(s) as specified under regulation 11 of the Competition Commission of India (General) Regulations, 2009.

Provided that in case of a company, apart from the persons specified under clause (c) of sub-regulation (1) of regulation 11 of the Competition Commission of India (General) Regulations, 2009, Form I or Form II may also be signed by any person duly authorised by the company.

(4) Where the ultimate intended effect of a business transaction is achieved by way of a series of steps or smaller individual transactions which are inter-connected 26, one or more of which may amount to a combination, a single notice, covering all these transactions, shall be filed by the parties to the combination.

(5) The requirement of filing notice under regulation 5 of these regulations shall be determined with respect to the substance of the transaction and any structure of the transaction(s), comprising a combination, that has the effect of avoiding notice in respect of the whole or a part of the combination shall be disregarded.

Obligation to Pay the Fee (Regulation 10)

(1) The person or enterprise filing notice under regulation 5 or regulation 8 shall pay the fee as specified under regulation 11 of Combination Regulations. Where the notice is filed jointly, the fee shall be payable jointly or severally.

Prima Facie Opinion on the Combination (Regulation 19)

(1) The Commission shall form its prima facie opinion under sub-section (1) of section 29 of the Act, on the notice filed in Form I or Form II, as the case may be, as to whether the combination is likely to cause or has caused an appreciable adverse effect on competition within the relevant market in India, within thirty working days of receipt of the said notice.

(2) Before the Commission forming an opinion under sub-section (1) of section 29 of the Act, the parties to the combination may offer modification to the combination and on that basis, the Commission may approve the proposed combination under sub-section (1) of section 31 of the Act.

Provided that where modification is offered by the parties to the combination, the additional time, not exceeding fifteen days, needed for evaluation of the offered modification, shall be excluded from the period provided in sub-regulation (1) of this regulation, sub-section (2A) of section 6 of the Act and sub-section (11) of section 31 of the Act.

(3) Where the Commission deems it necessary, it may call for information from any other enterprise while inquiring as to whether a combination has caused or is likely to cause an appreciable adverse effect on competition in India.

Provided that the time taken in obtaining the information from such enterprise(s) shall be excluded from the time, not exceeding fifteen working days, provided in sub-regulation (1) of this regulation.

Summary of Combination

A summary of the combination, not containing any confidential information, in not less than 2000 words, comprising *inter alia* the details regarding: (a) the products, services and business(es) of the parties to the combination; (b) the values of assets/turnover for the purpose of section 5 of the Act; (c) the respective markets in which the parties to the combination operate; (d) the details of agreement(s)/other documents and the board resolution(s) executed/ passed in relation to the combination; (e) the nature and purpose of the combination; and (f) the likely impact of the combination on the state of the competition in the relevant market(s) in which the parties to the combination operate, along with nine copies and an electronic version thereof shall be separately given while delivering the notice.

Summary for Website

A summary of the combination, not containing any confidential information, in not more than 500 words, comprising details regarding: (a) name of the parties to the combination; (b) the type of the combination; (c) the area of activity of the parties to the combination; and (d) the relevant market(s) to which the combination relates, along with an electronic version thereof shall be separately given while delivering the notice. The summary so submitted shall be published on the website of the Commission.

Consultation with the Commission

Consultation prior to filing of notice of the proposed combination

In accordance with international best practices, the Commission allows for an informal and verbal consultation with the staff of the Commission prior to filing of the notice to a proposed combination in terms of regulation 5 of Combinations Regulations, under section 6(2).

Such pre-filing consultations help the parties intending to file a notice with the Commission in identifying the information required for filing a complete and correct Form I/II/III as well in identifying additional information that the Commission may require to assess the likely impact of the proposed combination on competition in the relevant markets.

The parties intending to file a notice with the Commission are encouraged to approach the Commission for pre- filing consultations. A request for pre-filing consultation should be made by the parties intending to file a notice at the earliest and at least 10 days before the intended date of filing, to allow time for allocating a case team for the pre-filing consultation. A copy of draft application comprising of Form I/II/, as the case may be and supporting documents should be forwarded along with the request for scheduling a pre-filing consultation.

A summary of the proposed combination along with the following details should also be submitted:

(a) Basic details of the proposed combination including various steps involved in the same;

(b) A brief description of the relevant market(s) and sector(s) involved;

(c) The likely impact of the proposed combination on competition in those markets and sectors in general terms;

(d) Key issues regarding which the parties wish to seek consultation from the Commission;

(e) Any other details which according to the parties may be pertinent for a meaningful consultation.

Publication of the details of combination

Where the Commission forms a prima facie opinion that the combination has caused or is likely to cause appreciable adverse effect on competition within the relevant market in India, the Secretary shall, within 7 working days of such decision convey the direction of the Commission to the parties to the combination, to publish the details of the combination within 10 working days of the date of such direction. The details of combination shall be published by the parties in Form IV, as specified in Schedule II to the Regulations. The parties shall publish the details of the combination in all India editions of four leading daily newspapers including at least two business newspapers. Any person(s) adversely affected or likely to be affected by the combination may send comments / objections/ suggestions in writing with supporting documents within 15 working days from the date of this publication.

Procedure for investigation of combination

The Competition Commission of India (CCI) has been empowered to deal with Form I or Form II in accordance with provisions of sections 29, 30 and 31 of the Act. Section 29 prescribes procedure for investigation of combinations. Section 30 empowers the Commission to determine whether the disclosure made to it under section 6(2) is correct and whether the combination has, or is likely to have, an appreciable adverse effect on the competition. Section 31 provides that the Commission may allow the combination if it will not have any appreciable adverse effect on competition or pass an order that the combination shall not take effect, if in its opinion, such a combination has or is likely to have an appreciable adverse effect on competition.

Section 29 of the Act deals with procedure of investigation of Combinations. It provides that:

1) Where the Commission is of the prima facie opinion that a combination is likely to cause, or has caused an appreciable adverse effect on competition within the relevant market in India, it shall issue a notice to show cause to the parties to combination calling upon them to respond within fifteen days of the receipt of the notice, as to why investigation in respect of such combination should not be conducted.

(1A) After receipt of the response of the parties to the combination under sub-section (1), the Commission may call for a report from the Director General and such report shall be submitted by the Director General within such time as the Commission may direct.

(1B) The Commission shall, within thirty days of receipt of notice under sub-section (2) of section 6, form its prima facie opinion referred to in sub-section (1).

2) The Commission, if it is prima facie of the opinion that the combination has, or is likely to have, an appreciable adverse effect on competition, it shall, within seven days from the date of receipt of the response of the parties to the combination, or the receipt of the report from Director General called under sub section (1A), whichever is later, direct the parties to the said combination to publish details of the combination within seven days of such direction, in such manner, as it thinks appropriate, for bringing the combination to the knowledge or information of the public and persons affected or likely to be affected by such combination.

3) The Commission may invite any person or member of the public, affected or likely to be affected by the said combination, to file his written objections, if any, before the Commission within ten days from the date on which the details of the combination were published under sub-section (2).

4) The Commission may, within seven days from the expiry of the period specified in sub-section (3), call for such additional or other information as it may deem fit from the parties to the said combination.

5) The additional or other information called for by the Commission shall be furnished by the parties referred to in sub-section (4) within ten days from the expiry of the period specified in sub- section (4).

6) After receipt of all information, the Commission shall proceed to deal with the case in accordance with the provisions contained in section 29A or section 31, as the case may be.

7) Notwithstanding anything contained in this section, the Commission may accept appropriate modifications offered by the parties to the combination or suo motu propose modifications, as the case may be, before forming a prima facie opinion under sub-section (1).

Issue of statement of objections by Commission and proposal of modifications

Section 29A (*1*) of the Act states that upon completion of the process under section 29, where the Commission is of the opinion that the combination has, or is likely to have, an appreciable adverse effect on competition, it shall issue a statement of objections to the parties identifying such appreciable adverse effect on competition and direct the parties to explain within twenty-five days of receipt of the statement of objections, why such combination should be allowed to take effect.

As per sub-section (*2*) where the parties to the combination consider that such appreciable adverse effect on competition can be eliminated by suitable modification to such combination, they may submit an offer of appropriate modification to the combination along with their explanation to the statement of objections issued under sub-section (*1*) in such manner as may be specified by regulations.

Sub-section (*3*) provides that if the Commission does not accept the modification submitted by the parties under sub-section (*2*) it shall, within seven days from the date of receipt of the proposed modifications under that sub-section, communicate to the parties as to why the modification is not sufficient to eliminate the appreciable adverse effect on competition and call upon the parties to furnish, within twelve days of the receipt of the said communication, revised modification, if any, to eliminate the appreciable adverse effects on competition:

Provided that the Commission shall evaluate such proposal for modification within twelve days from receipt of such proposal:

Provided further that the Commission may *suo motu* propose appropriate modifications to the combination which may be considered by the parties to the combination.

Orders of Commission on Combinations

The Commission, after consideration of the relevant facts and circumstances of the case under investigation by it under section 28 or 30 and assessing the effect of any combination on the relevant market in India, may pass any of the written orders indicated herein below:

(a) *Approve:* Where the Commission comes to a conclusion that any combination does not, or is not likely to, have an appreciable adverse effect on the Competition in relevant market in India, it may, approve that Combination.

(b) *Reject:* Where the Commission is of the opinion that the combination has, or is likely to have an adverse effect on competition, it shall direct that the combination shall not take effect.

(c) *Modify:* Where the Commission is of the opinion that adverse effect which has been caused or is likely to be caused on competition can be eliminated by modifying such combination then it shall direct the parties to such combination to carry out necessary modifications to the combination.

Orders of Commission on certain Combinations

Section 31 of the Act provides that:

(1) where the Commission is of the opinion that any combination does not, or is not likely to, have an appreciable adverse effect on competition, it shall, by order, approve that combination including the combination in respect of which a notice has been given under sub-section (2) of section 6.

(2) Where the Commission is of the opinion that the combination has, or is likely to have, an appreciable adverse effect on competition, it shall direct that the combination shall not take effect.

(3) Where the Commission is of the opinion that any appreciable adverse effect on competition that the combination has, or is likely to have, can be eliminated by modification proposed by the parties or the Commission, as the case may be, under sub-section (*7*) of section 29 or sub-section (*2*) or sub-section (*3*) of section 29A, it may approve the combination subject to such modifications as it thinks fit.

(4) Where a combination is approved by the Commission under sub-section (*3*), the parties to the combination shall carry out such modification within such period as may be specified by the Commission.

(5) Where (*a*) the Commission has directed under sub-section (*2*) that the combination shall not take effect; or (*b*) the parties to the combination, fail to carry out the modification within such period as may be specified by the Commission under sub-section (*4*); or (*c*) the Commission is of the opinion that the combination has, or is likely to have, an appreciable adverse effect on competition which cannot be eliminated by suitable modification to such combination, then, without prejudice to any penalty which may be imposed or any prosecution which may be initiated under this Act, the Commission may order that such combination

shall not be given effect to, or be declared void, or frame a scheme to be implemented by the parties to address the appreciable adverse effect on competition, as the case may be.

(*6*) If no order is passed or direction issued by the Commission in accordance with the provisions of sub-section (*1*) or sub-section (*2*) or sub-section (*3*) or sub-section (*5*), as the case may be, within a period of one hundred and fifty days from the date of notice given to the Commission under sub-section (*2*) of section 6, the combination shall be deemed to have been approved by the Commission.

Extra Territorial Jurisdiction of Commission

Section 32 extends the jurisdiction of Competition Commission of India to inquire and pass orders in accordance with the provisions of the Act into an agreement or dominant position or combination, which is likely to have, an appreciable adverse effect on competition in relevant market in India, notwithstanding that,

(a) an agreement referred to in section 3 has been entered into outside India; or

(b) any party to such agreement is outside India; or

(c) any enterprise abusing the dominant position is outside India; or

(d) a combination has taken place outside India; or

(e) any party to combination is outside India; or

(f) any other matter or practice or action arising out of such agreement or dominant position or combination is outside India.have power to inquire in accordance with the provisions contained in sections 19, 20, 26, 29, 29A and 30 of the Act into such agreement or abuse of dominant position or combination if such agreement or dominant position or combination has, or is likely to have, an appreciable adverse effect on competition in the relevant market in India 1 [and pass such orders as it may deem fit in accordance with the provisions of this Act.

The above clearly demonstrate that acts taking place outside India but having an effect on competition in India will be subject to the jurisdiction of Commission. The Commission will have jurisdiction even if both the parties to an agreement are outside India but only if the agreement, dominant position or combination entered into by them has an appreciable adverse effect on competition in the relevant market of India.

Power to impose penalty for non-furnishing of information on Combination

Section 43A provides that if any person or enterprise fails to give notice to the Commission under sub-section (*2*) or sub-section (*4*) of section 6 or contravenes sub-section (*2A*) of section 6 or submit information pursuant to an inquiry under sub-section (*1*) of section 20, the Commission may impose on such person or enterprise, a penalty which may extend to one per cent., of the total turnover or assets or the value of transaction referred to in clause (*d*) of section 5, whichever is higher, of such a combination:

Provided that in case any person or enterprise has given a notice under sub-section (*4*) of section 6 and such notice is found to be void *ab initio* under sub-section (*6*) of section 6, then a notice under sub-section (*2*) of section 6 may be given by the acquirer or parties to the combination, as may be applicable, within a period of thirty days of the order of the Commission under sub-section (*6*) of that section and no action under this section shall be taken by the Commission till the expiry of such period of thirty days.

LESSON ROUND-UP

- The preamble of the Competition Act, 2002 states that this is an Act to establish a Commission to prevent anti-competitive practices, promote and sustain competition, protect the interests of the consumers and ensure freedom of trade in markets in India.
- Section 4 prohibits the abuse of dominance by an enterprise or a group.

- Section 5 and 6 provides for regulation of the combinations beyond the prescribed threshold.
- Section 5 provides the financial thresholds and all combinations exceeding prescribed financial thresholds are required to be mandatorily approved by the Commission.
- Section 6 provides that no person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be void.
- Combination means acquisition of control, shares, voting rights or assets, acquisition of control by a person over an enterprise where such person has direct or indirect control over another enterprise engaged in competing businesses, mergers and amalgamations between or amongst enterprises.
- Any person or enterprise, who or which proposes to enter into any combination, shall give a notice to the Commission disclosing details of the proposed combination, in the form, prescribed and submit the form together with the fee prescribed by regulations. Such intimation should be submitted before consummation of the proposed combination.
- The Competition Commission of India has been empowered to deal with Form I or Form II in accordance with provisions of sections 29, 30 and 31 of the Act. Section 29 prescribes procedure for investigation of combinations.
- Section 32 of the Competition Act, 2002 extends the extra territorial jurisdiction of the Competition Commission of India to enquiry and pass orders in accordance with the provisions of the Act into an agreement, dominant position and regulates combinations i.e., mergers and acquisitions with a view to ensure that there is no adverse effect on competition in India.

GLOSSARY

Acquisition: Acquisition means, directly or indirectly, acquiring or agreeing to acquire (i) shares, voting rights or assets of any enterprise; or (ii) control over management or control over assets of any enterprise.

Combination: An acquisition of one or more enterprises by one or more persons or merger or amalgamation of enterprises if the thresholds prescribed under Section 5 of the Act are met.

Group: Two or more enterprises which, directly or indirectly, are in a position to —

(i) exercise fifty per cent or more of the voting rights in the other enterprise; or

(ii) appoint more than fifty per cent of the members of the board of directors in the other enterprise; or

(iii) control the management or affairs of the other enterprise.

Control: It the ability to exercise material influence, in any manner whatsoever, over the management or affairs or strategic commercial decisions by— (i) one or more enterprises, either jointly or singly, over another enterprise or group; or (ii) one or more groups, either jointly or singly, over another group or enterprise.

Relevant Market: Relevant market to mean the market which may be determined by the Commission with reference to the relevant product market or the relevant geographic market or with reference to both the markets.

Relevant geographic market: A market comprising the area in which the conditions of competition for supply of goods or provision of services or demand of goods or services are distinctly homogenous and can be distinguished from the conditions prevailing in the neighboring areas.

Relevant product market: A market comprising all those products or services which are regarded as interchangeable or substitutable by the consumer, by reason of characteristics of the products or services, their prices and intended use. The amendment act 2022 expands the definition of relevant product market to include the perspective of suppliers. The revised definition includes all those products or services that are regarded as interchangeable or substitutable by the consumers as well as those whose production or supply is regarded as interchangeable or substitutable by suppliers.

TEST YOURSELF

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. What is a combination in terms of the Competition Act, 2002?
2. What parameters are applied by the Competition Commission of India to determine if the proposed combination is likely to have appreciable adverse effect on competition in relevant market in India?
3. What factors are considered by the Competition Commission of India to determine the relevant market?
4. Discuss about the threshold limits of Combination.
5. What are the powers of the Competition Commission of India to penalise the parties who have given effect to a combination without seeking approval of the Commission?
6. What is the procedure for investigation of combinations?
7. What do you understand by extra territorial jurisdiction of the Commission?

LIST OF FURTHER READINGS

- Merger Control in India by Tarun Mathur, EBC Publications
- Competition Law in India by T. Ramappa, Oxford Publications
- Competition Law in India by Roy and Kumar, 2nd Edition, Eastern Law House
- Competition Act, 2002.- Bare Act.

Regulatory Approvals of Scheme

Lesson 9

KEY CONCEPTS

■ Competition Commission of India ■ Reserve Bank of India ■ Foreign Exchange ■ Cross Boarder Merger

Learning Objectives

To understand:

- Regulatory Approval of Merger or amalgamation
- Regulatory approvals from RD / ROC/ OL
- Approval under Competition Act
- Approval from SEBI / Stock Exchange(s)
- Regulatory approvals from RBI
- Approvals from IRDA/ TRAI

Lesson Outline

- Introduction
- Regulatory approvals from Competition Commission of India (CCI), Income Tax Authorities, Stock Exchange, SEBI
- Regulatory approvals from RBI, RD, ROC and Official Liquidator
- Approvals from Sector Regulators such as IRDA, TRAI, etc.
- Lesson Round-Up
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

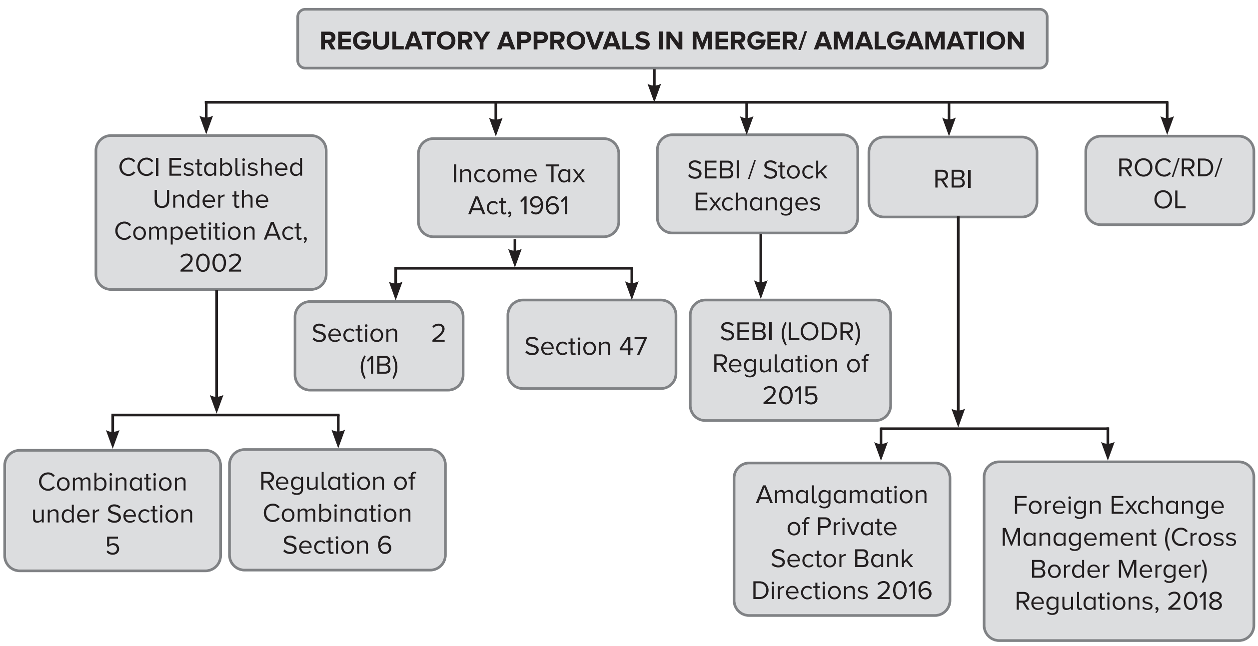
- The Companies Act, 2013
- The Competition Act, 2002
- The Income Tax Act, 1961
- The Banking Regulation Act, 1949
- The Foreign Exchange Management (Cross Border Merger) Regulations 2018

INTRODUCTION

The Companies Act, 2013 requires that notice of the Merger be sent along with such other documents as the Scheme and valuation report, not only to shareholders and creditors, but also to various regulators like the Ministry of Corporate Affairs, the Reserve Bank of India (in cases, where non-resident investors are involved), SEBI and Stock Exchanges (for listed companies), Competition Commission of India (in cases where the prescribed fiscal thresholds are being crossed and the proposed merger could have an adverse effect on competition), Income Tax authorities and any other relevant industry regulators or authorities which are likely to be affected by the merger. This ensures compliance of the Scheme with any and all other regulatory and statutory requirements that need to be followed by the merging entities. The Companies Act 2013 also prescribes a 30-day period for the regulators to make representations, failing which the right would cease to exist.

Merger or amalgamation of companies involves various issues including the regulatory approvals. These regulatory approvals are to be obtained not only from the sector in which the company is operating (for example in case of merger of two banks, RBI's approval is needed) but from other departments like Income Tax, SEBI, ROC, etc.

In this chapter, we shall discuss the various regulatory requirements which are needed for the smooth merger and amalgamation etc.



REGULATORY APPROVALS FROM COMPETITION COMMISSION OF INDIA (CCI), INCOME TAX AUTHORITIES, STOCK EXCHANGE, SEBI

Approval under Competition Act, 2002

Combination (Section 5 of Competition Act, 2002)

The Competition Act, 2002 is the principal legislation that regulates combinations (acquisitions, mergers, amalgamations and de-mergers) in India. Sections 5 and 6 of the Competition Act, which deal with the regulation of combinations, have been in force since 1st June 2011. Prior to this date there was no statutory obligation to notify to any antitrust authority before completing merger and amalgamations.

Section 5 of the Act prescribes the jurisdictional thresholds limits (based on asset and turnover of combining companies) for transactions that must be notified to CCI prior to implementation of merger and acquisition.

Meaning of Combination for the purpose of Competition Act, 2002

Any acquisition, merger or amalgamation that meets the following jurisdictional thresholds limits, as provided in Section 5 of the Competition Act, 2002, is a "combination" for the purpose of the Act.

The thresholds relate to the assets and turnover of the parties to the combination, i.e., target enterprise and acquirer (or acquirer group) / merging parties (or the group to which merged entity would belong).

Mandatory or voluntary

If the jurisdictional thresholds are met and exemptions are unavailable, it is mandatory to notify the Competition Commission of India (CCI) of the combination. Approval of CCI is must. CCI will consider whether proposed Combination is having any appreciable adverse impact on competition in India or not.

Regulatory Authority for Notifying Combinations

The Competition Commission of India (CCI) is the statutory authority responsible for reviewing combinations and assessing whether or not they cause or are likely to cause an appreciable adverse effect on competition within the relevant market(s) in India. CCI approval is required for combinations where the parties involved exceed the assets/turnover thresholds set out in section 5 of the Competition Act.

Triggering events

Any one of the following events requires approval of CCI:

1. The acquisition of
   - shares,
   - voting rights,
   - assets, or
   - control in one or more enterprises, or
2. A merger or amalgamation of enterprises,that meets the thresholds constitutes a combination and must be pre-notified to Competition Commission of India (CCI), and the approval of the Competition Commission of India (CCI) is required before the transaction can be completed.

Types of Notifiable Transactions

Section 5 of the Competition Act, 2002 covers three broad categories of combinations:

1. The acquisition by one or more persons of control, shares, voting rights or assets of one or more enterprises, where the parties, or the group to which the target will belong post-acquisition, meet the specified assets/ turnover thresholds.

2. The acquisition by a person of control over an enterprise where the person concerned already has direct and indirect control over another enterprise with which it compete, where the parties, or the group to which the target will belong post-acquisition, meet the specified assets/turnover thresholds.

3. Mergers or amalgamations, where the enterprise remaining, or enterprise created, or the group to which the enterprise will belong after the merger/amalgamation, meets the specified assets/turnover thresholds.

Time Period for CCI for giving Approval

The Combination Regulations provide that the CCI will "endeavour" to pass an order or issue directions within a period of 150 days from the date of notification. Section 6 deals with the Regulation of Combinations:

(1) No person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be *void*.

(2) Subject to the provisions contained in sub-section (1), any person or enterprise, who or which proposes to enter into a combination, shall give notice to the Commission, in the form as may be specified, and the fee which may be determined, by regulations, disclosing the details of the proposed combination, after any of the following, but before consummation of the combination—

(a) approval of the proposal relating to merger or amalgamation, referred to in clause (d) of section 5, by the board of directors of the enterprises concerned with such merger or amalgamation, as the case may be;

(b) execution of any agreement or other document for acquisition referred to in clause (d) of section 5 or acquiring of control referred to in clause (b) of that section.

It may be noted that "other document" means any document, by whatever name called, conveying an agreement or decision to acquire control, shares, voting rights or assets or if the acquisition is without the consent of the enterprise being acquired, any document executed by the acquiring enterprise, by whatever name called, conveying a decision to acquire control, shares or voting rights or where a public announcement has been made in accordance with the provisions of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 made under the Securities and Exchange Board of India Act, 1992 for acquisition of shares, voting rights or control such public document

(2A) No combination shall come into effect until ***one hundred and fifty*** dayshave passed from the day on which the notice has been given to the Commission under sub-section (2) or the Commission has passed orders under section 31, whichever is earlier.

(3) The Commission shall, after receipt of notice under sub-section (2), deal with such notice in accordance with the provisions contained in sections 29, 29A, 30 and 31.

(4) Notwithstanding anything contained in sub-sections (2A) and (3) and section 43A, if a combination fulfils such criteria as may be prescribed and is not otherwise exempted under this Act from the requirement to give notice to the Commission under sub-section (2), then notice for such combination may be given to the Commission in such form and on payment of such fee as may be specified by regulations, disclosing the details of the proposed combination and thereupon a separate notice under sub-section (2) shall not be required to be given for such combination.

(5) Upon filing of a notice under sub-section (4) and acknowledgement thereof by the Commission, the proposed combination shall be deemed to have been approved by the Commission under sub-section (1) of section 31 and no other approval shall be required under sub-section (2) or sub-section (2A).

(6) If within the period referred to in sub-section (1) of section 20, the Commission finds that the combination notified under sub-section (*4*) does not fulfil the requirements specified under that sub-section or the information or declarations provided are materially incorrect or incomplete, the approval under sub-section (*5*) shall be void *ab initio* and the Commission may pass such order as it may deem fit:

Provided that no such order shall be passed unless the parties to the combination have been given an opportunity of being heard.

(7) Notwithstanding anything contained in this section and section 43A, upon fulfilment of such criteria as may be prescribed, certain categories of combinations shall be exempted from the requirement to comply with sub-sections (2), (2A) and (4).

(8) Notwithstanding anything contained in sub-sections (4), (5), (6) and (7)—

(i) the rules and regulations made under this Act on the matters referred to in these sub-sections as they stood immediately before the commencement of the Competition (Amendment) Act, 2023 and in force at such commencement, shall continue to be in force, till such time as the rules or regulations, as the case may be, made under this Act; and

(ii) any order passed or any fee imposed or combination consummated or resolution passed or direction given or instrument executed or issued or thing done under or in pursuance of any rules and regulations made under this Act shall, if in force at the commencement of the Competition (Amendment) Act, 2023, continue to be in force, and shall have effect as if such order passed or such fee imposed or such combination consummated or such resolution passed or such direction given or such instrument executed or issued or done under or in pursuance of this Act.

(9) The provisions of this section shall not apply to share subscription or financing facility or any acquisition, by a public financial institution, foreign portfolio investor, bank or Category I alternative investment fund, pursuant to any covenant of a loan agreement or investment agreement.

THE COMPETITION COMMISSION OF INDIA (PROCEDURE IN REGARD TO THE TRANSACTION OF BUSINESS RELATING TO COMBINATIONS) REGULATIONS, 2011

- **Regulation 5(9):** Where, in a series of steps or individual transactions that are related to each other, assets are being transferred to an enterprise for the purpose of such enterprise entering into an agreement relating to an acquisition or merger or amalgamation with another person or enterprise, for the purpose of section 5 of the Competition Act, 2002, the value of assets and turnover of the enterprise whose assets are being transferred shall also be attributed to the value of assets and turnover of the enterprise to which the assets are being transferred.

- **Regulation 9(3):** In case of a merger or an amalgamation, parties to the combination shall jointly file the notice in Form I or Form II, as the case may be, duly signed by the person(s) as specified under regulation 11 of the Competition Commission of India (General) Regulations, 2009. Provided that in case of a company, apart from the persons specified under clause (c) of sub-regulation (1) of regulation 11 of the Competition Commission of India (General) Regulations, 2009, Form I or Form II may also be signed by any person duly authorised by the company.

- **Schedule I-Para 9:** A merger or amalgamation of two enterprises where one of the enterprises has more than fifty per cent (50%) shares or voting rights of the other enterprise, and/or merger or amalgamation of enterprises in which more than fifty per cent (50%) shares or voting rights in each of such enterprises are held by enterprise(s) within the same group: Provided that the transaction does not result in transfer from joint control to sole control.

- **Schedule II-Para 6.5:** Furnish copies of approval of the proposal relating to merger or amalgamation by the board of directors of the enterprise(s) concerned referred to in clause (a) of sub- section (2) of section 6 of the Act and/or agreement /other document executed in relation to the acquisition or acquiring of control referred to in clause (b) of sub-section (2) of section 6 of the Act along with the supporting documents as listed in the Notes to Form I, if applicable.

- **Form I: Registration No:** (to be assigned by the Competition Commission of India) Information required to be filled in by the notifying party(ies).

- **Form II:** Form of filing notice with the Competition Commission of India under sub-section (2) of section 6 of the Competition Act, 2002.

- **Form III:** Form for filing of details of acquisition under sub-section (5) of section 6 of the Competition Act, 2002.

Approval under Income Tax Act, 1961

The Income Tax Act, 1961 contemplates and recognizes the following types of merger and acquisition activities:

- Merger/Amalgamation;
- Demerger or spin-off;
- Slump sale/asset sale; and
- Transfer of shares/Share Sale.

Merger has not been defined under the Income Tax Act, 1961 but has been covered under the term 'amalgamation' as defined in section 2(1B) of the Act. To encourage restructuring, merger and demerger, it has been given a special treatment in the Income-Tax Act, 1961 since the beginning. The Finance Act, 1999 clarified many issues relating to business reorganizations thereby facilitating and making business restructuring tax neutral.

Every scheme involving restructuring is required to be submitted to jurisdictional assessing officer and no-objection is required from income-tax department before a scheme is approved by NCLT.

Certain provisions of Income Tax Act, 1961 applicable to mergers/demergers are as under:

Meaning of Amalgamation [Section 2(1B)]

"Amalgamation", in relation to companies, means the merger of one or more companies with another company or the merger of two or more companies to form one company (the company or companies which so merge being referred to as the amalgamating company or companies and the company with which they merge or which is formed as a result of the merger, as the amalgamated company) in such a manner that —

(i) all the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation;

(ii) all the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation;

(iii) shareholders holding not less than three-fourths in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee for, the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of the amalgamation,otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first-mentioned company.

Section 45 of the Income Tax Act, 1961 levies tax on capital gains arising on the transfer of a capital asset. Section 2(47) of the Act defines the term 'transfer' in relation to a capital asset. If a merger or any other kind of restructuring results in a transfer of a capital asset by a resident or a capital asset that is situated in India to a non-resident, it would lead to a taxable event.

Section 47 of the Act sets out certain transfers that are exempt from the provisions of Section 45 (the charging provision for tax on capital gains) and such transfers are exempt from tax on capital gains. The relevant exemptions are mentioned in Lesson 8 of this Study Material.

Approval from SEBI / Stock Exchange(s)

Securities Contracts (Regulation) Rules, 1957: Sub-rule (7) of rule 19 of the Securities Contracts (Regulation) Rules, 1957 provides that Securities and Exchange Board of India (SEBI) may, at its own discretion or on the recommendation of a recognised Stock Exchange, waive or relax the strict enforcement of any or all of the requirements with respect to listing prescribed by these rules.

Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015.

Regulation 11: Scheme of Arrangement

The listed entity shall ensure that any scheme of arrangement /amalgamation /merger /reconstruction / reduction of capital etc. to be presented to any Court or Tribunal does not in any way violate, override or limit the provisions of securities laws or requirements of the stock exchange(s):

Provided that this regulation shall not be applicable for the units issued by Mutual Funds which are listed on a recognised stock exchange(s).

Regulation 37: Draft Scheme of Arrangement & Scheme of Arrangement

1. Without prejudice to provisions of regulation 11, the listed entity desirous of undertaking a scheme of arrangement or involved in a scheme of arrangement, shall file the draft scheme of arrangement, proposed to be filed before Tribunal under Sections 230-234 and an scheme of arrangement by way of reduction of capital under Section 66 of Companies Act, 2013, *along with a non- refundable fee as specified in Schedule XI,* with the stock exchange(s) for obtaining No- objection letter, before filing such scheme with any Court or Tribunal, in terms of requirements specified by the Board or stock exchange(s) from time to time.

2. The listed entity shall not file any scheme of arrangement under sections 230-234 and scheme of arrangement by way of reduction of capital under Section 66 of Companies Act, 2013, with Tribunal unless it has obtained the No-objection letter from the stock exchange(s).

3. The listed entity shall place the No-objection letter of the stock exchange(s) before the Tribunal at the time of seeking approval of the scheme of arrangement:

   Provided that the validity of the No-objection letter of stock exchanges shall be six months from the date of issuance, within which the draft scheme of arrangement shall be submitted to the Court or Tribunal.

4. The listed entity shall ensure compliance with the other requirements as may be prescribed by the Board from time to time.

5. Upon sanction of the Scheme by the Court or Tribunal, the listed entity shall submit the documents, to the stock exchange(s), as prescribed by the Board and/or stock exchange(s) from time to time.

6. Nothing contained in this regulation shall apply to draft schemes which solely provide for merger of a wholly owned subsidiary with its holding company:

   Provided that such draft schemes shall be filed with the stock exchanges for the purpose of disclosures.

7. The requirements as specified under this regulation and under regulation 94 of these regulations shall not apply to a restructuring proposal approved as part of a resolution plan by the Tribunal under section 31 of the Insolvency and Bankruptcy Code, 2016 subject to the details being disclosed to the recognized stock exchanges within one day of the resolution plan being approved.

Regulation 94: Draft Scheme of Arrangement & Scheme of Arrangement

1. The designated stock exchange, upon receipt of draft schemes of arrangement and the documents prescribed by the Board, as per sub-regulation (1) of regulation 37, shall forward the same to the Board, in the manner prescribed by the Board.

2. The stock exchange(s) shall submit to the Board its No-Objection Letter on the draft scheme of arrangement after inter-alia ascertaining whether the draft scheme of arrangement is in compliance with securities laws within thirty days of receipt of draft scheme of arrangement or within seven days of date of receipt of satisfactory reply on clarifications from the listed entity and/or opinion from independent chartered accountant, if any, sought by stock exchange(s), as applicable.

3. The stock exchange(s), shall issue No-objection letter to the listed entity within seven days of receipt of comments from the Board, after suitably incorporating such comments in the No-objection letter:

   Provided that the validity of the No-objection letter of stock exchanges shall be six months from the date of issuance.

4. The stock exchange(s) shall bring the objections to the notice of Court or Tribunal at the time of approval of the scheme of arrangement.

5. Upon sanction of the Scheme by the Tribunal, the designated stock exchange shall forward its recommendations to the Board on the documents submitted by the listed entity in terms of sub-regulation (5) of regulation 37.

REGULATORY APPROVALS FROM RBI, REGIONAL DIRECTOR (RD), ROC, OFFICIAL LIQUIDATOR

Regulatory approvals from RBI

Procedure for amalgamation of banking companies. —

The Reserve Bank has discretionary powers to approve the voluntary amalgamation of two banking companies under the provisions of Section 44A of the Banking Regulation Act, 1949.

Section 44A provides that:

1. Notwithstanding anything contained in any law for the time being in force, no banking company shall be amalgamated with another banking company, unless a scheme containing the terms of such amalgamation has been placed in draft before the shareholders of each of the banking companies concerned separately, and approved by a resolution passed by a majority in number representing two-thirds in value of the shareholders of each of the said companies, present either in person or by proxy at a meeting called for the purpose.

2. Notice of every such meeting as is referred to in sub-section (1) shall be given to every shareholder of each of the banking companies concerned in accordance with the relevant articles of association indicating the time, place and object of the meeting, and shall also be published at least once a week for three consecutive weeks in not less than two newspapers which circulate in the locality or localities where the registered offices of the banking companies concerned are situated, one of such newspapers being in a language commonly understood in the locality or localities.

3. Any shareholder, who has voted against the scheme of amalgamation at the meeting or has given notice in writing at or prior to the meeting of the company concerned or to the presiding officer of the meeting that he dissents from the scheme of amalgamation, shall be entitled, in the event of the scheme being sanctioned by the Reserve Bank, to claim from the banking company concerned, in respect of the shares held by him in that company, their value as determined by the Reserve Bank

when sanctioning the scheme and such determination by the Reserve Bank as to the value of the shares to be paid to the dissenting shareholder shall be final for all purposes.

4. If the scheme of amalgamation is approved by the requisite majority of shareholders in accordance with the provisions of this section, it shall be submitted to the Reserve Bank for sanction and shall, if sanctioned by the Reserve Bank by an order in writing passed in this behalf, be binding on the banking companies concerned and also on all the shareholders thereof.

5. On the sanctioning of a scheme of amalgamation by the Reserve Bank, the property of the amalgamated banking company shall, by virtue of the order of sanction, be transferred to and vest in, and the liabilities of the said company shall, by virtue of the said order be transferred to, and become the liabilities of, the banking company which under the scheme of amalgamation is to acquire the business of the amalgamated banking company, subject in all cases to the provisions of the scheme as sanctioned.

6A. Where a scheme of amalgamation is sanctioned by the Reserve Bank under the provisions of this section, the Reserve Bank may, by a further order in writing, direct that on such date as may be specified therein the banking company (hereinafter in this section referred to as the amalgamated banking company) which by reason of the amalgamation will cease to function, shall stand dissolved and any such direction shall take effect notwithstanding anything to the contrary contained in any other law.

6B. Where the Reserve Bank directs a dissolution of the amalgamated banking company, it shall transmit a copy of the order directing such dissolution to the Registrar before whom the banking company has been registered and on receipt of such order the Registrar shall strike off the name of the company.

6C. An order under sub-section (4) whether made before or after the commencement of section 19 of the Banking Laws (Miscellaneous Provisions) Act, 1963 shall be conclusive evidence that all the requirements of this section relating to amalgamation have been complied with, and a copy of the said order certified in writing by an officer of the Reserve Bank to be a true copy of such order and a copy of the scheme certified in the like manner to be a true copy thereof shall, in all legal proceedings (whether in appeal or otherwise and whether instituted before or after the commencement of the said section 19), be admitted as evidence to the same extent as the original order and the original scheme.

7. Nothing in the foregoing provisions of this section shall affect the power of the Central Government to provide for the amalgamation of two or more banking companies under section 396 of the Companies Act, 1956, [corresponding to Section 237 of the Companies Act, 2013], Provided that no such power shall be exercised by the Central Government except after consultation with the Reserve Bank.

Regulatory approvals from RD / ROC/ OL

Section 233 deals with the merger or amalgamation of certain companies. It provides as under:

1. Notwithstanding the provisions of section 230 and section 232, a scheme of merger or amalgamation may be entered into between two or more small companies or between a holding company and its wholly-owned subsidiary company or such other class or classes of companies as may be prescribed, subject to the following, namely:

   (a) a notice of the proposed scheme inviting objections or suggestions, if any, from the Registrar and Official Liquidator where registered office of the respective companies are situated or persons affected by the scheme within thirty days is issued by the transferor company or companies and the transferee company;

   (b) the objections and suggestions received are considered by the companies in their respective general meetings and the scheme is approved by the respective members or class of members at a general meeting holding at least ninety per cent of the total number of shares;

(c) each of the companies involved in the merger files a declaration of solvency, in the prescribed form, with the Registrar of the place where the registered office of the company is situated; and

(d) the scheme is approved by majority representing nine-tenths in value of the creditors or class of creditors of respective companies indicated in a meeting convened by the company by giving a notice of twenty-one days along with the scheme to its creditors for the purpose or otherwise approved in writing.

2. The transferee company shall file a copy of the scheme so approved in the manner as may be prescribed, with the Central Government[3] Registrar and the Official Liquidator where the registered office of the company is situated.

3. On the receipt of the scheme, if the Registrar or the Official Liquidator has no objections or suggestions to the scheme, the Central Government shall register the same and issue a confirmation thereof to the companies.

4. If the Registrar or Official Liquidator has any objections or suggestions, he may communicate the same in writing to the Central Government within a period of thirty days:

Provided that if no such communication is made, it shall be presumed that he has no objection to the scheme.

5. If the Central Government after receiving the objections or suggestions or for any reason is of the opinion that such a scheme is not in public interest or in the interest of the creditors, it may file an application before the Tribunal within a period of sixty days of the receipt of the scheme under sub-section (2) stating its objections and requesting that the Tribunal may consider the scheme under section 232.

6. On receipt of an application from the Central Government or from any person, if the Tribunal, for reasons to be recorded in writing, is of the opinion that the scheme should be considered as per the procedure laid down in section 232, the Tribunal may direct accordingly or it may confirm the scheme by passing such order as it deems fit.

Provided that if the Central Government does not have any objection to the scheme or it does not file any application under this section before the Tribunal, it shall be deemed that it has no objection to the scheme.

7. A copy of the order under sub-section (6) confirming the scheme shall be communicated to the Registrar having jurisdiction over the transferee company and the persons concerned and the Registrar shall register the scheme and issue a confirmation thereof to the companies and such confirmation shall be communicated to the Registrars where transferor company or companies were situated.

8. The registration of the scheme under sub-section (3) or sub-section (7) shall be deemed to have the effect of dissolution of the transferor company without process of winding up.

9. The registration of the scheme shall have the following effects, namely:—

(a) transfer of property or liabilities of the transferor company to the transferee company so that the property becomes the property of the transferee company and the liabilities become the liabilities of the transferee company;

(b) the charges, if any, on the property of the transferor company shall be applicable and enforceable as if the charges were on the property of the transferee company;

(c) legal proceedings by or against the transferor company pending before any court of law shall be continued by or against the transferee company; and

(d) where the scheme provides for purchase of shares held by the dissenting shareholders or settlement of debt due to dissenting creditors, such amount, to the extent it is unpaid, shall become the liability of the transferee company.

10. A transferee company shall not on merger or amalgamation, hold any shares in its own name or in the name of any trust either on its behalf or on behalf of any of its subsidiary or associate company and all such shares shall be cancelled or extinguished on the merger or amalgamation.

11. The transferee company shall file an application with the Registrar along with the scheme registered, indicating the revised authorised capital and pay the prescribed fees due on revised capital:

    Provided that the fee, if any, paid by the transferor company on its authorised capital prior to its merger or amalgamation with the transferee company shall be set-off against the fees payable by the transferee company on its authorised capital enhanced by the merger or amalgamation.

12. The provisions of this section shall *mutatis mutandis* apply to a company or companies specified in sub-section (1) in respect of a scheme of compromise or arrangement referred to in section 230 or division or transfer of a company referred to clause (*b*) of sub-section (1) of section 232.

13. The Central Government may provide for the merger or amalgamation of companies in such manner as may be prescribed.

14. A company covered under this section may use the provisions of section 232 for the approval of any scheme for merger or amalgamation.

Foreign Exchange Management (Cross Border Merger) Regulations 2018

Section 234 of the Companies Act, 2013 deals with the merger or amalgamation of company with foreign company. Sub-section (1) provides that the provisions of this Chapter unless otherwise provided under any other law for the time being in force, shall apply *mutatis mutandis* to schemes of mergers and amalgamations between companies registered under Companies Act, 2013 and companies incorporated in the jurisdictions of such countries as may be notified from time to time by the Central Government:

Provided that the Central Government may make rules, in consultation with the Reserve Bank of India, in connection with mergers and amalgamations provided under this section.

Subject to the provisions of any other law for the time being in force, a foreign company, may with the prior approval of the Reserve Bank of India, merge into a company registered under Companies Act, 2013 or *vice versa* and the terms and conditions of the scheme of merger may provide, among other things, for the payment of consideration to the shareholders of the merging company in cash, or in Depository Receipts, or partly in cash and partly in Depository Receipts, as the case may be, as per the scheme to be drawn up for the purpose.

Explanation.—For the purposes of sub-section (2), the expression "foreign company" means any company or body corporate incorporated outside India whether having a place of business in India or not.

Further Rule 25A was added by the Companies (Compromise, Arrangements & Amalgamation) Amendment Rules 2017.

The said rule deals with the merger or amalgamation of a foreign company with a Company and *vice versa* and provides as under:

1. A foreign company incorporated outside India may merge with an Indian company after obtaining prior approval of Reserve Bank of India and after complying with the provisions of sections 230 to 232 of the Companies Act, 2013 and these rules.

2. (a) A company may merge with a foreign company incorporated in any of the jurisdictions specified in Annexure B after obtaining prior approval of the Reserve Bank of India and after complying with provisions of sections 230 to 232 of the Companies Act, 2013 and these rules.

   (b) The transferee company shall ensure that valuation is conducted by valuers who are members of a recognised professional body in the jurisdiction of the transferee company and further that such valuation is in accordance with internationally accepted principles on accounting and valuation. A declaration to this effect shall be attached with the application made to Reserve Bank of India for obtaining its approval under clause (a) of this sub-rule.

3. The concerned company shall file an application before the Tribunal as per provisions of section 230 to section 232 of the Act and these rules after obtaining approvals specified in sub-rule (1) and sub-rule (2), as the case may be.

4. Notwithstanding anything contained in sub-rule (3), in case of a compromise or an arrangement or merger or demerger between an Indian company and a company or body corporate which has been incorporated in a country which shares land border with India, a declaration in Form No. CAA-16 shall be required at the stage of submission of application under section 230 of the Act.

Explanation 1. For the purposes of this rule the term "company" means a company as defined in clause (20) of section 2 of the Act and the term "foreign company" means a company or body corporate incorporated outside India whether having a place of business in India or not:

Explanation 2. For the purposes of this rule, it is clarified that no amendment shall be made in this rule without consultation of the Reserve Bank of India."

RBI's Guidelines: As mentioned in the proviso to section 234 that Central Government may make rules, in consultation with the Reserve Bank of India, in connection with mergers and amalgamations, the RBI *vide* its Press Release dated 20th March, 2018 placed on its website the regulations on cross border merger transactions pursuant to the Rules notified by Ministry of Corporate Affairs through Companies (Compromises, Arrangements and Amalgamations) Amendment Rules, 2017 on April 13, 2017.

Provisions under the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016

Merger or Amalgamation of certain companies (Rule 25)

1. The notice of the proposed scheme, under clause (*a*) of sub-section (1) of section 233 of the Act, to invite objections or suggestions from the Registrar and Official Liquidator or persons affected by the scheme shall be in Form No. CAA.9.

   (1A) A scheme of merger or amalgamation under section 233 of the Act may be entered into between any of the following class of companies, namely: -

   (i) two or more start-up companies; or

   (ii) one or more start-up company with one or more small company.

   Explanation. - For the purposes of this sub-rule, "start-up company" means a private company incorporated under the Companies Act, 2013or Companies Act, 1956 and recognized as such in accordance with notification number G.S.R. 127 (E), dated the 19th February, 2019 issued by the Department for Promotion of Industry and Internal Trade.

2. For the purposes of clause (c) of sub-section (1) of section 233 of the Act the declaration of solvency shall be filed by each of the companies involved in the scheme of merger or amalgamation in Form No. CAA.10 along with the fee as provided in the Companies (Registration Offices and Fees) Rules, 2014, before convening the meeting of members and creditors for approval of the scheme.

3. For the purposes of clause (b) and (d) of sub-section (1) of section 233 of the Act, the notice of the meeting to the members and creditors shall be accompanied by –

   (a) a statement, as far as applicable, referred to in sub-section (3) of section 230ofthe Act read with sub- rule (3) of rule 6 hereof;

   (b) the declaration of solvency made in pursuance of clause (c) of sub-section (1) of section 233 of the Act in Form No. CAA.10;

   (c) a copy of the scheme.

4. (*a*) For the purposes of sub-section (2) of section 233 of the Act, the transferee company shall, within seven days after the conclusion of the meeting of members or class of members or creditors or class of creditors, file a copy of the scheme as agreed to by the members and creditors, along with a report of the result of each of the meetings in Form No. CAA.11 with the Central Government, along with the fees as provided under the Companies (Registration Offices and Fees) Rules, 2014.

   (b) Copy of the scheme shall also be filed, along with Form No. CAA. 11 with:

      (i) the Registrar of Companies in Form No. GNL-1 along with fees provided under the Companies (Registration Offices and Fees) Rules, 2014; and

      (ii) the Official Liquidator through hand delivery or by registered post or speed post.

5. Where no objection or suggestion is received within a period of thirty days of receipt of copy of scheme under sub-section (2) of section 233, from the Registrar of Companies and Official Liquidator by the Central Government and the Central Government is of the opinion that the scheme is in the public interest or in the interest of creditors, it may, within a period of fifteen days after the expiry of said thirty days, issue a confirmation order of such scheme of merger or amalgamation in Form No. CAA.12.

   Provided that if the Central Government does not issue the confirmation order within a period of sixty days of the receipt of the scheme under sub-section (2) of section 233, it shall be deemed that it has no objection to the scheme and a confirmation order shall be issued accordingly.

(6) Where objections or suggestions are received within a period of thirty days of receipt of copy of scheme under sub-section (2) of section 233 from the Registrar of Companies or Official Liquidator or both by the Central Government and –

   (a) such objections or suggestions of Registrar of Companies or Official Liquidator, are not sustainable and the Central Government is of the opinion that the scheme is in the public interest or in the interest of creditors, it may within a period of thirty days after expiry of thirty days referred to above, issue a confirmation order of such scheme of merger or amalgamation in Form No. CAA.12.

   (b) the Central Government is of the opinion, whether on the basis of such objections or otherwise, that the scheme is not in the public interest or in the interest of creditors, it may within sixty days of the receipt of the scheme file an application before the Tribunal in Form No. CAA.13 stating the objections or opinion and requesting that Tribunal may consider the scheme under section 232 of the Act:

   Provided that if the Central Government does not issue a confirmation order under clause (a) or does not file any application under clause (b) within a period of sixty days of the receipt of the scheme under subsection (2) of section 233 of the Act, it shall be deemed that it has no objection to the scheme and a confirmation order shall be issued accordingly.

7. The confirmation order of the scheme issued by the Central Government or Tribunal under sub-section of section 233 of the Act, shall be filed within thirty days of the receipt of the order of confirmation in Form INC-28 along with the fees as provided under Companies (Registration Official and Fees) Rules, 2014 with the Registrar of Companies having jurisdiction over the transferee and transferor companies respectively.

8. For the purpose of this rule, it is clarified that with respect to schemes of arrangement or compromise falling within the purview of section 233 of the Act, the concerned companies may,at their discretion, opt to undertake such schemes under sections 230 to 232 of the Act, including where the condition prescribed in clause (*d*) of sub-section (1) of section 233 of the Act has not been met

APPROVALS FROM SECTOR REGULATORS SUCH AS IRDA, TRAI, ETC.

When arrangement, amalgamation or merger involves companies being regulated by a sectoral regulator like IRDA, TRAI, RBI, etc. then approval of such Regulators is also required in addition to compliance with Companies Act, 2013. Further these Regulators have issued detailed guidelines to be complied with while amalgamation/ merger between such companies.

Approvals from Insurance Regulatory and Development Authority (IRDA)

Section 36 of the Insurance Act, 1938 deals with the sanction of amalgamation and transfer by Authority.

When any application under sub-section (3) of section 35 is made to the Authority, the Authority shall cause, a notice of the application to be given to the holders of any kind of policy of insurer concerned along with statement of the nature and terms of the amalgamation or transfer, as the case may be, to be published in such manner and for such period as it may direct, and, after hearing the directors and considering the objections of the policyholders and any other persons whom it considers entitled to be heard, may approve the arrangement, and shall make such consequential orders as are necessary to give effect to the arrangement.

Section 37 of the Insurance Act, 1938 deals with the statements required after amalgamation and transfer

Where an amalgamation takes place between any two or more insurers, or where any business of an insurer is transferred, whether in accordance with a scheme confirmed by the Authority or otherwise, the insurer carrying on the amalgamated business or the person to whom the business is transferred, as the case may be, shall, within three months from the date of the completion of the amalgamation or transfer, furnish in duplicate to the Authority-

(a) a certified copy of the scheme, agreement or deed under which the amalgamation or transfer has been effected, and

(b) a declaration signed by every party concerned or in the case of a company by the chairman and the principal officer that to the best of their belief every payment made or to be made to any person whatsoever on account of the amalgamation or transfer is therein fully set forth and that no other payments beyond those set forth have been made or are to be made either in money, policies, bonds, valuable securities or other property by or with the knowledge of any parties to the amalgamation or transfer, and

(c) where the amalgamation or transfer has not been made in accordance with a scheme approved by the Authority under Section 36:

   (i) balance-sheet in respect of the insurance business of each of the insurers concerned in such amalgamation or transfer, prepared in the Form set forth in Part II of the First Schedule and in accordance with the regulations contained in Part I of that Schedule, and

   (ii) certified copies of any other reports on which the scheme of amalgamation or transfer was founded.

Section 37A of the Insurance Act, 1938 deals with the power of the authority to prepare scheme of Amalgamation

1. If the Authority is satisfied that-

   (i) in the public interest; or

   (ii) in the interests of the policy-holders; or

   (iii) in order to secure the proper management of an insurer; or

   (iv) in the interests of insurance business of the country as a whole.

it is necessary so to do, it may prepare a scheme for the amalgamation of that insurer with any other insurer (hereinafter referred to in this section as the transferee insurer):

Provided that no such scheme shall be prepared unless the other insurer has given his written consent to the proposal for such amalgamation

2. The scheme aforesaid may contain provisions for all or any of the following matters, namely:

(a) the constitution, name and registered office, the capital, assets, powers, rights, interests, authorities and privileges, and the liabilities, duties and obligations of the transferee insurer;

(b) the transfer to the transferee insurer the business, properties, assets and liabilities of the insurer on such terms and conditions as may be specified in the scheme;

(c) any change in the Board of Directors, or the appointment of a new Board of directors of the transferee-insurer and the authority by whom, the manner in which, and the other terms and conditions on which such change or appointment shall be made, and in the case of appointment of a new Board of Director or of any director, the period for which such appointment shall be made;

(d) the alteration of the memorandum and articles of association of the transferee insurer for the purpose of altering the capital thereof or for such other purposes as may be necessary to give effect to the amalgamation;

(e) subject to the provisions of the scheme, the continuation by or against the transferee insurer, of any actions or proceedings pending against the insurer;

(f) the reduction of the interest or rights which the shareholders, policy holders and other creditors have in or against the insurer before the amalgamation to such extent as the Authority considers necessary in the public interest or in the interests of the shareholders, policy-holders and other creditors or for the maintenance of the business of the insurer;

(g) the payment in cash or otherwise to policy-holders, and other creditors in full satisfaction of their claim, -

(i) in respect of their interest or rights in or against the insurer before the amalgamation; or

(ii) where their interest or rights aforesaid in or against the insurer has or have been reduced under clause (f), in respect of such interest or rights as so reduced.

(h) the allotment to the shareholders of the insurer for shares held by them therein before the amalgamation Whether their interest in such shares has been reduced under clause (f) or not] of shares in the transferee insurer and where any shareholders claim payment in cash and not allotment of shares, or where it is not possible to allot shares to any sharp holders the payment in cash to those shareholders in full satisfaction of their claim—

(i) in respect of their interest in shares in the insurer before the amalgamation; or

(ii) where such interest has been reduced under clause (f) in respect of their interest in shares as so reduced;

(i) the continuance of their services of all the employees of the insurer (excepting such of them as not being workmen within the meaning of the Industrial Disputes Act, 1947, are specifically mentioned in the scheme) in the transferee insurer at the same remuneration and on the same terms and conditions of service, which they were getting or, as the case may be, which they were being governed, immediately before the date of the amalgamation:

Provided that the scheme shall contain a provision that the transferee insurer shall pay or grant not later than the expiry of the period of three years, from the date of the amalgamation, to the said employees the same remuneration and the same terms and conditions of service as are applicable to the other employees of corresponding rank on status of the transferee insurer subject to the qualifications and experience of the said employees being the same as or equivalent to those of such other employees of the transferee insurer:

Provided further that if in any case any doubt or difference arises as to whether the qualification and experience of any of the said employees are the same as or are equivalent to the qualifications and experience of the other employees of corresponding rank or status of the transferee insurer, the doubt or difference shall be referred to the Authority whose decision thereon shall be final.

(j) notwithstanding anything contained in clause (i), where any of the employee, of the insurer not being workmen within the meaning of the Industrial Disputes Act, 1947, are specifically mentioned in the scheme under clause (i) or where any employees of the insurer have by notice in writing given to the insurer or, as the case may be, the transferee insurer at any time before the expiry of one month next following the date on which the scheme is sanctioned by the Central Government, intimated their intention of not becoming employees of the transferee insurer, the payment to such employees of compensation, if any, to which they are entitled under the Industrial Disputes Act, 1947, and such pension, gratuity, provident fund, or other retirement benefits ordinarily admissible to them under the rules or authorizations of the insurer immediately before the date of the amalgamation;

(k) any other terms and conditions for the amalgamation of the insurer;

(l) such incidental, consequential and supplemental matters as are necessary to secure that the amalgamation shall be fully and effectively carried out.

3. (a) A copy of the scheme prepared by the Authority shall be sent in draft to the insurer and also to the transferee insurer and any other insurer concerned in the amalgamation, for suggestions and objections, if any, within such period as the Authority may specify for this purpose.

(b) The Authority may make such modifications, if any, in the draft scheme as he may consider necessary in the light of suggestions and objections received from the insurer and also from the transferee insurer, and any other insurer concerned in the amalgamation and from any shareholder, policyholder or other creditor of each of those insurers and the transferee insurer.

4. The scheme shall thereafter be placed before the Central Government for its sanction and the Central Government may sanction the scheme without any modification or with such modifications as it may consider necessary, and the scheme as sanctioned by the Central Government shall come into force on such date as the Central Government may notify in this behalf in the Official Gazette:

Provided that different dates may be specified for different provisions of the scheme.

4A. Everypolicyholder orshareholderor memberof each of theinsurers, before amalgamation, shallhave the same interest in, or rights against the insurer resulting from amalgamation as he had in the company of which he was originally a policyholder or shareholder or member:

Provided that where the interests or rights of any shareholder or member are less than his interest in, or rights against, the original insurer, he shall be entitled to compensation, which shall be assessed by the Authority in such manner as may be specified by the regulations.

4B. The compensation so assessed shall be paid to the shareholder or member by the insurance company resulting from such amalgamation.

4C. Any member or shareholder aggrieved by the assessment of compensation made by the Authority under sub-section (4A) may within thirty days from the publication of such assessment *prefer an appeal to the Securities Appellate Tribunal.*

5. The sanction accorded by the Central Government under sub-section (4) shall be conclusive evidence that all the requirements of this section relating to amalgamation have been complied with and a

copy of the sanctioned scheme certified in writing by an officer of the Central Government to be a true copy thereof, shall, in all legal proceedings (whetherin appeal or otherwise) be admitted as evidence to the same extent as the original scheme.

6. The Authority may, in like-manner, add to, amend or vary any scheme made under this section.
7. On and from the date of the coming into operation of the scheme or any provision thereof; the scheme or such provision shall be binding on the insurer or, as the case may be, on the transferee-insurer and any other insurer concerned in the amalgamation and also on all the shareholders, policy-holders and other creditors and employees of each of those insurers and of the transferee insurer, and on any other person having any right or liability in relation to any of those insurers or the transferee insurer.
8. On and from such date as may be specified by the Central Government in this behalf, their properties and assets of the insurer shall, by virtue of and to the extent provided in the scheme, stand transferred to, and vest in, and the liabilities of the insurer shall, by virtue of and to the extent provided in the scheme, stand transferred to and become the liabilities of, the transferee insurer.
9. If any difficulty arises in giving effect to the provisions of the scheme the Central Government may by order do anything not inconsistent with such provisions which appears to it necessary or expedient for the purpose of removing the difficulty.
10. Copies of every scheme made under this section and of every order made under sub-section (9) shall be laid before each House of Parliament, as soon as may be, after the scheme has been sanctioned by the Central Government or, as the case may be, the order has been made.
11. Nothing in this section shall be deemed to prevent the amalgamation with an insurer by a single scheme of several insurers.
12. The provisions of this section and of any scheme made under it shall have effect notwithstanding anything to the contrary contained in any other provisions of this Act or in any other law or any agreement, award or other instrument for the time being in force.
13. The provisions of section 37 shall not apply to an amalgamation given effect to under provisions of this section.

Approvals from Telecom Regulatory Authority of India (TRAI)

The Department of Telecommunications, Govt. of India vide its circular No. 20-281/2010-AS-I (Volume-VII) dated 20th February, 2014 issued 'Guidelines for Transfer/ Merger of various categories of Telecommunication service licenses / authorisation under Unified Licence (UL) on compromise, arrangements and amalgamation of the companies'. The details of these guidelines are mentioned in *Annexure*.

Production Linked Incentive (PLI) scheme for Promoting Telecom & Networking Products Manufacturing in India

With the objective to boost domestic manufacturing, investments and export in the telecom and networking products Department of Telecommunications (DoT) notified the "Production Linked Incentive (PLI) Scheme" on 24th February 2021.The PLI Scheme will be implemented within the overall financial limits of Rs. 12,195 Crores only (Rupees Twelve Thousand One Hundred and Ninety-Five Crore only) for implementation of the Scheme over a period of 5 years. For MSME category, financial allocation will be Rs. 1000 Crores. Small Industries Development Bank of India (SIDBI) has been appointed as the Project Management Agency (PMA) for the PLI scheme.The scheme will be effective from 1st April, 2021. Investment made by successful applicants in India from 1 st April, 2021 onwards and up to Financial Year (FY) 2024-2025 shall be eligible, subject to qualifying incremental annual thresholds. The support under the Scheme shall be provided for a period of five (5) years, i.e. from FY 2021-22 to FY 2025-26.

Annexure

Merger and Acquisition Guidelines 2014 by the Department of Telecommunications, Govt. of India

Government of India

Ministry of Communications and Information Technology Department of Telecommunications

Sanchar Bhawan, 20 Ashok road, New Delhi (AS-I Division)

No. 20-281/2010-AS-I(Volume –VII) 20th February, 2014

Subject: Guidelines for Transfer / Merger of various categories of Telecommunication service licenses / authorisation under Unified Licence (UL) on compromises, arrangements and amalgamation of the companies.

1. National Telecom Policy-2012 envisages one of the strategy for the telecom sector to put in place simplified Merger & Acquisition regime in telecom service sector while ensuring adequate competition. This sector has been further liberalised by allowing 100% FDI. Further, it has been decided in principle to allow trading of spectrum. The Companies Act, of 1956 has also been amended by Companies Act of 2013 and the amendments have been made in reference to compromise / arrangements and amalgamations of companies. SEBI has also prescribed procedure for IPO.

2. The Scheme of compromise, arrangements and amalgamation of companies is governed by the various provisions of the Companies Act, 2013 as amended from time to time. Such scheme is to be approved by National Company Law Tribunal to be constituted under the provisions of Companies Act, 2013. Consequently, the various licences granted under section 4 of the Indian Telegraph Act, 1885 to such companies need to be transferred to the resultant entity (ies). It is also noted that such schemes may comprise of merger by formation or merger by absorption or arrangements or amalgamation etc. of company (ies) and thereafter merging/transferring such licences / authorisation subject to the condition that the resultant entity being eligible to acquire such licence /authorisation in terms of extant guidelines issued from time to time.

3. Earlier department has issued Guidelines for intra service area Merger of Cellular Mobile Telephone Service (CMTS) / Unified Access Services (UAS) Licences vide Office Memo No. 20-232/2004-BS-III dated 22nd April, 2008. Taking into consideration the TRAI's Recommendations dated 11.05.2010 and 03.11.2011 and National Telecom Policy 2012, in supersession of these guidelines, it has been further decided that Transfer / Merger of various categories of Telecom Services Licences/ authorisation under UL shall be permitted as per the guidelines mentioned below for proper conduct of Telegraphs and Telecommunication services, thereby serving the public interest in general interest in particular:-

   (a) The licensor shall be notified for any proposal for compromise arrangements and amalgamation of companies as filed before the Tribunal or the Company Judge. Further, representation / objection, if any, by the Licensor on such scheme has to be made and informed to all concerned within 30 days of receipt of such notice.

   (b) A time period of one year will be allowed for transfer/ merger of various licences in different service areas in such cases subsequent to the appropriate approval of such scheme by the Tribunal /Company Judge.

   (c) If a licensee participates in an auction and is consequently subject to a lock-in condition, then if such a licensee propose to merger/ compromise/ arrange/amalgamate into another licensee as the provisions of applicable Companies Act, the lock-in period would apply in respect of new shares which would be issued in respect of the resultants company (transferee Company). The substantial Equity/ Cross Holding clause shall not be applicable during this period of one year unless extended otherwise. This period can be extended by the Licensor by recording reasons in writing.

   (d) The merger of licensee/ authorisation shall be for respective service category. As access service license/ authorisation allows provision of internet services, the merger of ISP license/ authorisation shall also be permitted.

(e) Consequent to transfer of assets/ licences/ authorisation held by transferor (acquired) company to the transferee (acquiring) company, the licences / authorisation of transferor (acquired) company will be subsumed in the re sultant entity. Consequently, the date of validity of various licences / authorisation shall be as per licenses/ authorisation and will be equal to the higher of the two period on the date of merger subject to prorate payments, if any, for the extended period of the licence / authorisation for that service. However, the validity period of the spectrum shall remain unchanged subsequent to such transfer of asset/ licences/authorisation held by the transferor (acquired) company.

(f) For any additional service orany licence area/ service area, Unified Licence with respective authorisation is to be obtained.

(g) Taking into consideration the spectrum cap of 50% in a band for access services, transfer/ merger of licences consequent to compromise, arrangements or amalgamation of companies shall be allowed where market share for access services area of the resultant entity is upto 50%. In case the merger or acquisition or amalgamation proposals results in market share in any service area(s) exceeding 50%, the resultant entity should reduce its market share to the limit of 50% within a period of one year from the date of approval of merger or acquisition or amalgamation by the competent authority. If the resultant entity fails to reduce its market share to the limit of 50% within the specified period of one year, then suitable action shall be initiated by the licensor.

(h) For determining the aforesaid market share, market share of both subscriber base and Adjusted Gross Revenue (AGR) of licensee in the relevant market shall be considered. The entire access market will be relevant market for determining the market share which will included wire line as well as wireless subscribers. Exchange Data Records (EDR) shall be used in the calculation of wire line subscribers and Visitor Location Register (VLR) data of equivalent, in the calculation of wireless subscribers for the purpose of computing market share based on subscriber base. The reference date for taking into account EDR/ VLR data of equivalent shall be 31st December or 30th June of each year depending on the date of application. The duly audited AGR shall be the basis of computing revenue based market share for operators in the relevant market. The date for duly audited AGR would be 31st March of the preceding year.

(i) If a transferor (acquired) company holds a part of spectrum, which (4.4 MHz/2.5 MHz) has been assigned against the entry fee paid, the transferee (acquiring) company (i.e. resultant merged entity), at the time of merger, shall pay to the Government, the differential between the entry fee and the market determined price of spectrum from the date of approval of such arrangements by the National Company Law Tribunal / Company Judge on a pro-rate basis for the remaining period of the license(s). No separate charge shall be levied for spectrum acquired through auctions conducted from year2010 onwards. Since auction determined price of the spect rum is valid for a period of one year, thereafter, PLR at State Bank of India rates shall be added to the last auction determined price to arrive at market determined price after a period of one year. In the event of judicial intervention in respect of the spectrum holding beyond 4.4 MHz in GSM band / 2.5. MHz in CDMA band before merger in respect of transferee (i.e. acquiring entity) company, a bank guarantee for an amount equal to the demand raised by the department for one time spectrum charge shall be submitted pending final outcome of the court case.

(j) The Spectrum Usage Charge (SUC) as prescribed by the Government from time to time, on the total spectrum holding of the resultant entity shall also be payable.

(k) Consequent upon the implementation of scheme of compromises, arrangements or amalgamations and merger of licenses in a service area there upon, the total spectrum held by the Resultant entity shall not exceed 25% of the total spectrum assigned for access services and 50% of the spectrum assigned in a given band, by way of auction or otherwise, in the concerned service area. The bands will be as counted for such cap in respective NIAs for auction of spectrum. In respect of 800 MHz band, the ceiling will be 10 MHz. Moreover, the relevant conditions pertaining to auction of that spectrum shall apply. In case of future auctions, the relevant conditions prescribed for such auction shall be applicable. However, in case transferor and transferee company had been allocated one block of 3G spectrum through the auction conducted for 3G/ BWA spectrum in 2010, the resultant entity shall also be allowed to retain two blocks of 3G spectrum in respective service areas as a result of compromise, arrangements and amalgamation of the companies and Transfer / Merger of various categories of Telecommunication service licences / authorisation under Unified License (UL), being within 50% of spectrum band cap.

(l) If, as a result of merger, the total spectrum held by the relevant entity is beyond the limits prescribed, the excess spectrum must be surrendered within one year of the permission being granted. The applicable Spectrum Usage Charges on the total spectrum holding of the resultant entity shall be levied for such period. If the spectrum beyond prescribed limit is not surrendered by the merged entity within one year, then, separate action in such cases, under the respective licenses/ statutory provisions, may be taken by the Government for non surrender of the excess spectrum. However, no refund or set off of money paid and / or payable for excess spectrum will be made.

(m) All demands, if any, relating to the licences of merging entities, will have to be cleared by either of the two licensees before issue of the permission for merger/ transfer of licenses/ authorisation. This shall be as per demand raised by the Government / licensor based on the returns filed by the company notwithstanding any pending legal cases or disputes. An undertaking shall be submitted by the resultant entity to the effect that any demand raised for pre-merger period or transferor or transferee company shall be paid. However, the demand except for one time spectrum charges of transferor and transferee company, stayed by the Court of Law shall be subject to outcome of decision of such litigation. The one time spectrum charge shall be payable as per provisions in para 3(i) above of these guidelines.

(n) If consequent to transfer / merger of licenses in a service area, the Resultant entity becomes a 'Significant Market Power' (SMP), then the extant rules & regulations applicable to SMPs would also apply to the Resultant entity. SMP in respect of access services is as defined in TRAI's 'The Telecommunications Interconnect (Reference Interconnect Offer) Regulations, 2002 (2 of 2002)' as amended from time to time.

4. The dispute resolution shall lie with Telecom Dispute Settlement and Appellate Tribunal as per TRAI Act, 1997 as amended from time to time.

5. LICENSOR reserves the right to modify these guidelines or incorporate new guidelines considered necessary in the interest of national security, public interest and for proper conduct of telegraphs.

LESSON ROUND-UP

- Merger or amalgamation of companies involves various issues and compliance not even of the Companies Act, 2013, but from the Regulators also depending upon the nature of business of the company and sector under which it is operating. These may include SEBI, RBI, CCI, Stock Exchanges, IRDAI, TRAI, etc.
- Section 5 of the Competition Act 2002 deals with the Combination and section 6 with the Regulation of combinations. The Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011 prescribes the procedure and relevant forms for taking approvals in case of such combinations.
- To encourage restructuring, merger and demerger, it has been given a special treatment in the Income-Tax Act, 1961 since the beginning. The Finance Act, 1999 clarified many issues relating to Business Reorganizations thereby facilitating and making business restructuring tax neutral. Section 47 of the Income Tax Act, 1961 deals with the transactions which are not regarded as transfer.

- The unlisted companies are to follow the provisions of the Companies Act, 2013. Whereas a listed company has to comply with the guidelines contained in the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 in addition to the Companies Act, 2013.
- Regulatory approval of the RBI is required for the merger /amalgamation of the Banking companies. The Master Direction on amalgamation of Private Sector Banks, Directions, 2016 issued by the RBI vide its Circular No. RBI/DBR/2015-16/22 Master Direction DBR. PSBD. No. 96/16.13.100/2015- 16, dated April 21, 2016 provides the detailed issues relating to the amalgamation of Private Sector Banks. The provisions of these Directions shall apply to all private sector banks licensed to operate in India by the RBI and to the Non-Banking Financial Companies (NBFC) registered with the RBI. The principles underlying these Directions would be applicable, as appropriate, to public sector banks.
- Similarly the merger and amalgamation of the insurance companies requires the regulatory approvals from the IRDA and the telecom companies require approval from TRAI.

TEST YOURSELF

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. In the matter of merger/ takeover of the listed companies, they are required to comply with the provisions of the Companies Act as well as of SEBI Regulations. List out relevant provisions of the Companies Act and the SEBI Regulations in this respect.
2. Mention the merger and acquisition cases in which approval from the CCI is required. Discuss the relevant provisions of the Competition Act, 2002.
3. Describe in detail the regulatory requirements in case of merger/ takeover of insurance companies.
4. Write down the procedure to be followed in brief for the amalgamation of private sector banks.
5. The Department of Telecommunications and TRAI has issued detailed guidelines relating to the merger/ takeover of Telecom companies. Discuss the same in brief.

LIST OF FURTHER READINGS

- Hand book on Mergers and Amalgamation and Takeovers- ICSI Publication
- Mergers/ Amalgamation, Takeovers, Joint ventures, LLP and Corporate Restructure: Snow White Publication
- www.rbi.org
- www.cci.gov.in
- www.irdai.gov.in
- www.trai.gov.in
- www.mca.gov.in
- www.nclt.gov.in

Fast Track Mergers

Lesson 10

KEY CONCEPTS

■ Small Company ■ Fast Track Merger ■ Appointed Date ■ Start up

Learning Objectives

To understand:

- Fast Track Mergers
- Basic Concepts around Fast Track Mergers
- Provisions of Companies Act, 2013 for Merger & Amalgamation
- Procedural Aspect of fast track mergers
- Post-Merger Effect

Lesson Outline

- Introduction
- Legal regime behind fast track mergers
- Small company
- Procedural aspects of fast track mergers
- Steps involved in fast track mergers
- Post-merger effect
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

- The Companies Act, 2013
- The Companies (Compromises, Arrangements and Amalgamations) Rules 2016
- The National Company Law Tribunal Rules, 2016

INTRODUCTION

Mergers and Amalgamations (M&As) have become the buzz words in corporate echelons these days. It is the process of amalgamation of two or more entities / companies through inorganic means.

There may be different means and modes to affect this process. As a result of this process, a new entity may be formed or one entity may be subsumed by another. All the assets and liabilities of the amalgamating or the merging entity will transfer to the resultant entity.

Companies Act, 1956 did not provide a simple procedure for mergers and amalgamations of certain type of companies. It prescribed a cumbersome and time-consuming process for all companies irrespective of their size, net worth and turnover. The legal provisions pertaining to merger process were stipulated in sections 391-394 of the Companies Act, 1956. This procedure was perceived to be very confusing, complex and time-taking by all stakeholders involved in the process. The process involved, *inter alia,* drafting a merger scheme, taking judicial approval for the scheme, getting Board and shareholders authorisation, etc. It defeated the very purpose for which mergers were entered into and proved to be a deterrent for companies looking for collaborations, rather than a facilitator.

Small companies with fewer resources were also subject to same complex procedure. This was proving to be an obstacle in the way of their growth and expansion. Having the same procedure for merger for all companies was proving to be counter-productive. The complexities of the earlier regime gave rise to the need for a simplified procedure and a more efficient legal regime for merger process. This need was embedded in the following benefits which a fast track merger offered under Section 233 of the Companies Act, 2013:

- Simplified procedure for merger
- No judicial approval required
- Separate procedures for certain type of companies would enable them to expand without any roadblocks
- Form filings required also significantly reduced.

The Companies Act, 2013 replaced the earlier tedious process with a new concept called the 'fast track mergers'. Fast track mergers have dispensed with Tribunal approval for mergers. Regional Directors, Registrar of Companies (RoC) and Official Liquidator are the authorities whose approval is required. The process has been simplified to a great extent.

However, it is to be noted that this process is applicable only to merger between small companies and holding and subsidiary companies.

A provision allowing the government to notify any other company in this regard has also been made. Before we set out to analyse and understand fast track mergers, it is pertinent to understand the legal framework behind fast track mergers and what is meant by small companies.

Legal Regime behind Fast Track Mergers

Section 233 of the Companies Act, 2013 has introduced the concept of fast track mergers. It carved out an exception from the regular merger procedure. It exempted small companies and holding and subsidiary companies entering into merger arrangements from the regular merger procedure as stipulated under sections 230-232 of the Companies Act, 2013. Section 233 of the Companies Act, 2013 along with Rule 25 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 lay down the entire legal framework of fast track mergers.

MERGER OR AMALGAMATION OF CERTAIN COMPANIES – SECTION 233

1. Notwithstanding the provisions of section 230 and section 232, a scheme of merger or amalgamation may be entered into between two or more small companies or between a holding company and its wholly-owned subsidiary company or such other class or classes of companies as may be prescribed, subject to the following, namely: —

   (a) a notice of the proposed scheme inviting objections or suggestions, if any, from the Registrar and Official Liquidators where registered office of the respective companies are situated or persons affected by the scheme within thirty days is issued by the transferor company or companies and the transferee company;

   (b) the objections and suggestions received are considered by the companies in their respective general meetings and the scheme is approved by the respective members or class of members at a general meeting holding at least ninety per cent. of the total number of shares;

   (c) each of the companies involved in the merger files a declaration of solvency, in the prescribed form, with the Registrar of the place where the registered office of the company is situated; and

   (d) the scheme is approved by majority representing nine-tenth sin value of the creditors or class of creditors of respective companies indicated in a meeting convened by the company by giving a notice of twenty- one days along with the scheme to its creditors for the purpose or otherwise approved in writing.

2. The transferee company shall file a copy of the scheme so approved in the manner as may be prescribed, with the Central Government, Registrar and the Official Liquidator where the registered office of the company is situated.

3. On the receipt of the scheme, if the Registrar or the Official Liquidator has no objections or suggestions to the scheme, the Central Government shall register the same and issue a confirmation thereof to the companies.

4. If the Registrar or Official Liquidator has any objections or suggestions, he may communicate the same in writing to the Central Government within a period of thirty days:

   Provided that if no such communication is made, it shall be presumed that he has no objection to the scheme.

5. If the Central Government after receiving the objections or suggestions or for any reason is of the opinion that such a scheme is not in public interest or in the interest of the creditors, it may file an application before the Tribunal within a period of sixty days of the receipt of the scheme under subsection (2) stating its objections and requesting that the Tribunal may consider the scheme under section 232.

6. On receipt of an application from the Central Government or from any person, if the Tribunal, for reasons to be recorded in writing, is of the opinion that the scheme should be considered as per the procedure laid down in section 232, the Tribunal may direct accordingly or it may confirm the scheme by passing such order as it deems fit: Provided that if the Central Government does not have any objection to the scheme or it does not file any application under this section before the Tribunal, it shall be deemed that it has no objection to the scheme.

7. A copy of the order under sub-section (6) confirming the scheme shall be communicated to the Registrar having jurisdiction over the transferee company and the persons concerned and the Registrar shall register the scheme and issue a confirmation thereof to the companies and such confirmation shall be communicated to the Registrars where transferor company or companies were situated.

8. The registration of the scheme under sub-section (3) or sub-section (7) shall be deemed to have the effect of dissolution of the transferor company without process of winding-up.
9. The registration of the scheme shall have the following effects, namely: —
   (a) transfer of property or liabilities of the transferor company to the transferee company so that the property becomes the property of the transferee company and the liabilities become the liabilities of the transferee company
   (b) the charges, if any, on the property of the transferor company shall be applicable and enforceable as if the charges were on the property of the transferee company;
   (c) legal proceedings by or against the transferor company pending before any court of law shall be continued by or against the transferee company; and (d) where the scheme provides for purchase of shares held by the dissenting shareholders or settlement of debt due to dissenting creditors, such amount, to the extent it is unpaid, shall become the liability of the transferee company.
10. A transferee company shall not on merger or amalgamation, hold any shares in its own name or in the name of any trust either on its behalf or on behalf of any of its subsidiary or associate company and all such shares shall be cancelled or extinguished on the merger or amalgamation.
11. The transferee company shall file an application with the Registrar along with the scheme registered, indicating the revised authorised capital and pay the prescribed fees due on revised capital: Provided that the fee, if any, paid by the transferor company on its authorised capital prior to its merger or amalgamation with the transferee company shall be set-off against the fees payable by the transferee company on its authorised capital enhanced by the merger or amalgamation.
12. The provisions of this section shall mutatis mutandis apply to a company or companies specified in sub-section (1) in respect of a scheme of compromise or arrangement referred to in section 230 or division or transfer of a company referred to clause (b) of subsection (1) of section 232.
13. The Central Government may provide for the merger or amalgamation of companies in such manner as may be prescribed.
14. A company covered under this section may use the provisions of section 232 for the approval of any scheme for merger or amalgamation.

Therefore, as it can be seen, section 233 outlines a list of conditions which companies proposing to enter into fast track mergers are required to follow:

- A notice of the proposed scheme soliciting objections or suggestions from the Registrar and the official liquidators to be issued by the transferor or the transferee companies within thirty (30) days.
- If any objections or suggestions are received, then the same are considered in their respective general meetings and approved/disapproved by their respective members.
- A declaration of solvency is required to be filed by both the companies involved in the merger.
- The scheme has to be approved by majority of creditors representing nine-tenths in value of the creditors or class of creditors of the respective companies.
- The transferee company is required to file a copy of the approval in the prescribed manner, with the Central Government, Registrar and the Official Liquidator where the registered office of the company is situated.
- On receiving the said scheme, if the Registrar or the Official Liquidator does not have any objections or suggestions to the scheme, the Central Government shall register the said scheme and issue a confirmation thereof to the companies.
- If the Registrar or Official Liquidator has any objections or suggestions, the same may be communicated to the Central government within a period of thirty days. In the absence of any such communication, it would be presumed that no objections were raised.

- If the Central Government after receiving the objections or suggestions or for any other reason forms the opinion that the said scheme is not in public interest or in the interest of the creditors, it can file an application before the Tribunal within a period of sixty days.
- After filing of such application, the Tribunal has to render its judgment. If it is of the opinion (with reasons recorded in writing) that the scheme should be considered as per the procedure laid down in section 232, it may give directions accordingly.

RELEVANT PROVISIONS FOR MERGER & AMALGAMATION

Under Companies Act, 2013, the provisions of section 230 provide the additional disclosure if the proposed scheme involves; Reduction of Share Capital or the scheme is of Corporate Debt restructuring; consented by not less than 75% in value of secured creditors, every notice of meeting about scheme to disclose valuation report explaining effect on various shareholders.

Further, no compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company's auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the Accounting Standards prescribed under section 133 of the Companies Act, 2013. Apart from this, dealing with the Arrangements; notice of meeting to consider compromise or arrangement to be given to Central Government, Income Tax Authorities, Reserve Bank of India, Securities Exchange Board of India, Registrar of Companies, respective Stock Exchange, Official Liquidator, Competition Commission of India and other Authorities likely to be affected by the same. So, these Authorities can voice their concern within 30 days of receipt of notice, failing which it will be presumed that they have no objection to the scheme.

Following are the benefits of section 233 or fast track mergers:

- No requirement to apply to the National Company Law Tribunal
- No requirement to get a special audit conducted for the transferor company
- No requirement to issue public advertisements announcing the merger
- Less cost intensive and less time consuming.

Rule 25 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 reads as under:

1. The notice of the proposed scheme, under clause (a) of sub-section (1) of section 233 of the Act, to invite objections or suggestions from the Registrar and Official Liquidator or persons affected by the scheme shall be in Form No. CAA.9.
2. For the purposes of clause (c) of sub-section (1) of section 233 of the Act the declaration of solvency shall be filed by each of the companies involved in the scheme of merger or amalgamation in Form No. CAA.10 along with the fee as provided in the Companies (Registration Offices and Fees) Rules, 2014, before convening the meeting of members and creditors for approval of the scheme.
3. For the purposes of clause (b) and (d) of sub-section (1) of section 233 of the Act, the notice of the meeting to the members and creditors shall be accompanied by –

   (a) a statement, as far as applicable,referred to in sub-section (3) of section 230 of the Act read with sub- rule (3) of rule 6 thereof;

   (b) the declaration of solvency made in pursuance of clause (c) of sub-section (1) of section 233 of the Act in Form No. CAA.10;

   (c) a copy of the scheme.
4. (a) For the purposes of sub-section (2) of section 233 of the Act, the transferee company shall, within seven days after the conclusion of the meeting of members or class of members or creditors or class of creditors, file a copy of the scheme as agreed to by the members and creditors, along with a report of the result of each of the meetings in Form No. CAA.11 with

the Central Government, along with the fees as provided under the Companies (Registration Offices and Fees) Rules, 2014.

(b) Copy of the scheme shall also be filed, along with Form No. CAA. 11 with –

(i) the Registrar of Companies in Form No. GNL-1 along with fees provided under the Companies (Registration Offices and Fees) Rules, 2014; and

(ii) the Official Liquidator through hand delivery or by registered post or speed post.

5. Where no objection or suggestion is received within a period of thirty days of receipt of copy of scheme under sub-section (2) of section 233, from the Registrar of Companies and Official Liquidator by the Central Government and the Central Government is of the opinion that the scheme is in the public interest or in the interest of creditors, it may, within a period of fifteen days after the expiry of said thirty days, issue a confirmation order of such scheme of merger or amalgamation in **Form No. CAA.12**:

Provided that if the Central Government does not issue the confirmation order within a period of sixty days of the receipt of the scheme under sub-section (2) of section 233, it shall be deemed that it has no objection to the scheme and a confirmation order shall be issued accordingly.

6. Where objections or suggestions are received within a period of thirty days of receipt of copy of scheme under sub-section (2) of section 233 from the Registrar of Companies or Official Liquidator or both by the Central Government and –

(a) such objections or suggestions of Registrar of Companies or Official Liquidator, are not sustainable and the Central Government is of the opinion that the scheme is in the public interest or in the interest of creditors, it may within a period of thirty days after expiry of thirty days referred to above, issue a confirmation order of such scheme of merger or amalgamation in **Form No. CAA.12**.

(b) the Central Government is of the opinion, whether on the basis of such objections or otherwise, that the scheme is not in the public interest or in the interest of creditors, it may within sixty days of the receipt of the scheme file an application before the Tribunal in **Form No. CAA.13** stating the objections or opinion and requesting that Tribunal may consider the scheme under section 232 of the Act:

Provided that if the Central Government does not issue a confirmation order under clause (a) or does not file any application under clause (b) within a period of sixty days of the receipt of the scheme under subsection (2) of section 233 of the Act, it shall be deemed that it has no objection to the scheme and a confirmation order shall be issued accordingly.

7. The confirmation order of the scheme issued by the Central Government or Tribunal under sub-section (7) of section 233 of the Act, shall be filed, within thirty days of the receipt of the order of confirmation, in Form INC-28 along with the fees as provided under Companies (Registration Offices and Fees) Rules, 2014 with the Registrar of Companies having jurisdiction over the transferee and transferor companies respectively.

8. For the purpose of this rule, it is clarified that with respect to schemes of arrangement or compromise falling within the purview of section 233 of the Act, the concerned companies may, at their discretion, opt to undertake such schemes under sections 230 to 232 of the Act, including where the condition prescribed in clause (d) of sub-section (1) of section 233 of the Act has not been met.

9. As per Rule 25(1)(1A) of the Companies (Compromises, Arrangements and Amalgamations) Amendment Rules, 2021 :

A scheme of merger or amalgamation under section 233 of the Act may be entered into between any of the following class of companies, namely:-

(i) two or more start-up companies; or

(ii) one or more start-up company with one or more small company.

Explanation.- For the purposes of this sub-rule, “start-up company” means a private company incorporated under the Companies Act, 2013 or Companies Act, 1956 and recognized as such in accordance with notification number G.S.R. 127 (E), dated the 19th February, 2019 issued by the Department for Promotion of Industry and Internal Trade.

Small Company

The Companies Act, 2013 introduced the concept of small company. This new category of company was introduced in order to provide certain advantages to businesses operating with a small capital and scale.

In the wake of the rising start-up culture in India, it was imperative that certain benefits be given to small enterprises and businesses allowing them to grow organically or inorganically. Such small companies form the backbone of an economy and encourage entrepreneurship and, therefore, lesser stringent legal procedures pertaining to mergers and acquisitions would act as an incentive encouraging more people to start such businesses.

"Small Company" under section 2(85) of the Companies Act, 2013 is defined as:

"Small company'' means a company, other than a public company, -

(i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees; and

(ii) turnover of which as per profit and loss account for the immediately preceding financial year does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than one hundred crore rupees:

Provided that nothing in this clause shall apply to,

(a) a holding company or a subsidiary company;

(b) a company registered under section 8; or

(c) a company or body corporate governed by any special Act; There are various advantages of being a small company. Some of these are:

- **Filing Annual Return**

  The procedure of filing annual returns of a small company is comparatively easier than that of other private limited companies. The annual return of a small company can be signed by either its company secretary or its director, whereas an annual return of a private limited company other than a small company has to be necessarily signed by both the company secretary and the director.

- **Board Meeting**

  Small companies are required to conduct only 2 board meetings in a year whereas private limited companies not classified as small companies have to conduct four board meetings in a year.

- **Cash Flow Statement**

  A small company is not required to prepare a cash flow statement as a part of its financial statement unlike other private limited companies.

- **Rotation of Auditors**

  A small company is not required to rotate its auditors unlike other private limited companies who are required to rotate their auditors every 5 or 10 years.

Procedural Aspects of Fast Track Mergers

Section 233 of the Companies Act, 2013 along with the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 lay down the procedure for fast track mergers. The table given below explain the process, forms required and the stipulated timelines involved in a fast track merger:

Procedure	Timeline	Forms required	Who shall be required to comply
Convene a Board Meeting: The board meeting shall approve the scheme and pass resolutions for holding and fixing date and time for a shareholder and a creditors meeting.	NA	NA	Both the transferor and the transferee companies are required to comply.
Notice of the Proposed Scheme: The notice of the proposed scheme is to be sent to the Registrar where registered offices of both the companies are situated. The notice shall invite objections/ suggestions, if any, from the respective registrars.	To be done after the Board meeting.	Form CAA 9	Both the transferor and the transferee companies are required to comply.
Declaration of solvency: Both the companies are required to file a declaration solvency with the ROC of the place where their registered offices are situated.	This is to be done before the meeting of shareholders or the meeting of creditors is convened.	Form CAA 10	Both the transferor and the transferee companies are required to comply.
Convening a Meeting of Members: A notice convening a meeting of the members or shareholders of the company should be sent to all the members. This notice should contain, the details of the merger, copy of the scheme and a copy of the declaration of solvency. The objections/ suggestions received by the company from the registrar would be discussed and voted upon in this meeting.	Notice should be sent 21 days prior to the meeting.	NA	Both the transferor and the transferee companies are required to comply.
Filing of the Scheme: A copy of the scheme along with the results of all the meetings shall be filed with the regional director. A copy of the scheme along with Form CAA 11 is also required to be formed with the ROC and the Official Liquidator. The former shall be filed in Form GNL1 and the latter shall be hand-delivered or sent through speed post or registered post.	Within 7 days of the meeting.	Form CAA 11. Form GNL 1	Only transferee of company is required to comply.

Approval of the Scheme by Regional Director: If the ROC or the Official Liquidator approves the scheme then the regional director shall register the same and issue a confirmation. If the ROC or Official Liquidator have objections then they may communicate the same to the Regional Director. The Regional Director, if is of the opinion that the scheme is not in public interest then it may file an application in Form CAA 12 before the Tribunal, to consider the scheme under section 232 (regular merger process).	NA	NA	NA
Filing the confirmation order with the ROC: A copy of the confirmation of the scheme approved by the Official Liquidator should be sent to the Registrar where the transferee's registered office is situated. The registrar shall register the scheme and issue a confirmation which shall then be filed with ROC of the place where the transferor's registered office is situated.	Within 30 days of Form the receipt of the 28 confirmation of the ROC or Scheme.	NA	Both the transferor and the transferee companies are required to comply.

Steps involved in Fast Track Mergers

The following steps need to be followed in a fast track merger:

1. First of all, both the companies need to check their Articles of Association (AoA) and assess if they have the requisite authority under them to enter into a merger. If no, then the AoA need to be amended before such merger can take place.
2. Convene the Board Meeting and prepare a draft scheme of merger or amalgamation.
3. Prepare a financial statement of assets and liabilities and get an auditor's report prepared.
4. Get the draft scheme approved in the Board Meeting.
5. Both the companies need to send a notice to the Registrar of Companies (RoC) and Official Liquidator (OL) of their respective regions inviting suggestions/objections to the scheme, if any within 30 days of issuing the notice.
6. Such notice to the RoC should be in Form CAA 9 and have the following attachments:
   - Copy of the scheme
   - Shareholding pattern of the transferee pre and post-merger

- Last 3 years audited financial statements
- Memorandum and Articles of Association
- Board Resolution
- Valuation Report.

7. Both the companies are required to file a declaration of solvency with their respective ROCs. This declaration of solvency shall be accompanied by the following:
   - Board Resolution
   - Statement of Assets and Liabilities
   - Auditors Report.
8. Sending notice of shareholders' meeting and creditors' meeting.
9. Conducting the shareholders' meeting and getting the scheme approved.
10. Conducting creditors' meeting and getting the scheme approved.
11. Filing of the results of each meeting with the Regional Director and the Official Liquidator by the transferee company.
12. Objections/Suggestions to be sent to the Regional Director by the RoC / Official Liquidator.
13. Regional director may file an application with the Tribunal if he is of the opinion that the scheme is against public interest.
14. The Tribunal can approve or disapprove the scheme.
15. If approved it shall be filed with the RoC of the transferee company and the transferor company respectively.

So far, we have discussed the procedure as mandated by law and the steps required to enter into a fast track merger. However, from a practical standpoint, it is also imperative to know what are the ingredients / contents one should include in a scheme of merger. These ingredients are:

- Preamble
- Definitions of the terms used in the scheme
- A detailing of the pre-merger and the post-merger capital
- The way the assets and liabilities shall be transferred
- Appointed and effective date of the scheme
- Tax treatment of the scheme
- Benefits to be given to the staff
- Consolidation of the authorised share capital
- Dissolution without resorting to winding-up
- Notice of approval of the scheme
- Any amendments or modifications to the scheme.

Post-Merger Effect

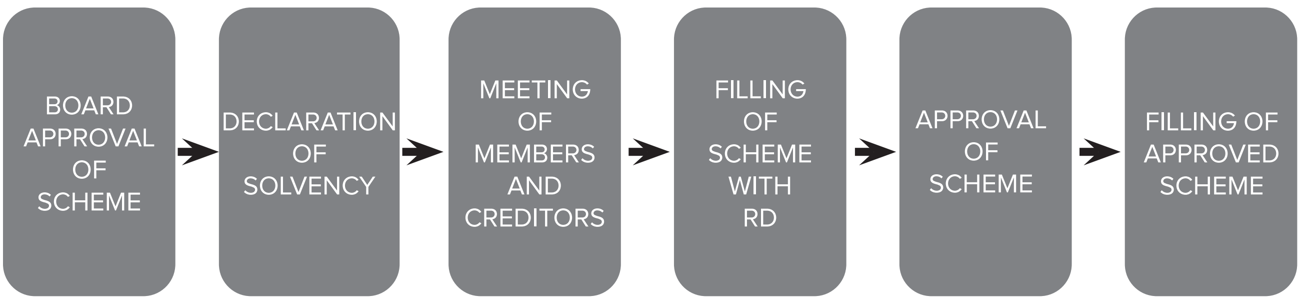
The following consequences shall result out of the merger:

- The transferor company shall stand dissolved on the registration of the scheme. No winding-up shall be required for the same.
- All the assets and liabilities of the transferor company shall be transferred to the transferee company.
- Any charge on the transferor's property shall stand transferred to the transferee.
- Payment of social security benefits of employees will now be the responsibility of the transferee company.

Despite, fast track mergers being an innovative and convenient concept it poses certain practical difficulties. These practical difficulties are:

- Merging the authorised capital of all companies in the transferee company may not be practically viable.
- Form INC 28 which finally registers the scheme does not provide for the following:
  - A separate drop-down menu for Section 233;
  - Change in the status of the transferor company.
- There is doubt regarding whether the Regional Director can suggest changes to the scheme. It appears that if the ROC, Official Liquidator does not have objections to the scheme, the Regional Director has to confirm without any suggestions of his own.

The following flowchart would help understand the procedure of fast track merger better:



Practical Insights

Knowing and learning the basic theoretic concepts around fast track mergers is important. However, one also must know how to use this theory in practice. Whenever asked to render a legal opinion on fast track mergers or if your firm is entering into one, keep in mind the following practical steps:

(a) Assess whether the merger is beneficial before entering into one.

(b) Conduct due diligence on the firm sought to be merged with.

(c) Remember both the companies need to be small companies for FTM to apply.

(d) Have a prescribed timeline and a strategy in place in order to avoid undue delay.

(e) Think of all the possible objections you may receive from ROC and already keep solutions ready so as to save time.

LESSON ROUND-UP

- Fast track mergers have been introduced in order to encourage small companies to grow and expand. Small companies should not be dissuaded from entering into mergers just because the process is long, tedious and complicated.
- Section 233 of the Companies Act, 2013 provides for a simplistic procedure without the requirement of Tribunal approval for mergers.
- Section 233 of the Companies Act, 2013 lays down the legal framework for fast track mergers.
- Fast track mergers are applicable only to small companies, holding and subsidiary companies and any other company as may be prescribed by the government.
- A small company is defined as a private limited company with paid-up capital less than INR 2 lakh or turnover less than INR 2 crore.

The following is the procedure for a fast track merger:

- Convening a board meeting for approval of the draft scheme of merger.
- Sending a notice of the proposed scheme inviting objections or suggestions from the Registrar and the Official Liquidator.
- Declaration of solvency by each party to the merger.
- Approving/disapproving/modifying the scheme in the general meeting of shareholders and the meeting of creditors.
- Filing of the result of each meeting with the ROC and regional directors.
- If the ROC/Official Liquidator has any objections the same may be sent to the regional director.
- If the regional director thinks that the scheme is opposed to public interest, he may file an application before the Tribunal.
- The Tribunal may approve or disapprove the scheme. If the former happens, the scheme shall be registered, if the latter happens the scheme will have to seek approval through the procedure mentioned in section 232 of the Companies Act, 2013.

GLOSSARY

Turnover: Section 2(91) of the Companies Act, 2013 describes turnover as: “the aggregate value of the realisation of amount made from the sale, supply or distribution of goods or on account of services rendered, or both, by the company during a financial

Private company: Section 2(68) of the Companies Act 2013 defines a private company as a company having a minimum paid-up share capital as may be prescribed, and which by its articles, —

(i) restricts the right to transfer its shares;

(ii) except in case of One Person Company, limits the number of its members to two hundred:

Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member.

Holding Company: Section 2(46) of the Companies Act, 2013 describes holding company as: “holding company in relation to one or more other companies, means a company of which such companies are subsidiary companies.” Explanation: For the purpose of this clause, the expression ‘company’ includes any body corporate.

Wholly owned subsidiaries (WOS): This is a company whose 100% shares are owned by its holding company.

Appointed Date: This is the date when the scheme comes into effect.

Effective Date: This is the date when the merger gets completed in all respects.

TEST YOURSELF

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. What is a fast-track merger? Why is it important to have legal framework around a fast track merger in India?
2. What is the procedure of a fast-track merger?
3. Critically analyse the concept of fast track merger in India.
4. Discuss salient features of Section 233 of the Companies Act, 2013.
5. Discuss in brief Rule 25 of Companies (Compromise, Arrangements and Amalgamations) Rules, 2016

LIST OF FURTHER READINGS

- A Ramaiya Guide to Companies Act, 18th Edition, Lexis Nexis
- Deepak Verma, "A study of Mergers and Acquisitions in India under Companies Act, 2013", UNI JOURNAL OF RESEARCH, Vol.2 (3), March (2015)
- Ms. M. Nirmala, "Corporate Restructuring and Companies Act, 2013: An Impact Analysis", International Journal of Management and Social Science Research Review, Vol.1, Issue.5, Nov – 2014.

Cross Border Mergers

Lesson 11

KEY CONCEPTS

■ Cross Border Mergers ■ Inbound Merger ■ Outbound Merger

Learning Objectives

To understand:

- Cross Border Mergers
- Benefits of Cross Border Mergers & Acquisitions
- Merger or Amalgamation of foreign company
- Taxation Aspect
- Cross Border Demergers

Lesson Outline

- Introduction
- Type of mergers – inbound and outbound
- Section 234 of Companies Act, 2013
- Drivers and returns behind cross border mergers.
- Valuation of cross border firm
- Regulatory, competition and taxation aspects
- Case Laws
- Post-merger performance evaluation
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

- Companies Act, 2013
- The Companies (Compromises, Arrangements and Amalgamations) Rules, 2016
- SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011
- Foreign Exchange Management (Cross Border Merger) Regulations, 2018
- Competition Act, 2002
- Insolvency and Bankruptcy Code, 2016
- Income Tax Act, 1961
- Foreign Exchange Management Act, 1999.

INTRODUCTION

A company in one country can be acquired by an entity (another company) from other countries. The local company can be private, public, or state-owned company. In the event ofthe merger or acquisition by foreign investors referred to as cross-border merger and acquisitions will result in the transfer of control and authority in operating the merged or acquired company. Assets and liabilities of the two companies from two different countries are combined into a new legal entity in terms of the merger, while in terms of acquisition, there is a transformation process of assets and liabilities of local company to foreign company (foreign investor), and automatically, the local company will be affiliated. Since the cross border M&As involve two countries, according to the applicable legal terminology, the state where the origin of the companies that make an acquisition (the acquiring company) in other countries refer to as the Home Country, while countries where the target company is situated refers to as the Host Country.

Benefits of Cross Border Mergers & Acquisitions

- Expansion of markets
- Geographic and industrial diversification
- Technology transfer
- Avoiding entry barriers
- Industry consolidation
- Tax planning and benefits
- Foreign exchange earnings
- Accelerating growth
- Utilisation of material and labour at lower costs
- Increased customers base
- Competitive advantage.

Challenges with Cross Border Mergers & Acquisitions

- Legal issues in different countries
- Accounting challenges

- Taxation aspects
- Technological differences
- Political landscape
- Strategic issues
- Overpayment in the deal
- Failure to integrate
- HR challenges.

Cross-border mergers and acquisitions have been rapidly ascending in quantum and value in recent years.

In the Indian context, a cross border merger refers to any merger, amalgamation or arrangement between an Indian company and foreign company in accordance with Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 notified under the Companies Act, 2013.

A cross border merger essentially helps in global expansion of companies. If India needs to be put on the global commercial map, it is imperative that a sound and stable legal framework pertaining to cross border mergers be devised. This is the rationale behind the introduction of section 234. The need for a cross border merger stems from the need for economic growth and achieving economies of scale.

Section 234 of the Companies Act, 2013 notified by the Ministry of Corporate Affairs provides the legal framework for cross border mergers in India. This has been brought into effect from 13th April, 2017, hence operationalising the concept of cross border merger.

The following laws, govern cross border mergers in India:

- Companies Act, 2013
- SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011
- Foreign Exchange Management (Cross Border Merger) Regulations, 2018
- Competition Act, 2002
- Insolvency and Bankruptcy Code, 2016
- Income Tax Act, 1961
- The Department for Promotion of Industry & Internal Trade (DPIIT)
- Transfer of Property Act, 1882
- Indian Stamp Act, 1899
- Foreign Exchange Management Act, 1999 (FEMA)
- IFRS 3 Business Combinations.

In this lesson we shall holistically examine cross border mergers and would discuss issues such as their valuation, taxation, inbound and outbound mergers, etc.

TYPES OF MERGERS

The most popular types of mergers are horizontal, vertical, market extension or marketing/technology related concentric, product extension, conglomerate, congeneric and reverse. Recently, the concept of inbound and outbound mergers was also introduced in the Companies Act, 2013 as part of Section 234 of the Act.

Inbound Merger

An Inbound merger is one where a foreign company merges with an Indian company resulting in an Indian company being formed. Following are the key regulations which need to be followed during an inbound merger:

Transfer of Securities

Typically, the resultant company of the cross-border merger can transfer any security including a foreign security to a person resident outside India in accordance with the provisions of Foreign Exchange Management (Mode of Payment and Reporting of Non-Debt Instrument) Regulations, 2019. However, where the foreign company is a joint venture/ wholly owned subsidiary of an Indian company, such foreign company is required to comply with the provisions of Foreign Exchange Management (Overseas Investment) Rules & Regulations, 2022.

Branch/Office outside India

An office/branch outside India of the foreign company shall be deemed to be the resultant company's office outside India for in accordance with the Foreign Exchange Management. In case of transfer of securities both Buyer as well as Target can use the service of a Tripartite whose job is to have Securities in the Books and doing all back-office operations (including valuation of the Securities).

Borrowings

The borrowings of the transferor company would become the borrowings of the resulting company. The Merger Regulations has provided a period of 2 years to comply with the requirements under the External Commercial Borrowings (ECB) regime. The end use restrictions are not applicable here. Cross Border Mergers require hedging of External Commercial Borrowings (ECB) as well. An External Commercial Borrowings (ECB) is an arrangement between Indian Buyer and Foreign Bank whereby Foreign Bank is funding to Indian Corporate via Foreign Currency Loan having specific amount, tenor. FEMA does permit hedging of loan taken from outside Bank in Indian Books.

Transfer of Assets

Assets acquired by the resulting company can be transferred in accordance with the Companies Act, 2013 or any regulations framed thereunder for this purpose. If any asset is not permitted to be acquired, the same shall be sold within two years from the date when the National Company Law Tribunal (NCLT) had given sanction. The proceeds of such sale shall be repatriated to India.

Opening of overseas bank accounts for resultant company

The resultant company is allowed to open a bank account in foreign currency in the overseas jurisdiction for a maximum period of 2 years in order to carry out transactions pertinent to the cross-border merger.

Outbound Mergers

An outbound merger is one where an Indian company merges with a foreign company resulting in a foreign company being formed. The following are the major rules governing an outbound merger:

Issue of Securities

The securities issued by a foreign company to the Indian entity, may be issued to both,persons resident in and outside India. For the securities being issued to persons resident in India, the acquisition should be compliant with the ODI Regulations. Securities in the resultant company may be acquired provided that the fair market value of such securities is within the limits prescribed under the Liberalized Remittance Scheme.

Branch Office

An office of the Indian company in India may be treated as the branch office of the resultant company in India in accordance with the Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016.

Other changes

a) The borrowings of the resulting company shall be repaid in accordance with the sanctioned scheme.

b) Assets which cannot be acquired or held by the resultant company should be sold within a period of two years from the date of the sanction of the scheme.

c) The resulting foreign company can now open a Special Non-Resident Rupee Account in terms of the FEMA (Deposit) Regulations, 2016 for a period of two years to facilitate the outbound merger.

Section 234 of Companies Act, 2013

Merger or amalgamation of company with foreign company. —

1. The provisions of this Chapter unless otherwise provided under any other law for the time being in force, shall apply *mutatis mutandis* to schemes of mergers and amalgamations between companies registered under this Act and companies incorporated in the jurisdictions of such countries as may be notified from time to time by the Central Government: Provided that the Central Government may make rules, in consultation with the Reserve Bank of India, in connection with mergers and amalgamations provided under this section.

2. Subject to the provisions of any other law for the time being in force, a foreign company, may with the prior approval of the Reserve Bank of India, merge into a company registered under this Act or vice versa and the terms and conditions of the scheme of merger may provide, among other things, for the payment of consideration to the shareholders of the merging company in cash, or in Depository Receipts, or partly in cash and partly in Depository Receipts, as the case may be, as per the scheme to be drawn up for the purpose.

Explanation. — For the purposes of sub-section (2), the expression — foreign company means any company or body corporate incorporated outside India whether having a place of business in India or not."

A cross border merger explained in simplistic terms is a merger of two companies which are located in different countries resulting in a third company. A cross border merger could involve an Indian company merging with a foreign company or *vice versa*.

If the resultant company being formed due to the merger is an Indian company, it is termed an inbound merger and if the resultant company is a foreign company, it is an outbound merger. Cross border mergers play a vital role in the commercial growth of the economy. Companies Act, 1956 also dealt with cross border mergers. Sections 391-394 of the Companies Act, 1956 laid down provisions with respect to cross border mergers. However, under the Companies Act, 1956, only inbound mergers were permitted.

The term `transferee company' defined under section 394(4)(b) of Companies Act, 1956 included only Indian companies and hence transfers were not allowed to be made to foreign companies. Companies Act, 2013 brought about a significant change in this position.

Section 234 of the Companies Act, 2013 which was notified in December, 2017 has made provisions for both inbound and outbound mergers. It enables the Central government in consultation with the RBI to make rules pertaining to cross border mergers. In pursuance of the same, the Foreign Exchange Management (Cross Border Merger) Regulations, 2018 (Merger Regulations 2018) have been notified and are effective from March 20, 2018, placed at ***Annexure A***.

Mergers which follow the Merger Regulations are deemed to be automatically approved by the RBI and do not require a separate approval. The Merger Regulations are a comprehensive set of rules which deal holistically with cross border mergers.

Cross border mergers are defined under the Merger Regulations as any merger, arrangement or amalgamation in accordance with the Companies (Compromises, Arrangements and Amalgamations) Rules 2016 ("Companies Amalgamation Rules") notified under the Companies Act, 2013.

A foreign company under the Merger Regulations means a company which is incorporated outside India. Similarly, an Indian company is one which is incorporated in India. Outbound investment is permitted only with companies incorporated in the countries mentioned in the Annexure-B of the Companies Amalgamation Rules.

The company which take over the assets and liabilities of the companies involved in the cross-border merger is called 'Resultant Company'. A Resultant Company may be either Indian or foreign.

Rule 25A of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016

Rule 25A of the Companies Amalgamation Rules reads as under:

"25A. Merger or amalgamation of a foreign company with a Company and vice versa.

1. A foreign company incorporated outside India may merge with an Indian company after obtaining prior approval of Reserve Bank of India and after complying with the provisions of sections 230 to 232 of the Act and these rules.

2. (a) A company may merge with a foreign company incorporated in any of the jurisdictions specified in *Annexure B* after obtaining prior approval of the Reserve Bank of India and after complying with provisions of sections 230 to 232 of the Act and these rules.

   (b) The transferee company shall ensure that valuation is conducted by valuers who are members of a recognised professional body in the jurisdiction of the transferee company and further that such valuation is in accordance with internationally accepted principles on accounting and valuation. A declaration to this effect shall be attached with the application made to Reserve Bank of India for obtaining its approval under clause (a) of this sub-rule.

3. The concerned company shall file an application before the Tribunal as per provisions of section 230 to section 232 of the Act and these rules after obtaining approvals specified in sub-rule (1) and sub-rule (2), as the case may be.

   Explanation 1. For the purposes of this rule the term "company" means a company as defined in clause (20) of section 2 of the Act and the term "foreign company" means a company or body corporate incorporated outside India whether having a place of business in India or not:

   Explanation 2. For the purposes of this rule, it is clarified that no amendment shall be made in this rule without consultation of the Reserve Bank of India.

(4) Notwithstanding anything contained in sub-rule (3), in case of a compromise or an arrangement or merger or demerger between an Indian company and a company or body corporate which has been incorporated in a country which shares land border with India, a declaration in Form No. CAA-16 shall be required at the stage of submission of application under section 230 of the Act.

Rule 25A of the Companies Amalgamation Rules provides for the following:

- A foreign company is defined as a company incorporated outside India. The Companies Amalgamation Rules permit foreign companies to merge with an Indian company subject to obtaining prior approval of Reserve Bank of India and after complying with the provisions of sections 230 to 232 of the Act and the Rules.
- The Companies Amalgamation Rules, 2016 also mandates that the valuation should be conducted by valuers who are members of a recognised professional body and in accordance with the internationally accepted principles.
- Additionally, the following would also need to be fulfilled:
  - Merger of an Indian company is permitted only with a foreign company, which is incorporated in specified jurisdictions.

- Burden is on the foreign company to ensure valuation is done by a valuer, who is a member of a recognized professional body in its jurisdiction and in accordance with internationally accepted principles on accounting and valuation;

Jurisdictions specified in clause (a) of sub-rule (2) of rule 25A [Annexure-B]

(i) Whose securities market regulator is a signatory to International Organization of Securities Commission's Multilateral Memorandum of Understanding (Appendix A Signatories) or a signatory to bilateral Memorandum of Understanding with SEBI, or

(ii) Whose central bank is a member of Bank for International Settlements (BIS), and

(iii) A jurisdiction, which is not identified in the public statement of Financial Action Task Force (FATF) as:

(a) a jurisdiction having a strategic Anti-Money Laundering or Combating the Financing of Terrorism deficiencies to which counter measures apply; or

(b) a jurisdiction that has not made sufficient progress in addressing the deficiencies or has not committed to an action plan developed with the Financial Action Task Force to address the deficiencies.

Drivers and returns of Cross Border Mergers

BENEFITS OF CROSS BORDER MERGERS	RISKS ASSOCATED WITH CROSS BORDER MERGERS
● DIVERSIFICATION	● TAX IMPLICATIONS
● COST EFFECTIVENESS	● REGULATORY LANDSCAPE
● TECHNOLOGICAL ADVANCEMENT	● POLITICAL SCENARIO
● EFFICIENT DISTRIBUTION	

The trend of cross border mergers has increased recently. Cross border mergers have opened up vistas of opportunities. It enables an Indian company to utilise sophisticated levels of technical know-how offered by the foreign collaborator whereas enables the latter to utilise the large market and resources of India. The following are the benefits of entering into a cross border merger:

- **Diversification:** A merger often leads to product diversification, whereas a cross border in addition to offering diversification of products also leads to geographical diversification. This is extremely important for companies which want to make their global presence felt.
- **Achieving cost effectiveness:** When a company seeks to enter new markets, it takes some resources and money to build capacity. Having an existing infrastructure and resources in the new market helps in achieving cost effectiveness.
- **Technological advancement:** Mergers enable both the parties to use each other's intellectual properties hence enhancing technical know-how.
- **Distribution:** Cross border mergers help in creating a large distribution network transcending boundary.

However, with bouquets come brickbats, hence with the benefits also come risks associated with cross border mergers. Some of the risks posed by cross border mergers are:

- Despite Double Tax Avoidance Agreements, the tax implications in the host countries may prove to be complex and tedious. This may increase costs as a local professional is required to be hired.
- Regulatory landscape: The laws and regulations in the host country would be different and may be difficult to comply. An unusable regulatory landscape may pose risks to a cross border merger.
- Political scenario: It is essential to assess the political situation of the country before one enters into a merger with an entity belonging to that country. Unstable politics may lead to difficulties in carrying out business.

Valuation of Cross Border Firm

In cross border acquisitions, there can be factors important for considerations which are not considered at all in domestic acquisitions. Valuation is one such factor which changes with countries due to changes in exchange rate, stock market transactions and other macroeconomic developments.

Once identification has been completed, the process of valuing the target begins. A variety of valuation techniques are widely used in global business today each with its relative merits. In addition to the fundamental methodologies of Discounted Cash Flow (DCF) and multiples (earnings and cash flow), there are also a variety of industry-specific measures that focus on the most significant elements of value in business lines.

We shall discuss a few valuation methods below:

- The DCF (Discounted Cash Flow) approach to valuation calculates the value of the enterprise as the present value of all future free cash flows less the cash flows due to creditors and minority shareholders.
- The P/E ratio is an indication of what the market is willing to pay for a currency unit of earnings. It is also an indication of how secure the markets perception is about the future earnings of the firm and its riskiness.
- The market-to-book ratio (M/B) is a method of valuing a firm on the basis of what the market believes the firm is worth over and above its capital, its original capital investment, and subsequent retained earnings. Like the P/E Ratio, the magnitude of the M/B ratio as compared with its major competitors, reflects the market's perception of the quality of the firm's earnings, management, and general strategic opportunities.

The completion of a variety of alternative valuations for the target firm aids not only in gaining a more complete picture of what price must be paid to complete the transaction, but also in determining whether the price is attractive.

REGULATORY, COMPETITION, ACCOUNTING AND TAXATION ASPECTS

Taxation of mergers and acquisitions in India

There can be different methods of asset acquisition. Irrespective of the method, the tax losses are not generally transferred to the buyer thereby remaining operating in the domain of the seller. When the undertaking is acquired via slump sale where the particular picking up of assets by the buyer is not possible, some of the tax benefits/ deductions of the undertaking are made available to the buyer.

If the transfer is made for inadequate consideration and the tax proceedings are going on against the transferor then the authorities have the power to claim the amount from the transferee on the completion of the proceedings, if the consideration for the transfer is found to be inadequate.

No GST is applicable to a slump sale, i.e., wherein all the assets, rights, property and liabilities are transferred to the transferee. On the other hand, in a situation where particular assets are bought, the GST rate pertaining to the asset is applicable.

When the acquisition is via sale of shares, Securities Transition Tax (STT) is payable by both the buyer and when the shares are sold through a recognized stock exchange, STT is imposed on purchases and sales of equity shares listed on a recognized stock exchange in India at 0.1 percent based on the purchase or sale price.

Where a foreign company transfers shares of a foreign company to another company and the value of the shares is derived substantially from assets situated in India, then capital gains derived on the transfer are subject to income tax in India.

Further, payment for such shares is subject to Indian Withholding Tax (WHT). Shares of a foreign company are deemed to derive their value substantially from assets in India if such Indian assets are valued at a minimum of INR100 million and constitute at least 50 percent of the value of all the assets owned by such foreign company. A tax neutral status is provided where the resultant company is Indian (inbound merger) given that the transfer occurs through a slump sale and shareholders continue holding three-fourths of the shares.

If the foreign company is the parent company and the subsidiary is in India then the merger of the foreign company with another foreign company makes the newly created company, the owner of the Indian company provided that 25% of the shareholders of the amalgamating company remain the shareholders of the amalgamated company as well. Such a situation warrants for tax exemptions.

Regulatory Aspect

We have seen the regulatory framework around cross border mergers in the sections above. Let us now see how other key legislations regulate cross border mergers:

- The Foreign Exchange Management (Non-Debt Instrument) Regulations, 2019 and Foreign Exchange Management (Overseas Investment) Regulations, 2022 are extremely important pieces of legislation for allowing foreign investment in India and hence prove to be pertinent to cross border mergers as well. In addition to this, the Reserve Bank of India (the RBI) has notified Foreign Exchange Management (Cross-Border Merger) Regulations, 2018 (the Cross-Border Regulation) under the Foreign Exchange Management Act, 1999. These Regulations specifically deal with cross border mergers and contain provisions pertaining to mergers, demergers, amalgamations and arrangements between Indian companies and foreign companies. These regulations also discuss the concepts of inbound and outbound investments. If the foreign company is a JV/WOS then it is required to adhere to the conditions mentioned in (Overseas Investment) Rules & Regulations, 2022. Further, if the inbound merger of the JV/WOS leads to the acquisition of a subsidiary of the JV/WOS, then it is required to comply with the ODI Regulations, specifically regulations 6 and 7. If in an outbound merger, shares are being acquired by a person resident in India, then such acquisition becomes subject to the ODI Regulations as prescribed by the RBI.

- **FDI Regulations:** Cross border mergers essentially lead to inflow of foreign direct investment in the country and hence would be required to comply with the same. Foreign Direct Investment or FDI as it is called in common parlance is an investment by an entity or person who is resident outside India in the capital of an Indian company. An Indian company for the purposes of FDI would be a company incorporated in India under the applicable Companies Act. FDI can only be made through equity shares (shares which entitle its holder to vote), fully, compulsorily and mandatorily convertible debentures (instruments issued against loans) and fully, compulsorily and mandatorily convertible preference shares (shares which do not give voting rights). The two routes through which foreign investors may enter the country are government approval and automatic route. In a cross-border merger, the companies would have to comply with the FDI regulations as there would be inflow of foreign cash in the economy.

- **Takeover Code:** These come into picture, if the merger is happening with a listed company in India. If voting rights or control over the company is acquired then these regulations get triggered.

Competition Law

The Competition Commission of India (CCI) regulates the mergers in order to prevent the rise of monopolistic mergers. While mergers help in creating economies of scale and lead to increase in profits, they may also contribute to the creation of monopolistic structure. Hence mergers are made subject to the competition laws of the country.

The CCI has to assess and inquire into any merger which may have an adverse impact on the healthy competition in the market. While making such assessment as to the adverse effects the commission takes account of a number of factors such as actual and potential level of competition through imports in the market, extent of barriers to entry into the market, level of combination in the market etc.

Even a likelihood of causing of adverse impact is adequate for the competition commission to rule that the merger is creating an adverse impact. If the merged enterprise created post a cross-border merger possesses assets worth more than US $ 1 bn, or turnover more than US $ 3 bn; or the group to which the merged enterprise belongs possesses assets worth more than US $ 4 billion, or turnover more than US $ 12 billion then the competition commission is required to examine such combination.

Conflict of Jurisdictions is another such problem wherein whether or not the merger would affect the competition in the market positively or negatively would depend on the market situation which is unique to every country.

Accounting

In merger accounting, all the assets and liabilities of the transferor are consolidated at their existing book values. Under acquisition accounting, the consideration is allocated among the assets and liabilities acquired (on a fair value basis). Therefore, acquisition accounting may give rise to goodwill, which is normally amortized over 5 years.

Further, goodwill arising on merger will not be amortized; instead it will be tested for impairment. The accounting treatment of merger within a group is separately dealt with under the new Ind AS, which requires all assets and liabilities of the transferor to be recognized at their existing book values only.

> The new IndAS are to be implemented in a phased manner. All listed companies and companies with net worth of INR 500 crore or more are required to adopt the Ind AS from 1 April, 2016. Companies with net worth of INR 250 crore or more are required to adopt Ind AS from 1 April, 2017. Other companies will continue to apply existing accounting standards.

Cross Border Mergers – Earnouts: Cross Borders Mergers are subject to earnouts. An earnout is a contingent consideration whereby Buyer of the Target would decide an amount which is to be paid provided certain contingent considerations to happen. Cross Border Mergers specially covering Information Technology (IT), Technological Mergers, Banking Mergers are subject to Contingent Considerations. Earnouts are divided into 3 types:

- Cash Earnouts
- Equity Earnouts
- Stock Compensation Earnouts.

Cross Borders Mergers – Carveouts: A Carve out is a Potential divestiture of a Business unit in which a parent company sells minority interest of a Child Company to outside Investors. A Carveout allows a company to capitalize on a Business segment that many not be part of its core operations.

Example of Cross-border Mergers & Acquisitions

INFOSYS KALEIDOSCOPE

(4) Notwithstanding anything contained in sub-rule (3), in case of a compromise or an arrangement or merger or demerger between an Indian company and a company or body corporate which has been incorporated in a country which shares land border with India, a declaration in Form No. CAA-16 shall be required at the stage of submission of application under section 230 of the Act.

TATA- CORUS DEAL

This acquisition of Corus Group Plc by Tata Steel Limited (TSL), was the biggest overseas acquisition by an Indian company. TSL emerged as the fifth largest steel producer in the world after the acquisition. The acquisition gave Tata Steel access to Corus' strong distribution network in Europe.

Tata Steel had first offered to pay 455 pence per share of Corus, to close the deal at US$ 7.6 billion on October 17, 2006. CSN then counter offered 475 pence per share of Corus on November 17, 2006. Within hours of Tata Steel increasing its original bid for Corus to 500 pence per share, Brazil's CSN made its formal counter bid for Corus at 515 pence per share in cash, 3% more than Tata Steel's Offer.

Finally, an auction was initiated on January 31, 2007, and after nine rounds of bidding, TSL could finally clinch the deal with its final bid 608 pence per share, almost 34% higher than the first bid of 455 pence per share of Corus. The deal (between Tata & Corus) was officially announced on April 2nd, 2007 at a price of 608 pence per ordinary share in cash.

Indian Steel Giant Tata Steel Limited (TSL) finally acquired the Corus Group Plc (Corus), European steel giant for US$ 13.70 billion. The merged entity, Tata-Corus, employed 84,000 people across 45 countries in the world. It had the capacity to produce 27 million tons of steel per annum, making it the fifth largest steel producer in the world as of early 2007.

Tata Corus Deal Synergy

1. Tata was one of the lowest cost steel producers in the world and had self-sufficiency in raw material. Corus was fighting to keep its productions costs under control and was on the lookout for sources of iron ore.
2. Tata had a strong retail and distribution network in India and South East Asia and was a major supplier to the Indian auto industry and hence there would be a powerful combination of high quality developed and low cost high growth markets.
3. Technology transfer and enhanced R&D capabilities between the two companies that specializes in different areas of the value chain.
4. There was a strong culture fit between the two organizations both of which highly emphasized on continuous improvement and ethics, i.e. 'The Corus Way'with the core values and code of ethics, integrity, creating value in steel, customer focus, selective growth and respect for people etc. were strong synergies.

CASE LAWS

Vodafone International Holdings v Union of India *decision of 2012* was a landmark decision. This case pertained to taxation of transfer of shares between two non-resident companies by virtue of which the controlling interest of an Indian resident company was acquired. The Supreme Court clarified the doubt over imposition of taxes in such situations and shed light on the following:

- The parameters of tax planning
- Business entities are permitted to structure their transactions in such a way so as to reduce their tax liability, in the absence of any law prohibiting them from doing the same
- Lifting of corporate veil
- Business transactions should be looked at holistically.

While commenting upon the creation of subsidiaries through the process of mergers and acquisitions, the SCsaid that "the legal position of any company incorporated abroad is that its powers, functions and responsibilities are governed by the law of its incorporation. No multinational company can operate in a foreign jurisdiction save by operating as a good local citizen. If the owned company is wound up, the liquidator, and not the parent company, would get hold of the assets of the subsidiary. The difference is between having power or having a persuasive position".

Cross-Border Demerger

In this case of ***Sun Pharmaceutical Industries Limited (19.12.2019),*** a scheme of arrangement under Section 230 - 234 of the Companies Act, 2013 in the nature of de-merger was filed before National Company Law Tribunal ("NCLT"), Ahmedabad Bench. The Scheme contemplated transfer of two specified investment undertakings of

Sun Pharmaceutical Industries Limited to two overseas Resulting Companies, viz. Sun Pharma (Netherlands) B.V., and Sun Pharmaceutical Holdings USA Inc. Since, Petitioner Company is listed company having its shares listed on BSE Limited and National Stock Exchange of India Limited therefore the company sought the approval of the Stock Exchanges and SEBI which provided their no objection to the Scheme of Demerger. On presentation of Petition before NCLT meetings of equity shareholders and unsecured creditors were convened, whereby scheme was approved by majority of equity shareholders and unsecured creditors. However, Regional Director (North Western Region) took the following observation on scheme of demerger–

(i) Section 234 refers to cross border mergers and amalgamations and not to demergers.

(ii) Section 2 (19AA) of the Income Tax,1961 is violated and same will not amount to tax neutral transaction.

(iii) Company to comply with provisions of FEMA and RBI.

Petitioner company while replying to aforesaid observation held that, scheme of arrangement, either in the nature of merger or demerger and the petitioner demerged company has complied with the applicable frame work under FEMA and RBI guidelines. Hence, there was deemed approval of RBI to the Scheme.

While going through the provisions of Section 234 it is evident that same applies to cross border mergers of Indian companies with foreign companies and vice versa and the provisions mention only about the words ''Merger'' and/ or ''Amalgamation'' so the Section 234 do not provide for or rather restrict the demerger of the Indian Companies with foreign company. In addition to the above, Rule 25A of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 is silent on 'Demergers' and mentions only 'Mergers' and 'Amalgamations'. Moreover, Foreign Exchange Management (Cross Border Merger) Regulations, 2018 are applicable to the mergers and amalgamations of the Indian companies with the foreign companies only. Thus, the NCLT rejected the scheme.

Post-merger performance evaluation

Cross border mergers can be truly assessed only by evaluating the post-merger performance of the merged entities. The following parameters may be used to assess the post-merger performance:

- **Returns:** A comparative analysis of the returns being generated by the entity pre and post-merger should be carried out. If the merged entity is earning significantly higher returns than the merger is deemed successful.
- **Cash flow and operational efficiency:** If post-merger the cash flow significantly increases and this increased cash flow is put to use to obtain operational efficiency, this too shows that the newly created entity is performing well.
- **Stock market reaction:** If the stock market reaction to the announcement of merger is positive then the merger appears to be a positive step.

Practical Insights

Some practicalities which need to be kept in mind while entering cross border mergers are:

a) Conduct due diligence on the other firm.

b) Conduct a risk-benefit analysis before entering into the merger.

c) Valuation of both the firms is essential so as to predict the competition law treatment of the merger.

d) Make sure that when you enter into an outbound merger it is with a company from one of the prescribed jurisdictions.

e) Have an in-depth analysis of the host country's regulatory and political landscape ready before you take the decision of the merger.

ANNEXURE A

Foreign Exchange Management (Cross Border Merger) Regulations, 2018

Notification No. FEMA.389/2018-RB **Dated: March 20, 2018**

In exercise of the powers conferred by sub-section (3) of section (6) read with section 47 of the Foreign Exchange Management Act, 1999 (42 of 1999), the Reserve Bank makes the following regulations relating to merger, amalgamation and arrangement between Indian companies and foreign companies:

1. Short title and commencement

(i) These regulations may be called the Foreign Exchange Management (Cross border Merger) Regulations, 2018.

(ii) They shall come into force from the date of their publication in the Official Gazette.

2. Definitions

In these Regulations unless the context requires otherwise, -

(i) 'Act' means the Foreign Exchange Management Act, 1999 (42 of 1999);

(ii) 'Companies Act' means The Companies Act, 2013;

(iii) 'Cross border merger' means any merger, amalgamation or arrangement between an Indian company and foreign company in accordance with Companies (Compromises, Arrangements and Amalgamation) Rules, 2016 notified under the Companies Act, 2013;

(iv) 'Foreign company' means any company or body corporate incorporated outside India whether having a place of business in India or not;

Explanation: for the purpose of outbound mergers, the foreign company should be incorporated in a jurisdiction specified in Annexure B to Companies (Compromises, Arrangements and Amalgamation) Rules, 2016;

(v) 'Inbound merger' means a cross border merger where the resultant company is an Indian company;

(vi) 'Indian company' means a company incorporated under the Companies Act, 2013 or under any previous company law;

(vii) 'NCLT' means National Company Law Tribunal as defined under the Companies Act, 2013 or rules framed thereunder;

(viii) 'Outbound merger' means a cross border merger where the resultant company is a foreign company;

(ix) 'Resultant company' means an Indian company or a foreign company which takes over the assets and liabilities of the companies involved in the cross border merger;

(x) The words and expressions used but not defined in these Regulations shall have the same meanings respectively assigned to them in the Act.

3. Save as otherwise provided in the Act or rules or regulations framed thereunder or with the general or special permission of Reserve Bank, no person resident in India shall acquire or transfer any security or debt or asset outside India and no person resident outside India shall acquire or transfer any security or debt or asset in India on account of cross border mergers.

Explanation: Cross Border Mergers pending before the competent authority as on date of commencement of these regulations shall be governed by these Regulations.

4. Inbound merger: A merger or amalgamation of foreign company with an Indian company

1. the resultant company may issue or transfer any security and/or a foreign security, as the case may be, to a person resident outside India in accordance with the pricing guidelines, entry

routes, sectoral caps, attendant conditions and reporting requirements for foreign investment as laid down in Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2017.

Provided that

(i) where the foreign company is a joint venture (JV)/ wholly owned subsidiary (WOS) of the Indian company, it shall comply with the conditions prescribed for transfer of shares of such JV/ WOS by the Indian party as laid down in Foreign Exchange Management (Transfer or issue of any foreign security) Regulations, 2004;

(ii) where the inbound merger of the JV/WOS results into acquisition of the Step down subsidiary of JV/ WOS of the Indian party by the resultant company, then such acquisition should be in compliance with Regulation 6 and 7 of Foreign Exchange Management (Transfer or issue of any foreign security) Regulations, 2004.

2. An office outside India of the foreign company, pursuant to the sanction of the Scheme of cross border merger shall be deemed to be the branch/office outside India of the resultant company in accordance with the Foreign Exchange Management (Foreign Currency Account by a person resident in India) Regulations, 2015. Accordingly, the resultant company may undertake any transaction as permitted to a branch/office under the aforesaid Regulations.

3. The guarantees or outstanding borrowings of the foreign company from overseas sources which become the borrowing of the resultant company or any borrowing from overseas sources entering into the books of resultant company shall conform, within a period of two years, to the External Commercial Borrowing norms or Trade Credit norms or other foreign borrowing norms, as laid down under Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000 or Foreign Exchange Management (Borrowing or Lending in Rupees) Regulations, 2000 or Foreign Exchange Management (Guarantee) Regulations, 2000, as applicable.

   Provided that no remittance for repayment of such liability is made from India with in such period of two years; Provided further that the conditions with respect to end use shall not apply.

4. The resultant company may acquire and hold any asset outside India which an Indian company is permitted to acquire under the provisions of the Act,rules or regulations framed there under. Such assets can be transferred in any manner for undertaking a transaction permissible under the Act or rules or regulations framed thereunder.

5. Where the asset or security outside India is not permitted to be acquired or held by the resultant company under the Act, rules or regulations, the resultant company shall sell such asset or security within a period of two years from the date of sanction of the Scheme by NCLT and the sale proceeds shall be repatriated to India immediately through banking channels. Where any liability outside India is not permitted to be held by the resultant company, the same may be extinguished from the sale proceeds of such overseas assets within the period of two years.

6. The resultant company may open a bank account in foreign currency in the overseas jurisdiction for the purpose of putting through transactions incidental to the cross border merger for a maximum period of two years from the date of sanction of the Scheme by NCLT.

5. Outbound merger: A merger or amalgamation of Indian company with a foreign company

1. a person resident in India may acquire or hold securities of the resultant company in accordance with the Foreign Exchange Management (Transfer or issue of any Foreign Security) Regulations, 2004.

2. a resident individual may acquire securities outside India provided that the fair market value of such securities is within the limits prescribed under the Liberalized Remittance Scheme laid down in the Act or rules or regulations framed there under.

3. An office in India of the Indian company, pursuant to sanction of the Scheme of cross border merger, may be deemed to be a branch office in India of the resultant company in accordance with the

Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016. Accordingly, the resultant company may undertake any transaction as permitted to a branch office under the aforesaid Regulations.

4. The guarantees or outstanding borrowings of the Indian company which become the liabilities of the resultant company shall be repaid as per the Scheme sanctioned by the NCLT in terms of the Companies (Compromises, Arrangement or Amalgamation) Rules, 2016.

   Provided that the resultant company shall not acquire any liability payable towards a lender in India in Rupees which is not in conformity with the Act or rules or regulations framed thereunder.

   Provided further that a no-objection certificate to this effect should be obtained from the lenders in India of the Indian company.

5. The resultant company may acquire and hold any asset in India which a foreign company is permitted to acquire under the provisions of the Act, rules or regulations framed thereunder. Such assets can be transferred in any manner for undertaking a transaction permissible under the Act or rules or regulations framed thereunder.

6. Where the asset or security in India cannot be acquired or held by the resultant company under the Act, rules or regulations, the resultant company shall sell such asset or security within a period of two years from the date of sanction of the Scheme by NCLT and the sale proceeds shall be repatriated outside India immediately through banking channels. Repayment of Indian liabilities from sale proceeds of such assets or securities within the period of two years shall be permissible.

7. The resultant company may open a Special Non-Resident Rupee Account (SNRR Account) in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016 for the purpose of putting through transactions under these Regulations. The account shall run for a maximum period of two years from the date of sanction of the Scheme by NCLT.

6. Valuation of companies involved in cross border merger

The valuation of the Indian company and the foreign company shall be done in accordance with Rule 25Aof the Companies (Compromises, Arrangement or Amalgamation) Rules, 2016.

7. Miscellaneous

1. Compensation by the resultant company, to a holder of a security of the Indian company or the foreign company, as the case may be, may be paid, in accordance with the Scheme sanctioned by the NCLT.

2. The companies involved in the cross border merger shall ensure that regulatory actions, if any, prior to merger,with respect to non-compliance,contravention, violation, as the case may be,of the Act or the Rules or the Regulations framed thereunder shall be completed.

8. Reporting

1. The resultant company and/or the companies involved in the cross border merger shall be required to furnish reports as may be prescribed by the Reserve Bank, in consultation with the Government of India, from time to time.

9. Deemed approval

1. Any transaction on account of a cross border merger undertaken in accordance with these Regulations shall be deemed to have prior approval of the Reserve Bank as required under Rule 25A of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

2. A certificate from the Managing Director/Whole Time Director and Company Secretary, if available, of the company(ies) concerned ensuring compliance to these Regulations shall be furnished along with the application made to the NCLT under the Companies (Compromises, Arrangements or Amalgamations) Rules, 2016.

LESSON ROUND-UP

- Cross border merger is a recent trend and a very profitable one. If Indian companies have to make their presence felt globally, it is essential for India to have a sound legal framework pertaining to cross border mergers.
- The recent merger regulations, section 234 and the Companies Amalgamation Rules are a step towards strengthening this legal regime. Apart from the company law, other legislations such as tax and competition laws also play a key role in perpetuating cross border merger transactions.
- Section 234 of the Companies Act, 2013 notified in 2017 is the key legal provision governing cross border mergers.
- Companies Amalgamation Rules and sections 230-234 of the Companies Act, 2013 regulate the procedure of mergers.
- Foreign Exchange Management (Cross Border Merger) Regulations, 2018, have brought the concept of outbound merger in the country as well.
- Discounted cash flow, private equity and market to book ratios are some of the ways in which a cross border firm may be valued.
- Apart from companies Act, other considerations such as tax and competition laws also play a major role in cross border mergers.

GLOSSARY

Foreign company : means company incorporated outside India.

Indian company : means company incorporated under Companies Act, 2013.

Inbound merger : is a merger wherein as a result of the merger of a foreign entity and an Indian entity an Indian company is formed.

Outbound merger : is one wherein as a result of the merger of a foreign entity with an Indian entity a foreign company is formed.

Cross border merger : means any merger, amalgamation or arrangement between an Indian company and foreign company under the Act.

Resultant Company : means an Indian company or a foreign company which takes over assets and liabilities of the companies involved in a merger.

Earnout : is a contingent consideration agreed between both Buyer and Seller at the time of acquisition. It is subject to P&L Impact at the time of Books Close.

TEST YOURSELF

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. What is a cross border merger? Explain the legal regime in India around a cross border merger?
2. What are the changes brought about by the Foreign Exchange Management (Cross Border Merger) Regulations, 2018. Critically analyse the same.
3. Explain the tax implications and the accounting parameters associated with cross border mergers?
4. Discuss the taxation of cross border mergers in India.

5. Mention the jurisdictions specified in Rule 25A of Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

LIST OF FURTHER READINGS

- Guide to Companies Act by A Ramaiya 18th Edition, Lexis Nexis
- Companies Act, 2013 - Bare Act

PART II

VALUATION

Overview of Business Valuation

Lesson 12

KEY CONCEPTS

■ Valuation ■ Price ■ Principle of Valuation ■ Merger & Acquisition ■ Registered Valuers

Learning Objectives

To understand:

- Genesis of Valuation
- Need for Valuation
- Hindrances /Bottlenecks in Valuation
- Various Expression of Value
- Price vs. Value
- Process of valuation
- Business Valuation Approaches
- Principles of Valuation
- Sources of Information for Valuation

Lesson Outline

- Introduction
- Meaning of valuation
- Need to do valuation of a business
- Identifying the areas where valuation can be used
- Identifying the purpose of valuation and its impact on the value estimates
- Main hindrances in value estimates of a business
- Learning the concept of business valuation approaches
- Learning the main principles of valuation
- Identifying the main sources of information for valuation
- Lesson Round-Up
- Test Yourself
- List of Further Readings/References

REGULATORY FRAMEWORK

- The Companies Act, 2013
- The Insolvency and Bankruptcy Code,2016
- SEBI Regulations
- Valuation Standards-IVS and ICAI Valuation Standards

INTRODUCTION

Market usually discovers price, which reflects the worth of an asset. It discovers different prices for the same asset in different contexts. Thus, price is not absolute; it is context specific. Often, it is neither feasible nor desirable to pass an asset through the market to discover its worth. In such cases, worth of an asset is estimated in a simulated context. The person who estimates the worth is a Valuer, the process of estimation is valuation and the worth so estimated is the value. If value of an asset is what the price ought to be in the given context, the valuation is accurate. While the market may discover a dirty price occasionally failing to reflect the accurate worth of an asset, a value cannot be dirty. If price converges with value in the simulated context, the price discovery is perfect.

Valuation is a process of appraisal or determination of the value of certain assets, i.e., tangible or intangible, securities, liabilities and a specific business as a going concern or any company listed or unlisted or company undergoing liquidation or other forms of organization, partnership or proprietorship. 'Value' is a term signifying the material or monetary worth of a thing, which can be estimated in terms of medium of exchange. In other words, it is an assessment resulting in an expression of opinion rather than arithmetical exactness.

Business valuation requires a working knowledge of a variety of factors, and professional judgment and experience. This includes recognizing the purpose of the valuation, the value drivers impacting the subject company, and an understanding of industry, competitive and economic factors, as well as the selection and application of the appropriate valuation approach (es) and method(s).

The parties need a value for exchange goods or services for which either market does not exist, or market discovers a spurious price for a variety of reasons, including manipulation. They may also need value of an asset for a variety of purposes. Valuation is a key financial information relied upon by investors and used to support decisions in financial markets, having direct impact on the public interest (IVSC, 2014). The services rendered by valuers also helps in avoiding 'market collapse' due to imperfect information (Bartke & Reimund, 2015). Some of the NPAs in the banking system are attributed to decisions based on such valuations. The Committee of Creditors may unjustly liquidate a company if it uses an inflated reference value for comparison with the value offered by resolution plans. Such decisions arising from use of inappropriate values has the potential to distort market and misallocate resources in a market economy. Sustainable economic growth can only be built on valuations that are trusted by investors, creditors, tax authorities, governments, regulators and others.

Generally, the valuation process has four parts.

(i) First, pre-valuation process where the valuer and the client agree on the terms of engagement.

(ii) Second, investigation which is the formal or systematic examination or research undertaken on the property.

(iii) Third, data handling and interpretation which requires processing and calculation of data, qualification and verification of data, and analysis of data.

(iv) Fourth, post-valuation process reporting, which provides for a single value, presented in the valuation report.

The valuation report provides clients with an independent, comparable evidence and a written confirmation of the value of a property that is neither ambiguous nor misleading. Further, the determination of the value and delivery of the valuation report is made by the valuer on the basis of a framework such as RICS Red Book or the IVS (International Valuation Standards). These standards inter alia provide for the bases of value which are the fundamental measurement assumptions on which values are based, and the approaches and methods which are used to attain different valuation bases.

The valuation process is a complex process and requires multiple skills. In order to determine value, a valuer is required to make several judgments and must possess a mix of competencies.

GENESIS OF VALUATION

Valuation is the process of determining economic worth of an asset or a company under certain assumptions and limiting conditions and subject to data available on valuation date. (International Valuation Standard Council).

The economic agents take several financial decisions on the basis of an estimated value of an asset. They need value of an asset for purposes such as determination of the amount of loan that can be sanctioned against security of an asset or guarantee of a guarantor; levy of taxes like municipal tax, stamp duty, income-tax on capital gains; compensation for compulsory acquisition of property; assessment of loss and insurance premium; distribution of property among children / beneficiaries; etc. They may also need a value for reference or comparison to enable them to take an informed decision such as submitting or accepting a resolution plan in an insolvency proceeding. The purpose is defeated if the value is not authentic and genuine. A banker may not have adequate protection, where it gives loan against the security of an asset whose value is overestimated or guarantee of a person whose net worth is overestimated. Some of the Non-Performing Assets in the banking system is attributed to such inappropriate valuations. The Committee of Creditors may unjustly liquidate a company if it uses an inflated reference value for comparison with the value offered by resolution plans. In market economies, property forms the basis of majority of financial decisions. An improper valuation of the property risks financial exposure for a wide range of stakeholders (Gilbertson & Preston, 2005). The decisions arising from use of inappropriate values, in addition to causing unfair gain or loss to parties, has the potential to distort market and misallocate resources which may impinge upon economic growth in a market economy. This calls for a professional valuation.

Valuations are an essential part of most reporting and business decisions and play a crucial role in many real estate-related decisions. In fact, the evolution of valuation profession is attributed to the development of property markets. Internationally, the pressures driving demand for the professionalisation of valuers include valuation induced financial crisis or the determination to avoid such a crisis; the move towards market economies; and property tax reforms (Gilbertson & Preston, 2005). Further, several financial crises around the world are attributed to consequences of poor valuation. Valuation and prices have served as signals and incentives for both the bubbles as well as of the ensuing collapse in case of real estate market crashes. Therefore, it is observed that after every financial crisis the valuation profession comes into spotlight and efforts are made to increase its accuracy and reliability.

For example, pursuant to the property crash in UK in 1970s, the RICS published Red Book for setting out standards of valuation and professional conduct expected of valuers. In response to the “saving and loan” crisis in USA in late-1980s, the Government created a mechanism for uniform appraisal standards and licensing of valuers in each State. Further, the role of valuation profession was also highlighted in the global financial crisis of 2008.

NEED FOR VALUATION

Valuation of business plays a very vital role, therefore a business owner or individual may need to know the value of a business. The fair market value standard consists of an independent buyer and seller having the requisite knowledge and facts, not under any undue influence or stressors and having access to all of the information to make an informed decision.

Business valuation is carried out to know the business and helps in strategic decision making. Appropriate purpose for valuation becomes the bases of valuation. The strategic decision making in Business Valuation may be related to following:

1. **Merger, acquisition or take over** so that interested party can obtain fair market value - A Party who enters into a transaction with another for acquiring a business would like to acquire a business as a going concern for the purpose of continuing to carry the same business, he might compute the valuation of the target company on a going concern basis. On the other hand, if the intention of the acquirer is to acquire any property such as land, rights, or brands, the valuation would be closely connected to the market price for such property or linked to the possible future revenue generation likely to arise from such acquisition. In every such transaction, therefore, the predominant objective in carrying out a valuation is to put parties to a transaction in a comfortable position so that no one feels aggrieved.

2. **Strategic Partnership, Joint Venture and Collaborations -** Valuation is needed while evaluating decision on Strategic Partnership or Joint Venture or Foreign Collaboration. These have potential to give competitive edge over others in the form of advanced technology or production processes, additional finance, expanding customer base, reengineering of existing product, new products or services, intensive and extensive market coverage.

3. **ESOP, ESPS and Employee Retention -** These are various tools to retain employees for longer period. ESOP is incentive arrangement made by employer for retaining its key employees by allowing them to purchase the shares of company at a fixed price on the date of the grant. In this waiting period is known as 'vesting period' and the period in which ESOP can be availed by the employee is known as 'exercise period'. Certain percentage of shares is kept in ESOP trust fund until the option to buy share is exercised by the employee. If the employee leaves the company or his services are terminated before the completion of vesting period, then he loses the options to buy the share at pre-decided price which is usually less than market price at the time of exercise period. Lapsed options cannot be converted into shares. ESOPs are taxable at the time of purchase of shares as salary income (perquisites) in the hands of employees. Difference in fair market price and issued price is taxable as salary on the date of issue of shares whereas difference between actual sale price and fair market value is taxable as capital gain in the hands of employees.

4. **At the time of Peaceful Exit -** Valuation is required to be worked out at the time of resolving the disputes among stakeholders; purchase of equity from dissenting shareholders; stake sale or exit by co-venturers, strategic partners, foreign collaborator or strategic investors; divestment by existing promoters in favour of strategic investors.

5. **Specific Situations -** Minority oppression cases, economic damages computations, ownership disputes, cases of insolvency and bankruptcy, breach of contract, during submission of resolution plans, during liquidation and winding up, as part of succession planning, the death or disability of the owner.

6. **Under Company Law provisions -** Valuation is mandatorily required at the time of further issue of shares; issue of shares for consideration other than cash; private placement of shares.

7. **Under Other Laws -** Valuation is required to be carried out under various laws in various situations. Regulations and Rules issued under various Acts have situation specific requirement for valuation like SEBI Act, Foreign Exchange Management Act (FEMA), Income Tax Act, Customs Act, Stamp Duty Act, IBC Code, 2016.

8. **For Insurance Coverage -** Valuation of asset for insurance cover need to be carefully assessed so that, on side it covers the damage to the fullest extent possible and on the other insurance premium is not in excess. In the matter of insurance, valuation is twin edge sword. Over valuation is harmful because it results into higher premium whereas under valuation is equally harmful as it will lead to exposed coverage in case of accidental damage to the assets.

9. **Court Directed Valuations -** Some times, business valuations are carried out as per the directions of the court. NCLT issues directives and appoint valuers in the matters of oppression and mismanagement. High Courts appoints valuers to resolve disputes and in winding up matters. ITAT and other tribunals may also engage valuers in certain situations.

10. **During winding up process -** The business assets are valued by the office of Official Liquidators. They are attached to High Courts. In Insolvency and Bankruptcies, valuers are appointed by Resolution Professionals to carry out valuation on Insolvency commencement date. In liquidation, company liquidators are required to appoint valuers to carry out valuation on liquidation commencement date. In case of voluntary winding up, company Board is required to engage valuer before issuing solvency certificate.

11. For IPO and FPO - Valuation of securities is required to be worked out at the time of listing of securities of the company. SEBI is regulatory authority. Under various regulations, SEBI has prescribed the requirement of valuation as well as valuation methodology.

12. **At the Time of Debt Funding -** At the time of business loans and debt funding, valuation is required to be worked out for the purpose of assessing security cover and need of funds of the business.

A market economy needs valuations of assets to facilitate a variety of transactions. For example, the corporate insolvency resolution process under the Insolvency and Bankruptcy Code, 2016 (Code) envisages estimation of fair value and liquidation value of the assets of the corporate debtor. These values serve as reference for evaluation of choices, including liquidation, and selection of the choice that decides the fate of the corporate debtor, and consequently of the stakeholders. A wrong valuation may liquidate an otherwise viable company, which may be disastrous for an economy. A banker determines the amount of loan that can be sanctioned against security of an asset. He may not have adequate protection, where it gives loan against the security of an asset whose value is overestimated. Some of the NPAs in the banking system are attributed to decisions based on such valuations.

A business valuation is a complex financial analysis that should be undertaken by a qualified valuation professional with the appropriate credentials. Business owners who seek a low-cost business valuation are seriously missing out on the important benefits received from a comprehensive valuation analysis and valuation report performed by a certified valuation expert. These benefits help business owners negotiate a strategic sale of their business, minimize the financial risk of a business owner in a litigation matter, minimize the potential tax that a business owner or estate may pay in gift or estate tax as well as provide defense in an audit situation.

FACTORS INFLUENCING VALUATION

After having done the due diligence process, the next step is to value the business for the purpose of deciding the swap ratio. A company will change the hand of ownership only when the fair market value is arrived to the satisfaction of the owner's of the seller company. Similarly the buyer company will be ready to pay for the price if it is in the beneficial interest of its owners too. The valuation of the assets and liabilities of the business entity depends upon the various factors. These factors may be as under:

- The past dividend track record of the companies.
- The past earning of the companies.
- The price of shares trading at the bourses of the companies, before the news of the merger deal and after the announcement of the deal.
- Bonus track record of the companies.
- IPO/ FPO of the companies.
- Past history of the prices of the shares of the companies.
- The voting strength in the merged entity of the shareholders.

- The net worth of the companies.
- Net assets of the companies.
- Liquidity in the Company.
- The underlying net tangible asset.
- Conditions of business (Running/closed).
- Future earnings and projections.
- Order Book status, number of ongoing projects, customer future projections.
- Future capacity utilisation.
- Cash flows.
- Net Present Value (NPV).
- Expected Rate of Return (ERR).

GENERAL PRINCIPLES OF BUSINESS VALUATION

In almost all business valuations, there are some principles, which are:

Principle of Time Value of Money: This principle suggests that the value can be measured by calculating the present value of future cash flows discounted at the appropriate discount rate.

Principle of Risk and Return: This principle believes that the investors are basically risk averse and on the other hand expects higher amount of wealth. Higher the risk, higher may be possibility of return and vice versa.

Principle of Substitution: This principle believes that understanding the market with competitive forces are very important in order to decide the price consideration. The risk averse investor will not pay more than that of the substitute available in the market.

Principle of Alternatives: This principle suggests that one should explore the various alternatives available in the market and should not rest only on one option. The benefits of vetting of various alternatives will give a comparative valuation and a prudent investor will choose the most beneficial alternative to his portfolio.

Principle of Expectation: Cash flows are based on the expectations about the performance in future and not the past. In the case of mature companies, we may assume that the growth from today or after some certain period would be constant.

Principle of Reasonableness: In valuation the principle of reasonableness is most important. It takes into consideration various aspects viz: nature of business, historical background, brand image, book value of the stock, earning capacity, dividend tract record, etc.

PURPOSE OF VALUATION

Valuation has been debated in India as an art or science and substantial part of the litigation in Mergers & Acquisitions (M&A) takes place on the issue of valuation as it involves an element of subjectivity that often gets challenged. The introduction of concept of Registered Valuer had been notified under Chapter XVII of the Companies Act 2013 to set the Indian valuation standards for standardizing the use of valuation practices in India, leading to transparency and better governance. The Institute of Chartered Accountants of India (ICAI) has issued and adopted Valuation Standards known as ICAI-Valuation Standards.

Section 247 (2) of the Companies Act, 2013 mandates that a valuer shall (a) make an impartial, true and fair valuation of any assets; (b) exercise due diligence while performing the functions as valuer; (c) make the valuation in accordance with the Valuation. Rules; and (d) not undertake valuation of any assets in which he has a direct or indirect interest or becomes so interested at any time during three years prior to his appointment as valuer or three years after valuation of assets was conducted by him.

Companies (Registered Valuers and Valuation) Rules, 2017 (Valuation Rules) *inter alia* provides for (a) registration of valuers, who may be individuals or partnership firms or companies, with Insolvency and Bankruptcy Board of India(IBBI) for conduct of valuation of different classes of assets under the Companies Act, 2013; (b) recognition of Registered Valuers Organisations (RVOs) to enroll valuer members, enforce a code of conduct on them, and conduct training and educational courses for its members; and (c) mechanism for notification and modification of valuation standards based on the recommendations of the "Committee to advise on valuation matters".

The Central Government delegated its powers and functions under section 247 of the Act to the Insolvency and Bankruptcy Board of India (IBBI) and specified it as the Authority under the said Rules.

Only a person registered with the Authority as Registered Valuers can conduct valuations required under the Companies Act, 2013 and the Code. Subject to meeting other requirements, an individual is eligible to be an Registered Valuers , if he: (a) is a fit and proper person, (b) has the necessary qualification and experience, (c) is a valuer member of an RVO, (d) has completed a recognised educational course as member of an RVO, (e) has passed the valuation examination conducted by the Authority within three years preceding the date of making the application for registration, and (f) is recommended by the RVO for registration as a valuer. The individual is required to have either a post-graduate qualification in the specified discipline and three years' experience, or a bachelor's degree in the specified discipline and five years' experience.

VALUATION STANDARDS

Emphasis on valuation standards assumed greater prominence in the last quarter of the 20th Century as a result of the financial collapses which was traced to property related valuations /transactions. The concern to avoid such collapses led to the emergence of valuation standards, first on a national and then on an international level (Gilbertson & Preston, 2005). RICS responded to the 1970s property crash in the UK by publishing the Red Book, setting out standards of valuation and professional conduct expected of valuers, while the Federal Government in the USA responded to the "savings and loan" crisis of the late-1980s by insisting on uniform appraisal standards and the licensing of valuers in each State.

Two sets of standards, namely, (i) International Valuation Standards (IVS) issued by the International Valuation Standards Council (IVSC), and (ii) the Royal Institution of Chartered Surveyors (RICS) Red Book, command great respect among the stakeholders. IVS comprises five 'General Standards' and six 'Asset-specific Standards'.

- The General Standards contain standards applicable to valuation of all asset classes, covering scope of work, investigations and compliance, bases of value, valuation approaches and methods, and reporting.
- The Asset-specific Standards include requirements related to specific types of asset valuation, including background information on the characteristics of each asset type that influence value and additional asset-specific requirements regarding common valuation approaches and methods used. These cover businesses and business interests, intangible assets, plant and equipment, real property interests, development property and financial instruments.

IVS allows flexibility to meet national requirements. Reportedly, some countries have adopted IVS as national standards, and some have adopted IVS with amendments to meet the requirements of national legislations.

RICS Red Book adopts and applies IVS. The standards take three forms: (a) professional standards centred around ethics and conduct, (b) technical standards centred on common definitions and conventions, (c) performance or delivery standards centred on rigour in analysis and objectivity of judgement. RICS also allows departures to meet local statutory or regulatory requirements. Red Book with departures is called national association valuation standards, which have been published in some countries. RICS Valuation Standards – Global and India issued in May 2011 provides four India-specific guidance notes: (a) valuation for financial statements, (b) valuation for secured lending, (c) development land in India, and (d) valuation for tax purposes in India. It is understood that RICS is working on a national supplement to Red Book for India for valuations undertaken subject to Indian jurisdiction.

The Valuation Rules (Rule 8) mandate that an RV shall, while conducting a valuation, comply with the valuation standards as notified or modified by the Central Government. Until the valuation standards are notified or modified by the Central Government, a valuer shall make valuations as per

(a) internationally accepted valuation standards; or

(b) valuation standards adopted by any RVO.

Rule 18 of the Valuation Rules enables the Central Government to notify and modify, from time to time, the valuation standards based on the recommendations of the Committee to advise on valuation matters.

Rule 19 of the Valuation Rules empowers the Central Government to constitute a committee to make recommendations on formulation and laying down of valuation standards and policies for compliance by companies and RVs. The Central Government constituted the Committee to advise on valuation matters.

REGULATORY ASPECTS AS TO VALUATION

Valuation provisions under the Companies Act, 2013

Section 247 of the Companies Act, 2013 Section 247 seeks to provide that valuation in respect of any property, stocks, shares, debentures, securities, goodwill or any other assets or net worth of a company or its assets or liabilities shall be valued by a person having such qualification and experience and registered as a valuer, in accordance with such rules as may be prescribed.

Valuation by Registered Valuers

(1) Where a valuation is required to be made in respect of any property, stocks, shares, debentures, securities or goodwill or any other assets (herein referred to as the assets) or net worth of a company or its liabilities under the provision of this Act, it shall be valued by a person having such qualifications and experience, registered as a valuer and being a member of an organisation recognised, in such manner, on such terms and conditions as may be prescribed and appointed by the audit committee or in its absence by the Board of Directors of that company.

(2) The valuer appointed under sub-section (1) shall,—

(a) make an impartial, true and fair valuation of any assets which may be required to be valued;

(b) exercise due diligence while performing the functions as valuer;

(c) make the valuation in accordance with such rules as may be prescribed; and

(d) not undertake valuation of any assets in which he has a direct or indirect interest or becomes so interested at any time during a period of three years prior to his appointment as valuer or three years after the valuation of assets was conducted by him.

(3) If a valuer contravenes the provisions of this section or the rules made thereunder, the valuer shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees: Provided that if the valuer has contravened such provisions with the intention to defraud the company or its members, he shall be punishable with imprisonment for a term which may extend to one year and with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

(4) Where a valuer has been convicted under sub-section (3), he shall be liable to

(i) refund the remuneration received by him to the company; and

(ii) pay for damages to the company or to any other person for loss arising out of incorrect or misleading statements of particulars made in his report.

The Companies (Registered Valuers and Valuation) Rules, 2017

The Central Government vide its Notification No. NO.GSR 1316(E) [F.NO.1/27/2013-CL-V], dated 18-10-2017 notified the Companies (Registered Valuers and Valuation) Rules, 2017. The notification of these Rules shall, while bringing about a clarity regarding various aspect of valuation will have a major impact on the industry, professionals, stakeholders and the government as well. These rules envisage formation of Registered Valuers Organisations for enrolling and imparting continuous education to Registered Valuers.

Though there is some consensus among professional valuers about generally accepted approaches, methods and procedures; however, a need was felt for education, training, regulation and standardization of prevalent practices in valuation.

The notification of these Rules will lead to the setting-up of Valuation Standards that will improve transparency and governance. Introduction of Valuation Standards will ensure that the valuation reports disclose a true, fair and complete view and result in greater objectivity in valuation procedures. The increased transparency and fairness in the valuation system shall also boost stakeholders' confidence alongside plugging of loopholes in valuation.

Eligibility for registered valuers (Rule 3)

Sub-rule (1) provides that a person shall be eligible to be a registered valuer if he-

(a) is a valuer member of a registered valuers organisation; Explanation —For the purposes of this clause, "a valuer member" is a member of a registered valuers organisation who possesses the requisite educational qualifications and experience for being registered as a valuer;

(b) is recommended by the registered valuers organisation of which he is a valuer member for registration as a valuer;

(c) has passed the valuation examination under rule 5 within three years preceding the date of making an application for registration under rule 6;

(d) possesses the qualifications and experience as specified in rule 4

(e) is not a minor;

(f) has not been declared to be of unsound mind;

(g) is not an undischarged bankrupt, or has not applied to be adjudicated as a bankrupt;

(h) is a person resident in India;

Explanation – For the purposes of these rules 'person resident in India' shall have the same meaning as defined in clause (v) of section 2 of the Foreign Exchange Management Act, 1999 as far as it is applicable to an individual;

(i) has not been convicted by any competent court for an offence punishable with imprisonment for a term exceeding six months or for an offence involving moral turpitude, and a period of five years has not elapsed from the date of expiry of the sentence: Provided that if a person has been convicted of any offence and sentenced in respect thereof to imprisonment for a period of seven years or more, he shall not be eligible to be registered;

(j) has not been levied a penalty under section 271J of Income-tax Act, 1961 and time limit for filing appeal before Commissioner of Income-tax (Appeals) or Income-tax Appellate Tribunal, as the case may be has expired, or such penalty has been confirmed by Income-tax Appellate Tribunal, and five years have not elapsed after levy of such penalty; and

(k) is a fit and proper person:

Explanation – For determining whether an individual is a fit and proper person under these rules, the authority may take account of any relevant consideration, including but not limited to the following criteria-

(i) integrity, reputation and character,

(ii) absence of convictions and restraint orders, and

(iii) competence and financial solvency.

(2) No partnership entity or company shall be eligible to be a registered valuer if-

(a) it has been set up for objects other than for rendering professional or financial services, including valuation services and that in the case of a company, it is a subsidiary, joint venture or associate of another company or body corporate;

(b) it is undergoing an insolvency resolution or is an undischarged bankrupt

(c) all the partners or directors, as the case may be, are not ineligible under clauses (c), (d), (e), (f), (g), (h), (i), (j) and (k) of sub-rule (1);

(d) three or all the partners or directors, whichever is lower, of the partnership entity or company, as the case may be, are not registered valuers; or

(e) none of its partners or directors, as the case may be, is a registered valuer for the asset class, for the valuation of which it seeks to be a registered valuer.

Qualifications and experience (Rule 4)

An individual shall have the following qualifications and experience to be eligible for registration under rule 3, namely: -

(a) post-graduate degree or post-graduate diploma, in the specified discipline, from a University or Institute established, recognised or incorporated by law in India and at least three years of experience in the specified discipline thereafter; or

(b) a Bachelor's degree or equivalent, in the specified discipline, from a University or Institute established, recognised or incorporated by law in India and at least five years of experience in the specified discipline thereafter; or

(c) membership of a professional institute established by an Act of Parliament enacted for the purpose of regulation of a profession with at least three years' experience after such membership.

Explanation-I: For the purposes of this clause the 'specified discipline' shall mean the specific discipline which is relevant for valuation of an asset class for which the registration as a valuer or recognition as a registered valuers organisation is sought under these rules.

Explanation-II: Qualifying education and experience for various asset classes is given in an indicative manner in Annexure-IV of these rules.

Explanation-III: for the purposes of this rule and Annexure IV, 'equivalent' shall mean professional and technical qualifications which are recognised by the Ministry of Human Resources and Development as equivalent to professional and technical degree.

Valuation examination & certificate of registration (Rule 5 & 6)

(1) An individual who passes the valuation examination shall receive the acknowledgment of passing the examination.

(2) After submitting necessary papers along with application for examination, the authority upon satisfaction may grant the certificate of registration to the applicant to carry out activities of registered valuer.

Conditions of Registration (Rule 7)

The registration granted under rule 6 shall be subject to the conditions that the valuer shall -

(a) at all times possess the eligibility and qualification and experience criteria as specified under rule 3 and rule 4;

(b) at all times comply with the provisions of the Act , these rules and the Bye-laws or internal regulations, as the case may be, of the respective registered valuers organisation;

(c) in his capacity as a registered valuer, not conduct valuation of the assets or class(es) of assets other than for which he/it has been registered by the authority;

(d) take prior permission of the authority for shifting his/ its membership from one registered valuers organisation to another;

(e) take adequate steps for redressal of grievances;

(f) maintain records of each assignment undertaken by him for at least three years from the completion of such assignment;

(g) comply with the Code of Conduct of the registered valuers organisation of which he is a member;

(h) in case a partnership entity or company is the registered valuer, allow only the partner or director who is a registered valuer for the asset class(es) that is being valued to sign and act on behalf of it;

(i) in case a partnership entity or company is the registered valuer, it shall disclose to the company concerned, the extent of capital employed or contributed in the partnership entity or the company by the partner or director, as the case may be, who would sign and act in respect of relevant valuation assignment for the company;

(j) in case a partnership entity is the registered valuer, be liable jointly and severally along with the partner who signs and acts in respect of a valuation assignment on behalf of the partnership entity;

(k) in case a company is the registered valuer, be liable alongwith director who signs and acts in respect of a valuation assignment on behalf of the company;

(l) in case a partnership entity or company is the registered valuer, immediately inform the authority on the removal of a partner or director, as the case may be, who is a registered valuer along with detailed reasons for such removal; and

(m) comply with such other conditions as may be imposed by the authority.

Conduct of valuation (Rule 8)

(1) The registered valuer shall, while conducting a valuation, comply with the valuation standards as notified or modified under rule 18:

Provided that until the valuation standards are notified or modified by the Central Government, a valuer shall make valuations as per-

(a) internationally accepted valuation standards;

(b) valuation standards adopted by any registered valuer's organisation.

(2) The registered valuer may obtain inputs for his valuation report or get a separate valuation for an asset class conducted from another registered valuer, in which case he shall fully disclose the details of the inputs and the particulars etc. of the other registered valuer in his report and the liabilities against the resultant valuation, irrespective of the nature of inputs or valuation by the other registered valuer, shall remain of the first mentioned registered valuer.

(3) The valuer shall, in his report, state the following: -

(a) background information of the asset being valued;

(b) purpose of valuation and appointing authority;

(c) identity of the valuer and any other experts involved in the valuation;

(d) disclosure of valuer interest or conflict, if any;

(e) date of appointment, valuation date and date of report;

(f) inspections and/or investigations undertaken;

(g) nature and sources of the information used or relied upon;

(h) procedures adopted in carrying out the valuation and valuation standards followed;

(i) restrictions on use of the report, if any;

(j) major factors that were taken into account during the valuation;

(k) conclusion; and

(l) caveats, limitations and disclaimers to the extent they explain or elucidate the limitations faced by valuer, which shall not be for the purpose of limiting his responsibility for the valuation report.

Functions of a Valuer (Rule 10)

A valuer shall conduct valuation required under the Act as per these rules.

Eligibility for Registered Valuers Organisations (Rule 12)

(1) An organisation that meets requirements under sub-rule (2) may be recognised as a registered valuers organisation for valuation of a specific asset class or asset classes if

(i) it has been registered under section 25 of the Companies Act, 1956 (1 of 1956) or section 8 of the Companies Act, 2013 (18 of 2013) with the sole object of dealing with matters relating to regulation of valuers of an asset class or asset classes;

(ii) it is a professional institute established by an Act of Parliament enacted for the purpose of regulation of a profession; Provided that, subject to sub-rule (3), the following organisations may also be recognised as a registered valuers organisation for valuation of a specific asset class or asset classes, namely:-

(a) an organisation registered as a society under the Societies Registration Act, 1860 or any relevant state law, or;

(b) an organisation set up as a trust governed by the Indian Trust Act, 1882.

(2) The organisation referred to in sub-rule (1) shall be recognised if it –

(a) conducts educational courses in valuation, in accordance with the syllabus determined by the authority, under rule 5, for individuals who may be its valuers' members, and delivered in class room or through distance education modules and which includes practical training;

(b) grants membership or certificate of practice to individuals, who possess the qualifications and experience as specified in rule 4, in respect of valuation of asset class for which it is recognised as a registered valuers organisation;

(c) conducts training for the individual members before a certificate of practice is issued to them;

(d) lays down and enforces a code of conduct for valuers who are its members;

(e) provides for continuing education of individuals who are its members;

(f) monitors and reviews the functioning, including quality of service, of valuers who are its members; and

(g) has a mechanism to address grievances and conduct disciplinary proceedings against valuers who are its members.

(3) A registered valuers organisation, being an entity under proviso to sub-rule (1), shall convert into or register itself as a company under section 8 of the Companies Act, 2013, within one year from the date of commencement of these rules.

Model Code of Conduct for Registered Valuers

Integrity and Fairness

1. A valuer shall, in the conduct of his/its business, follow high standards of integrity and fairness in all his/its dealings with his/its clients and other valuers.
2. A valuer shall maintain integrity by being honest, straightforward, and forthright in all professional relationships.
3. A valuer shall endeavour to ensure that he/it provides true and adequate information and shall not misrepresent any facts or situations.
4. A valuer shall refrain from being involved in any action that would bring disrepute to the profession.
5. A valuer shall keep public interest foremost while delivering his services.

Professional Competence and Due Care

6. A valuer shall render at all times high standards of service, exercise due diligence, ensure proper care and exercise independent professional judgment.
7. A valuer shall carry out professional services in accordance with the relevant technical and professional standards that may be specified from time to time
8. A valuer shall continuously maintain professional knowledge and skill to provide competent professional service based on up-to-date developments in practice, prevailing regulations/guidelines and techniques.
9. In the preparation of a valuation report, the valuer shall not disclaim liability for his/its expertise or deny his/its duty of care, except to the extent that the assumptions are based on statements of fact provided by the company or its auditors or consultants or information available in public domain and not generated by the valuer.
10. A valuer shall not carry out any instruction of the client insofar as they are incompatible with the requirements of integrity, objectivity and independence.
11. A valuer shall clearly state to his client the services that he would be competent to provide and the services for which he would be relying on other valuers or professionals or for which the client can have a separate arrangement with other valuers.

Independence and Disclosure of Interest

12. A valuer shall act with objectivity in his/its professional dealings by ensuring that his/its decisions are made without the presence of any bias, conflict of interest, coercion, or undue influence of any party, whether directly connected to the valuation assignment or not.
13. A valuer shall not take up an assignment if he/it or any of his/its relatives or associates is not independent in terms of association to the company.
14. A valuer shall maintain complete independence in his/its professional relationships and shall conduct the valuation independent of external influences.

15. A valuer shall wherever necessary disclose to the clients, possible sources of conflicts of duties and interests, while providing unbiased services.

16. A valuer shall not deal in securities of any subject company after any time when he/it first becomes aware of the possibility of his/its association with the valuation, and in accordance with the Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015 or till the time the valuation report becomes public, whichever is earlier.

17. A valuer shall not indulge in "mandate snatching" or offering "convenience valuations" in order to cater to a company or client's needs.

18. As an independent valuer, the valuer shall not charge success fee.

19. In any fairness opinion or independent expert opinion submitted by a valuer, if there has been a prior engagement in an unconnected transaction, the valuer shall declare the association with the company during the last five years.

Confidentiality

20. A valuer shall not use or divulge to other clients or any other party any confidential information about the subject company, which has come to his/its knowledge without proper and specific authority or unless there is a legal or professional right or duty to disclose.

Information Management

21. A valuer shall ensure that he/ it maintains written contemporaneous records for any decision taken, the reasons for taking the decision, and the information and evidence in support of such decision. This shall be maintained so as to sufficiently enable a reasonable person to take a view on the appropriateness of his/its decisions and actions.

22. A valuer shall appear, co-operate and be available for inspections and investigations carried out by the authority, any person authorised by the authority, the registered valuers organisation with which he/it is registered or any other statutory regulatory body.

23. A valuer shall provide all information and records as may be required by the authority, the Tribunal, Appellate Tribunal, the registered valuers organisation with which he/it is registered, or any other statutory regulatory body.

24. A valuer while respecting the confidentiality of information acquired during the course of performing professional services, shall maintain proper working papers for a period of three years or such longer period as required in its contract for a specific valuation, for production before a regulatory authority or for a peer review. In the event of a pending case before the Tribunal or Appellate Tribunal, the record shall be maintained till the disposal of the case.

Gifts and hospitality

25. A valuer or his/its relative shall not accept gifts or hospitality which undermines or affects his independence as a valuer.

    Explanation. -For the purposes of this code the term 'relative' shall have the same meaning as defined in clause (77) of Section 2 of the Companies Act, 2013 (18 of 2013).

26. A valuer shall not offer gifts or hospitality or a financial or any other advantage to a public servant or any other person with a view to obtain or retain work for himself/ itself, or to obtain or retain an advantage in the conduct of profession for himself/ itself.

Remuneration and Costs

27. A valuer shall provide services for remuneration which is charged in a transparent manner, is a reasonable reflection of the work necessarily and properly undertaken, and is not inconsistent with the applicable rules.

28. A valuer shall not accept any fees or charges other than those which are disclosed in a written contract with the person to whom he would be rendering service.

Occupation, employability and restrictions.

29. A valuer shall refrain from accepting too many assignments, if he/it is unlikely to be able to devote adequate time to each of his/ its assignments.

30. A valuer shall not conduct business which in the opinion of the authority or the registered valuer organisation discredits the profession.

THE SECURITIES AND EXCHANGE BOARD OF INDIA (ISSUE OF CAPITAL AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2018

Face Value of Equity Shares (Regulation 27)

The disclosure about the face value of equity shares shall be made in the draft offer document, offer document, advertisements and application forms, along with the price band or the issue price in identical font size.

Pricing (Regulation 28)

(1) The issuer may determine the price of equity shares, and in case of convertible securities, the coupon rate and the conversion price, in consultation with the lead manager(s) or through the book building process, as the case may be.

(2) The issuer shall undertake the book building process in the manner specified in Schedule XIII.

Price and price band (Regulation 29)

(1) The issuer may mention a price or a price band in the off er document (in case of a fixed price issue) and a floor price or a price band in the red herring prospectus (in case of a book built issue) and determine the price at a later date before filing the prospectus with the Registrar of Companies:

Provided that the prospectus filed with the Registrar of Companies shall contain only one price or the specific coupon rate, as the case may be.

(2) The cap on the price band, and the coupon rate in case of convertible debt instruments, shall be less than or equal to one hundred and twenty per cent. of the floor price.

Provided that the cap of the price band shall be at least one hundred and five percent of the floor price.

(3) The floor price or the final price shall not be less than the face value of the specified securities.

(4) Where the issuer opts not to make the disclosure of the floor price or price band in the red herring prospectus, the issuer shall announce the floor price or the price band at least two working days before the opening of the issue in the same newspapers in which the pre-issue advertisement was released or together with the pre-issue advertisement in the format prescribed under Part A of Schedule X.

(5) The announcement referred to in sub-regulation (4) shall contain relevant financial ratios computed for both upper and lower end of the price band and also a statement drawing attention of the investors to the section titled “basis of issue price” of the offer document.

(6) The announcement referred to in sub-regulation (4) and the relevant financial ratios referred to in sub-regulation (5) shall be disclosed on the websites of the stock exchange(s) and shall also be pre-filled in the application forms to be made available on the websites of the stock exchange(s).

Differential Pricing (Regulation 30)

(1) The issuer may offer its specified securities at different prices, subject to the following:

(a) retail individual investors or retail individual shareholders or employees entitled for reservation made under regulation 33 may be offered specified securities at a price not lower than by more than ten per cent. of the price at which net offer is made to other categories of applicants, excluding anchor investors;

(b) in case of a book-built issue, the price of the specified securities offered to the anchor investors shall not be lower than the price offered to other applicants;

(c) In case the issuer opts for the alternate method of book building in terms of Part D of Schedule XIII, the issuer may offer the specified securities to its employees at a price not lower than by more than ten per cent. of the floor price.

(2) Discount, if any, shall be expressed in rupee terms in the offer document.

Pricing of Frequently Traded Shares (Regulation 164)

(1) If the equity shares of the issuer have been listed on a recognised stock exchange for a period of 90 trading days or more as on the relevant date, the price of the equity shares to be allotted pursuant to the preferential issue shall be not less than higher of the following:

a. The 90 trading days 'volume weighted average price of the related equity shares quoted on the recognised stock exchange preceding the relevant date; or

b. the 10 trading days' volume weighted average prices of the related equity shares quoted on a recognised stock exchange preceding the relevant date.

Provided that if the Articles of Association of the issuer provide for a method of determination which results in a floor price higher than that determined under these regulations, then the same shall be considered as the floor price for equity shares to be allotted pursuant to the preferential issue.

(2) If the equity shares of the issuer have been listed on a recognised stock exchange for a period of less than 90 trading days as on the relevant date, the price of the equity shares to be allotted pursuant to the preferential issue shall be not less than the higher of the following:

a) the price at which equity shares were issued by the issuer in its initial public offer or the value per share arrived at in a scheme of compromise, arrangement and amalgamation under sections 230 to 234 the Companies Act, 2013, as applicable, pursuant to which the equity shares of the issuer were listed, as the case may be; or

b) the average of the volume weighted average prices of the related equity shares quoted on the recognised stock exchange during the period the equity shares have been listed preceding the relevant date; or

c) the average of the 10 trading days' volume weighted average prices of the related equity shares quoted on a recognised stock exchange during the two weeks preceding the relevant date. [Provided that if the Articles of Association of the issuer provide for a method of determination which results in a floor price higher than that determined under these regulations, then the same shall be considered as the floor price for equity shares to be allotted pursuant to the preferential issue.

(3) Where the price of the equity shares is determined in terms of sub-regulation (2), such price shall be recomputed by the issuer on completion of 90 trading days from the date of listing on a recognised stock exchange with reference to the 90 trading days' volume weighted average prices of the related equity shares quoted on the recognised stock exchange during these 90 trading days and if such

recomputed price is higher than the price paid on allotment, the difference shall be paid by the allottees to the issuer.

Provided that if the Articles of Association of the issuer provide for a method of determination which results in a floor price higher than that determined under these regulations, then the same shall be considered as the floor price for equity shares to be allotted pursuant to the preferential issue.

(4) (a) A preferential issue of specified securities to qualified institutional buyers, not exceeding five in number, shall be made at a price not less than the 10 trading days' volume weighted average prices of the related equity shares quoted on a recognised stock exchange preceding the relevant date.

Provided that if the Articles of Association of the issuer provide for a method of determination which results in a floor price higher than that determined under these regulations, then the same shall be considered as the floor price for equity shares to be allotted pursuant to the preferential issue:

(b) no allotment shall be made, either directly or indirectly, to any qualified institutional buyer who is a promoter or any person related to the promoters of the issuer:

Provided that a qualified institutional buyer who does not hold any shares in the issuer and who has acquired rights in the capacity of a lender shall not be deemed to be a person related to the promoters.

Explanation. —For the purpose of this clause, a qualified institutional buyer who has any of the following rights shall be deemed to be a person related to the promoters of the issuer:-

(a) rights under a shareholders' agreement or voting agreement entered into with promoters or promoter group;

(b) veto rights; or

(c) right to appoint any nominee director on the board of the issuer.

(5) For the purpose of this Chapter, "frequently traded shares" means the shares of the issuer, in which the traded turnover on any recognised stock exchange during the 240 trading days preceding the relevant date, is at least ten per cent of the total number of shares of such class of shares of the issuer:

Provided that where the share capital of a particular class of shares of the issuer is not identical throughout such period, the weighted average number of total shares of such class of the issuer shall represent the total number of shares.

Explanation: For the purpose of this regulation, 'stock exchange' means any of the recognised stock exchange(s) in which the equity shares of the issuer are listed and in which the highest trading volume in respect of the equity shares of the issuer has been recorded during the preceding 90 trading days prior to the relevant date.

SECURITIES AND EXCHANGE BOARD OF INDIA (SHARE BASED EMPLOYEE BENEFITS AND SWEAT EQUITY) REGULATIONS, 2021

Employee Stock Option Scheme (ESOS)

Pricing-Regulation 17

The company granting options to its employees pursuant to an ESOS shall be free to determine the exercise price subject to conforming to the accounting policies specified in regulation 15 of these regulations.

Accounting Policies - Regulation 15

Any company implementing any of the share-based schemes shall follow the requirements including the disclosure requirements of the Accounting Standards prescribed by the Central Government in terms of section

133 of the Companies Act, 2013 including any 'Guidance Note on Accounting for employee share-based Payments' issued in that regard from time to time.

Employee Stock Purchase Scheme (ESPS)

Pricing and lock-in-Regulation 22

(1) A company may determine the price of shares to be issued under an ESPS, subject to conforming to the accounting policies specified under regulation 15 of these regulations.

(2) Shares issued under an ESPS shall be locked-in for a minimum period of one year from the date of allotment: Provided that in case where shares are allotted by a company under an ESPS in lieu of shares acquired by the employee under an ESPS in another company which has merged or amalgamated with the first mentioned company, the lock-in period already undergone in respect of shares of the transferor company shall be adjusted against the lock-in period required under this sub-regulation. Provided further that in the event of death or permanent incapacity of an employee, the requirement of lock-in shall not be applicable from the date of death or permanent incapacity.

(3) If ESPS is part of a public issue and the shares are issued to employees at the same price as in the public issue, the shares issued to employees pursuant to ESPS shall not be subject to any lock-in.

Issue of Sweat Equity by a Listed Company

Pricing-Regulation 33

The price of sweat equity shares shall be determined in accordance with the pricing requirements stipulated for a preferential issue to a person other than a qualified institutional buyer under the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018.

SECURITIES AND EXCHANGE BOARD OF INDIA (DELISTING OF EQUITY SHARES) REGULATIONS, 2021

Discovered Price-Regulation 20

(1) After fixation of the floor price under sub-regulation (2), the discovered price shall be determined through the reverse book building process in the manner specified in Schedule II of these regulations, and the Manager to the offer shall disclose the same in the detailed public announcement and the letter of offer.

(2) The floor price shall be determined in terms of regulation 8 of Takeover Regulations as may be applicable.

(3) The reference date for computing the floor price would be the date on which the recognized stock exchange(s) was required to be notified of the board meeting in which the delisting proposal was considered and approved.

(4) The acquirer shall have the option to provide an indicative price in respect of the delisting offer, which shall be higher than the floor price calculated in terms of sub-regulation (2).

(5) The acquirer shall also have the option to revise the indicative price upwards before the start of the bidding period and the same shall be duly disclosed to the shareholders.

(6) The acquirer may, if it deems fit, pay a price higher than the discovered price determined in terms of sub-regulation (1).

THE COMPANIES (SHARE CAPITAL AND DEBENTURES) RULES, 2014

Issue of sweat equity shares (Rule 8)

Under the Companies (Share Capital and Debentures) Rules, 2014, the sub rules of rule 8 states that the:

- The sweat equity shares to be issued shall be valued at a price determined by a registered valuer as the fair price giving justification for such valuation.
- The valuation of intellectual property rights or of know how or value additions for which sweat equity shares are to be issued, shall be carried out by a registered valuer, who shall provide a proper report addressed to the Board of directors with justification for such valuation.
- A copy of gist along with critical elements of the valuation report obtained under clause (6) and clause (7) shall be sent to the shareholders with the notice of the general meeting.
- Where sweat equity shares are issued for a non-cash consideration on the basis of a valuation report in respect there of obtained from the registered valuer, such non-cash consideration shall be treated in the following manner in the books of account of the company-
  (a) where the non-cash consideration takes the form of a depreciable or amortizable asset, it shall be carried to the balance sheet of the company in accordance with the accounting standards; or
  (b) where clause (a) is not applicable, it shall be expensed as provided in the accounting standards.

SEBI (SAST) REGULATIONS, 2011

Offer Price

Offer price is the price at which the acquirer announces to acquire shares from the public shareholders under the open offer. The offer price shall not be less than the price as calculated under regulation 8 of the SEBI (SAST) Regulations, 2011 for frequently or infrequently traded shares.

Consolidated FDI Policy 2020

Issue Price of Shares

Price of shares issued to persons resident outside India under the FDI Policy, shall not be less than –

(a) the price worked out in accordance with the SEBI guidelines, as applicable, where the shares of the company are listed on any recognised stock exchange in India;

(b) the fair valuation of shares done by a SEBI registered Merchant Banker or a Chartered Accountant as per any internationally accepted pricing methodology on arm's length basis, where the shares of the company are not listed on any recognised stock exchange in India; and

(c) the price as applicable to transfer of shares from resident to non-resident as per the pricing guidelines laid down by the Reserve Bank from time to time, where the issue of shares is on preferential allotment.

However, where non-residents (including NRIs) are making investments in an Indian company in compliance with the provisions of the Companies Act, as applicable, by way of subscription to its Memorandum of Association, such investments may be made at face value subject to their eligibility to invest under the FDI scheme.

VALUATION REQUIREMENTS UNDER DIFFERENT STATUTES IN INDIA

There are various laws in India which requires valuations from professionals e.g. the Companies Act, 2013, the Insolvency and Bankruptcy Code, 2016, the Indian Accounting Standards (IndAS), the Securities and Exchange Board of India Regulations, the Income Tax Act, 1961 and the Foreign Exchange Management Act, 1999.

Valuations Requirements Under Companies Act, 2013

Under the Companies Act, 2013 the valuations of financial instruments such as shares, securities, business are required for various purpose such as further issue of shares, transactions in kind, Merger and Acquisitions, Corporate Debt Restructuring, purchase of minority and valuation for the companies under winding up.

S.No.	Section and relevant Rules of the Companies Act, 2013	Subject	Role of Registered Valuer
1.	Section 39 & Companies (Prospectus and Allotment of Securities) Rules, 2014	Return of Allotment.	A report of a registered valuer in respect of valuation of the consideration shall also be attached along with the contract in the case of securities (not being bonus shares) allotted as fully or partly paid up for consideration other than cash, there shall be attached to the Form PAS-3 a report of a registered valuer in respect of valuation of the consideration.
2.	Section 54 and Rule 8 of the Companies (Share Capital and Debentures) Rules, 2014	Issue of Sweat Equity Shares by an unlisted company	(i) Sweat Equity Shares issued by unlisted company shall be valued at a price determined by a registered valuer as the fair price giving justification for such valuation. (ii) The valuation of intellectual property rights or of know how or value additions for which sweat equity shares are to be issued, shall be carried out by a registered valuer, who shall provide a proper report addressed to the Board of directors with justification for such valuation.
3.	Section 62 (1) (b) and Rule 16 of the Companies (Share Capital and Debentures) Rules, 2014	Grant of Employee Stock Option or Employee Stock Purchase Scheme	In pursuance of the approved scheme of provision of money for purchase of or subscription for the shares by the trustees in the company or its holding company, where such shares are to be held by or for the benefit of the employees of the company, the valuation at which shares are to be purchased shall be made by a registered valuer, if shares of the company are not listed on a recognized stock exchange.
4.	Section 62(1) (c) and Rule 13 of the Companies (Share Capital and Debentures) Rules, 2014	Issue of Shares on Preferential Basis	Where at any time, an unlisted company having a share capital proposes to increase its subscribed capital by the issue of further shares through preferential allotment, either for cash or for a consideration other than cash, the price of such shares shall be determined by the valuation report of a registered valuer. Such company shall make the disclosures w.r.t. basis on which the price has been arrived at along with report of the registered valuer as well as the justification for the allotment proposed to be made for consideration other than cash together with valuation report of the registered valuer in the explanatory statement to be annexed to the notice of the general meeting pursuant to section 102 of the Act.

			The price of the shares or other securities to be issued on a preferential basis, either for cash or for consideration other than cash, shall be determined on the basis of valuation report of a registered valuer. Where convertible securities are offered on a preferential basis with an option to apply for and get equity shares allotted, the price of the resultant shares pursuant to conversion shall be determined- (i) either upfront at the time when the offer of convertible securities is made, on the basis of valuation report of the registered valuer given at the stage of such offer, or (ii) at the time, which shall not be earlier than thirty days to the date when the holder of convertible security becomes entitled to apply for shares, on the basis of valuation report of the registered valuer given not earlier than sixty days of the date when the holder of convertible security becomes entitled to apply for shares: Where shares or other securities are to be allotted for consideration other than cash, the valuation of such consideration shall be done by a registered valuer who shall submit a valuation report to the company giving justification for the valuation; The price of shares or other securities to be issued on preferential basis shall not be less than the price determined on the basis of valuation report of a registered valuer.
5.	Section 73 & Rule 2 (c) of the Companies (Acceptance of Deposits) Rules, 2014	Acceptance of Deposits	"Deposit" includes any receipt of money by way of deposit or loan or in any other form, by a company, but does not include – (ix) any amount raised by the issue of bonds or debentures secured by a first charge or a charge ranking pari passu with the first charge on any assets referred to in Schedule III of the Act excluding intangible assets of the company or bonds or debentures compulsorily convertible into shares of the company within ten years: Provided that if such bonds or debentures are secured by the charge of any assets referred to in Schedule III of the Act, excluding intangible assets, the amount of such bonds or debentures shall not exceed the market value of such assets as assessed by a registered valuer.
6.	Section 73 & Rule 6 of the Companies (Acceptance of Deposits) Rules, 2014	Creation of Security	For the purposes of providing security, every company referred to in sub-section (2) of section 73 and every eligible company inviting secured deposits shall provide for security by way of a charge on its assets as referred to in Schedule III of the Act excluding intangible assets of the company for the due repayment of the amount of deposit and interest thereon for an amount which shall not be less than the amount remaining unsecured by the deposit insurance:

			Provided that in the case of deposits which are secured by the charge on the assets referred to in Schedule III of the Act excluding intangible assets, the amount of such deposits and the interest payable thereon shall not exceed the market value of such assets as assessed by a registered valuer.
7.	Section 192 of the Companies Act, 2013	Restriction on Non-cash Transactions Involving Directors	No company shall enter into an arrangement by which— (a) a director of the company or its holding, subsidiary or associate company or a person connected with him acquires or is to acquire assets for consideration other than cash, from the company; or (b) the company acquires or is to acquire assets for consideration other than cash, from such director or person so connected unless prior approval for such arrangement is accorded by a resolution in general meeting of the company including holding company if director or connected person belong to holding company. The notice for approval of the resolution by the company or holding company in general meeting shall include the particulars of the arrangement along with the value of the assets involved in such arrangement duly calculated by a registered valuer.
8.	Section 230	Power to Compromise or Make Arrangements with Creditors and members	Where a compromise or arrangement is proposed— (a) between a company and its creditors or any class of them; or (b) between a company and its members or any class of them, the Tribunal may, on the application of the company or of any creditor or member of the company, or in the case of a company which is being wound up, of the liquidator, appointed under this Act or under the Insolvency and Bankruptcy Code, 2016, as the case may be," order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal directs. The company or any other person, by whom such application is made, shall disclose to the Tribunal by affidavit any scheme of corporate debt restructuring consented to by not less than seventy-five per cent of the secured creditors in value, including—a valuation report in respect of the shares and the property and all assets, tangible and intangible, movable and immovable, of the company by a registered valuer.

	Rule 3 of the Companies (Compromises, Arrangements and Amalgamations) Rules	Application for order of meeting of the Companies	An application of arrangement for takeover offer shall contain: - (a) the report of a registered valuer disclosing the details of the valuation of the shares proposed to be acquired by the member after taking into account the following factors: - (i) the highest price paid by any person or group of persons for acquisition of shares during last twelve months; (ii) the fair price of shares of the company to be determined by the registered valuer after taking into account valuation parameters including return on net worth, book value of shares, earning per share, price earning multiple vis-d-vis the industry average, and such other parameters as are customary for valuation of shares of such companies.
	Section 234 and Rule 25A of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016	Merger or amalgamation of a foreign company with a Company and vice versa	The transferee company shall ensure that valuation is conducted by valuers who are members of a recognised professional body in the jurisdiction of the transferee company and further that such valuation is in accordance with internationally accepted principles on accounting and valuation. So, if transferee company is an Indian Company, then valuation will be conducted by Registered Valuer.
	Section 236 & Rule 27 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016	Determination of price for purchase of minority shareholding	In the event of an acquirer, or a person acting in concert with such acquirer, becoming registered holder of ninety per cent. or more of the issued equity share capital of a company or any person or group of persons becoming ninety per cent. majority or holding ninety per cent. of the issued equity share capital of a company, by virtue of an amalgamation, share exchange, conversion of securities or for any other reason, such acquirer, person or group of persons, as the case may be, shall notify the company of their intention to buy the remaining equity shares. Such acquirer or person acting in concert shall offer to the minority shareholders of the company for buying the equity shares held by such shareholders at a price determined on the basis of valuation by a registered valuer in accordance with such rules as may be prescribed.

			The registered valuer shall determine the price (hereinafter called as offer price) to be paid by such acquirer, person or group of persons for purchase of equity shares of the minority shareholders of the company, in accordance with the following rules: (1) In case of a listed company; (i) The offer price shall be determined in the manner as may be specified by the Securities and Exchange Board Of India under the relevant regulations framed by it, as may be applicable; and (ii) The registered valuer shall also provide a valuation report on the basis of valuation addressed to the board of directors of the company giving justification for such valuation. (2) In the case of an unlisted company and a private company, (i) the offer price shall be determined after taking into account the following factors:- (a) the highest price paid by the acquirer, person or group of persons for acquisition during last twelve months; (b) the fair price of shares of the company to be determined by the registered valuer after taking into account valuation parameters including return on net worth, book value of shares, earning per share, price earning multiple vis-à-vis the industry average, and such other parameters as are customary for valuation of shares of such companies; and (ii) the registered valuer shall also provide a valuation report on the basis of valuation addressed to the board of directors of the company giving justification for such valuation.
	Section 281	Submission of report by Company Liquidator.	(1) Where the Tribunal has made a winding up order or appointed a Company Liquidator, such liquidator shall, within sixty days from the order, submit to the Tribunal, a report containing the following particulars, namely: — (a) the nature and details of the assets of the company including their location and value, stating separately the cash balance in hand and in the bank, if any, and the negotiable securities, if any, held by the company: Provided that the valuation of the assets shall be obtained from registered valuers for this purpose;

Further, Rule 8 of the Companies (Registered Valuers and Valuation) Rules, provides for the requisites w.r.t. conduct of valuation in terms of mandatory contents to be stated by the valuer in his report: -

(a) background information of the asset being valued;

(b) purpose of valuation and appointing authority;

(c) identity of the valuer and any other experts involved in the valuation;

(d) disclosure of valuer interest or conflict, if any;

(e) date of appointment, valuation date and date of report;

(f) inspections and/or investigations undertaken;

(g) nature and sources of the information used or relied upon;

(h) procedures adopted in carrying out the valuation and valuation standards followed;

(i) restrictions on use of the report, if any;

(j) major factors that were taken into account during the valuation;

(k) conclusion; and

(l) caveats, limitations and disclaimers to the extent they explain or elucidate the limitations faced by valuer, which shall not be for the purpose of limiting his responsibility for the valuation report.

Valuation Requirement under the Insolvency and Bankruptcy Code,2016 & IBBI Regulations

S.No.	Section/Regulation	Subject	Provisions w.r.t. Valuation
1.	Regulation 27 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016	Appointment of Registered Valuer	The resolution professional shall, ● within seven days of his appointment but not later than forty-seventh day from the insolvency commencement date, ● appoint two registered valuers, ● to determine the fair value and the liquidation value of the corporate debtor in accordance with regulation 35.
2	Regulation 35 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016	Determination of Fair Value and Liquidation Value	Fair value and liquidation value shall be determined in the following manner: - (a) the two registered valuers appointed under regulation 27 shall submit to the resolution professional an estimate of the fair value and of the liquidation value computed in accordance with internationally accepted valuation standards, after physical verification of the inventory and fixed assets of the corporate debtor; (b) *if in the opinion of the resolution professional, the two estimates of a value are significantly different, he may appoint another registered valuer who shall submit an estimate of the value computed in the same manner; and* (c) the average of the two closest estimates of a value shall be considered the fair value or the liquidation value, as the case may be.

3.	Regulation 38 of the IBBI (Pre-Packaged Insolvency Resolution Process) Regulations, 2021	Appointment of Registered Valuers	The resolution professional shall within three days of his appointment, *appoint two registered* valuers to determine the fair value and the liquidation value of the corporate debtor.
4.	Regulation 35 of the IBBI (Liquidation Process) Regulations, 2016	Valuation of assets intended to be sold	(1) Where the valuation has been conducted under regulation 35 of the IBBI(CIRP) Regulations, 2016 or regulation 34 of the IBBI (Fast Track CIRP) Regulations, 2017, as the case may be, the liquidator shall consider the average of the estimates of the values arrived under those provisions for the purposes of valuations under these regulations. Liquidator can take the average of the value of earlier two valuers under IBBI(IRPCP) Regulation or if liquidator is of the opinion to get fresh valuation of assets or business, shall obtain valuation report(s) from two Registered valuers ,who estimates the realisable value. (Six manner) Reg 35(2), In cases not covered under sub-regulation (1) or where the liquidator is of the opinion that fresh valuation is required under the circumstances, he shall within seven days of the liquidation commencement date, appoint two registered valuers to determine the realisable value of the assets or businesses under clauses (a) to (f) of regulation 32 of the corporate debtor.
5.	Section 59(3)(b)(ii)	Voluntary liquidation of corporate persons, the solvency declaration along with a report on Valuation	For Voluntary liquidation of corporate persons, the solvency declaration along with a report on Valuation of the assets from Registered Valuer, is to be filed by Corporate Person.
6.	Regulation 3(1)(b)(ii) of the IBBI (Voluntary Liquidation Process) Regulations, 2017	Report of valuation of assets of corporate person	The solvency report along with report of valuation of assets of corporate person prepared by Registered Valuer is to be attached.
7.	Regulation 30 of the IBBI (Bankruptcy Process for Personal Guarantors to Corporate Debtors) Regulations, 2019	Valuation of assets	(2) The registered valuer appointed under sub-regulation (1) shall submit to the bankruptcy trustee the estimates of the realisable value of the asset computed in accordance with internationally accepted valuation standards, after physical verification of the assets of the bankrupt.

Valuation requirements have been mentioned in other statutes/ Regulations like SEBI Regulations, the Income Tax Act, 1961, the Goods and Service Tax Act, 2017, the Foreign Exchange and Management Act, 1999 etc and a Draft Valuers Bill, 2020 has been drafted to establish a National Institute of Valuers (NIV) on basis of recommendations by a Committee of Experts constituted by the Ministry of Corporate Affairs (MCA) to examine the need for an Institutional Framework to regulate and develop valuation as a profession.

VARIOUS EXPRESSION OF VALUE

The definition of "value" is appearing in International Valuation Standards, ICAI Valuation Standards, Indian Accounting Standards and IBBI Regulations. The definition of value is in fact linked with the purpose of valuations. Upon comparison of these definitions one can observe that in all these definitions, it is specially mentioned that the value is an estimated amount or it may be an estimated amount for which an asset or liability should be exchanged or an estimated amount that would be realised on sale of assets or group of assets.

The various expression used for valuation are: -

Fair Market value

Estimated amount for which an *asset* or liability *should* exchange between willing buyer and a willing seller in an arm length transaction after proper marketing the parties acted knowledgeably, prudently and without compulsion. The concept of market value presumes a price negotiated in an open and competitive market where the participants are acting freely.

In other words, fair market value is price at which the property would change hands between a willing buyer and a willing seller, where both are not under any compulsion to buy and sell and they have reasonable knowledge of relevant facts and information. This means that any representative price would not work if it affects buyer's or seller's unique motivations. This would be an example of investment value, defined by real estate terminology as "value to a particular investor based on individual investment requirements."

Fair Value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the valuation date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Thus, fair value is defined as

(i) Exit price: The price that would be received to sell an asset

(ii) Market based: Fair value is determined by transaction between market participants and it is not entity based

(iii) Orderly transaction: A transaction that assumes exposure to the market for a period before the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities; it is not a forced transaction (e.g. a forced liquidation or distress sale)

(iv) Price: The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability.

Book Value

Book value is the historical value, synonymous to shareholders' equity, net worth, and net book value. It is the difference between total assets and the total liabilities appearing in the balance sheet of a company on a particular date. In any balance sheet, assets are recorded at historical costs, while the net of accumulated depreciation and liabilities are recorded at the face value.

Intrinsic Value

Intrinsic value is the real value of a company based on fundamental analysis of qualitative and quantitative factor and does not consider the Market value in any manner. It is measured as the present value of future cash flows from an asset or company by using an appropriate discount rate.

The qualitative factors include company's performance, productivity, business management and market factors. The quantitative factors include financial statement and accounting data. The qualitative and quantitative factors assess in projecting future cash flows, growth rate and appropriate discount rate.

Replacement Value

Replacement value is the current cost of acquiring a similar new property which is likely to produce the nearest equivalent utility to the property being valued. An estimate of replacement cost takes into account how an asset would be replaced with newer materials and current technology. Replacement value is not the same as reproduction value, which is the cost of a duplicate asset, based on current prices. Replacement value and reproduction cost are used in the valuation of tangible assets that do not produce income directly, such as furniture and fixture, office equipment, and so on.

Going Concern Value

Going concern value is the value of a business that is expected to continue to the future. It takes into account various intangible assets of the organization. The intangible elements of going concern value result from successful continuation of business. Factors like trained workforce, brands, formulations, trademarks, recipes (in fast food and eating joints), operational systems, necessary licenses, and so on, generate value for intangible assets, for which substantial costs are incurred by the company. The going concern value is relevant in the decision of mergers and acquisitions. Sometimes, an 'in-place value' is said to be relevant to assets because they are in working condition and they help produce income. For example, a fully depreciated asset can fetch some value because it is in place, functioning satisfactorily and generating cash.

According to ICAI Valuation Standard 102, "Going concern value is the value of a business enterprise that is expected to continue to operate in the future". The intangible elements of Going Concern Value result from factors such as having a trained work force, an operational plant, the necessary licenses, marketing systems, and procedures in place etc

Example of Going-Concern Value For example, suppose that the liquidation value of Widget Corp. is $10 million. This sum represents the current value of inventory, buildings and other tangible assets that can be sold assuming that the company is completely liquidated. However, Widget Corp. as going-concern value could very well be $60 million, as the compan's reputation of being the world's leading widget producer and its ownership of patents and associated rights for widget production mean that the company should have a large and steady stream of future cash flows.

Equity Interest Value

Equity interest of an investor in a business can be considered as an investment. The purchase of an equity interest in a closely held company can be considered as a long-term investment and in a listed company; it can be viewed as short-term investment. The equity investors not only expect to receive the investment (amount invested or principal) back from the company, but also expect to receive a fair return on the investment in the form of dividend. In addition, in the case of listed companies, the investors have an exit route through the stock market. Therefore, capital appreciation is regarded as an important part of return. This can be expressed in terms of the equation.

$$\text{Return on equity investment} = \frac{\text{Cash Flow (dividend) + closing market price - opening market price}}{\text{opening market price}}$$

Insurable Value

Insurable value is the value of destructible portion of an asset that requires to be insured to indemnify the owner in the event of loss. This type of value has significant relevance, sometimes in M&A decisions as insurance reduces the risk of the property. Of course, post-acquisition review of insurance coverage of property can be done with little impact on the valuation.

For example, in case of a real estate property, the insurable interest will mostly be the market value of the property. However, the insurable value does not include the land on which the property stands.

Value-in-use and Value-in-exchange

Value-in-use or value-in-exchange is a condition under which certain assumptions are made in valuing assets. It is associated with assets that are already in productive use and can be described as the value of an asset, for a particular use or to a particular user, as part of a going concern. However, it is important to understand the concept since the value of acquired assets (especially furniture, fixtures, equipment, and premises) in M&A transactions is influenced significantly by their use in the post-acquisition period. When specific assets used by any going business are valued, it is generally assumed that those assets will remain in their most productive use. Value-in exchange is opposite to value-in-use; it relates to the value of a property or an asset exchanged for itself, and separate from an operating entity. Typically, the value-in-exchange is less than the value-in-use of an asset in a going business enterprise.

Goodwill Value

The term goodwill is defined as an asset representing the future economic benefits arising from a business, business interest or a group of assets, which has not been separately recognised in other assets. (ICAI Valuation Standard-101)

Goodwill is a specific type of intangible asset that arises when a business as a whole has value greater than the value of its identified intangible assets. Goodwill is also the sum total of imponderable qualities of a company which attract the customers to a business and it makes the stakeholders of the company give continued patronage. From M&A perspective, the value of goodwill is calculated as the difference between the price paid for an acquired business and the fair market value of the assets acquired (both tangible and separately identified intangible) and the net of the liabilities. The concept of goodwill value has important applicability to banks for tax, financial reporting, and regulatory reasons.

Salvage Value

Salvage value is the amount that can be realised upon sale or disposal of an asset after it is found no longer useful to the current owner and is to be taken out of service. This is not as era value, which is no more useful to any one for any purpose. Knowledge of salvage value in the target company is significant for any acquisition decision.

Liquidation Value

According to IVS 104 Bases of Value: Liquidation Value is the amount that would be realised when an asset or group of assets are sold on a piecemeal basis. Liquidation Value should take into account the costs of getting the assets into saleable condition as well as those of the disposal activity.

“Liquidation Value” according to IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, Clause 2(k) means the estimated realizable value of the assets of the corporate debtor, if the corporate debtor were to be liquidated on the insolvency commencement date.

According to ICAI Valuation Standard 102 (Valuation Bases), Liquidation value is the amount that will be realised on sale of an asset or a group of assets when an actual/hypothetical termination of the business is contemplated/ assumed. Liquidation value can be carried out

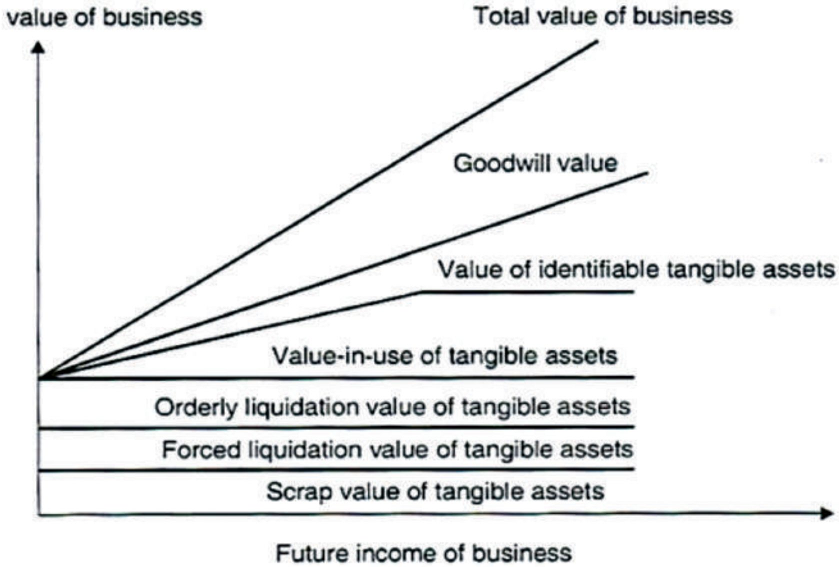
(i) under the premise of an orderly transaction with a typical marketing period; or

(ii) under the premise of forced transaction with a shortened marketing period.

The valuer must disclose whether an orderly or forced transaction is assumed. The net amount is determined after considering estimated cost of disposal.

RELATIONSHIP AMONG DIFFERENT TYPES OF VALUE

Relationship among different types of value and future income.



The relationship among the various types of values discussed earlier in the context of total business value or enterprise value. The diagram exhibits how different levels of future income of a business affect the various types of value.

- The *lowest expected value* of a business is the *scrap value of tangible assets*, which is the same no matter what the income level is of the enterprise. The scrap value of equipment is constant, at a given point in time, irrespective of the earnings of the business that owns it.
- *Forced liquidation value* is the *second lowest potential value*, but from a practical point of view, this is perhaps the lowest value a business as a whole. Like scrap value, forced liquidation value remains the same, no matter what the income of the enterprise.
- *Orderly liquidation value* is conceptually identical to forced liquidation, except that a higher value is usually received because more time is allowed to find a buyer.
- *Value-in-use* of the tangible assets typically increases with the income of the business up to the point at which the value-in-use equals the replacement value of the asset.
- At zero income, the value-in-use and orderly liquidation value are theoretically equivalent, but as the business becomes more successful, the importance of the tangible assets becomes more significant. Hence, value-in-use exceeds orderly liquidation value.
- The value of identifiable intangible assets also tends to increase as the income of the business increases Along with the tangible assets and the income of the business, the importance of the identifiable intangibles also grows. *Goodwill value* will always increase with the earnings of the business because it is computed as the difference between the value of the total business and the value of the tangible and identified intangible assets. Consequently, as the earnings of the business grow, so does its total goodwill and enterprise value. The cumulative result is therefore the total business value. This is the value of the tangible and intangible assets, and it increases along with the future income prospects of the business.

PRICE AND VALUE DIFFERENTIATION

Generally, the term value and price are used interchangeably. However, both are different terms having different meaning. Price is determined by demand and supply of underlying asset while valuation is a process of estimating economic worth of a given asset or undertaking which depends upon the purpose of valuation as well as judgement of valuer. Price is the valuable consideration for which a thing is bought and sold. Most of the time, price and value differ indicating differences in perceptions between the buyers and sellers. The fact that price obtained for an asset differs from its valuation does not necessarily indicate that the valuation was wrong. It may arise because the purchaser is unaware of the availability of the asset or the buyer believes that the price is lower than the worth of the asset. A reverse situation may also arise when the seller feels that the price he is charging is much above the worth of the asset.

In essence, the difference between the price obtained and the valuation is the result of only the market imperfections and not necessarily indicate imperfections in the valuation process. The difference may arise because the valuer has adopted advisory approach rather than act as impartial appraiser of value. Owing to the complexities and interrelationships of value, purpose of valuation, methodologies used and information considered, rarely will two valuers value the same company at the same amount. The subjective components involved in the valuation, even though mitigated by professional judgment and experience, can hardly be eliminated.

PROCESS OF VALUATION

Valuation is a process used to determine the economic value of a company, asset, or investment opportunity. The process typically involves several steps, methodologies, and considerations. Here's a general outline of the valuation process:

1. *Gather Information:* Collect all relevant data about the company or asset being valued. This includes financial statements, market trends, industry benchmarks, and any other pertinent information.

2. *Select Valuation Method:* Choose the appropriate valuation method based on the nature of the asset and the purpose of the valuation. Common valuation methods include:

   - Comparable Company Analysis (CCA): Compares the target company to similar publicly traded companies to determine a valuation multiple.

   - Comparable Transactions Analysis (CTA): Examines recent transactions involving similar companies to estimate the value of the target company.

   - Discounted Cash Flow (DCF) Analysis: Calculates the present value of future cash flows generated by the company.

   - Asset-Based Valuation: Determines the value of a company based on the value of its assets minus liabilities.

3. *Conduct Financial Analysis:* Analyze the financial statements of the company, including the income statement, balance sheet, and cash flow statement. This helps assess the company's historical performance, growth prospects, and financial health.

4. *Perform Market Analysis:* Evaluate the industry and market conditions in which the company operates. Consider factors such as competition, regulatory environment, technological advancements, and market trends.

5. *Apply Valuation Methodology:* Utilize the selected valuation method to calculate the value of the company or asset. This may involve applying financial ratios, estimating future cash flows, or adjusting for market comparable.

6. *Consider Risk Factors:* Assess the risks associated with the company or investment opportunity. Factors such as market volatility, operational risks, competitive landscape, and regulatory compliance can impact valuation.

7. *Sensitivity Analysis:* Conduct sensitivity analysis to evaluate how changes in key assumptions or variables affect the valuation results. This helps identify the sensitivity of the valuation to different scenarios.

8. *Finalize Valuation Report*: Prepare a comprehensive valuation report summarizing the analysis, methodologies used, key assumptions, and valuation conclusions. The report should be well-documented and clearly communicate the rationale behind the valuation.

9. *Review and Validation*: Review the valuation report for accuracy and consistency. Validate the results by seeking feedback from other stakeholders or industry experts if necessary.

10. *Present Findings*: Present the valuation findings to relevant parties, such as company management, investors, lenders, or regulatory authorities. Be prepared to address any questions or concerns raised during the presentation.

11. *Update Valuation*: Periodically review and update the valuation as conditions change, such as significant events, changes in market dynamics, or new information becoming available.

For carrying out any valuations, the valuer has to look into the purpose of valuation. The next step will be to finalise the Bases of Value/Premises and accordingly the valuation approaches and methods will be decided by considering various factors.

The steps involved in valuation process are:

- Purpose of valuation
- Bases of Value
- Premises of Value
- Business Valuation Approaches
- Determination of Required Value
- Documentation
- Preparation of Valuation Report.

The purposes of valuation are important because different methods of valuations produce different values. Before a valuation exercise is undertaken, the valuer has to define the purpose of each valuation in clear terms. In fact, there is no single method of valuation that can be universally applied to all valuation purposes. Unless carefully done, a business valuation may fail to arrive at a conclusive valuation figure. The valuer may fail to match the valuation methodology with the purpose for which it is being done. The value conclusion can become useless if it is used for a purpose other than that intended for. Valuations, especially business valuations, are needed for different purposes and their purpose is to have an impact on the type of value derived and the methodologies adopted.

As already mentioned, different statutes have laid down provisions w.r.t. valuation standards to be adopted for the purpose of valuation like IVS in IBC,2016, formulae-based valuation in case of listed companies having frequent trading of shares and Income Tax Act,1961 regarding issue of shares by a closely held company or transfer of shares.

For any valuation the "Bases of value" describe the fundamental premises on which the reported values will be based. Therefore, it is critical that the basis (or bases) of value be appropriate to the terms and purpose of the valuation assignment. List of Bases of Value have been described in International Valuation Standards IVS 104 and ICAI Valuation Standards, ICAI VS 102. Before commencement of any valuations, the valuer must consider the parameters for selection of bases of like (a) nature of the asset to be valued; (b) scope and purpose of the valuation engagement; (c) valuation date/ measurement date; (d) intended purpose of the valuation; (e) applicable bases /standard of value; (f) applicable premises of value; (g) assumptions and limiting conditions; and (h) applicable governmental regulations.

It has been specifically mentioned that ICAI VS 102 will not be applicable in those cases where a valuer is required to adopt valuation bases that are prescribed either (a) by a Statute/ Regulations; or (b) agreed between the parties.

The Premises of value describes the circumstances of how an asset or liability is used. In a given set of circumstances, a single premise of value may be adopted while in some situations multiple premises of value may be considered.

Accurate valuation requires appropriate application of the available approaches to determine value, a clear understanding of the exact investment in a business that is being sold or acquired, and a clear measure of the returns that the company generates. Business varies in the nature of their operations, the markets they serve, and the assets they own. For this reason, the body of business valuation knowledge has established three primary approaches by which businesses may be appraised.

The three Principal Business Valuation Approaches are:

- Market Approach
- Income approach
- Asset Approach

Market Approach

Market approach is a valuation approach that uses prices and other relevant information generated by market transactions involving identical or comparable (i.e., similar) assets, liabilities or a group of assets and liabilities, such as a business.

In market approach, the valuer has to get reliable information about the comparable or identical asset is traded in the active market and such transactions must be a recent and orderly transaction as well identical or comparable asset(s).

Valuer should not use market approach if:

- the asset has fewer identical or comparable assets
- the asset to be valued or its market comparable are not traded in the active market;
- sufficient information on the comparable transaction(s) is not available;
- there is no recent transaction either in the asset or in the market comparable; or
- there are material differences between the asset to be valued and the market comparable, which require significant adjustments.

Three Valuation methods under the market approach:

- Market Price Method
- Comparable Companies Multiple (CCM) Method
- Comparable Transaction Multiple (CTM) Method

Income Approach

The income business valuation approach is based on the idea of valuing the present value of future economic monetary benefits. This approach estimates business value by considering the present value of future income accruing over a period of time. Present Value of future income is calculated using time value of money concept:

$$FV = PV * (1 + i)^n$$

Where, FV = Future Value

PV = Present Value

i = Periodic Interest rate

n = number of times compounding takes place in a year

The methods most commonly used by business valuation professionals include

(i) the Capitalization of Earnings Method;

(ii) the Discounted Earnings Method (Discounted Cash Flow Method); and

(iii) Dividend Discount Method (used for valuation of shares).

Cost Approach

The cost approach provides an indication of value using the economic principle that a buyer will pay no more for an *asset* than the cost to obtain an *asset* of equal utility, whether by purchase or by construction, unless undue time, inconvenience, risk or other factors are involved. This approach tends to determine the business value on the basis of value of assets of the business. It is specifically useful for asset intensive firms, valuing holding companies as well as distressed entities that are not worth more than their overall net tangible value.

The cost approach should be applied and afforded *significant weight* under the following circumstances:

(a) participants would be able to recreate an *asset* with substantially the same utility as the subject *asset*, without regulatory or legal restrictions, and the *asset* could be recreated quickly enough that a *participant* would not be willing to pay a *significant* premium for the ability to use the subject *asset* immediately (nothing special in the assets).

(b) the asset is not directly income-generating and the not in unique nature of the *asset* makes using an income approach or market approach unfeasible.

The methodologies adopted under cost approach are as under:

- Replacement Cost Method
- Reproduction Cost Method
- Summation Method-Sum of part Method.

PRINCIPLES OF VALUATION

Valuation principles serve as guiding concepts or standards that underpin the process of determining the value of assets, companies, or investments. These principles help ensure that valuations are conducted consistently, objectively, and accurately. Some of the key principles of valuation include:

Principle of Value Maximization: The primary objective of valuation is to determine the maximum value of an asset or investment opportunity. This principle reflects the notion that investors seek to maximize their returns and that asset should be valued based on their potential to generate future cash flows or benefits.

Principle of Market Efficiency: Valuations should take into account market prices and information. In efficient markets, asset prices reflect all available information and are considered fair representations of their intrinsic value. Valuations should consider market dynamics and incorporate relevant market data and trends.

Principle of Risk and Return: Valuations should incorporate the relationship between risk and expected return. Assets with higher risk levels should command higher expected returns to compensate investors for taking on additional risk. Valuations should assess and quantify the risks associated with an investment and adjust the discount rate or required rate of return accordingly.

Principle of Time Value of Money: The time value of money principle recognizes that a dollar received today is worth more than a dollar received in the future due to the opportunity to invest and earn returns. Valuations should discount future cash flows or benefits to their present value using an appropriate discount rate, such as the cost of capital or the risk-free rate.

Principle of Substitution: The principle of substitution suggests that the value of an asset is determined by the cost of acquiring a substitute asset with similar characteristics and utility. This principle is particularly relevant in the valuation of tangible assets and real estate, where the value is often determined by comparing prices of similar properties or assets.

Principle of Arm's Length Transaction: Valuations should be based on hypothetical transactions that would take place between willing and knowledgeable parties, each acting in their self-interest and without undue pressure or compulsion. This principle ensures that valuations reflect fair market value and are not influenced by external factors or special circumstances.

Principle of Consistency: Valuations should be conducted using consistent methodologies, assumptions, and data sources to ensure reliability and comparability. Consistency in valuation practices allows for meaningful comparisons over time and across different assets or companies.

Principle of Transparency and Disclosure: Valuation processes and methodologies should be transparent, well-documented, and disclosed to relevant stakeholders. Transparency enhances credibility and allows stakeholders to understand the basis for the valuation conclusions.

1. The value of anything tends to be determined by the cost of acquiring an equally desirable substitute, and this is known as the principle of substitution.
2. The amount of return (profit) that a business provides to its owner is based on the rate of return expected on the investment. A fundamental relationship exists between the rate of return from an investment and the amount of risk involved in the investment. The greater the risk involved, the greater the required rate of return.

   In other words, the greater the risk that an owner will lose a particular deal, the greater the 'odds' (ROI) that will be placed on that owner. There are various types of investments that carry different levels of risk and, therefore, different potential returns.
3. Many owners of businesses feel that their businesses have- no intangible assets value. Therefore, such businesses are sold and transferred at tangible asset values only. It follows that intangibles exist if a business has excess earnings, and values are determined by capitalizing the excess earnings.
4. The given fact gives rise to two key questions:
   (i) What are excess earnings?
   (ii) What is an appropriate capitalization rate?
   - Excess earnings are the earnings of the company in excess of the average earnings of companies with similar activities and size. But it is difficult to define an appropriate capitalization rate. Today, valuation has become an important topic of interest. Various methods and factors are used in valuing closely held businesses.
   - These methods are not alternatives to one another; but all or many of the methods may need to be considered.
   - Many formulas are tied to 'earnings' rather than 'excess earnings. Earnings are multiplied or capitalized by certain industry factors or 'public' company comparable factors.
   - It is recognized that if 'comparable' factors are not available, then other methods can be used.

5. Valuations cannot be made on the basis of a prescribed formula. There is no means whereby mathematical weights and the various applicable factors in a particular valuation case can be assigned in deriving the fair market value. Thus, no useful purpose is served by taking an average of several factors (for example, book value, capitalized earnings and capitalized dividends) and basing the valuation on the result. Such a process excludes active consideration of other pertinent factors, and the end result cannot be supported by a realistic application of the significant facts in the case except by mere chance.
6. Sometimes, it may not be possible to make a separate appraisal of the tangible and intangible assets of the business. An enterprise has a value on an ongoing concern basis. Whatever intangible values are available, may be measured by the amount by which the appraised value of the tangible assets exceeds the net book value of such assets. In addition to the fundamentals of business valuation, there are other sources of information which valuation professionals should read and/or add to their library in the valuation business assignments. In particular, the valuer should be familiar with the business related texts which may include books, research papers, articles, seminars, and interactions with notable valuation mentors or other business mentors. It is in fact a subject of continuous learning.

HINDRANCES / BOTTLENECKS IN VALUATION

Business valuations are an important aspect of transferring ownership of a closely-held business. Whether buying or selling a business, valuing assets during a divorce or gifting to the next generation, an accurate business valuation can save or make you money. When selling or purchasing a privately-held company, sellers look to maximize their return at a value based on a rose-colored future. Buyers want to purchase at a discounted value based on the business's weaknesses. The right business valuator helps bridge the gap between buyers and sellers, provides a thorough understanding of the company's real value and structures the transition to take maximum advantage of the opportunity. So, when we are in the process of valuing a business, a detailed, comprehensive analysis and the ability to develop accurate projections and assumptions are necessities. Business valuation also requires the application of finance theory in the appropriate places and using professional judgment. Some of the most common hindrances include:

1. Value, as a concept, is ambiguous. An asset has different values depending on the purpose or context. Thus an asset has several values: market value (amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing); fair value (amount that will fairly compensate an owner who was involuntarily deprived of the economic enjoyment of a property where there is neither a willing buyer nor a willing seller); liquidation or forced sale value (amount which may reasonably be expected to be obtained from the sale of a property within a time-frame too short to obtain a value under open market conditions); going concern value (amount ascribed to an established business, not to its constituent parts); investment value (value of a property to a particular investor, or a class of investors for specified investment objectives).
2. Everyone has an opinion of value about a business, a tangible asset, or an intangible asset but actually, the term 'value' means different things to different people. The problems faced by the valuers are enormous. They have to bring forward an appropriate definition of value for a specific valuation. The Webster's dictionary puts value as:

   "A fair return or equivalent in goods, services, or money for something exchanged: the monetary worth of something: marketable price; relative worth, utility, or importance: something intrinsically valuable or desirable."
3. Mathematical certainty or certainty of one output based on specific set of inputs is neither demanded, nor possible in valuation discipline. Being context specific, the value keeps on fluctuating. It is for the valuers to express the value attributed by them to the asset, which is estimated on the basis of the facts drawn from the evidence before them. Valuation is an art more than a science and is an interdisciplinary study drawing upon law, economics, finance, accounting, and investment. It is a procedure, essentially, a bringing together of the economic concept of value and the legal concept of property. Valuation discipline is neither science nor an art; it is a craft, i.e., a skill that one learns by doing. The more one does it, the better one gets at it.

4. Valuation may be considered a science but, to a large extent, valuation variables require inherent subjectivity. In other words, valuation is not a precise science as there is always imperfection in the market. Even in rare instances, where the valuer has perfect knowledge of the market, the market does not have the perfect knowledge of value as well as the valuation methodology and process. On every occasion, there may not be a definitive valuation method or a definitive value conclusion, but every valuation is based only on its circumstances. Right valuation requires logical and methodical approach and careful application of the basic principles. This means that there may not be a prescribed format or a preferred methodology, which is to be adopted always.
5. Any business valuation activity is based on the hypothetical consideration that there is an arm's length sale of a business between a willing buyer and a willing seller, usually for cash. Any valuation theory attempts to search for truth and relates to the practice in order to understand valuation theory.
6. One of the frequent sources of legal confusion between cost and value is the tendency of courts, in common with other persons, to think of value as something inherent in the thing being valued, rather than an attitude of persons toward that thing in view of its estimated capacity to perform a service. Whether or not, as a matter of abstract philosophy, a thing has value except to people to when it has value, is a question that need not be answered for the sake of appraisal theory. Certainly, for the purpose of a monetary valuation, property has no value unless there is a prospect that it can be exploited by human beings.
7. In a business valuation, the value of an interest in business is typically considered to be equal to the future benefits that are to be received from the business, discounted to the present value, at an appropriate discount rate. However, this simple definition of value raises the following issues to be addressed:
   (i) How to define 'benefits'?
   (ii) Future projections may be extremely difficult to make and also very difficult to get interested parties to agree to.
   (iii) What is an appropriate discount rate that reflects the risk inherent in the subject entity
8. Developing reasonable assumptions for projections based on historical trends and expected future occurrences and documenting the reasoning behind those assumption choices.
9. Gathering the appropriate market comparable (both public and private) and documenting the reasoning behind the market comparable choices.
10. Choice of Valuation Standards to be followed.
11. Drafting a comprehensive valuation report.
12. Remaining compliant with International Valuation Standards (IVS) or ICAI Valuation Standards IRS guidelines and other industry standards.

PRINCIPLES OF VALUATION TO BE FOLLOWED BY VALUERS

Core Principles of Valuation	
Ethics	Valuers must follow the ethical principles of integrity, objectivity, impartiality, confidentiality, competence and professionalism to promote and preserve the public trust.
Competency	At the time the valuation is submitted, valuers must have the technical skills and knowledge required to appropriately complete the valuation assignment.
Compliance	Valuers must disclose or report the published valuation standards used for the assignment and comply with those standards.
Basis (ie, Type or Standard) of Value	Valuers must select the basis (or bases) of value appropriate for the assignment and follow all applicable requirements. The basis of value (or bases) must be either defined or cited.

Core Principles of Valuation	
Date of Value-Effective Date/Date of Valuation	Valuers must disclose or report the date of value that is the basis of their analyses, opinions or conclusions. Valuers must also state the date they disclose or report their valuation
Assumptions and Conditions	Valuers must disclose significant assumptions and conditions specific to the assignment that may affect the assignment result.
Intended Use	Valuers must disclose or report a clear and accurate description of the intended use of the valuation.
Intended User(s)	Valuers must disclose or report a clear and accurate description of the intended user(s) of the valuation
Scope of Work	Valuers must determine, perform, and disclose or report a scope of work that is appropriate for the assignment that will result in a credible valuation
Identification of Subject of Valuation	Valuers must clearly identify what is being valued.
Data	Valuers must use appropriate information and data inputs in a clear and transparent manner so as to provide a credible valuation.
Valuation Methodology	Valuers must properly use the appropriate valuation methodology (ies) to develop a credible valuation.
Communication of Valuation	Valuers must clearly communicate the analyses, opinions and conclusions of the valuation to the intended user(s).

LESSON ROUND-UP

- Valuation is a process of appraisal or determination of the value of certain assets: tangible or intangible, securities, liabilities and a specific business as a going concern or any company listed or unlisted or other forms of organization, partnership or proprietorship. Business valuation requires a working knowledge of a variety of factors, and professional judgment and experience.
- Valuation may be considered a science but, to a large extent, valuation variables require inherent subjectivity.
- Enhanced credibility of the valuation process requires establishing various estimates of values with minimum most possible range between the highest and lowest values arrived at though various methods.
- Valuation is a vital subject which will be used in different areas like merger & acquisition, amalgamation, acquisition, dispute resolution etc.
- The subject of the valuation is of vital importance to the valuation process, the selection of inputs and approach and method.
- The main objectives of corporate valuation are to assist a purchaser or a seller in deciding the acceptable purchase consideration & assist an arbitrator in settling a dispute between parties.
- Developing reasonable assumptions for projections based on historical trends and expected future occurrences and documenting the reasoning behind those assumption choices is a bottleneck during valuation process.
- Accurate valuation requires appropriate application of the available approaches to determine value, a clear understanding of the exact investment in a business that is being sold or acquired, and a clear measure of the returns that the company generates.
- The three types of Business Valuation Approaches are Income approach, Market Approach & Asset Approach.

- The income business valuation approach is based on the idea of valuing the present value of future benefits. The capitalization method basically divides the business expected earnings by the so-called 'capitalization rate'. DCF expresses the present value of the business as a function of its future cash earnings capacity. In this method, the appraiser estimates the cash flows of any business after all operating expenses, taxes, and necessary investments in working capital and capital expenditure is being met.
- Market Approach refers to the notion of arriving at the value of a company by comparing it to the market value of similar publicly listed companies. Fair Market Value (FMV) is, in its simplest expression, the price that a person reasonable interested in buying a given asset would pay to a person reasonably interested in selling it for the purchase of the asset or asset would fetch in the marketplace.
- Broadly, there are three cost approach methods: (1) Replacement cost method: a method that indicates value by calculating the cost of a similar asset offering equivalent utility, (2) Reproduction cost method: a method under the cost that indicates value by calculating the cost to recreating a replica of an asset, and (3) Summation method: a method that calculates the value of an asset by the addition of the separate values of its component parts. Care is to be taken about deducting depreciation/obsolescence.

TEST YOURSELF

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. What is the purpose of valuation?
2. Discuss the core principle of valuation.
3. In which circumstances, income-based approach to valuation useful.
4. "Valuation is an important aspect in merger and acquisition". Comment
5. How is Swap Ratio determined in merger and acquisition?

LIST OF FURTHER READINGS/REFERENCES

- Ready Reckoner for Valuers by CA Harish Chander Dhamija and CA Raveesh Chaudhary
- ICSI RVO Education Material
- ICSI Final Certificate Course on Valuation
- EM on ICAI Valuation Standard 103 Valuation Approaches & Method.

Valuation of Business and Assets for Corporate Restructuring

Lesson 13

KEY CONCEPTS

■ Business Valuation ■ Method of Valuation ■ Takeover ■ Slump Sale ■ Valuation Report

Learning Objectives

To understand:

- Business Valuation and its types
- Circumstances when valuation becomes essential
- Method of Valuation
- Amalgamation
- Valuation for Slump Sale
- Demerger
- Principles and techniques of Reporting
- Swap Ratio

Lesson Outline

- Introduction
- Need of valuation
- Business valuation methods
- Valuation principles and techniques
- Valuation under SEBI (SAST) Regulations, 2011
- Valuation of Slump Sale
- Valuation of demergers
- Principles and techniques of reporting
- Relative valuation
- Swap ratio
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings
- References

BUSINESS VALUATION

Valuation is the process of determining the economic worth of a company/business based on its business model and external environment and supported with reasons and empirical evidence. During valuation, a valuer looks at the company's management, composition of its capital structure, the prospect of future earnings and market value of assets, etc. Proper valuation helps an entity or business make an intelligent decision. In a merger or amalgamation or demerger or acquisition, valuation is essential to fix the value of the shares to be exchanged in a merger or the consideration payable for an acquisition. The valuation plays a very important role during the resolution of existing debts, unlocking of hidden value and assets, introduction of risk capital and in some cases a turnaround of the underlying business can lead to substantial profits on exit from the investments.

The use of different valuation techniques and principles has made valuation a subjective process. Conflict in valuation could result from the choices with respect to any of these namely valuation base or approach or method or technique. In the case of merger, for instance, the asset value can be determined both at the market price and the cost price. A great deal depends upon the rationale of the parties to a transaction and therefore, it is important that the merging parties should first discuss and agree upon the valuation bases, approaches, methods and techniques.

When it comes to merger / amalgamation, calculating the swap ratio is at the core of the valuation process. It is the ratio at which the shares of the acquiring company will be exchanged with the shares of the acquired company. For instance, a swap ratio of 1:2 means that the acquiring company will provide its one share for every two shares of the other company.

Valuation models are used to determine the true value of a business mostly by financial market participants. Business valuation can be for the entire company or a part of the operations of a company. There are tools and methods used for valuation. Usually the valuation is done by analysing the financial statements, the cash flows and other market factors.

Valuation involves financial modelling. This financial model can be different for different entities, as because one financial model for an industry may not be suitable for another industry and the choice of model to use for the industry is subjective.

Valuation Motives

An important aspect in the merger/amalgamation/takeover activity is the valuation aspect. The method of valuation of business, however, depends to a great extent on the acquisition motives. The acquisition activity is usually guided by strategic behavioural motives. The reasons could be

(a) either purely financial (taxation, asset-stripping/correcting valuation errors, financial restructuring involving an attempt to augment the resources base and portfolio-investment) or

(b) business related (expansion/ diversification, addressing poor performance) or

(c) behavioural reasons have more to do with the personal ambitions or objectives (desire to grow big) of the top management.

The expansion and diversification objectives are achievable either by building capacities on one's own or by buying the existing capacities or a combination of both. The decision criteria in such a situation would be the present value of the differential cash flows. These differential cash flows would, therefore, be the limit on the premium which the acquirer would be willing to pay. On the other hand, if the acquisition is motivated by financial considerations (specifically taxation and asset-stripping), the expected financial gains would form the limit on the premium, over and above the price of physical assets in the company. The cash flow from operations may not be the main consideration in such situations. Similarly, a merger with financial restructuring as its objective will have to be valued mainly in terms of financial gains. It would, however, not be easy to determine the level of financial gains because the financial gains would be a function of the use to which these resources are put.

NEED FOR BUSINESS VALUATION

Business valuation refers to the process of determining the economic worth or value of a business or company. It involves assessing the various factors that contribute to the financial value of the business, such as its assets, liabilities, financial performance, market position, and growth potential.

The need for business valuation arises in several situations:

1. Mergers and Acquisitions: Valuation is crucial when companies are considering buying or selling businesses. It helps determine a fair price for the acquisition or sale and enables negotiation between the parties involved.

2. Investment Analysis: Investors, both individual and institutional, require business valuations to assess the potential return on investment and determine if a business is a viable investment opportunity.

3. Financial Reporting: In some cases, businesses need to estimate the value of their assets for financial reporting purposes, such as for accounting standards or compliance requirements.

4. Shareholder Disputes: During shareholder disputes, business valuation can help determine the fair value of shares or ownership interests.

5. Estate Planning: Valuing a business is essential for estate planning and determining the value of business assets to distribute among beneficiaries or for tax purposes.

6. Litigation and Legal Proceedings: Business valuations may be necessary in legal situations, such as divorce settlements, partnership dissolutions, or damage claims.

7. Strategic Planning: Valuations are useful in strategic planning to assess the overall financial health of the business, identify areas for improvement, and make informed decisions about growth strategies or restructuring.

By conducting a business valuation, stakeholders gain insights into the financial worth of the business, which helps them make informed decisions. It provides a foundation for negotiation, investment decisions, and overall strategic planning. Furthermore, business valuation helps ensure fair transactions, protects the interests of stakeholders, and provides a benchmark for future growth and performance evaluations.

Situations requiring Valuation

The following are some of the usual circumstances when valuation of shares or enterprise becomes essential:

1. When issuing shares to public either through an initial public offer or by offer for sale of shares of promoters or for further issue of shares to public.

2. When promoters want to invite strategic investors or for pricing a first issue or a further issue, whether by way of a preferential allotment or rights issue.

3. In making investment in a joint venture by subscription or acquisition of shares or other securities convertible into shares.

4. For making an ‘open offer’ for acquisition of shares.

5. When company intends to introduce a ‘buy back’ or ‘delisting of shares’.

6. In schemes involving mergers/demergers, share valuation is resorted to determine the consideration for the purpose of issue of shares or any other consideration to shareholders or transferor of demerged companies.

7. On directions of Tribunal or or other statutory Authority.

8. For determining fair price for effecting sale or transfer of shares as per Articles of Association of the company.

9. As required by the agreements between two parties.
10. To determine purchase price of a 'block of shares', which may or may not give the holder thereof a controlling interest in the company.
11. To value the interest of dissenting shareholders under a scheme of amalgamation, merger or reconstruction.
12. Conversion of debt instruments into shares.
13. Advancing a loan against the security of shares of the company by the Bank/Financial Institution.
14. As required by provisions of law such as the Companies Act, 2013 or Foreign Exchange Management Act, 1999 or Income Tax Act, 1961 or the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 [the Takeover Code] or SEBI (Buy Back of Securities) Regulations, 2018 or Delisting Guidelines.

Factors Influencing Valuation

Determining the value of a business is a complicated and intricate process. Valuing a business requires the determination of its future earnings potential and the risks inherent to those future earnings. The process of arriving at this value includes a detailed analysis of its mix of physical and intangible assets, and the general economic and industry conditions. Major factors influencing the valuation of a business include:

- debt equity ratio
- nature of business and its growth history
- customer base
- areas of operations
- audited financial statements
- management team and its competency
- litigation and disputes
- related party transactions, etc.

The other salient factors include:

1. The stock exchange price of the shares of the two companies before the commencement of negotiations or the announcement of the bid.
2. Dividends paid on the shares.
3. Relative growth prospects of the two companies.
4. In case of equity shares, the relative gearing of the shares of the two companies. ('gearing' means ratio of the amount of issued preference share capital and debenture stock to the amount of issued ordinary share capital.)
5. Net assets of the two companies.
6. Voting strength in the merged (amalgamated) enterprise of the shareholders of the two companies.
7. Past history of the prices of shares of the two companies.
8. Merger and amalgamation deals can take a number of months to complete during which time valuations can fluctuate substantially. Hence provisions must be made to protect against such swings.

Preliminary Steps in Valuation

A business valuation involves analytical and logical application/analysis of historical/future tangible and intangible attributes of business. The preliminary study to valuation involves the following aspects:

1. Purpose of valuation.
2. Goodwill/Brand name in the market.
3. Business environment of the entity to be valued.
4. Estimation/forecast of future cash flows as accurately as possible.
5. Is company listed on any stock exchange?
6. If listed, whether shares of the company are traded frequently?
7. The industry in which the entity is part of.
8. The industry P/E ratio, past and future growth rate.
9. Who are the competitors locally, internationally?
10. Whether any similar valuation has been done recently
11. The technology concerning the enterprise and its probability of obsolescence.
12. The accepted discounting rate.
13. Study of market capitalization aspects.
14. Identification of hidden liabilities through analysis of material contracts.

BUSINESS VALUATION METHODS

Valuing a business typically involves assessing its assets, liabilities, financial performance, market position, growth potential, and other relevant factors. Several different methods and approaches are used to determine the value of a business, and the choice of method depends on the nature of the business, industry, purpose of the valuation, and available data.

Followings are some commonly used business valuation methods:

1. *Market Approach:* This method determines the value of a business by comparing it to similar businesses that have recently been sold or are publicly traded. It relies on market data and transactions to estimate the value.
2. *Income Approach:* This method values a business based on its expected future income or cash flow. It involves discounting projected future cash flows to their present value using an appropriate discount rate.
3. *Asset Approach:* This method focuses on the value of the assets and liabilities of a business. It assesses the net asset value by subtracting liabilities from the fair market value of the assets.
4. *Multiple-based Approach:* This method uses financial ratios or multiples (such as price-to-earnings ratio or price-to-sales ratio) derived from comparable companies or industry averages to estimate the value of a business.

The choice of valuation method depends on factors such as the purpose of the valuation, the industry in which the business operates, the availability and reliability of data, and the specific circumstances surrounding the valuation.

It's worth noting that business valuation is not an exact science, and different methods may yield different results. Professional valuation experts or appraisers are often hired to conduct thorough and objective business valuations, taking into account all relevant factors and applying their expertise to ensure an accurate and reasonable valuation.

It's important to consult with professionals or conduct in-depth research when conducting a business valuation, as it can have significant implications for decision-making, negotiations, and financial transactions related to the business.

VALUATION PRINCIPLES AND TECHNIQUES FOR MERGER

When conducting a valuation for a merger, there are several principles and techniques that can be applied. Here are some key principles and techniques used in merger valuation:

1. *Comparable Company Analysis:* This technique involves identifying comparable companies in the same industry or sector and analyzing their financial metrics, such as price-to-earnings ratio (P/E), price-to-sales ratio (P/S), or enterprise value-to-EBITDA ratio (EV/EBITDA). The valuation multiples derived from these comparable companies can then be applied to the target company to estimate its value.

2. *Discounted Cash Flow (DCF) Analysis:* DCF analysis is a widely used valuation technique that estimates the present value of a company's future cash flows. It involves projecting the expected cash flows of the merged entity and discounting them back to their present value using an appropriate discount rate, such as the weighted average cost of capital (WACC). The sum of these discounted cash flows represents the estimated value of the merged entity.

3. *Synergy Analysis:* Synergy refers to the potential benefits and cost savings that can be achieved through the merger. It is important to assess and quantify the synergistic effects of the merger, such as increased revenue, cost reductions, economies of scale, or market expansion. These synergies can then be incorporated into the valuation analysis to determine the enhanced value of the merged entity.

4. *Asset-Based Valuation:* This approach involves assessing the value of the tangible and intangible assets of the companies involved in the merger. It includes analyzing the fair market value of assets, such as property, plant, and equipment (PP&E), inventory, intellectual property, and brand value. Liabilities are subtracted from the asset value to derive the net asset value, which forms the basis of the valuation.

5. *Market Capitalization:* Market capitalization is a straightforward valuation technique that calculates the value of a company based on its market price per share multiplied by the number of outstanding shares. In the context of a merger, this technique can be used to determine the relative value of the merging entities and the resulting ownership structure.

6. *Transaction Multiples:* Transaction multiples involve analyzing historical merger and acquisition transactions in the same industry to determine valuation benchmarks. This includes assessing multiples such as the purchase price-to-sales ratio (PP/S), purchase price-to-earnings ratio (PP/E), or enterprise value-to-revenue ratio (EV/Revenue) observed in past transactions. These multiples can then be applied to the financial metrics of the merging entities to estimate their value.

It's important to note that valuing a merger is a complex task, and a combination of multiple valuation techniques is often used to arrive at a reasonable valuation. Professional expertise, careful analysis of financial data, and consideration of industry-specific factors are crucial in accurately valuing the merging entities and assessing the potential value creation resulting from the merger.

ASSET-BASED APPROACH

The Asset-Based Approach is a valuation method that assesses the value of a business based on its net asset value. It involves calculating the fair market value of the company's assets and subtracting its liabilities to arrive at the net asset value.

Illustration:

Let's consider a company called ABC Manufacturing. ABC Manufacturing has the following assets and liabilities:

- Cash and Cash Equivalents: Rs. 100,000
- Accounts Receivable: Rs. 200,000
- Inventory: Rs. 300,000
- Property, Plant, and Equipment: Rs.1,000,000
- Total Assets: Rs. 1,600,000
- Accounts Payable: Rs. 150,000
- Long-Term Debt: Rs. 500,000
- Total Liabilities: Rs. 650,000

To calculate the net asset value using the Asset-Based Approach, we subtract the total liabilities from the total assets:

Net Asset Value = Total Assets - Total Liabilities

Net Asset Value = Rs. 1,600,000 - Rs. 650,000 = Rs.950,000

In this example, the net asset value of ABC Manufacturing is Rs.950,000. This represents the estimated value of the company's assets after deducting its liabilities.

It's important to note that the Asset-Based Approach may not capture intangible assets such as intellectual property, brand value, or customer relationships, which could significantly impact the overall value of a business. Therefore, this approach is most suitable for asset-intensive industries or situations where the company's tangible assets represent a significant portion of its value.

The Asset-Based Approach is one of several valuation methods, and it's advisable to consider other approaches and factors when conducting a comprehensive business valuation.

Illustration:

Let's assume we're valuing a company called XYZ Services. XYZ Services has the following assets and liabilities:

- Cash and Cash Equivalents: Rs.150,000
- Accounts Receivable: Rs.200,000
- Inventory: Rs. 100,000
- Property, Plant, and Equipment: Rs. 500,000
- Intangible Assets (e.g., patents, trademarks): Rs. 300,000
- Total Assets: Rs.1,250,000
- Accounts Payable: Rs. 100,000
- Long-Term Debt: Rs. 400,000
- Total Liabilities: Rs.500,000

To calculate the net asset value using the Asset-Based Approach, we subtract the total liabilities from the total assets:

Net Asset Value = Total Assets - Total Liabilities Net Asset Value = Rs.1,250,000 - Rs.500,000

Net Asset Value = Rs. 750,000

In this example, the net asset value of XYZ Services is Rs.750,000. This represents the estimated value of the company's assets after deducting its liabilities.

It's important to note that the Asset-Based Approach focuses primarily on tangible assets and may not fully capture the value of intangible assets, such as brand reputation, customer relationships, or intellectual property. Therefore, when using this approach, it's crucial to consider the specific industry, market conditions, and the relevance of intangible assets to get a comprehensive understanding of the business's value.

Please note that business valuation involves various factors and considerations, and the Asset-Based Approach is just one method among several others. It's always advisable to consult with valuation professionals and consider multiple approaches to arrive at a well-rounded assessment of a company's value.

Illustration:

ABC Ltd. has the following values in its books:

Particulars	(₹ in thousand)
Land and building	300
Plant and machinery	200
Inventory	200
Investment	100
Receivables	300
Cash	100
Current liabilities	300
Term loans	200

Land and buildings will fetch 500 more. Plant and machinery will fetch 100 less. Inventory will fetch 50 less. Receivables will fetch 50 less. Current liabilities of 50 will not be payable.

Calculate the net realizable value of this business.

	Book Value	Impairment/Appreciation	Realizable Value
Assets			
Land & Buildings	300	+500	800
Plant & Machinery	200	-100	100
Investments	100		100
Inventory	200	-50	150
Receivables	300	-50	250
Cash	100		100
TOTAL	1200	300	1500
Liabilities			
Bank Borrowings	200		200
Current Liabilities	300	-50	250
		Net Realisable Value	1050

INCOME-BASED APPROACH

In the income-based approach, as the name suggests, value of the business is calculated based on future income flows of the entity. In this approach the most important factor is determination of future cash flows of the business. The more accurate the forecast of cash flows, more correct will be the valuation. The future cash flows of the business are discounted at a predetermined rate to arrive at the present value of the business.

Another way of income approach is based on market capitalisation. In this approach the net earnings are capitalised. For this the earnings before interest and tax depreciation and amortization is considered. Another method used is to look at the price earnings of similar businesses. By comparing similar businesses, model is built and the share price of the company under consideration is estimated.

For example, company-A is in FMCG business, and we want to find out the value of the business. The earnings per share of company-A is Rs. 5.5. Now let us look at businesses in the FMCG industry which are listed on the stock exchange. Company-B has price earnings ratio of 39. Company-C has a price earnings ratio of 45. Another FMCG company-D has a price earnings ratio of 33. The average price earnings ratio of companies B, C and D is 39. Now let us apply this average ratio to company-A's earnings per share. 5.5 × 39 = 214.5. So, the value of the company A per share is Rs. 214.5.

Suppose the earnings of the company is Rs. 2 crore then the value of the company is 2 × 39 equal to Rs. 68 crores. This method of calculation can be tricky because in a volatile market the prices of stocks may fluctuate widely. Moreover, listed companies always have a better valuation because of the liquidity. Normally unlisted companies' evaluation is reduced by 30 to 50%. That is if a listed company's value is Rs. 100 crore then a similar but unlisted company will have a value of only Rs.50 crore with other things remaining same. The price earnings approach is useful in takeovers and mergers.

MARKET BASED APPROACH

Under the market-based approach, we look for a similar business which has changed hands in the recent past and value the target entity on the same basis. If exactly similar business transaction is not available, a closely similar transaction can be taken, and adjustments can be made for any variations in any parameter to arrive at the correct valuation. The adjustments can be for difference in size, quantity, or quality. It is easy to value a company which is publicly traded. However, when a similar company is not available then it becomes necessary to adjust as mentioned above.

There are two popular types of market approach methods, one is based on guideline transaction method and the other based on guideline public method, i.e., publicly traded entity. Market approach method is useful in case of Real Estate Company because we can easily estimate by looking at similar sale transactions. Also, we can look at recent merger and acquisition transactions in the same industry and make adjustments for any size, product or other relevant factor to arrive at the target company valuation. There is also another method called back solve method. This involves analysis of equity transactions of the target entity in the past 12 months with unrelated investors.

Importance of Market-Based Approach

1. **Relies on Real Market Data:** The Market-Based Approach utilizes actual transaction data from the market, providing a real-world benchmark for valuation.

2. **Consideration of Market Perception:** This approach considers how the market perceives the value of similar assets or businesses, reflecting investor sentiment and market dynamics.

3. **Simplicity and Transparency:** Market comparables are relatively easy to understand and transparent, making this approach accessible to a wide range of users.

4. **Validation of Other Methods:** Market-based valuations can serve as a validation or sanity check for other valuation methods, providing additional insight into the value of the subject entity.

Calculation Technique:

The Market-Based Approach involves comparing the subject entity to similar entities or transactions in the market and applying relevant valuation multiples. Common multiples used in the Market-Based Approach include Price-to-Earnings (P/E) ratio, Price-to-Book (P/B) ratio, Price-to-Sales (P/S) ratio, and Price-to-EBITDA (P/EBITDA) ratio.

Illustration:

Let's consider an example of using the Market-Based Approach to value a manufacturing company, AMBA Manufacturing Inc.:

Company Description: AMBA Manufacturing Inc. is a medium-sized manufacturing company producing automotive components.

Valuation Date: December 31, 2023

Comparable Company Transactions:

1. Company A: Similar size and business model as AMBA Manufacturing Inc. Recently sold for $50 million.
2. Company B: Larger than AMBA Manufacturing Inc. with a broader product portfolio. Recently sold for $75 million.
3. Company C: Smaller than AMBA Manufacturing Inc. with a niche market focus. Recently sold for $30 million.

Financial Metrics for AMBA Manufacturing Inc.:

- Net Income for the year ending December 31, 2023: $10 million
- Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA) for the year ending December 31, 2023: $15 million
- Revenue for the year ending December 31, 2023: $100 million

Calculation:

1. Market-Based Approach (P/E Ratio):

   Calculate the Price-to-Earnings (P/E) ratio for each comparable transaction:

   - P/E Ratio for Company A: $50 million / $10 million = 5x
   - P/E Ratio for Company B: $75 million / $X million = Yx
   - P/E Ratio for Company C: $30 million / $X million = Yx

   Apply the average P/E ratio to AMBA Manufacturing Inc.:

   - Average P/E Ratio = (5x + Yx + Yx) / 3

2. Market-Based Approach (P/EBITDA Ratio):

   Calculate the Price-to-EBITDA (P/EBITDA) ratio for each comparable transaction:

   - P/EBITDA Ratio for Company A: $50 million / $15 million = 3.33x
   - P/EBITDA Ratio for Company B: $75 million / $X million = Yx
   - P/EBITDA Ratio for Company C: $30 million / $X million = Yx

   Apply the average P/EBITDA ratio to AMBA Manufacturing Inc.:

   - Average P/EBITDA Ratio = (3.33x + Yx + Yx) / 3

Conclusion:

The Market-Based Approach to valuation provides a comparative analysis of the subject entity to similar entities or transactions in the market. By applying relevant valuation multiples derived from comparable transactions, this approach helps estimate the value of the subject entity based on real market data. However, it's essential to select appropriate comparables and consider qualitative factors to ensure the accuracy and reliability of the valuation.

DISCOUNTED CASH FLOW (DCF) APPROACH

The Discounted Cash Flow (DCF) technique is a widely used method for business valuation. It estimates the present value of a company's projected future cash flows, taking into account the time value of money. The DCF technique involves the following steps:

1. Project Future Cash Flows: Forecast the future cash flows of the business over a specific period. Cash flows typically include operating cash flows, capital expenditures, working capital changes, and any other significant cash flow components.

2. Determine the Discount Rate: Select an appropriate discount rate, often the company's weighted average cost of capital (WACC). The discount rate represents the required rate of return expected by an investor considering the risk associated with the investment. It reflects the opportunity cost of investing in the company rather than alternative investments.

3. Discount Cash Flows: Apply the discount rate to each projected period's cash flow to calculate the present value of the cash flows. This involves dividing each projected cash flow by (1 + discount rate) raised to the power of the respective period.

4. Calculate Terminal Value: Estimate the value of the company beyond the projected period, usually based on a perpetuity or exit multiple. The terminal value represents the value of the business's cash flows beyond the projection period.

5. Sum the Present Values: Sum up the present values of the projected cash flows and the terminal value to obtain the total present value of the future cash flows. This represents the estimated value of the business.

6. Sensitivity Analysis: Perform sensitivity analysis by varying key assumptions such as cash flow projections, discount rate, and terminal value to assess the impact on the estimated value.

7. Compare to Market and Comparable Companies: Consider market conditions, industry trends, and comparable company valuations to evaluate the reasonableness of the estimated value.

It's important to note that the accuracy of the valuation heavily depends on the quality of cash flow projections, appropriate selection of the discount rate, and other assumptions made during the process. The DCF technique requires careful consideration and professional expertise in financial analysis to ensure a comprehensive and accurate valuation of the business.

Illustration:

Assume ABC Manufacturing Company is projected to generate the following cash flows over the next five years:

Year 1: 500,000

Year 2: 600,000

Year 3: 700,000

Year 4: 800,000

Year 5: 900,000

The discount rate for ABC Manufacturing Company is determined to be 10%.

Step 1: Calculate the Present Value (PV) of Cash Flows

PV Year 1 = 500,000 / (1 + 0.10)^1 = 454,545 PV Year 2 = 600,000 / (1 + 0.10)^2 = 495,868 PV Year 3 = 700,000 / (1 + 0.10)^3 = 513,310 PV Year 4 = 800,000 / (1 + 0.10)^4 = 526,446 PV Year 5 = 900,000 / (1 + 0.10)^5 = 535,714

Step 2: Calculate the Sum of PV Cash Flows

Sum of PV Cash Flows = PV Year 1 + PV Year 2 + PV Year 3 + PV Year 4 + PV Year 5 Sum of PV Cash Flows = 454,545 + 495,868 + 513,310 + 526,446 + 535,714

Sum of PV Cash Flows = 2,525,883

Step 3: Determine the Terminal Value

Assume the terminal value is estimated to be 10 million. To calculate the present value of the terminal value, we need to select an appropriate exit year and discount it back to the present value using the discount rate.

Assuming the exit year is Year 5: PV Terminal Value = 10,000,000 / (1 + 0.10)^5 = 6,209,677

Step 4: Calculate the Total Present Value

Total Present Value = Sum of PV Cash Flows + PV Terminal Value Total Present Value = 2,525,883 + 6,209,677 Total Present Value = 8,735,560

In this example, the estimated valuation of ABC Manufacturing Company using the DCF technique is approximately 8,735,560. This represents the present value of the projected cash flows and the terminal value discounted at the appropriate rate. Remember that this is a simplified example, and additional factors, such as growth rates, risk factors, and sensitivity analysis, should be considered for a comprehensive valuation.

VALUATION UNDER SEBI (SAST) REGULATIONS, 2011

The Securities and Exchange Board of India (SEBI) Substantial Acquisition of Shares and Takeovers (SAST) Regulations, 2011, govern the acquisition of shares and control of companies in India. The regulations aim to ensure fair practices and protect the interests of shareholders during the acquisition process. While the SEBI (SAST) Regulations primarily focus on the acquisition of shares, they also include provisions related to valuation. Here are some key aspects of valuation under the SEBI (SAST) Regulations, 2011:

1. Valuation of Shares:
   - Regulation 8 of the SEBI (SAST) Regulations mandates that the acquirer must disclose the highest price paid for the shares of the target company in the 26 weeks preceding the public announcement of the acquisition.
   - If the acquisition involves a preferential issue of shares, the price at which the preferential issue is made must be disclosed.
   - The valuation of shares is important in determining the price to be paid by the acquirer and for assessing the fairness of the transaction.
2. Open Offer Price:
   - Regulation 20 of the SEBI (SAST) Regulations specifies that the open offer price should be determined by the acquirer based on the valuation of the shares of the target company.
   - The open offer price is the price at which the acquirer intends to acquire shares from the public shareholders of the target company.
   - The acquirer must ensure that the open offer price is fair and in compliance with the SEBI (SAST) Regulations.
3. Registered Valuers:
   - The SEBI (SAST) Regulations require the appointment of a registered valuer for determining the valuation of shares.

- Regulation 22 mandates that the valuer must be a merchant banker, registered with SEBI, and should have expertise in valuation.
- The valuer plays a crucial role in assessing the fair value of shares and providing an independent opinion on the valuation.

4. Valuation Report:
   - Regulation 35 of the SEBI (SAST) Regulations requires the acquirer to submit a valuation report to SEBI.
   - The valuation report provides details of the valuation methodology, assumptions, and factors considered in determining the valuation of shares.
   - The report is a crucial document that helps establish the fairness of the acquisition and provides transparency to the regulators and shareholders.

CASE STUDIES

One notable case study in the Indian context is the valuation of Flipkart, a leading e-commerce company in India. Flipkart was founded in 2007 by Sachin Bansal and Binny Bansal and grew rapidly to become one of India's largest online marketplaces. Over the years, the company attracted significant investments from various investors, resulting in multiple valuation rounds. Here is a summary of Flipkart's valuation journey:

Case Study 1:

1. Initial Valuation: In its early stages, Flipkart secured its initial funding from small investors and angel investors. In 2009, the company raised approximately $1 million in its first round of funding at a valuation of around $5 million.

2. Early Growth and Investor Interest: Flipkart experienced significant growth and gained traction in the Indian e-commerce market. As a result, it attracted investments from prominent venture capital firms. In 2010, the company raised $10 million from Accel Partners and Tiger Global Management at a valuation of around $50 million.

3. Continued Expansion and Funding: Flipkart continued to expand its operations and gained market share. The company received multiple rounds of funding in subsequent years. In 2011, Flipkart raised $20 million in a funding round led by Tiger Global Management, valuing the company at around $1 billion.

4. Steady Growth and Billion-Dollar Valuation: Flipkart's growth trajectory remained strong, and it secured significant investments from both existing and new investors. In 2014, the company raised $1 billion in a funding round led by Tiger Global Management, DST Global, and others, valuing Flipkart at approximately $7 billion. This marked the first Indian e-commerce company to achieve a billion-dollar valuation.

5. Valuation Ups and Downs: Flipkart faced intense competition from international players and witnessed increased competition in the Indian e-commerce market. In subsequent years, the company faced some downward adjustments in valuation due to changes in market dynamics and increased competition. For instance, in 2017, SoftBank Vision Fund invested $2.5 billion in Flipkart, valuing the company at around $11.6 billion.

6. Walmart Acquisition: In 2018, US retail giant Walmart acquired a majority stake in Flipkart for $16 billion, valuing the company at approximately $20 billion. This acquisition provided an exit for several early investors and represented one of the largest acquisitions in the Indian startup ecosystem.

The Flipkart case study showcases the valuation journey of an Indian e-commerce company, highlighting the different stages of funding, investor interest, market dynamics, and the impact of competition on the company's valuation. It demonstrates how a startup's valuation can evolve over time based on its growth, performance, and external factors influencing the market.

Case Study 2:

XYZ Tech Solutions is a fast-growing technology company specializing in software development and IT services. The company was founded five years ago and has experienced rapid revenue growth and a strong customer base. The management team is exploring options for fundraising and needs to determine the valuation of the business.

Key Information:

1. Financial Performance:
   - Year 1: Revenue - $2 million, Net Income - $500,000
   - Year 2: Revenue - $3 million, Net Income - $800,000
   - Year 3: Revenue - $5 million, Net Income - $1.2 million
   - Year 4: Revenue - $7 million, Net Income - $1.8 million
   - Year 5: Revenue - $10 million, Net Income - $2.5 million
2. Industry Analysis:
   - Comparable companies in the same industry are trading at an average Price-to-Earnings (P/E) ratio of 15x.
   - The average Enterprise Value-to-Revenue (EV/Revenue) multiple is 2.5x.
3. Discount Rate: 10% The discount rate represents the required rate of return considering the risk associated with the investment.

Solution:

1. Calculate Average Net Income: Average Net Income = (Net Income Year 1 + Net Income Year 2 + Net Income Year 3 + Net Income Year 4 + Net Income Year 5) / 5 Average Net Income = ($500,000 + $800,000 + $1,200,000 + $1,800,000 + $2,500,000) / 5 Average Net Income = $1,360,000
2. Estimate the Earnings Value: Earnings Value = Average Net Income * P/E Ratio Earnings Value = $1,360,000 * 15 Earnings Value = $20,400,000
3. Estimate the Revenue Value: Revenue Value = Revenue Year 5 * EV/Revenue Multiple Revenue Value = $10,000,000 * 2.5 Revenue Value = $25,000,000
4. Calculate Present Value (PV) of Earnings Value: PV of Earnings Value = Earnings Value / (1 + Discount Rate) ^ Number of Years Assuming a projection period of 5 years, PV of Earnings Value = $20,400,000 / (1 + 0.10) ^ 5 PV of Earnings Value = $12,187,365
5. Calculate Present Value (PV) of Revenue Value: PV of Revenue Value = Revenue Value / (1 + Discount Rate) ^ Number of Years Assuming a projection period of 5 years, PV of Revenue Value = $25,000,000 / (1 + 0.10) ^ 5 PV of Revenue Value = $14,911,242
6. Calculate Valuation: Valuation = PV of Earnings Value + PV of Revenue Value Valuation = $12,187,365 + $14,911,242 Valuation = $27,098,607

In this case, the estimated valuation of XYZ Tech Solutions is approximately $27,098,607 based on the average net income, industry multiples, and discount rate applied to both earnings and revenue values. It's important to note that this is a simplified valuation approach, and additional factors, such as the company's growth prospects, market conditions, and competitive landscape, should be considered for a comprehensive valuation analysis.

AMALGAMATION AND VALUATION

Amalgamation refers to the combination of two or more companies into a single entity. It involves the merging of assets, liabilities, and operations of the companies to form a new entity or for one company to absorb another. Valuation plays a crucial role in determining the terms of the amalgamation, including the exchange ratio for the shares of the companies involved.

Valuation in the context of amalgamation involves assessing the value of each company participating in the amalgamation to determine the exchange ratio or share swap ratio. The exchange ratio determines the number of shares of the acquiring company that will be issued in exchange for the shares of the target company. Valuation methods such as the market value approach, asset-based approach, income-based approach, or a combination of these approaches can be used to determine the fair value of the companies involved.

The valuation process typically involves the following steps:

1. *Gather Financial Information:* Collect the financial statements and relevant information of the companies involved, including their assets, liabilities, revenues, and expenses.

2. *Select Valuation Method:* Determine the appropriate valuation method or combination of methods based on the nature of the business, industry standards, and regulatory requirements. Common methods include the market approach, income approach, and asset-based approach.

3. *Perform Valuation Analysis:* Apply the chosen valuation method(s) to assess the value of the companies. This may involve analysing financial statements, forecasting future cash flows, considering market comparable, and applying appropriate valuation multiples or discount rates.

4. *Determine Exchange Ratio:* Once the values of the companies are determined, the exchange ratio or share swap ratio is calculated. The ratio determines how many shares of the acquiring company will be issued for each share of the target company.

5. *Consider Other Factors:* Apart from valuation, other factors such as strategic fit, synergies, and management considerations are also considered during the amalgamation process.

6. *Obtain Approvals:* The valuation results and exchange ratio are presented to the board of directors and shareholders of the companies involved. They must approve the terms of the amalgamation, including the valuation methodology and the exchange ratio.

It's important to note that the specific details and requirements of amalgamation and valuation can vary depending on the jurisdiction, industry, and individual circumstances of the companies involved. Consulting with financial advisors, valuation experts, and legal professionals is recommended to ensure compliance with applicable laws and regulations and to obtain a fair and accurate valuation in the context of an amalgamation.

Case Study:

Assume Company A and Company B are merging through an amalgamation. The financial information of both companies is as follows:

Company A:

- Shareholders' Equity: 10 million
- Total Assets: 20 million
- Total Liabilities: 5 million

Company B:

- Shareholders' Equity: 15 million
- Total Assets: 25 million

- Total Liabilities: 8 million

To determine the exchange ratio for the amalgamation, we will use the book value method, which considers the net asset value of each company.

Step 1: Calculate the Net Asset Value (NAV) of each company:

Company A NAV = Shareholders' Equity of Company A = 10 million

Company B NAV = Shareholders' Equity of Company B = 15 million

Step 2: Determine the Exchange Ratio:

Exchange Ratio = NAV of Company A / NAV of Company B

Exchange Ratio = $10 million / $15 million Exchange Ratio = 0.67

This means that for every share of Company B, 0.67 shares of Company A will be issued in the amalgamation.

Step 3: Assess the Value of Amalgamated Company:

To assess the value of the amalgamated company, we need to consider the post-amalgamation financials.

Assuming the combined assets of the amalgamated company after the merger are 45 million and the total liabilities are 13 million:

Amalgamated Company Shareholders' Equity = Combined Assets - Total Liabilities Amalgamated Company Shareholders' Equity = 45 million - 13 million

Amalgamated Company Shareholders' Equity = 32 million

The value of the amalgamated company will be 32 million.

Step 4: Allocate Shares to Shareholders: Based on the exchange ratio, shareholders of Company B will receive 0.67 shares of Company A for each share of Company B held.

For example, if a shareholder of Company B holds 1,000 shares, they will receive 0.67 * 1,000 = 670 shares of Company A.

Note: This numerical example is simplified and does not consider other factors such as market conditions, synergies, or strategic considerations that could impact the valuation and exchange ratio in a real-world amalgamation. Additionally, professional advice from financial advisors and legal experts should be sought to ensure compliance with applicable regulations and to consider all relevant factors in an actual amalgamation scenario.

SLUMP SALE

A slump sale refers to the transfer of an undertaking, business, or division of a company as a going concern, where all assets and liabilities are transferred as a package to another entity. In a slump sale, the business is sold as a whole, and individual assets and liabilities are not separately identified or valued. The consideration for the slump sale is usually a lump sum amount.

Here's an example to illustrate the concept of a slump sale:

Company A owns and operates a manufacturing division that manufactures and sells electronic devices. Company B is interested in acquiring the entire manufacturing division through a slump sale.

In the slump sale agreement, Company A transfers the entire manufacturing division, including all its assets and liabilities, to Company B. This includes manufacturing equipment, inventory, intellectual property rights, customer contracts, employees, and any other assets and liabilities associated with the division.

The consideration for the slump sale is agreed upon between Company A and Company B. It could be a fixed amount, a combination of cash and shares, or any other form of consideration. The exact terms of the sale, including payment timelines and any warranties or representations, are negotiated and documented in the agreement.

After the slump sale is completed, Company A no longer operates the manufacturing division, and Company B becomes the new owner of the division. Company B assumes all the assets, liabilities, and ongoing operations of the division, including customer relationships, supplier contracts, and any legal or financial obligations.

It's important to note that the tax and legal implications of a slump sale can vary across jurisdictions. It is advisable to consult with tax and legal professionals to ensure compliance with applicable laws and regulations and to understand the specific implications of a slump sale in a particular context.

Slump sale is a strategic transaction used by companies to divest or acquire business divisions as a going concern. It offers advantages such as simplicity, continuity of operations, and tax efficiency. However, careful consideration of accounting and tax implications is essential for both the seller and the buyer to optimize the outcome of the transaction.

Features of Slump Sale

Transfer of Business as a Going Concern: The buyer acquires the business in its entirety, including all assets and liabilities necessary for its operation.

Single Transaction: Slump sale is typically executed as a single transaction, where the entire business is transferred for a lump sum consideration.

No Break in Continuity: The business continues to operate seamlessly after the transfer, ensuring continuity of operations and customer relationships.

Process of Slump Sale

Negotiation and Agreement: The buyer and seller negotiate the terms of the slump sale, including the consideration, assets and liabilities to be transferred, and any conditions precedent.

Due Diligence: The buyer conducts due diligence to assess the assets, liabilities, and potential risks associated with the business being acquired.

Documentation: Legal documents such as the slump sale agreement, transfer deeds, and relevant contracts are drafted and executed to affect the transfer.

Approval and Registration: The slump sale transaction may require approval from regulatory authorities and compliance with statutory requirements. The transfer documents are registered with the appropriate authorities.

Accounting Treatment of Slump Sale:

Purchase Price Allocation: The purchase price is allocated to the assets and liabilities acquired based on their fair values at the date of transfer.

Recognition of Gain or Loss: Any difference between the purchase price and the net assets acquired is recognized as a gain or loss in the financial statements of the seller.

Tax Implications of Slump Sale:

Capital Gains Tax: The seller may be liable to pay capital gains tax on the difference between the sale consideration and the cost of acquisition of the business.

Tax Treatment of Assets and Liabilities: The tax treatment of assets and liabilities transferred in a slump sale may vary based on applicable tax laws and regulations.

Illustration:

Company A sells its manufacturing division to Company B as a slump sale for a lump sum consideration of Rs. 10 million. The fair value of the assets transferred is Rs. 8 million, and the net liabilities assumed by Company B amount to Rs. 2 million.

Solution:

Purchase Price Allocation:

- The purchase price of Rs. 10 million is allocated to the assets and liabilities acquired based on their fair values.
- Assets acquired: Rs. 8 million
- Liabilities assumed: Rs. 2 million

Recognition of Gain or Loss:

- The difference between the purchase price and the net assets acquired represents the gain or loss on the slump sale.
- Gain on Slump Sale = Purchase Price - Net Assets Acquired
- Gain on Slump Sale = Rs. 10 million - (Rs. 8 million – Rs. 2 million) = Rs. 4 million

Tax Implications:

- Company A may be liable to pay capital gains tax on the gain realized from the slump sale transaction.
- The tax treatment of the transaction may vary based on applicable tax laws and regulations in the jurisdiction.

Case Study:

1. Introduction: This case study examines the slump sale of ABC Manufacturing Company, a leading player in the automotive components industry. The slump sale was executed to streamline operations, divest non-core assets, and consolidate resources for the company's core business activities.
2. Background: ABC Manufacturing Company had diversified its operations over the years, expanding into multiple sectors and product lines. However, this diversification had resulted in operational complexities and resource allocation challenges. To refocus on its core competencies and improve profitability, the company decided to undertake a slump sale of non-core business segments.
3. Rationale for Slump Sale: The key reasons for pursuing a slump sale were as follows:
   a. Strategic Focus: The slump sale aimed to enable ABC Manufacturing Company to concentrate its resources and efforts on its core business activities. By divesting non-core assets, the company could redirect its attention to areas where it held a competitive advantage and maximize growth opportunities.
   b. Cost Rationalization: The non-core business segments were associated with additional costs, such as separate management teams, infrastructure, and overhead expenses. Through the slump sale, the company could eliminate these costs and achieve operational efficiencies.
   c. Debt Reduction: In some cases, non-core business segments might have been burdened with significant debt. The proceeds from the slump sale could be utilized to repay debt, thereby strengthening the company's financial position and reducing interest obligations.
4. Slump Sale Process: The slump sale process involved the following steps:
   a. Identification of Non-Core Assets: The management conducted a thorough evaluation of the company's businesses and identified the non-core assets that would be divested. This assessment involved analyzing financial performance, growth prospects, and strategic alignment with the company's long-term objectives.
   b. Valuation and Pricing: The non-core assets were valued based on their fair market value, taking into account factors such as asset condition, market demand, and future cash flows.

The pricing of the slump sale was determined through negotiations with potential buyers or investors.

c. Due Diligence: The potential buyers or investors performed due diligence on the non-core assets to assess their financial, operational, and legal aspects. This step ensured transparency and minimized risks associated with the slump sale.

d. Agreement and Execution: Once the negotiations and due diligence were completed, a formal agreement was drafted, outlining the terms and conditions of the slump sale. The execution of the agreement involved the transfer of ownership and assets, including tangible and intangible assets, contracts, and employees.

e. Post-Sale Transition: Following the slump sale, ABC Manufacturing Company focused on smoothly transitioning the divested business segments to the new owners. This involved ensuring a seamless handover of operations, customer relationships, and support functions.

5. Outcomes and Results: The slump sale of non-core assets yielded several positive outcomes for ABC Manufacturing Company:

   a. Enhanced Focus and Efficiency: By divesting non-core assets, the company could concentrate its resources and expertise on its core business activities. This led to improved operational focus, increased efficiency, and better utilization of available resources.

   b. Improved Financial Performance: The slump sale resulted in a reduction of costs associated with non-core assets, leading to improved financial performance. The company could reallocate capital and reinvest in core business activities, thereby enhancing profitability and shareholder value.

   c. Debt Reduction: If the non-core assets carried significant debt, the proceeds from the slump sale could be utilized to repay debt obligations. This reduced interest expenses and improved the company's overall financial health.

   d. Strategic Alignment: The slump sale allowed ABC Manufacturing Company to align its business portfolio with its long-term strategic objectives. By divesting non-core assets, the company could focus on its core core competencies and capitalize on growth opportunities in its primary market.

6. Conclusion: The slump sale of non-core assets enabled ABC Manufacturing Company to streamline operations, consolidate resources, and improve profitability. By focusing on its core business activities, the company achieved strategic alignment, cost rationalization, and enhanced financial performance, ultimately leading to increased shareholder value.

DEMERGER

Demerger is a corporate restructuring process in which a company transfers one or more of its divisions, subsidiaries, or business units into separate independent entities. In a demerger, the assets, liabilities, and operations of the division or subsidiary are divided and distributed among the newly formed entities or existing companies.

Here's an example to illustrate the concept of a demerger:

Company XYZ is a conglomerate with diverse business operations, including a pharmaceutical division and a real estate division. The company decides to demerge its real estate division into a separate entity called Company R, which will be a standalone real estate company.

The demerger process involves the following steps:

1. *Planning and Announcement:* Company XYZ's management identifies the real estate division as a separate entity with its own growth potential. The decision to demerge the division is made, and the company announces its plans to shareholders and stakeholders.

2. *Valuation and Asset Allocation:* The real estate division's assets, liabilities, and operations are evaluated and valued. The valuation determines the distribution of assets and liabilities between the parent company (Company XYZ) and the new entity (Company R). This may involve conducting a separate business valuation for the real estate division.

3. *Legal and Regulatory Requirements:* Company XYZ complies with legal and regulatory requirements specific to the jurisdiction where the demerger is taking place. This may involve obtaining approvals from shareholders, regulatory authorities, and other relevant parties.

4. *Implementation:* The demerger is executed by transferring the identified assets, liabilities, and operations of the real estate division from Company XYZ to Company R. This could involve transferring property titles, contracts, employees, and other necessary arrangements to ensure the smooth functioning of the new entity.

5. *Shareholder Allocation:* Company XYZ determines how the shares of the newly formed entity (Company R) will be allocated among its existing shareholders. This can be done through a share swap ratio, where shareholders receive shares of the new entity in proportion to their holdings in the parent company.

6. *Independent Operations:* After the demerger, Company R operates as an independent real estate company, having its own management, board of directors, financials, and strategic direction. Company R can raise funds, make investments, and pursue growth opportunities specific to its real estate business.

A demerger allows the parent company to focus on its core operations, while the demerged entity can operate autonomously and pursue its own growth strategies. It can unlock value by creating separate entities with specialized expertise and clearer market positioning.

It's important to note that the specific details and processes of a demerger can vary based on legal requirements, regulatory frameworks, and company-specific considerations. Professional advice from legal, financial, and tax experts should be sought to ensure compliance with applicable laws and to handle the complexities involved in a demerger.

Reasons for Demergers

Focus on Core Business: Companies may opt for demergers to focus on their core competencies and streamline operations.

Unlocking Value: Demergers can unlock the hidden value of distinct business units by allowing them to operate independently and pursue their strategies.

Financial Flexibility: Separate entities can access capital markets and financing opportunities that may not have been available as part of a larger conglomerate.

Types of Demergers

Partial Demerger: Only a portion of the business is spun off into a separate entity.

Complete Demerger: The entire business is divided into separate entities.

Split-up Demerger: The parent company splits into multiple independent entities.

Equity Carve-out: The parent company sells a portion of its subsidiary's shares to the public while retaining control.

Legal and Regulatory Framework

Demergers are subject to various legal and regulatory requirements, including approval from shareholders, creditors, and regulatory authorities. Companies must comply with company law provisions, securities regulations, and taxation laws governing demergers.

Accounting Treatment

Accounting for demergers involves allocating the assets, liabilities, and equity of the parent company among the demerged entities based on their fair values. The process may include adjustments for goodwill, intangible assets, and contingent liabilities.

Taxation Implications

Demergers can have significant tax implications for both the parent company and the spun-off entities. Tax considerations include capital gains tax, stamp duty, transfer pricing, and tax consolidation rules. Companies must carefully plan the demerger structure to optimize tax outcomes.

Illustration 1: Partial Demerger

Company XYZ decides to spin off its software division into a separate entity. The fair value of the software division is Rs.50 million, and its net assets are Rs.40 million. The parent company's shareholders will receive one share in the new entity for every two shares they hold in XYZ.

Calculation:

- Fair value of the software division: Rs.50 million
- Net assets of the software division: Rs.40 million
- Shareholders' entitlement: 1 share in the new entity for every 2 shares in XYZ

Based on the above information, calculate the value of shares received by XYZ shareholders and the accounting treatment for the demerger.

Solution:

1. **Value per share in the new entity:**

   Value per share=Rs.50 million/1/2×Total shares of XYZ

   Since each shareholder receives 1 share in the new entity for every 2 shares in XYZ, the total number of shares issued to XYZ shareholders is 1/2×Total shares of XYZ. Therefore, the value per share in the new entity can be calculated once the total shares of XYZ are known.

2. **Value of shares received by XYZ shareholders:**

   Once we have the value per share in the new entity, we can multiply it by the number of shares each XYZ shareholder holds to find the total value of shares received.

Illustration 2: Tax Implications

In the demerger described in illustration 1, analyse the tax implications for both the parent company and the spun-off entity. Consider capital gains tax, stamp duty, and any other relevant tax considerations.

Solution:

Tax implications vary depending on the jurisdiction, applicable tax laws, and the specific circumstances of the demerger. Here are some potential tax considerations:

1. **Capital Gains Tax (CGT):**

   - The parent company may be subject to CGT on any capital gains realized from the demerger.

- The spun-off entity may also incur CGT if there is a transfer of assets at a value higher than their tax base.

2. **Stamp Duty:**

   - Stamp duty may apply to the transfer of assets or shares as part of the demerger, depending on the jurisdiction.
   - The rate and applicability of stamp duty vary based on the nature of the transaction and the assets involved.

3. **Tax Planning:**

   - Companies may engage in tax planning strategies to minimize the tax impact of the demerger, such as utilizing tax reliefs or exemptions available under the law.
   - Structuring the demerger efficiently can help optimize tax outcomes for both the parent company and the spun-off entity.

4. **Other Tax Considerations:**

   - Other tax considerations may include the treatment of tax losses, transfer pricing rules, and any specific tax incentives or concessions applicable to the industry or business sector.

PRINCIPLES AND TECHNIQUES OF REPORTING

Valuation Report exercise is based on the observation, inspection, analysis, and calculation. During this process, the valuer goes through various documents, records his observation, makes relevant calculation and records these calculations and analyses results. In this process, many documents are generated which forms the basis of his conclusion on the valuation of the subject matter. It is very necessary for him to preserve all such records so that these documents may help him to substantiate his conclusion on valuation. Moreover, all these documents also become the matter of reference in near future.

Contents of Summarized Valuation Report

An expert group of Ministry of Corporate Affairs suggested the following coverage in case of the Valuation Report for Corporate Strategies. Considering the share holder's interest and the need for transparency and upholding corporate governance principles and after taking into consideration aspects of minority interest, transparency and corporate governance the Expert Group recommended that the following matters should compulsorily be covered in the Valuation Report, in a clear, unambiguous and non-misleading manner, consistent with the need to maintain confidentiality:

1. Background Information
2. Purpose of Valuation and Appointing Authority
3. Identity of the valuer and any other experts involved in the valuation
4. Disclosure of valuer Interest/Conflict, if any
5. Date of Appointment, Valuation Date and Date of Report
6. Sources of Information
7. Procedures adopted in carrying out the Valuation
8. Valuation Methodology
9. Major Factors influencing the Valuation

10. Conclusion

11. Caveats, Limitations and Disclaimers.

1. Background Information

The valuation report should briefly cover the following:

- Brief particulars of company or business which is the valuation subject
- Proposed Transaction
- Key historical financials
- Capital structure of the company, if relevant, and any changes because of the proposed transaction
- Shareholding pattern, any significant changes (Promoters/FIs), and any changes as a result of the transaction (Note – a table of before and after shareholding patterns ought to be disclosed)
- High/low/average market volumes/price for last six months, where applicable
- Related party issues with respect to the transaction.

2. Purpose of Valuation & Appointing Authority

The context and purpose of the valuation and the appointing authority commissioning the exercise must be clearly stated e.g. the Management's decision to seek an advisory opinion should be disclosed, or, the Audit Committee Chairman's decision to appoint or the appointment of an independent valuer itself should be disclosed with the date of the decision.

3. Identity of the valuer and any other experts involved in the valuation

Identity of the Registered Valuer (with his registration number) as well as organization doing the valuation and any other experts consulted in the process of valuation. The separation of the advisory team and details of the Chinese walls maintained between the independent valuer team and the advisory team, if appointed with of the degree of strict separation and compliance of Chinese walls should be mentioned.

4. Disclosure of Valuer Interest/Conflict, if any

The Expert Group also recommends that a valuer shall disclose in his Report, possible sources of conflict and material interests, including association or proposed association/with the company, its associates, the counterparty to the transaction or its associates, in the form of auditor, lead advisor or in any other capacity, together with the nature of the fee arrangements for the same. If the valuer has a separate advisory engagement, the conflict disclosure should clearly record that neither the valuer or the members of the team working on the independent valuation have directly or indirectly, through the client or otherwise shared any advisory perspective or have been influenced or undertaken advocating a management position in determining the value.

5. Date of Appointment, Valuation Date and Date of Report

The Report should clearly state the date of the appointment of the valuer, Valuation Date (i.e. the date as of which the valuation assessment is done if this be other than the date of the report) and the date of the report.

6. Sources of Information

The valuer should clearly indicate in the report the principal sources of information, both internal and external, which have been relied upon for the purpose of valuation.

7. **Procedures adopted in carrying out the valuation**

Procedures adopted in carrying out a valuation may vary with circumstances, nature, and purpose of valuation as well as information and time available. The principal procedures adopted by the valuer in carrying out the valuation should be set out briefly in the report. Such procedures may typically include:

- Review of past Financials
- Review and analysis of financial projections
- Industry analysis
- SWOT analysis
- Comparison with similar transactions
- Comparison with other similar listed companies
- Discussions with Management
- Review of principal agreements/documents etc.

The valuer should also include in his report:

- an affirmative statement that information provided and assumptions used by Management/Others in developing projections have been appropriately reviewed and enquiries made regarding basis of key assumptions in the context of analysis of business being valued and the industry/economy; and
- an affirmative statement on adequacy of information and time for carrying out the valuations; with such modifications as may be appropriate and warranted. The affirmative statement shall not negate the professional liability for expertise applied in determining value and if the degree of inadequacy of information is severe, fundamental questions and information as assessed by the valuer as key for the appropriate stage of valuation needs to be disclosed.

8. **Valuation Methodology**

Where as one method may be more or less applicable to a particular case, they are often used in conjunction to arrive at the fair value of a company/asset/business. The following are some of the methods which are often used for valuations. The methods enumerated below are merely illustrative and not exhaustive.

- Asset Approach
- Book Value, Adjusted Book Value, and Liquidation Value
- Income Approach
- Capitalization of Earnings, Capitalization of Excess Earnings, and Discounted Future Earnings/ Cash Flows.
- Market Approach

Current Market Prices, Historical Market Prices, Price to Earnings, Price to Revenue, Price to Book Value, Price to Enterprise Value, etc.

- Comparable transactions/Valuations

Comparable International and Domestic Transactions.

The valuation methodology adopted by the valuer must be disclosed. The valuer should mention in the report the rationale and appropriateness for the adoption of a particular method, or a combination of methods and emphasis/reliance placed on the chosen method/combination of methods in reaching the final conclusion.

9. Major Factors influencing the Valuation

The valuer should also mention any key factors which have a material impact on the valuation of shares, including inter- alia the size or number of the corporate assets or shares, its/their materiality or significance, minority or majority holding and changes on account of the transaction, any impacts on controlling interest, proposed dividend, or past profit of the company, proportion of assets and liabilities, diminution or augmentation therein and marketability or lack thereof.

10. Conclusion

In conclusion, the report must contain clear statement of the value ascribed to the business/assets in question.

11. Caveats, Limitations and Disclaimers

Any caveats, limiting condition or other disclaimers to the report must be clearly stated with appropriate specificity i.e. the valuer shall not disclaim liabilities for his expertise or deny his duty of care.

RELATIVE VALUATION AND SWAP RATIO

Relative valuation is a method of valuing a company or asset by comparing it to similar companies or assets in the same industry or market. It involves analyzing various financial and non-financial metrics of comparable companies and using them as benchmarks to determine the relative value of the target company.

Swap ratio, on the other hand, is the ratio at which shares of one company are exchanged for shares of another company in a merger, acquisition, or demerger. It determines the proportionate ownership of shareholders in the combined or newly formed entity.

In the context of a merger or demerger, the swap ratio is determined based on the relative valuation of the companies involved.

Here's how the swap ratio and relative valuation are interconnected:

1. Relative Valuation Analysis:

    - Comparable Company Analysis: Comparable companies in the same industry are identified, and their financial metrics such as price-to-earnings ratio (P/E ratio), price-to-sales ratio (P/S ratio), or enterprise value-to-EBITDA (EV/EBITDA) are analyzed.
    - Relative Multiples: The financial metrics of the comparable companies are used as multiples. For example, if the average P/E ratio of comparable companies is 15, it implies that investors are willing to pay 15 times the earnings for similar companies.
    - Application to the Target Company: The multiples derived from the comparable company analysis are applied to the target company's financial metrics (such as earnings, sales, or EBITDA) to determine its estimated value.

2. Determining Swap Ratio:

    - Valuation of Companies: The relative valuation analysis helps determine the value of each company involved in the merger or demerger.
    - Negotiation and Agreement: The swap ratio is then negotiated between the companies based on their respective valuations and the ownership stake desired by each party.
    - Share Exchange: The agreed-upon swap ratio determines the number of shares of the acquiring company that will be exchanged for each share of the target company or vice versa.

The swap ratio is typically expressed as a fraction or ratio. For example, a swap ratio of 1:3 means that for every three shares of the target company, the shareholders will receive one share of the acquiring company.

The swap ratio considers the relative value of the companies to ensure a fair exchange of shares between the merging or demerging entities. It takes into account factors such as market conditions, financial performance, growth prospects, synergies, and shareholder interests.

It's important to note that the swap ratio is subject to negotiation and agreement between the companies involved, and it can be influenced by various other factors beyond relative valuation, including strategic considerations, regulatory requirements, and management decisions.

Professional advice from financial advisors, valuation experts, and legal professionals is essential to ensure that the swap ratio is fair and equitable for all parties involved and complies with applicable laws and regulations.

Illustration:

Company XYZ, the parent company, is demerging its subsidiary, SubCo, into a separate entity called NewCo. Let's assume the following information:

1. Company XYZ:
   - Number of outstanding shares: 10 million
   - Market price per share: Rs. 50
2. SubCo:
   - Number of outstanding shares: 5 million
   - Market price per share: Rs.30

To determine the swap ratio, we need to calculate the relative value of SubCo compared to Company XYZ. We can do this by comparing the market capitalization of the two companies.

Market capitalization of Company XYZ = Number of shares * Market price per share = 10 million * 50 = 500 million

Market capitalization of SubCo = Number of shares * Market price per share

= 5 million * 30 = 150 million

Now, let's calculate the swap ratio:

Swap ratio = Market capitalization of SubCo / Market capitalization of Company XYZ = 150 million / 500 million = 0.3

This means that for every 0.3 shares of SubCo, shareholders of Company XYZ will receive one share of NewCo.

Let's assume a shareholder of Company XYZ owns 1,000 shares. Based on the swap ratio, they would receive:

Number of NewCo shares = Number of Company XYZ shares * Swap ratio

= 1,000 * 0.3 = 300 shares of NewCo

Please note that this is a simplified numerical example to demonstrate the concept of a swap ratio in a demerger. The actual swap ratio would depend on various factors, including the valuation of the companies, negotiations, and regulatory requirements.

Case Study -1

Surendra Industries Inc. is a manufacturing company specializing in the production of electronic components. The company has been operating for the past ten years and has established itself as a market leader in its niche.

Valuation Date: December 31, 2023

Financial Information for Surendra Industries Inc.:

- Revenue for the year ending December 31, 2023: Rs.20 million
- Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA) for the year ending December 31, 2023: Rs.4 million
- Net Income for the year ending December 31, 2023: Rs.2.5 million
- Total Assets as of December 31, 2023: Rs.30 million
- Total Liabilities as of December 31, 2023: Rs.10 million
- Weighted Average Cost of Capital (WACC): 8%

Market Information:

- Industry Average Price-to-Earnings (P/E) Ratio: 12
- Industry Average Price-to-EBITDA (P/EBITDA) Ratio: 8

Calculate the valuation of Surendra Industries Inc. using the following methods:

a. Market-Based Approach (based on P/E ratio)

b. Market-Based Approach (based on P/EBITDA ratio)

c. Income-Based Approach (Discounted Cash Flow method)

d. Asset-Based Approach (Net Asset Value method)

Solution:

a. Market-Based Approach (P/E Ratio):

- Calculation:
  - Industry Average P/E Ratio: 12
  - Net Income of Surendra Industries Inc.: Rs.2.5 million
  - Valuation = Net Income x Industry Average P/E Ratio
  - Valuation = Rs.2.5 million x 12
  - Valuation = Rs.30 million

b. Market-Based Approach (P/EBITDA Ratio):

- Calculation:
  - Industry Average P/EBITDA Ratio: 8
  - EBITDA of Surendra Industries Inc.: Rs.4 million
  - Valuation = EBITDA x Industry Average P/EBITDA Ratio
  - Valuation = Rs.4 million x 8
  - Valuation = Rs.32 million

c. Income-Based Approach (Discounted Cash Flow):

- Projection of Future Cash Flows:

- Assume a conservative growth rate of 3% for the next five years.
- Projected Free Cash Flows (FCF) for the next five years:
  - Year 1: Rs.2.5 million x 1.03 = Rs.2.575 million
  - Year 2: Rs.2.575 million x 1.03 = Rs.2.651 million
  - Year 3: Rs.2.651 million x 1.03 = Rs.2.729 million
  - Year 4: Rs.2.729 million x 1.03 = Rs.2.810 million
  - Year 5: Rs.2.810 million x 1.03 = Rs.2.894 million

- Discounting Future Cash Flows:
  - Calculate the present value of projected free cash flows using the WACC of 8%.
  - Present Value (PV) of Future Cash Flows (FCF):
    - PV = FCF / (1 + r)^n
    - Where r is the discount rate (WACC), and n is the number of periods.
- Calculation of Terminal Value:
  - Estimate the terminal value of the business using the perpetuity growth method.
  - Terminal Value (TV) = FCF * (1 + g) / (r - g)
    - Assuming a perpetual growth rate (g) of 2%.
- Discounted Cash Flow (DCF) Valuation:
  - Sum the present value of projected cash flows and the terminal value to determine the total enterprise value (TEV) of the company.

d. Asset-Based Approach (Net Asset Value):

- Calculation:
  - Net Asset Value (NAV) = Total Assets - Total Liabilities
  - NAV = Rs.30 million - Rs.10 million
  - NAV = Rs.20 million

Conclusion:

Based on the above four valuation methods:

- Market-Based Approach (P/E Ratio): Rs.30 million
- Market-Based Approach (P/EBITDA Ratio): Rs.32 million
- Income-Based Approach (DCF): The total enterprise value (TEV) would be the sum of the present value of projected cash flows and the terminal value.
- Asset-Based Approach (Net Asset Value): Rs.20 million

The actual valuation of Surendra Industries Inc. may vary depending on factors such as industry dynamics, market conditions, growth prospects, and qualitative aspects of the business. It's essential to consider multiple valuation methods and factors to arrive at a comprehensive valuation estimate.

Case Study -2

AMBA Tech Solutions Ltd. is a software development company specializing in cloud-based applications. The company has been in operation for five years and has experienced rapid growth in revenue and market share.

Valuation Date: December 31, 2023

Financial Information for AMBA Tech Solutions Ltd.:

- Revenue for the year ending December 31, 2023: Rs.15 million
- Earnings Before Interest and Taxes (EBIT) for the year ending December 31, 2023: Rs.3 million
- Net Income for the year ending December 31, 2023: Rs.2 million
- Total Assets as of December 31, 2023: Rs.25 million
- Total Liabilities as of December 31, 2023: Rs.5 million
- Growth Rate: 15%

Calculate the valuation of AMBA Tech Solutions Ltd. using the Discounted Cash Flow (DCF) method.

Solution:

Discounted Cash Flow (DCF) Method:

1. **Projection of Future Cash Flows:**
   - Assume a growth rate of 15% for the next five years.
   - Projected Free Cash Flows (FCF) for the next five years:
     - Year 1: Rs.2 million x 1.15 = Rs.2.3 million
     - Year 2: Rs.2.3 million x 1.15 = Rs.2.645 million
     - Year 3: Rs.2.645 million x 1.15 = Rs.3.042 million
     - Year 4: Rs.3.042 million x 1.15 = Rs.3.498 million
     - Year 5: Rs.3.498 million x 1.15 = Rs.4.023 million
2. **Discounting Future Cash Flows:**
   - Calculate the present value of projected free cash flows using a discount rate.
   - We'll use the Weighted Average Cost of Capital (WACC) as the discount rate, assuming it's 10%.
   - Present Value (PV) of Future Cash Flows (FCF):
     - PV = FCF / (1 + r)^n
     - Where r is the discount rate (WACC), and n is the number of periods.
3. **Calculation of Terminal Value:**
   - Estimate the terminal value of the business using the perpetuity growth method.
   - Terminal Value (TV) = FCF * (1 + g) / (r - g)
     - Assuming a perpetual growth rate (g) of 5%.
4. **Discounted Cash Flow (DCF) Valuation:**
   - Sum the present value of projected cash flows and the terminal value to determine the total enterprise value (TEV) of the company.

Calculation:

- **Present Value of Future Cash Flows (FCF):**
  - Year 1: PV1 = Rs.2.3 million / (1 + 0.10)^1 = Rs.2.09 million
  - Year 2: PV2 = Rs.2.645 million / (1 + 0.10)^2 = Rs.2.13 million
  - Year 3: PV3 = Rs.3.042 million / (1 + 0.10)^3 = Rs.2.26 million
  - Year 4: PV4 = Rs.3.498 million / (1 + 0.10)^4 = Rs.2.38 million
  - Year 5: PV5 = Rs.4.023 million / (1 + 0.10)^5 = Rs.2.43 million
- **Terminal Value (TV):**
  - TV = Rs.4.023 million * (1 + 0.05) / (0.10 - 0.05) = Rs.104.46 million
- **Discounted Cash Flow (DCF) Valuation:**
  - DCF Valuation = PV1 + PV2 + PV3 + PV4 + PV5 + TV
  - DCF Valuation = Rs.2.09 million + Rs.2.13 million + Rs.2.26 million + Rs.2.38 million + Rs.2.43 million + Rs.104.46 million
  - DCF Valuation ≈ Rs.115.75 million

Conclusion:

Based on the Discounted Cash Flow (DCF) analysis, the total enterprise value (TEV) of AMBA Tech Solutions Ltd. is approximately Rs.115.75 million. This valuation approach accounts for the company's projected future cash flows and terminal value, discounted back to their present values using the weighted average cost of capital (WACC).

LESSON ROUND-UP

- Business valuation is necessitated in many circumstances such as mergers, acquisitions, demerger, takeovers, sale of a division, sale of intangible assets such as brands, patents, technical know-how, Goodwill, etc.
- Broadly there are three approaches to Valuation namely – Asset-based approach, Income-based approach and Market-based approach.
- Asset based valuation method is based on the simple assumption that adding the value of all the assets of the company and subtracting the liabilities, leaving a net asset valuation, can best determine the value of a business.
- Under Income based approach the methods are, Discounted cash flow method, Earnings capitalisation method, Excess earnings method, Incremental cash flows method.
- Under the Market based approach the methods are market price and comparable transaction multiple methods.
- Economic value added is another parameter to measure the financial performance of an enterprise.
- Valuation in takeovers, delisting, ESOPs of listed companies are subject to SEBI regulations.
- Valuation in a slump sale is governed by Income-tax Act, 1961.
- Swap ratio is the exchange ratio in a merger or acquisition between two entities.

GLOSSARY

- In 2018, IDFC Bank and Capital First announced merger between the two to form a combined entity with assets under management of `88,000 crore, branch network of 194 and customer base of over 5 million. As per the agreement, IDFC Bank will issue 139 shares for every 10 shares of Capital First. So, the swap ratio here is 1:13.9.
- The "Discovered Price" is the minimum price per Offer Share payable by the Acquirer for the Offer Shares it acquires pursuant to the Delisting Offer, as determined in accordance with the Delisting Regulations, which will be the price at which the shareholding of the Acquirer Group reaches 90% pursuant to a reverse book-building process conducted in the manner specified in Schedule II of the Delisting Regulations and shall not be lower than the Floor Price.
- Sweat equity shares are issued for consideration other than cash such as technical know-how, brand equity, design, patent or any other intangible asset. The intangible asset could come from promoters or director or even employee of the company.
- The financial performance can be determined by excess earnings of the enterprise over and above the cost of capital. This is known as the "economic value added" (EVA).

TEST YOURSELF

(These are meant for recapitulation only. Answers to these questions are not required to be submitted for evaluation.)

1. What is meant by business valuation?
2. What are the different approaches in business valuation?
3. What are the methods under Asset approach?
4. What are the methods under Income approach?
5. How business valuation is done under market approach?
6. What is slump sale? How the value is determined under the provisions of Income Tax Act, 1961?
7. What is meant by swap ratio? Where is it used?
8. Discuss in detail Contents of Summarized Valuation Report

LIST OF FURTHER READINGS

- Business Valuation in India, Wolters Kluwer Publications
- Valuation by Registered Valuers by Kamal Garg, Bharat's Publication
- Mergers and Acquisitions by Sheeba Kapil, Wiley Publications
- Mergers & Acquisitions and Corporate Valuation by Dr. Manu Sharma, Dreamtech press.

REFERENCES

- International Valuation Standards Council (IVSC) - www.ivsc.org
- American Society of Appraisers (ASA) - www.appraisers.org
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PART III

INSOLVENCY, LIQUIDATION & WINDING UP

Insolvency

Lesson 14

KEY CONCEPTS

■ Insolvency ■ Bankruptcy ■ Liquidation ■ Insolvency and Bankruptcy Board of India ■ Insolvency Professionals ■ Insolvency Professionals Agencies ■ Adjudicating Authority ■ Information utility ■ Corporate Debtor ■ Financial Creditor

Learning Objectives

To understand:

- Historical background of Insolvency Resolution
- Committees on Bankruptcy Reform
- Salient Features of I&B Code
- Pillars of I&B Code

Lesson Outline

- Introduction
- Concept of insolvency and bankruptcy
- Insolvency framework in other countries
- Historical developments in insolvency laws in India
- Need of the Code
- Scheme of the Code
- Pillars under IBC
- Key definitions and concepts
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings
- Other References (Including Websites / Video Links)

REGULATORY FRAMEWORK

- Insolvency and Bankruptcy Code, 2016
- IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016
- IBBI (Liquidation Process) Regulations, 2016
- IBBI (Voluntary Liquidation Process) Regulations, 2017
- IBBI (Insolvency Professionals) Regulations, 2016

INTRODUCTION

The word "bankruptcy" is widely believed to have originated from an Italian phrase "bancarotta"-"banca" means bench and "rotta" means broken. It is believed that the word "bankruptcy" originated from the trade that was carried out on Ponte Vecchio, a medieval segmental arch bridge over the Arno River, in Florence, Italy. In medieval Italy, if a banker, who conducted his market place transactions on a bench, was unable to meet business obligations and was in debt, his bench was broken in a symbolic show of failure and his in ability to continue. This act of "bancarotta" or "breaking the bench" is believed to have evolved into the modern concept of bankruptcy. The role of the law, in a formal bankruptcy process, is to lay down rules of procedure into which the conflict is channelled, and results in a solution. A sound legal framework provides procedural certainty about the process of negotiation, in such a way as to reduce problems of common property and reduce information asymmetry for all economic participants.

The objective of the bankruptcy process is to create a platform for negotiation between creditors and external financiers which can create the possibility of such rearrangements.

Creditors put money into debt investments today in return for the promise of fixed future cash flows. But the returns expected on these investments are still uncertain because at the time of repayment, the seller (debtor) may make repayments as promised, or he may default and does not make the payment. When this happens, the debtor is considered insolvent. Other than cases of outright fraud, the debtor may be insolvent because of

- *Financial failure* - a persistent mismatch between payments by the enterprise and receivables into the enterprise, even though the business model is generating revenues, or
- *Business failure* - which is a breakdown in the business model of the enterprise, and it is unable to generate sufficient revenues to meet payments. Often, an enterprise may be a successful business model while still failing to repay its creditors.

A sound bankruptcy process is one that helps creditors and debtors realise and agree on whether the entity is facing financial failure and business failure. This is important to allow both parties to realise the maximum value of the business in the insolvency.

CONCEPT OF INSOLVENCY, BANKRUPTCY AND LIQUIDATION

The words "Insolvency" and "Bankruptcy" are generally used interchangeably in common parlance but there is a marked distinction between the two. Insolvency and bankruptcy are not synonymous.

The term **"insolvency"** notes the state of one whose assets are in sufficient to pay his debts; or his general inability to pay his debts. The term "insolvency" is used in a

> Section 79(4) of the Insolvency and Bankruptcy Code, 2016 defines the term "bankruptcy" as the state of being bankrupt.
>
> According to Section 79(3) of the Code, **"bankrupt"** means
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> (a) a debtor who has been adjudged as bankrupt by a bankruptcy order under section 126;
>
> (b) each of the partners of a firm, where a bankruptcy order under section 126 has been made against a firm; or
>
> (c) any person adjudged as an undischarged insolvent.

restricted sense to express the inability of a party to pay his debts as they become due in the ordinary course of business.

The word **"bankruptcy"** is the condition of insolvency. It is a legal status of a person or an entity who cannot repay debts to creditors. The bankruptcy process begins with filing of a petition in a court or before an appropriate authority designated for this purpose. The debtor's as sets are then evaluated and used to pay the creditors in accordance with law.

Therefore, while insolvency is the inability of debtors to repay their debts, the bankruptcy, on the other hand, is a formal declaration of insolvency in accordance with law of the land. Insolvency describes a situation where the debtor is unable to meet his/her obligations and bankruptcy occurs when a court determines insolvency, and gives legal orders for it to be resolved. Thus insolvency is a state and bankruptcy is the conclusion. In case of insolvency, one cannot payoff the debts, whereas in the case of bankruptcy, a court order states as how an insolvent person or business has to pay off their debts-by way of selling their assets or erasing the debt that cannot be paid.

The term insolvency is used for individuals as well as organisations/corporates. If insolvency is not resolved, it leads to **bankruptcy** in case of individuals and **liquidation** in case of corporates.

Liquidation, on the other hand, in its general sense, means closure or winding up of a corporation or an incorporated entity through legal process on account of its inability to meet its obligations or to pay its debts. In order to clear the indebtedness, the assets are sold at the most reasonable rates by a competent liquidator appointed in this regard.

INSOLVENCY FRAMEWORK IN UK, USA AND INDIA

United Kingdom

In England, the Act of Parliament of 34 & 35 Henry VIII, c4 is regarded as the first legislation on the subject. Promulgated in 1542 under the reign of Henry VIII, it was a strict and creditor supportive legislation enacted mainly for the benefit of creditors. This Act of 1542, was in fact akin to a criminal statute directed against men who indulged in wasteful expenditures and then refused to pay off debts incurred during the course of extravagance. The 1542 Act looked upon the debtors as offenders. There was no provision for the discharge of debtors and even future earnings of the debtors were not exempt from execution for the debt.

The early bankruptcy laws of England were an instrument of debt-collection and aimed at seizing the debtor's assets against the strong protections to private property offered by the Common law, since medieval times.

In the beginning of the eighteenth century, these strict and creditor supportive medieval laws began to lose its punitive nature. That is why a few authors maintain that the first real bankruptcy laws in England were 4 Anne, c. 17(I705), and 10 Anne, c.15(1711) as unlike earlier statutes which looked upon debtors as offenders, the highlighting feature of the Statutes of Anne was the discharge of the bankrupt who conformed to the provisions of the law. While the additional rights given to the bankrupt under the 1705 Act were significant yet the Act was passed for the sole benefit of the creditors. In contrast, the primary focus of modern insolvency laws is not elimination of insolvent entities but on their rehabilitation and continuation of their business.

The Current Regulatory Framework in UK

The Insolvency Act, 1986 and the Insolvency Rules, 1986 regulate the insolvency framework is the United Kingdom. The Insolvency Act, 1986 was enacted on the recommendation of the Cork Review Committee Report on Insolvency Law and Practice (1982). Prior to the enactment of the Insolvency Act, 1986, the law relating to insolvency in the UK was fragmented and was contained in the Bankruptcy Act, 1914, the Deeds of Arrangement Act, 1914, the Companies Act, 1948 and parts of the County Courts Act, 1959. They Acts were supplemented by the principles of common law and equity.

The Act of 1986 consolidated all

- enactments relating to company insolvency and winding up,

- enactments relating to the insolvency and bankruptcy of individuals, and
- all other enactments bearing on these two subject matters, including the functions and qualification of insolvency practitioners, the public administration of insolvency, the penalisation and redress of malpractice and wrong doing, and the avoidance of certain transactions at an under value.

The Insolvency Act, 1986 deals with the insolvency of individuals and companies and is divided into the following three groups.

- Group 1 deals with Company Insolvency;
- Group 2 deals with Insolvency of Individuals; and
- Group 3 deals with Miscellaneous Matters Bearing on both Company & Individual Insolvency.

The Insolvency Act, 1986 introduced the following three new procedures in order to explore the possibility of bringing a burdened company back to life as a viable entity. These measures in the UK Insolvency Act, 1986 represent an attempt to emulate the 'rescue culture', a characteristic of the corporate sector in the US.

1. *'Company Voluntary Arrangements' (CVAs)*- It provides away where a company in financial difficulty can come to a binding agreement with its creditors. It is are negotiation by a company of the payments due to all of its creditors, or other form of financial restructuring, and is subject to creditors meeting and approval of 75% of the creditors present and voting.
2. *'Administration'*- In this second option, an administrator is appointed by a court to suggest proposals to deal with the company's financial difficulties. This option offers companies a breathing space as the creditors are restrained from taking any action during this period. It is designed to hold a business together while plans are formed, either to put in place a financial restructuring plan to rescue the company, or to sell the business and assets, to produce better results for the creditors, than a liquidation.
3. *'Administrative Receivership'*- This third option permits the appointment of a receiver by certain creditors (normally the holders of a floating charge).

United States of America

America being a colony of the United Kingdom, followed the English bankruptcy system and like the UK system, American bankruptcy laws involved imprisonment until debts were paid or creditors agreed for the release of the debtor. There was no uniform law in America as bankruptcy laws differed from State to State. Some of these American states became in famous as debtor's havens because of their unwillingness to enforce commercial obligations.

The lack of uniformity in bankruptcy and debt enforcement laws adversely affected business and commerce between the states. Article I, Section 8, Clause 4 of the United States Constitution as adopted in the year 1789, made provision for the grant to Congress the power to establish uniform bankruptcy law throughout the United States.

The Congress enacted temporary bankruptcy statutes in 1800, 1841 and 1867 to deal with economic recessions. The Acts of 1800 and 1841 vested jurisdiction in the federal district courts. The district court judges were given the power to appoint commissioners or assignees to take charge of and liquidate a debtor's property. However, these laws were temporary measures and were repealed as soon as economic conditions stabilized.

There was not a permanent bankruptcy law in the United States of America until 1898, when the National Bankruptcy Act was enacted. This Act of 1898 was later amended in 1938 to provide for the rehabilitation of a debtor as an alternative to liquidation of assets. The National Bankruptcy Act, 1898 governed bankruptcy in the United States for 80 years until 1978, when after a thorough review of the then existing law and practice, the Bankruptcy Reform Act, 1978 was enacted.

The Bankruptcy Reform Act, 1978 superseded the National Bankruptcy Act, 1898 and established bankruptcy courts in each district and made provisions for the appointment of separate bankruptcy judges.

The Current Regulatory Framework in USA

"Bankruptcy Code", a federal law, governs bankruptcy in the United States of America. It is a uniform federal law that governs all bankruptcy cases in America. The Bankruptcy Code was enacted in 1978 by § 101 of the Bankruptcy Reform Act, 1978 and is codified as title 11 of the United States Code. The procedural aspects of the bankruptcy process are governed by the Federal Rules of Bankruptcy Procedure (Bankruptcy Rules).

Six basic types of bankruptcy cases are provided for under the Bankruptcy Code.

Chapter 7 titled "Liquidation" - In Chapter 7 Bankruptcy, a court-appointed trustee or administrator takes possession of non-exempt assets, liquidates these assets and then uses the proceeds to pay creditors. He shall be accountable for all the property received and has the right to investigate the financial affairs of the debtor. He shall also file accounts of the administration of the estate with the United States Trustee and the Court.

Chapter 9 titled "Adjustment of Debts of a Municipality". - Chapter 9 Bankruptcy proceedings provides for reorganization which is available to municipalities. In Chapter 9 Bankruptcy proceedings a municipality (which includes cities, towns, villages, counties, taxing districts, municipal utilities, and school districts) get protection from creditors and a municipality can pay back debt through a confirmed payment plan.

Chapter 11 titled "Reorganization" - Unlike Chapter 7 where the business ceases operations and a trustee sells all of its assets, under Chapter 11 the debtor remains in control of its business operations and repay creditors concurrently through a court-approved reorganization plan. Generally, it is a debtor in possession regime. Section 1106 of the Bankruptcy Code requires the trustee, where appointed, to file a plan "as soon as practicable" or, alternatively, to file a report explaining why a plan will not be filed or to recommend that the case be converted to another chapter or dismissed.

Chapter 12 was added to the Bankruptcy Code in 1986. It allows a family farmer or fisherman to continue to operate the business while the plan is being carried out.

Chapter 13 enables individuals with regular income to develop a plan to repay all or part of their debts.

Chapter 15 was added to the Bankruptcy Code in 2005. It provides mechanism for dealing with insolvency cases involving debtors, claimants and other interested parties involving more than one country. Under Chapter 15 are presentative of a corporate bankruptcy proceeding outside the country can get access to the United States courts.

Historical developments of Insolvency Laws in India

The law of Insolvency in India owes its origin to English law. India being a colony of the United Kingdom, followed the English insolvency system. In India, the earliest provisions relating to insolvency can be traced to sections 23 and 24 of the Government of India Act, 1800. These sections conferred insolvency jurisdiction on Supreme Court at Fort Williams (Calcutta), Madras and Recorder's Court at Bombay as the need for an insolvency law was first felt in Presidency Towns of Calcutta, Bombay and Madras where the British majorly carried on their trade. These Courts were empowered to make rules and grant relief to insolvent debtors.

Later insolvency courts were established in the Presidency-Towns when Statute 9 (Geo. IV c. 73) was passed in 1828. This Act of 1828 marks the beginning of special insolvency legislation in India. The insolvency court had a distinct existence although the court was presided over by a Judge of the Supreme Court. The Act of 1828 was originally intended to remain in force for a period of four years but subsequent legislation extended its duration up to 1848. The Provisions of the Indian Insolvency Act was passed in 1848 and remained in force until the enactment of the Presidency Towns Insolvency Act, 1909. Later Provincial Insolvency Act was passed in 1920.

The Presidency Towns Insolvency Act, 1909 and Provincial Insolvency Act, 1920 were two major enactments that dealt with personal insolvency but the two differ in respect of their territorial jurisdiction. While Presidency Towns Insolvency Act, 1909 applied in Presidency towns of Calcutta, Bombay and Madras, the Provincial Insolvency Act, 1920 applied to all provinces of India. These two Acts were applicable to individuals as well as partnership firms.

Insolvency law usually has a two-fold purpose-(i) to give relief to the debtor from the harassment of creditors whose claims he is unable to meet, and (ii) to provide a machinery by which creditors who are not secured in the payment of their debts are to be satisfied.

The Insolvency and Bankruptcy Code, 2016 has repealed both the Presidency Towns Insolvency Act, 1909 and the Provincial Insolvency Act, 1920.

Before the enactment of the Insolvency and Bankruptcy Code, 2016, the provisions relating to insolvency and bankruptcy were fragmented and there was no single law to deal with insolvency and bankruptcy in India. Before the enactment of the Insolvency and Bankruptcy Code, 2016 the following Acts dealt with insolvency and Bankruptcy in India:

- The Presidency Towns Insolvency Act, 1909
- Provincial Insolvency Act, 1920
- Indian Partnership Act, 1932
- The Companies Act, 1956
- The Sick Industrial Companies (Special Provisions) Act, 1985 (SICA)
- The Recovery of Debts due to Banks and Financial Institutions Act, 1993 (RDDBFI Act)
- The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act, 2002)
- The Companies Act, 2013.

Under the Constitution of India 'Bankruptcy & Insolvency' is provided in Entry 9 of List III (Concurrent List) in the Seventh Schedule to the Constitution. Hence both the Centre and State Governments are authorised to make laws on the subject.

Government Committees on Bankruptcy Reforms

Various committees were constituted from time to time by the Government to review the existing bankruptcy and insolvency laws in India. These committees analysed the laws and suggested reforms to bring the law in tune with ever evolving circumstances. Following is a snapshot of various committees constituted along with the outcome.

S.No.	Year	Committee/ Commission	Recommendations/Outcome
1	1964	Third Law Commission	Third Law Commission was established in 1961 under the Chairmanship of Justice J L Kapur. It submitted 26th Law Commission Report in 1964 proposing amendments to the Provincial Insolvency Act, 1920.
2	1981	Tiwari Committee	Following the recommendations of the Tiwari Committee, the Government of India enacted the Sick Industrial Companies (Special Provisions) Act, 1985, (SICA) in order to provide for timely detection of sickness in industrial companies and for expeditious determination of preventive and remedial measures.
3	1991	Narasimham Committee I	The government enacted Recovery of Debts Due to Banks and Financial Institutions (RDDBFI) Act, 1993.

S.No.	Year	Committee/ Commission	Recommendations/Outcome
4	1998	Narasimham Committee II	The committee's recommendations led to the enactment of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFAESI), 2002.
5	1999	Justice Eradi Committee	Recommended setting up of a National Company Law Tribunal (NCLT) and proposed repeal of SICA.
6	2001	NL Mitra Committee	Proposed a comprehensive bankruptcy code.
7	2005	J J Irani Committee	The Committee proposed significant changes to make the restructuring and liquidation process speedier, efficient and effective and accordingly amendments were made to (RDDBFI) Act, 1993 and (SARFAESI), 2002.
8	2008	Raghuram Rajan Committee	Proposed improvements to credit infrastructure.
9	2013	Financial Sector Legislative Reforms Commission	Recommended changes in Indian Financial Sector.
10	2014	Bankruptcy Law Reforms committee (BLRC)	Reviewed the existing bankruptcy and insolvency framework in the country and proposed the enactment of Insolvency and Bankruptcy Code as a uniform and comprehensive legislation on the subject.

Need for a New Law

Before the enactment of the Insolvency and Bankruptcy Code, there was no single law in the country to deal with insolvency and bankruptcy. There were multiple overlapping laws and adjudicating forums dealing with financial failure and insolvency of companies and individuals in India. The framework for insolvency and bankruptcy was inadequate, ineffective and resulted in undue delays in resolution. The legal and institutional framework did not aid lenders in effective and timely recovery or restructuring of defaulted assets and causes undue strain on the Indian credit system.

Prior to the enactment of the Insolvency and Bankruptcy Code, the provisions relating to insolvency and bankruptcy for companies were made in the Sick Industrial Companies (Special Provisions) Act, 1985, the Recovery of Debt Due to Banks and Financial Institutions Act, 1993, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 and the Companies Act, 2013. These statutes provided for creation of multiple fora such as Board of Industrial and Financial Reconstruction (BIFR), Debt Recovery Tribunal (DRT) and their respective Appellate Tribunals. Liquidation of companies was handled by the High Courts. Individual bankruptcy and insolvency was dealt with under the Presidency Towns Insolvency Act, 1909, and the Provincial Insolvency Act, 1920.

The liquidation of companies was handled under various laws and different authorities such as High Court, and Debt Recovery Tribunal had overlapping jurisdiction which was adversely affecting the debt recovery process.

As per World Bank data in 2015, insolvency resolution in India took 4.3 years on an average, which was way higher when compared to other countries such as United Kingdom (1 year) and United States of America (1.5 years). These delays were caused due to time taken to resolve cases in courts, and confusion due to a lack of clarity about the current bankruptcy framework.

The objective of the Insolvency and Bankruptcy Code is to consolidate and amend the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner. An effective legal framework for timely resolution of insolvency and bankruptcy will not only encourage entrepreneurship but will also improve Ease of Doing Business, and facilitate more investments leading to higher economic growth and development.

The Insolvency and Bankruptcy Code, 2016 – Introduction

In India, the legal and institutional machinery for dealing with debt default has not been in line with global standards. The recovery action by creditors, either through the Contract Act or through special laws such as the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 and the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, has not had desired outcomes. Similarly, action through the Sick Industrial Companies (Special Provisions) Act, 1985 and the winding up provisions of the Companies Act, 1956 have neither been able to aid recovery for lenders nor aid restructuring of firms. Laws dealing with individual insolvency, the Presidential Towns Insolvency Act, 1909 and the Provincial Insolvency Act, 1920, are almost a century old. This has hampered the confidence of the lender. When lenders are unconfident, debt access for borrowers is diminished. This reflects in the state of the credit markets in India. Secured credit by banks is the largest component of the credit market in India. The corporate bond market is yet to develop.

The Insolvency and Bankruptcy Code Bill was drafted by a specially constituted "Bankruptcy Law Reforms Committee" (BLRC) under the Ministry of Finance. The Insolvency and Bankruptcy Code was introduced in the Lok Sabha on 21 December 2015 and was subsequently referred to a Joint Committee of Parliament. The Committee submitted its recommendations and the modified Code was passed by Lok Sabha on 5 May 2016. The Code was passed by Rajya Sabha on 11 May 2016 and it received the presidential assent on 28 May 2016.

The objective of the Code is to promote entrepreneurship, availability of credit, and balance the interests of all stakeholders by consolidating and amending the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner and for maximization of value of assets of such persons and matters connected therewith or incidental thereto.

The salient features of the law are as follows:

i. Clear, coherent and speedy process for early identification of financial distress and resolution of companies and limited liability entities if the underlying business is found to be viable.

ii. Two distinct processes for resolution of individuals, namely- "Fresh Start" and "Insolvency Resolution".

iii. Debt Recovery Tribunal and National Company Law Tribunal to act as Adjudicating Authority and deal with the cases related to insolvency, liquidation and bankruptcy process in respect of individuals and unlimited partnership firms and in respect of companies and limited liabilities entities respectively.

iv. Establishment of an Insolvency and Bankruptcy Board of India to exercise regulatory oversight over insolvency professionals, insolvency professional agencies and information utilities.

v. Insolvency professionals would handle the commercial aspects of insolvency resolution process. Insolvency professional agencies will develop professional standards, code of ethics and be first level regulator for insolvency professionals members leading to development of a competitive industry for such professionals.

vi. Information utilities would collect, collate, authenticate and disseminate financial information to be used in insolvency, liquidation and bankruptcy proceedings.

vii. Enabling provisions to deal with cross border insolvency.

The Insolvency and Bankruptcy Code, 2016 extends to the whole of India.

Section 1 of the Code provides that the Central Government may appoint different dates for different provisions of this Code and any reference in any such provision to the commencement of this Code shall be construed as a reference to the commencement of that provision.

The Insolvency and Bankruptcy Code, 2016 consolidates the existing framework by creating a single law for insolvency and bankruptcy. The Code applies to companies, partnerships, limited liability partnerships, individuals and any other body which the central government may specify.

Section 2 of the Insolvency and Bankruptcy Code, 2016 provides that the provisions of the Code shall apply to –

(a) any company incorporated under the Companies Act, 2013 or under any previous company law,

(b) any other company governed by any special Act for the time being in force,

(c) any Limited Liability Partnership incorporated under the Limited Liability Partnership Act, 2008,

(d) such other body incorporated under any law for the time being in force, as the Central Government may, by notification, specify in this behalf,

(e) personal guarantors to corporate debtors,

(f) partnership firms and proprietorship firms; and

(g) individuals, other than persons referred to in clause (e) in relation to their insolvency, liquidation, voluntary liquidation or bankruptcy, as the case may be.

> The Insolvency and bankruptcy Code, 2016 is one of the biggest economic reforms which provides a uniform and comprehensive insolvency legislation covering corporates, partnerships and individuals (other than financial firms). The Code gives both the creditors and debtors the power to initiate proceeding. It has helped India achieve a historic jump in the ease of doing business rankings by consolidating the law and providing for resolution of insolvencies in a time-bound manner.

Key Objectives of the Insolvency and Bankruptcy Code, 2016

The objects clause of the Insolvency and Bankruptcy Code lays down the following key objectives:

1. To consolidate and amend the laws relating to re-organisation and insolvency resolution of corporate persons, partnership firms and individuals to provide for a time bound insolvency resolution mechanism;
2. To ensure maximisation of value of assets;
3. To promote entrepreneurship;
4. To increase availability of credit;
5. To balance the interests of all the stakeholders including alteration in the order of priority of payment of Government dues; and
6. To establish an Insolvency and Bankruptcy Board of India as a regulatory body; and
7. To provide procedure for connected and incidental matters.

HOW CODE IS ORGANISED?

The Insolvency and Bankruptcy Code, 2016 consists of total 255 sections organised in five Parts. Part II deals with insolvency resolution and liquidation for corporate persons whereas Part III lays down procedure for insolvency resolution and bankruptcy for individuals and partnership firms. Part IV of the Code makes provisions for regulation of Insolvency Professionals, Agencies and Information Utilities and Part V includes provisions for miscellaneous matters. The Code also has eleven Schedules which amends various statutes.

Part I Preliminary (Sections 1 to 3)

Part II Insolvency Resolution and Liquidation for Corporate Persons

- Chapter I Preliminary (Sections 4 to 5)
- Chapter II Corporate Insolvency Resolution Process (Sections 6 to 32)
- Chapter III Liquidation Process (Sections 33 to 54)

- Chapter III A Pre-Packaged Insolvency Resolution Process (Section 54A-54P)
- Chapter IV Fast Track Corporate Insolvency Resolution Process (Sections 55 to 58)
- Chapter V Voluntary Liquidation of Corporate Persons (Section 59)
- Chapter VI Adjudicating Authority for Corporate Persons (Sections 60 to 67)
- Chapter VII Offences and Penalties (Sections 68 to 77).

Part III Insolvency Resolution and Bankruptcy for Individuals and Partnership Firms

- Chapter I Preliminary (Sections 78 to 79)
- Chapter II Fresh Start Process (Sections 80 to 93)
- Chapter III Insolvency Resolution Process (Sections 94 to 120)
- Chapter IV Bankruptcy Order for Individuals and Partnership Firms (Sections 121 to 148)
- Chapter V Administration and Distribution of the Estate of the Bankrupt (Sections 149 to 178)
- Chapter VI Adjudicating Authority for Individuals and Partnership Firms (Sections 179 to 187).

Part IV Regulation of Insolvency Professionals, Agencies and Information Utilities

- Chapter I The Insolvency and Bankruptcy Board of India (Sections 188 to 195)
- Chapter II Powers and Functions of the Board (Sections 196 to 198)
- Chapter III Insolvency Professional Agencies (Sections 199 to 205)
- Chapter IV Insolvency Professionals (Sections 206 to 208)
- Chapter V Information Utilities (Sections 209 to 216)
- Chapter VI Inspection and Investigation (Sections 217 to 220)
- Chapter VII Finance, Accounts and Audit (Sections 221 to 223).

Part V Miscellaneous (Sections 224 to 255)

- The First Schedule (see Section 245) amendment to the Indian Partnership Act, 1932
- The Second Schedule (see Section 246) amendment to the Central Excise Act, 1944
- The Third Schedule (see Section 247) amendment to the Income-Tax Act, 1961
- The Fourth Schedule (see Section 248) amendment to the Customs Act, 1962
- The Fifth Schedule (see Section 249) amendment to the Recovery of Debts Due to Banks and Financial Institutions Act, 1993
- The Sixth Schedule (see Section 250) amendment to the Finance Act, 1994
- The Seventh Schedule (see Section 251) amendment to the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
- The Eighth Schedule (see Section 252) amendment to the Sick Industrial Companies (Special Provisions) Repeal Act, 2003
- The Ninth Schedule (see Section 253) amendment to the Payment and Settlement Systems Act, 2007

- The Tenth Schedule (see Section 254) amendment to the Limited Liability Partnership Act, 2008
- The Eleventh Schedule (see Section 255) amendments to the Companies Act, 2013
- The Twelfth Schedule (see Section 29A(d)) Act for the pruposes of clause (d) of Section 29A.

Salient Features of the Insolvency and Bankruptcy Code, 2016

1. The Insolvency and bankruptcy Code, 2016 offers a uniform, comprehensive insolvency legislation covering all companies, partnerships and individuals. Financial service providers are not included in the ambit of the Insolvency and Bankruptcy Code, 2016.

2. To ensure a formal and time bound insolvency resolution process, the Code creates a new institutional framework consisting of the Insolvency and Bankruptcy Board of India (IBBI), Adjudicating Authorities (AAs), Insolvency Professionals (IPs), Insolvency Professional Agencies (IPAs) and Information Utilities (IUs).

3. The Code provides for Insolvency Professionals (IPs), a class of regulated but private professionals having minimum standards of professional and ethical conduct, to act as intermediary in the insolvency resolution process. Insolvency Professional Agencies are designated to regulate Insolvency Professionals. These agencies enrol Insolvency Professionals, provide pre-registration educational course to its enrolled members and enforce a code of conduct for their functioning. They also issue 'authorisation for assignment' to the IPs enrolled with them. Following are the designated Insolvency Professional Agencies (IPAs) established under the Code:

   - The Indian Institute of Insolvency Professionals of ICAI,
   - ICSI Institute of Insolvency Professionals, and
   - Insolvency Professional Agency of Institute of Cost Accountants of India.

> To regulate the working of Insolvency Professional Agencies (IPAs), the Insolvency and Bankruptcy Board of India (IBBI) has framed the following regulations in exercise of the powers conferred by the Insolvency and Bankruptcy Code, 2016:
>
> - The Insolvency and Bankruptcy Board of India (Model Bye-Laws and Governing Board of Insolvency Professional Agencies) Regulations, 2016; and
> - The Insolvency and Bankruptcy Board of India (Insolvency Professional Agencies) Regulations, 2016.

4. The Insolvency Professionals control the assets of the debtor during the insolvency resolution process. The insolvency professional verifies the claims of the creditors, constitutes a committee of creditors, runs the debtor's business as a going concern during the moratorium period and assists the creditors in finalising the revival plan. He also ensures that the debtor is in compliance with all laws applicable to it during the revival process. In liquidation, the insolvency professional acts as a liquidator and bankruptcy trustee. The Insolvency and Bankruptcy Board of India has framed the IBBI (Insolvency Professional) Regulations, 2016 to regulate the working of Insolvency Professionals. These regulations are amended from time to time by the Insolvency and Bankruptcy Board of India.

5. While the Insolvency professionals assist in the insolvency resolution proceedings envisaged in the Code, the Information Utilities, on the other hand, collect, collate, authenticate and disseminate financial information. The purpose of such collection, collation, authentication and dissemination financial information of debtors in centralised electronic databases is to facilitation swift decision making in the resolution proceedings. The Insolvency and Bankruptcy Board of India has framed the IBBI (Information Utilities) Regulations, 2017. These regulations are amended from time to time by the Insolvency and Bankruptcy Board of India.

6. The Code provides for the constitution of a new insolvency regulator i.e., the Insolvency and Bankruptcy Board of India (IBBI). Its role includes overseeing the functioning of insolvency intermediaries i.e., insolvency professionals, insolvency professional agencies and information utilities as well as regulating the insolvency process. The members of the Board include representatives from the central government as well as the Reserve Bank of India. The Board is empowered to frame and implement regulations to regulate the profession as well as processes envisaged in the Code. The Bankruptcy Board of India has also been designated as the 'Authority' under the Companies (Registered Valuers and Valuation Rules), 2017 for regulation and development of the profession of valuers in the country.

7. The Code proposes two Tribunals to adjudicate insolvency resolution cases. In the case of insolvency of companies and Limited Liability Partnerships (LLPs), the Adjudication Authority is the National Company Law Tribunal (NCLT), while the cases involving individuals and partnership firms are handled by the Debts Recovery Tribunals (DRTs). The insolvency proceeding will be initiated by NCLT or DRT, as the case may be, after verification of the claims of the initiator. Appeals from NCLT orders lie to the National Company Law Appellate Tribunal (NCLAT) and thereafter to the Supreme Court of India. For individuals and other persons, the Adjudicating Authority is the DRT. Appeals from DRT orders lie to the Debt Recovery Appellate Tribunal (DRAT) and thereafter to the Supreme Court.

To ensure that the insolvency resolution is commercially viable, the Code separates the commercial aspects from the judicial aspects and thus limits the role of adjudicating authorities to ensuring due process rather than adjudicating on the merits of the insolvency resolution.

8. To initiate an insolvency process for corporate debtors, the default should be atleast INR 1, 00, 00,000. Central Government may, by notification, specify such minimum amount of default of higher value, which shall not be more than one crore rupees, for matters relating to the prepackaged insolvency resolution process of corporate debtors under Chapter III-A. Central government vide Notification S.O. 1543(E) dated 9th April 2021 specified ten lakh rupees as the minimum amount of default for the matters relating to the pre-packaged insolvency resolution process of corporate debtor under Chapter III-A of the Code.

9. In resolution process for corporate persons, the Code proposes two independent stages:

   (i) Insolvency Resolution Process, during which the creditors assess the viability of debtor's business and the options for its rescue and revival

   (ii) Liquidation, in case the insolvency resolution process fails or financial creditors decide to wind up and distribute the assets of the debtor.

10. The Code envisages two distinct processes in case of Insolvency Resolution Process (IRP) for Individuals/ Unlimited Partnerships

    (i) Automatic Fresh Start

    (ii) Insolvency Resolution.

11. The Code provides a Fresh Start Process for individuals under which they will be eligible for a debt waiver of up to INR 35,000. The individual will be eligible for the waiver subject to certain limits prescribed under the Code. Under the automatic fresh start process, eligible debtors can apply to the Debt Recovery Tribunal (DRT) for discharge from certain debts not exceeding a specified threshold, allowing them to start afresh.

12. A financial creditor (for a defaulted financial debt) or an operational creditor (for an unpaid operational debt) can initiate an Insolvency Resolution Process (IRP) against a corporate debtor. The defaulting corporate debtor, its shareholders or employees, may also initiate voluntary insolvency proceedings. The National Company Law Tribunal (NCLT) is the designated adjudicating authority in case of corporate debtors.

In case of individuals and unlimited partnerships, the insolvency resolution process consists of preparation of a repayment plan by the debtor. If approved by creditors, the DRT passes an order binding the debtor and creditors to the repayment plan. If the plan is rejected or fails, the debtor or creditors may apply for a bankruptcy order.

Section 11 of the Code disentitles the following persons to make an application to initiate corporate insolvency resolution process:

(a) a corporate debtor undergoing a corporate insolvency resolution process; or

(aa) a financial creditor or an operational creditor of a corporate debtor undergoing a pre-packaged insolvency resolution process; or

(b) a corporate debtor having completed corporate insolvency resolution process twelve months preceding the date of making of the application; or

(ba) a corporate debtor in respect of whom a resolution plan has been approved under Chapter III-A, twelve months preceding the date of making of the application; or

(c) a corporate debtor or a financial creditor who has violated any of the terms of resolution plan which was approved twelve months before the date of making of an application under this Chapter; or

(d) a corporate debtor in respect of whom a liquidation order has been made.

It may be noted that a corporate debtor falling under the above clauses can initiate corporate insolvency resolution process against another corporate debtor.

13. The Code provides for a time bound Insolvency Resolution Process for companies and individuals, which is required to be completed within 180 days (subject to a one-time extension by 90 days) and mandatorily be completed within 330 days from the insolvency commencement date. Corporate insolvency resolution process shall mandatorily be completed within a period of three hundred and thirty days from the insolvency commencement date, including any extension of the period of corporate insolvency resolution process and the time taken in legal proceedings in relation to such resolution process of the corporate debtor. If the resolution plan does not get finalised or is rejected by NCLT or DRT on technical grounds, then assets of the debtor are sold to repay his outstanding dues.

14. The Code makes significant changes in the priority of claims for distribution of liquidation proceeds. In case of liquidation, the assets will be distributed in the following order: (i) fees of insolvency professional and costs related to the resolution process, (ii) workmen's dues for the preceding 24 months and secured creditors, (iii) employee wages, (iv) unsecured creditors, (v) government dues and remaining secured creditors (any remaining debt if they enforce their collateral), (vi) any remaining debt, and (vii) shareholders.

Before the enactment of the Insolvency and Bankruptcy Code, the Government dues were immediately below the claims of secured creditors and workmen in order of priority. Now the Central and State Government's dues stand below the claims of secured creditors, workmen dues, employee dues and other unsecured financial creditors.

15. The Code provides for the creation of Insolvency and Bankruptcy Fund. Section 224 of the Code provides that the following amounts shall be credited to the fund

- the grants made by the Central Government for the purposes of the Fund;
- the amount deposited by persons as contribution to the Fund;

- the amount received in the Fund from any other source; and
- the interest or other income received out of the investment made from the Fund.

Section 224(3) further provides that a person who has contributed any amount to the Fund may, in the event of proceedings initiated in respect of such person under the Code before an Adjudicating Authority, make an application to such Adjudicating Authority for withdrawal of funds not exceeding the amount contributed by it, for making payments to workmen, protecting the assets of such persons, meeting the incidental costs during the proceedings or such other purposes as may be prescribed.

16. The Code specifies stringent penalties for certain offences such as concealing property in case of corporate insolvency. The imprisonment in such cases may extend up to five years, or a fine of up to one crore rupees, or both.

17. In case of cross-border insolvency proceedings, the central government may enter into bilateral agreements and reciprocal arrangements with other countries to enforce provisions of the Code.

The Code repeals the Presidency Towns Insolvency Act, 1909 and the Provincial Insolvency Act, 1920.

In addition, it amends the following 11 Acts:

- The Indian Partnership Act, 1932
- The Central Excise Act, 1944
- The Income-Tax Act, 1961
- The Customs Act, 1962
- The Recovery of Debts Due to Banks and Financial Institutions Act, 1993
- The Finance Act, 1994
- The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
- The Sick Industrial Companies (Special Provisions) Repeal Act, 2003
- The Payment and Settlement Systems Act, 2007
- The Limited Liability Partnership Act, 2008
- The Companies Act, 2013.

PILLARS OF INSOLVENCY AND BANKRUPTCY CODE, 2016

(A) Insolvency and Bankruptcy Board of India (IBBI)

The Insolvency and Bankruptcy Code, 2016 provides for the constitution of a new insolvency regulator i.e., the Insolvency and Bankruptcy Board of India (IBBI). The Insolvency and Bankruptcy Board of India was established on 1st October 2016. It is a unique regulator which regulates a profession as well as processes under the Code. Its role includes over seeing the functioning of insolvency intermediaries i.e., insolvency professionals, insolvency professional agencies and information utilities. The Board is responsible for implementation of the Code that consolidates and amends the laws relating to insolvency resolution of **corporate persons, partnership firms and individuals** in a time bound manner. The Board is empowered to frame and enforce rules for various processes under the Code, namely, corporate insolvency resolution, corporate liquidation, individual insolvency resolution and individual bankruptcy.

Section 188 (2) of the Code provides that the Board shall be a body corporate having perpetual succession and a common seal, with power, subject to the provisions of this Code, to acquire, hold and dispose of property, both movable and immovable, and to contract, and shall, by the said name, sue or be sued. As per section 189 (4), the term of office of the Chairperson and members (other than ex officio members) shall be five years or till they attain the age of sixty-five years, whichever is earlier, and they shall be eligible for reappointment.

Removal of member from office

Section 190 empowers the Central Government to remove a member from office if he-

(a) is an undischarged bankrupt as defined under Part III;

(b) has become physically or mentally incapable of acting as a member;

(c) has been convicted of an offence, which in the opinion of the Central Government involves moral turpitude;

(d) has, so abused his position as to render his continuation in office detrimental to the public interest.

Section 190 mandates that no member shall be removed under clause (d) unless he has been given a reasonable opportunity of being heard in the matter.

Powers and Functions of the Board

Section 196(1) of the Insolvency and Bankruptcy Code provides that the Board shall, subject to the general direction of the Central Government, perform all or any of the following functions namely:

(a) Register insolvency professional agencies, insolvency professionals and information utilities and renew, withdraw, suspend or cancel such registrations.

(aa) promote the development of, and regulate, the working and practices of, insolvency professionals, insolvency professional agencies and information utilities and other institutions, in furtherance of the purposes of this Code.

(b) Specify the minimum eligibility requirements for registration of insolvency professional agencies, insolvency professionals and information utilities.

(c) Levy fee or other charges for carrying out the purposes of this Code, including fee for registration and renewal of insolvency professional agencies, insolvency professionals and information utilities.

(d) Specify by regulations standards for the functioning of insolvency professional agencies, insolvency professionals and information utilities.

(e) Lay down by regulations the minimum curriculum for the examination of the insolvency professionals for their enrolment as members of the insolvency professional agencies.

(f) Carry out inspections and investigations on insolvency professional agencies, insolvency professionals and information utilities and pass such orders as may be required for compliance of the provisions of this Code and the regulations issued hereunder.

(g) Monitor the performance of insolvency professional agencies, insolvency professionals and information utilities and pass any directions as may be required for compliance of the provisions of this Code and the regulations issued hereunder.

(h) Call for any information and records from the insolvency professional agencies, insolvency professionals and information utilities.

(i) Publish such information, data, research studies and other information as may be specified by regulations.

(j) Specify by regulations the manner of collecting and storing data by the information utilities and for providing access to such data.

(k) Collect and maintain records relating to insolvency and bankruptcy cases and disseminate information relating to such cases.

(l) Constitute such committees as may be required including in particular the committees laid down in Section 197.

(m) Promote transparency and best practices in its governance.

(n) Maintain websites and such other universally accessible repositories of electronic information as may be necessary.

(o) Enter into memorandum of understanding with any other statutory authorities.

(p) Issue necessary guidelines to the insolvency professional agencies, insolvency professionals and information utilities.

(q) Specify mechanism for redressal of grievances against insolvency professionals, insolvency professional agencies and information utilities and pass orders relating to complaints filed against the aforesaid for compliance of the provisions of this Code and the regulations issued hereunder.

(r) Conduct periodic study, research and audit the functioning and performance of to the insolvency professional agencies, insolvency professionals and information utilities at such intervals as may be specified by the Board.

(s) Specify mechanisms for issuing regulations, including the conduct of public consultation processes before notification of any regulations.

(t) Make regulations and guidelines on matters relating to insolvency and bankruptcy as may be required under this Code, including mechanism for time bound disposal of the assets of the corporate debtor or debtor.

(u) Perform such other functions as may be prescribed.

Section 196(2) of the Code further provides that the Board may make model bye-laws to be to adopted by insolvency professional agencies which may provide for:

(a) The minimum standards of professional competence of the members of insolvency professional agencies.

(b) The standards for professional and ethical conduct of the members of insolvency professional agencies.

(c) Requirements for enrolment of persons as members of insolvency professional agencies which shall be non-discriminatory.

Explanation.– For the purposes of this clause, the term "non-discriminatory" means lack of discrimination on the grounds of religion, caste, gender or place of birth and such other grounds as may be specified.

(d) The manner of granting membership.

(e) Setting up of a governing board for internal governance and management of insolvency professional agency in accordance with the regulations specified by the Board.

(f) The information required to be submitted by members including the form and the time for submitting such information.

(g) The specific classes of persons to whom services shall be provided at concessional rates or for no remuneration by members.

(h) The grounds on which penalties may be levied upon the members of insolvency professional agencies and the manner thereof.

(i) A fair and transparent mechanism for redressal of grievances against the members of insolvency professional agencies.

(j) The grounds under which the insolvency professionals may be expelled from the membership of insolvency professional agencies.

(k) The quantum of fee and the manner of collecting fee for inducting persons as its members.

(l) The procedure for enrolment of persons as members of insolvency professional agency.

(m) The manner of conducting examination for enrolment of insolvency professionals.

(n) The manner of monitoring and reviewing the working of insolvency professional who are members.

(o) The duties and other activities to be performed by members.

(p) The manner of conducting disciplinary proceedings against its members and imposing penalties.

(q) The manner of utilising the amount received as penalty imposed against any insolvency professional.

Section 196(3) states that the Board shall have the same powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit, in respect of the following matters, namely:

1. The discovery and production of books of account and other documents, at such place and such time as may be specified by the Board.
2. Summoning and enforcing the attendance of persons and examining them on oath.
3. Inspection of any books, registers and other documents of any person at any place.
4. Issuing of commissions for the examination of witnesses or documents.

(B) Insolvency Professionals (IPs)

The Code provides for Insolvency Professionals (IPs) to act as intermediary in the insolvency resolution process. Insolvency professionals are a class of regulated but private professionals having minimum standards of professional and ethical conduct. Section 3(19) of the Code defines an “insolvency professional” as a person enrolled under section 206 with an insolvency professional agency as its member and registered with the Board as an insolvency professional under section 207.

An insolvency professional plays a very important role under the Code. He acts as an “interim resolution professional” and/or as a “resolution professional” in the corporate insolvency resolution process (specified in Part II of the Code which deals with corporate persons) as well as Part III of the Code (which deals with Insolvency Resolution and Bankruptcy for Individuals and Partnership Firms) for conducting the fresh start process or insolvency resolution process.

An insolvency professional also acts as a liquidator in accordance with the provisions of Part II as well as a “bankruptcy trustee” for the estate of the bankrupt under section 125 in Part III of the Code.

Enrolment and Registration of Insolvency Professionals

Section 206 lays down that no person shall render his services as insolvency professional under this Code without being enrolled as a member of an insolvency professional agency and registered with the Board.

Section 207(1) further lays down that every insolvency professional shall, after obtaining the membership of any insolvency professional agency, register himself with the Board within such time, in such manner and on payment of such fee, as may be specified by regulations. Section 207(2) empowers the IBBI to specify the categories of professionals or persons possessing such qualifications and experience in the field of finance, law, management, insolvency or such other field to act as insolvency professionals.

The Insolvency and Bankruptcy Board of India has framed the IBBI (Insolvency Professional) Regulations, 2016 to regulate the working of Insolvency Professionals. These regulations are amended from time to time by the Insolvency and Bankruptcy Board of India.

Functions and obligations of insolvency professionals

Section 208(1) of the Code provides that where any insolvency resolution, fresh start, liquidation or bankruptcy process has been initiated, it shall be the function of an insolvency professional to take such actions as may be necessary, in the following matters, namely:–

(a) a fresh start order process under Chapter II of Part III;

(b) individual insolvency resolution process under Chapter III of Part III;

(c) corporate insolvency resolution process under Chapter II of Part II;

(d) individual bankruptcy process under Chapter IV of Part III; and

(e) liquidation of a corporate debtor firm under Chapter III of Part II.

Section 208(2) mandates that every insolvency professional shall abide by the following code of conduct:–

(a) to take reasonable care and diligence while performing his duties;

(b) to comply with all requirements and terms and conditions specified in the bye-laws of the insolvency professional agency of which he is a member;

(c) to allow the insolvency professional agency to inspect his records;

(d) to submit a copy of the records of every proceeding before the Adjudicating Authority to the Board as well as to the insolvency professional agency of which he is a member; and

(e) to perform his functions in such manner and subject to such conditions as may be specified.

(C) Insolvency Professional Agencies (IPA)

Section 3(20) of the Code defines "insolvency professional agency" as any person registered with the Board under section 201 as an insolvency professional agency.

Insolvency Professional Agencies are designated to regulate Insolvency Professionals. These agencies enrol Insolvency Professionals, provide pre-registration educational course to its enrolled members and enforce a code of conduct for their functioning. They also issue 'authorisation for assignment' to the IPs enrolled with them. In exercise of powers conferred by the Insolvency and Bankruptcy Code, 2016, the Insolvency and Bankruptcy Board of India (IBBI) has framed the following regulations to regulate the working of Insolvency Professional Agencies (IPAs):

- The Insolvency and Bankruptcy Board of India (Model Bye-Laws and Governing Board of Insolvency Professional Agencies) Regulations, 2016, and
- The Insolvency and Bankruptcy Board of India (Insolvency Professional Agencies) Regulations, 2016.

Following are the Insolvency Professional Agencies (IPAs) registered under the Code:

- The Indian Institute of Insolvency Professionals of ICAI;
- **ICSI Institute of Insolvency Professionals; and**
- Insolvency Professional Agency of Institute of Cost Accountants of India.

Section 199 of the Code provides that save as otherwise provided in this Code, no person shall carry on its business as insolvency professional agencies under this Code and enrol insolvency professionals as its members except under and in accordance with a certificate of registration issued in this behalf by the Board.

According to Section 204 of the Code, insolvency professional agencies perform the following functions, namely:

(a) grant membership to persons who fulfil all requirements set out in its byelaws on payment of membership fee;

(b) lay down standards of professional conduct for its members;

(c) monitor the performance of its members;

(d) safeguard the rights, privileges and interests of insolvency professionals who are its members;

(e) suspend or cancel the membership of insolvency professionals who are its members on the grounds set out in its bye-laws;

(f) redress the grievances of consumers against insolvency professionals who are its members; and

(g) publish information about its functions, list of its members, performance of its members and such other information as may be specified by regulations.

(D) Adjudicating Authority (AA)

Section 5(1) of the Code provides that the "Adjudicating Authority" for insolvency resolution and liquidation for corporate persons means National Company Law Tribunal constituted under section 408 of the Companies Act, 2013. Section 60(5) of the Code further provides that notwithstanding anything to the contrary contained in any other law for the time being in force, the National Company Law Tribunal shall have jurisdiction to entertain or dispose of –

(a) any application or proceeding by or against the corporate debtor or corporate person;

(b) any claim made by or against the corporate debtor or corporate person, including claims by or against any of its subsidiaries situated in India; and

(c) any question of priorities or any question of law or facts, arising out of or in relation to the insolvency resolution or liquidation proceedings of the corporate debtor or corporate person under this Code.

Section 63 of the Code excludes the jurisdiction of the civil courts. It provides that no civil court or authority shall have jurisdiction to entertain any suit or proceedings in respect of any matter on which National Company Law Tribunal (NCLT) or the National Company Law Appellate Tribunal (NCLAT) has jurisdiction under this Code.

Similarly, in case of individuals and partnership firms, section 79(1) of the Code provides that the "Adjudicating Authority" for insolvency resolution and bankruptcy for individuals and partnership firms is the Debt Recovery.

Tribunal constituted under sub-section (1) of section 3 of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993.

Section 179(1) of the Code provides that subject to the provisions of section 60, the Adjudicating Authority, in relation to insolvency matters of individuals and firms shall be the Debt Recovery Tribunal having territorial jurisdiction over the place where the individual debtor actually and voluntarily resides or carries on business or personally works for gain and can entertain an application under this Code regarding such person.

Section 179(2) of the Code further provides that the Debt Recovery Tribunal shall, have jurisdiction to entertain or dispose of –

(a) any suit or proceeding by or against the individual debtor;

(b) any claim made by or against the individual debtor;

(c) any question of priorities or any other question whether of law or facts, arising out of or in relation to insolvency and bankruptcy of the individual debtor or firm under this Code.

Section 180 of the Code excludes the jurisdiction of civil courts. The section provides that no civil court or authority shall have jurisdiction to entertain any suit or proceedings in respect of any matter on which the Debt Recovery Tribunal or the Debt Recovery Appellate Tribunal has jurisdiction under this Code.

Thus, the Insolvency and Bankruptcy Code proposes two tribunals to adjudicate insolvency resolution cases. In the case of insolvency of companies and Limited Liability Partnerships (LLPs), the adjudication authority is the National Company Law Tribunal (NCLT), while the cases involving individuals and partnership firms are handled by the Debts Recovery Tribunals (DRTs).

Appeals from NCLT orders lie to the National Company Law Appellate Tribunal (NCLAT) and thereafter to the Supreme Court of India. For individuals and other persons, the adjudicating authority is the DRT. Appeals from DRT orders lie to the Debt Recovery Appellate Tribunal (DRAT) and thereafter to the Supreme Court.

(E) Information Utility (IU)

Section 3(21) of the Code defines an "information utility" as a person who is registered with the Board as an information utility under section 210.

While the Insolvency professionals assist in the insolvency resolution proceedings envisaged in the Code, the Information Utility, on the other hand, collect, collate, authenticate and disseminate financial information. The purpose of such collection, collation, authentication and dissemination financial information of debtors is to facilitation swift decision making in the resolution proceedings. The Insolvency and Bankruptcy Board of India oversees the functioning of such information utilities. The Insolvency and Bankruptcy Board of India has framed the IBBI (Information Utilities) Regulations, 2017. These regulations are amended from time to time by the Insolvency and Bankruptcy Board of India.

Obligations of information utility (Section 214)

(a) create and store financial information in a universally accessible format;

(b) accept electronic submissions of financial information from persons who are under obligations to submit financial information under sub-section (1) of section 215, in such form and manner as may be specified by regulations;

(c) accept, in specified form and manner, electronic submissions of financial information from persons who intend to submit such information;

(d) meet such minimum service quality standards as may be specified by regulations;

(e) get the information received from various persons authenticated by all concerned parties before storing such information;

(f) provide access to the financial information stored by it to any person who intends to access such information in such manner as may be specified by regulations;

(g) publish such statistical information as may be specified by regulations;

(h) have inter-operatability with other information utilities.

Key Definitions and Concepts

Sections 3, 5 and 79 of the Insolvency and Bankruptcy Code, 2016 define important terms used in the Code. Section 3 of the Code defines general important terms used in the Code whereas section 5 of the Code defines important terms relating to Insolvency Resolution and Liquidation for Corporate Persons covered in Part II of the

Code. Similarly section 79 of the Code defines important terms relating to Insolvency Resolution and Bankruptcy for Individuals and Partnership Firms which is discussed in Part III of the Code.

Definitions in Section 3 of the Code

Section 3(37) provides that words and expressions used but not defined in the Insolvency and Bankruptcy Code, 2016 but defined in the Indian Contract Act, 1872, the Indian Partnership Act, 1932, the Securities Contact (Regulation) Act, 1956, the Securities Exchange Board of India Act, 1992, the Recovery of Debts Due to Banks and Financial Institutions Act, 1993, the Limited Liability Partnership act, 2008 and the Companies Act, 2013, shall have the meanings respectively assigned to them in those acts. Therefore, all such words and expressions not defined in the Code but defined in other acts shall have the meanings assigned to them in those other acts.

Section 3 states that unless the context otherwise requires,

"Board" means the Insolvency and Bankruptcy Board of India established under sub-section (1) of section 188 [Section 3(1)].

"Bench" means a bench of the Adjudicating Authority [Section 3(2)].

"Bye-laws" mean the bye-laws made by the insolvency professional agency under section 205 [Section 3(3)].

"Charge" means an interest or lien created on the property or assets of any person or any of its undertakings or both, as the case may be, as security and includes a mortgage [Section 3(4)].

"Claim" means –

(a) a right to payment, whether or not such right is reduced to judgment, fixed, disputed, undisputed, legal, equitable, secured or unsecured;

(b) right to remedy for breach of contract under any law for the time being in force, if such breach gives rise to a right to payment, whether or not such right is reduced to judgment, fixed, matured, unmatured, disputed, undisputed, secured or unsecured [Section 3(6)].

Claim' gives rise to 'debt' only when it is due and 'default' occurs only when debt becomes due and payable and is not paid by the debtor. *(Swiss Ribbons Pvt. Ltd. & Anr. Vs. Union of India & Ors. [WP (Civil) Nos. 99, 100, 115, 459, 598, 775, 822, 849, and 1221 of 2018, SLP (Civil) No. 28623 of 2018 and WP (Civil) 37 of 2019] SC judgement dated 25.01.2019).*

'Claim' under section 3(6) of the Code means a right to payment, even if it is disputed. *(Innoventive Industries Ltd. Vs. ICICI Bank & Anr. [Civil Appeal Nos. 8337-8338 of 2017] SC judgement dated 31.08.2017)*

"Corporate Person" means a company as defined in clause (20) of section 2 of the Companies Act, 2013, a limited liability partnership, as defined in clause (n) of sub-section (1) of section 2 of the Limited Liability Partnership Act, 2008, or any other person incorporated with limited liability under any law for the time being in force but shall not include any financial service provider [Section 3(7)].

National Highway Authority of India (NHAI) is a statutory body which functions as an extended limb of the Central Government and performs Governmental functions which obviously cannot be taken over by an RP, or by any other corporate body nor can NHAI ultimately be wound up under the Code. For all these reasons, it is not possible to either read in, or read down; the definition of 'corporate person' in section 3(7) of the Code to include NHAI. *(Hindustan Construction Company Ltd. & Anr. Vs. Union of India & Ors. [WP (Civil) No. 1074 of 2019 with other Civil Appeals] SC judgement dated 27.11.2019)*

"Corporate Debtor" means a corporate person who owes a debt to any person [Section 3(8)].

If a corporate person extends guarantee for the loan transaction concerning a principal borrower not being a corporate person, it would still be covered within the meaning of expression "corporate debtor" in section 3(8) of the Code. *(Laxmi Pat Surana Vs. Union Bank of India & Anr. [Civil Appeal No. 2734 of 2020] SC judgement dated 26.03.202)*

“Core Services” means services rendered by an information utility for –

(a) accepting electronic submission of financial information in such form and manner as may be specified;

(b) safe and accurate recording of financial information;

(c) authenticating and verifying the financial information submitted by a person; and

(d) providing access to information stored with the information utility to persons as may be specified [Section 3(9)].

“Creditor” means any person to whom a debt is owed and includes a financial creditor, an operational creditor, a secured creditor, an unsecured creditor and a decree holder [Section 3(10)].

In the matter of *Digamber Bhondwe Vs. JM Financial Asset Reconstruction [CA(AT)(Ins) No. 1379 of 2019]* it was held "......We further reject the submission that because in Section 3(10) of I&B Code in definition of “Creditor” the “decree holder” is included it shows that decree gives cause to initiate application under Section 7 of I&B Code. Section 3 is in Part I of I&B Code. Part II of I&B Code deals with “Insolvency Resolution and Liquidation for Corporate Person”, & has its own set of definitions in Section 5. Section 3 (10) definition of “Creditor” includes “financial creditor”, “operational creditor” “decree-holder” etc. But Section 7 or Section 9 dealing with “Financial Creditor” and “operational creditor” do not include “decree-holder” to initiate CIRP in Part II.”

Sh. Sushil Ansal Vs Ashok Tripathi and Ors, the National Company Law Appellate Tribunal, Delhi (NCLAT) held that no decree holder who is covered within the definitions of a creditor given under Section 3(10) of the Insolvency and Bankruptcy Code (IBC) can come within the ambit of the class of a financial creditor. This implies that a decree holder is not permitted to incorporate any corporate insolvency resolution process (CIRP) against any corporate debtor with the soul objective of executing a decree under it.

“Debt” means a liability or obligation in respect of a claim which is due from any person and includes a financial debt and operational debt [Section 3(11)].

“Default” means non-payment of debt when whole or any part or instalment of the amount of debt has become due and payable and is not paid by the debtor or the corporate debtor, as the case may be [Section 3(12)].

‘Default’ is defined in section 3(12) of the Code in very wide terms as non-payment of a ‘debt’ once it becomes due and payable, which includes non-payment of even part thereof or an instalment amount. (*Innoventive Industries Ltd. Vs. ICICI Bank & Anr. [Civil Appeal Nos. 8337-8338 of 2017] SC judgement dated 31.08.2017)*

The context of section 3(12) of the Code is actual non-payment by the CD when a ‘debt’ has become due and payable. *(B. K. Educational Services Pvt. Ltd. Vs. Parag Gupta and Associates [Civil Appeal No. 23988 of 2017 and other appeals] SC judgement dated 11.10.2018)*

“Financial Information”, in relation to a person, means one or more of the following categories of information, namely:–

(a) records of the debt of the person;

(b) records of liabilities when the person is solvent;

(c) records of assets of person over which security interest has been created;

(d) records, if any, of instances of default by the person against any debt;

(e) records of the balance sheet and cash-flow statements of the person; and

(f) such other information as may be specified [Section 3(13)].

“Financial Institution” means –

(a) a scheduled bank;

(b) financial institution as defined in section 45-I of the Reserve Bank of India Act, 1934;

(c) public financial institution as defined in clause (72) of section 2 of the Companies Act, 2013; and

(d) such other institution as the Central Government may by notification specify as a financial institution [Section 3(14)].

"Financial Product" means securities, contracts of insurance, deposits, credit arrangements including loans and advances by banks and financial institutions, retirement benefit plans, small savings instruments, foreign currency contracts other than contracts to exchange one currency (whether Indian or not) for another which are to be settled immediately, or any other instrument as may be prescribed [Section 3(15)].

"Financial Service" includes any of the following services, namely:–

(a) accepting of deposits;

(b) safeguarding and administering assets consisting of financial products, belonging to another person, or agreeing to do so;

(c) effecting contracts of insurance;

(d) offering, managing or agreeing to manage assets consisting of financial products belonging to another person;

(e) rendering or agreeing, for consideration, to render advice on or soliciting for the purposes of –

(i) buying, selling, or subscribing to, a financial product;

(ii) availing a financial service; or

(iii) exercising any right associated with a financial product or financial service.

(f) establishing or operating an investment scheme;

(g) maintaining or transferring records of ownership of a financial product;

(h) underwriting the issuance or subscription of a financial product; or

(i) selling, providing, or issuing stored value or payment instruments or providing payment services [Section 3(16)].

"Financial Service Provider" means a person engaged in the business of providing financial services in terms of authorisation issued or registration granted by a financial sector regulator [Section 3(17)].

"Financial Sector Regulator" means an authority or body constituted under any law for the time being in force to regulate services or transactions of financial sector and includes the Reserve Bank of India, the Securities and Exchange Board of India, the Insurance Regulatory and Development Authority of India, the Pension Fund Regulatory Authority and such other regulatory authorities as may be notified by the Central Government [Section 3(18)].

"Insolvency Professional" means a person enrolled under section 206 with an insolvency professional agency as its member and registered with the Board as an insolvency professional under section 207 [Section 3(19)].

"Insolvency Professional Agency" means any person registered with the Board under section 201 as an insolvency professional agency [Section 3(20)].

"Information Utility" means a person who is registered with the Board as an information utility under section 210 [Section 3(21)].

"Person" includes –

(a) an individual;

(b) a Hindu Undivided Family;

(c) a company;

(d) a trust;

(e) a partnership;

(f) a limited liability partnership; and

(g) any other entity established under a statute, and includes a person resident outside India [Section 3(23)].

A sole proprietary concern, not being a 'person' under section 3(23) of the Code and also when there is a pre-existing dispute, cannot file application under section 9. *(R.G. Steels Vs. Berrys Auto Ancillaries (P) Ltd. [IB722/ND/2019] NCLT, New Delhi judgement dated 23.09.2019)*

A 'trade union' is an entity established under a statute i.e. the Trade Unions Act, 1926 and is therefore, a 'person' under section 3(23) of the Code. *(JK Jute Mill Mazdoor Morcha Vs. Juggilal Kamlapat Jute Mills Company Ltd. & Ors. [Civil Appeal No. 20978 of 2017] SC judgement dated 30.04.2019)*

A proprietorship concern does not fall within the purview of "person" as per section 3(23) for the purpose of filing an application under section 9 of the Code. Proprietorship concern cannot sue and be sued unless it is represented by a proprietor. *(Shri Shakti Dyeing Works Vs. Berawala Textiles Pvt. Ltd. [CP (IB) No. 854/NCLT/AHM/2019] NCLT, Ahmedabad judgement dated 25.01.2021)*

"Property" includes money, goods, actionable claims, land and every description of property situated in India or outside India and every description of interest including present or future or vested or contingent interest arising out of, or incidental to, property [Section 3(27)].

"Secured Creditor" means a creditor in favour of whom security interest is created [Section 3(30)].

The State Tax Officer does not come within the meaning of 'secured creditor' as defined under section 3(30) read with section 3(31) of the Code. *(Tourism Finance Corporation of India Ltd. Vs. Rainbow Papers Ltd. & Ors. [CA (AT) (Ins.) No. 354 of 2019 and other appeals] NCLAT judgement dated 19.12.2019)*

In the matter of *Rainbow Papers Ltd.,* Hon'ble SC held that the State is a secured creditor as per the Gujarat Value Added Tax Act, 2003 and are to be rank equally with secured debts under section 53(1)(b). As per section 3(30) of the Code, secured creditor means a creditor in favour of whom security interest is created. Such security interest could be created by operation of law. The definition of secured creditor in the Code does not exclude any Governmental Authority. Therefore, the resolution plan ignores the statutory dues payable to any State Government or legal authority, the Adjudicating Authority is bound to reject the resolution plan.

"Security Interest" means right, title or interest or a claim to property, created in favour of, or provided for a secured creditor by a transaction which secures payment or performance of an obligation and includes mortgage, charge, hypothecation, assignment and encumbrance or any other agreement or arrangement securing payment or performance of any obligation of any person: Provided that security interest shall not include a performance guarantee; [Section 3(31)].

'Security Interest' does not include 'Performance Bank Guarantee' and it is not covered by section 14 of the Code. *(Indian Overseas Bank Vs. Arvind Kumar [CA (AT) (Ins.) No. 558 of 2020] NCLAT judgement dated 28.09.2020)*

"Transaction" includes an agreement or arrangement in writing for the transfer of assets, or funds, goods or services, from or to the corporate debtor [Section 3(33)].

"Transfer" includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien [Section 3(34)].

"Transfer of Property" means transfer of any property and includes a transfer of any interest in the property and creation of any charge upon such property [Section 3(35)].

Definitions in Section 5 of the Code

Section 5 belongs to Part II of the Code which lays down procedure for insolvency resolution and liquidation to be followed in case of corporate persons. Section 5 states that unless the context otherwise requires:

"Adjudicating Authority", for the purposes of Part II, means National Company Law Tribunal constituted under section 408 of the Companies Act, 2013 [Section 5(1)].

"Constitutional Document", in relation to a corporate person, includes articles of association, memorandum of association of a company and incorporation document of a Limited Liability Partnership [Section 5(4)].

"Corporate Applicant" means –

(a) corporate debtor; or

(b) a member or partner of the corporate debtor who is authorised to make an application for the corporate insolvency resolution process or the pre-packaged insolvency resolution process as the case may be, under the constitutional document of the corporate debtor; or

(c) an individual who is in charge of managing the operations and resources of the corporate debtor; or

(d) a person who has the control and supervision over the financial affairs of the corporate debtor [Section 5(5)].

"Corporate guarantor" means a corporate person who is the surety in a contract of guarantee to a corporate debtor [Section 5(5A)].

If CIRP has been initiated against the CD, the insolvency and bankruptcy process against the personal guarantor can be filed under section 60(2) before the same NCLT and not before the DRT. *(State Bank of India Vs. D. S. Rajender Kumar [CA (AT) (Ins.) No. 87 to 91 of 2018] NCLAT judgement dated 18.04.2018)*

Without initiating CIRP against the principal borrower, it is open to the FC to initiate CIRP under section 7 against corporate guarantors as the creditor is also the FC qua corporate guarantor. *(Rai Bahadur Shree Ram and Company Pvt. Ltd. Vs. Rural Electrification Corporation Ltd. & Ors. [Civil Appeal No. 1484 of 2019] SC judgement dated 11.02.2019)*

The principal debtor (CD) is discharged under the Code not on the instance of a creditor but due to operation of law, i.e., approval of resolution plan. Hence, the guarantor is not discharged of its liability merely because the creditor consented to a resolution plan of the principal debtor. *(State Bank of India Vs. Sungrowth Shares & Stocks Ltd. [CP (IB) No. 796/KB/2018] NCLT, Kolkata judgement dated 04.09.2019)*

The corporate guarantees given by the CD can be invoked only in the event of a default on the part of the borrower. *(Export Import Bank of India Vs. CHL Ltd. [CA (AT) (Ins.) 51 of 2018] NCLAT judgement dated 16.01.2019)*

It makes no difference as to whether the corporate person stood as guarantor to an individual or a corporate person, and as so long as the obligation in respect of a claim is due from a corporate person falling within the definition of 'financial debt', then it is obvious that the creditor can proceed under Section 7 of the Code against such corporate person. (*The Karur Vysya Bank Ltd. Vs. Maharaja Theme Parks and Resorts Pvt. Ltd. [CP/1314/IB/2018] NCLT, Chennai judgement dated 08.04.2019)*

The Code is at a nascent stage and it is better that the interpretation of the provisions is taken up by the SC to avoid any confusion and to authoritatively settle the law. It directed that no further petitions involving the challenge to the notification dated November 15, 2019, which brought into force certain provisions relating to the personal guarantors (PGs) to CDs, shall be entertained by any High Court *(Insolvency and Bankruptcy Board of India Vs. Lalit Kumar Jain & Ors. [TP (Civil) No.(s) 1034/2020 with other TPs] SC judgement dated 29.10.2020)*

Neither section 14 nor section 31 of the Code place any fetters on a bank/financial institution from initiation and continuation of proceedings against the guarantor for recovering of their dues. The liability of the principal borrower and guarantor remain coextensive and a bank/financial institution is entitled to initiate proceedings against the personal guarantor under the SARFAESI Act during the continuation of the CIRP against the principal borrower. *(Kiran Gupta Vs. State Bank of India & Anr. [W.P.(C) 7230/2020 & CM.APPL. 24414/2020 (stay)] HC, New Delhi judgement dated 02.11.2020)*

CIRP can be proceeded against the principal borrower as well as guarantor. *(State Bank of India Vs. Athena Energy Ventures Pvt. Ltd. [CA (AT) (Ins.) No. 633 of 2020] NCLAT judgement dated 24.11.2020)*

"Dispute" includes a suit or arbitration proceedings relating to –

(a) the existence of the amount of debt;

(b) the quality of goods or service; or

(c) the breach of a representation or warranty [Section 5(6)].

Any observations with regard to individual officer if made by a court of law or in any communication made by the operational creditor, the same cannot be treated to be an existence of dispute. *(Yogendra Yasupal Vs. Jigsaw Solutions & Anr. [CA (AT) (Ins.) No. 222 of 2017] NCLAT judgement dated 16.10.2017)*

The test of existence of a dispute is: (a) whether the corporate debtor has raised a plausible contention requiring further investigation which is not a patently feeble legal argument or an assertion of facts unsupported by evidence (b) whether the defence is not spurious, mere bluster, plainly frivolous or vexatious (c) a dispute, if it truly exists in fact between the parties, which may or may not ultimately succeed. *(Mobilox Innovations Pvt. Ltd. Vs. Kirusa Software Pvt. Ltd. [Civil Appeal No.9405 of 2017] SC judgement dated 21.09.2017)*

The dispute should not be a mere eyewash and attempt to derail the OC's entitlement to initiate the proceedings under sections 8 and 9 of the Code. *(Simplex Infrastructures Ltd. Vs. Agrante Infra Ltd. [IB No. (IB)- 167(ND)/2017] NCLT, New Delhi judgement dated 10.08.2017)*

A unilateral transfer of liability does not constitute a 'dispute' within the meaning of section 5(6) and an inter-se dispute between two groups of shareholders of the CD does not constitute a 'dispute' in reference to OCs. The 'dispute' under section 5(6) of the Code must be between the CD and the OCs. *(Chetan Sharma Vs. Jai Lakshmi Solvents (P) Ltd. & Anr. [CA (AT) (Ins.) No. 66 of 2017 and other appeals] NCLAT judgement dated 10.05.2018)*

On the ‘existence of a dispute’, it was observed that section 5(6) is an inclusive provision and does not confine the AA from considering the existence of a dispute from a broader angle. Therefore, dispute in terms of section 8(2)(a) of the Code shall not be limited to instances specified in the definition under section 5(6). *(Anuj Khanna Vs. Wishwa Naveen Traders & Anr. [CA (AT) (Ins.) No. 555 of 2020] NCLAT judgement dated 25.11.2020)*

“Financial Creditor” means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to [Section 5(7)].

Essential criteria for being an FC: (i) A person to whom a financial debt is owed and includes a person whom such debt has been legally assigned or transferred to (ii) The debt along with interest, if any, is disbursed against the consideration for time value of money and include any one or more mode of disbursed as mentioned in clause (a) to (i) of sub-section (8) of Section 5. *(B.V.S. Lakshmi Vs. Geometrix Laser Solutions Pvt. Ltd. [CA (AT) (Ins.) No. 38 of 2017] NCLAT judgement dated 22.12.2017)*

The allottees/home buyers were included in the main provision, i.e., section 5(8)(f) with effect from the inception of the Code. The Explanation was added in 2018 merely to clarify doubts that had arisen. The deeming fiction that is used by the Explanation is to put beyond doubt the fact that allottees are to be regarded as financial creditors within section 5(8)(f) of the Code. *(Pioneer Urban Land and Infrastructure Ltd. & Anr. Vs. Union of India & Ors. [WP (C) No. 43 of 2019 with other appeals] SC judgement dated 09.08.2019)*

“Financial Debt” means a debt along with 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;

Explanation – For the purposes of this sub-clause,

(i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and

(ii) the expressions, "allottee" and "real estate project" shall have the meanings respectively assigned to them in clauses (d) and (zn) of section 2 of the Real Estate (Regulation and Development) Act, 2016.

(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 [Section 5(8)].

The Joint Development Agreement entered, is a contract of reciprocal rights and obligations, both parties are admittedly Joint Development Partners, who entered into a consortium of sorts for developing an Integrated Township and for any breach of terms of contract, Section 7 Application is not maintainable as the amount cannot be construed as financial debt as defined under section 5(8) of the Code. *(Vipul Limited Vs. Solitaire Buildmart Pvt. Ltd. [CA (AT) (Ins.) No. 550 of 2020] NCLAT judgement dated 18.08.2020)*

A financial debt is a debt together with interest, if any, which is disbursed against the consideration for time value of money. *(Swiss Ribbons Pvt. Ltd. & Anr. Vs. Union of India & Ors. [WP (Civil) Nos. 99, 100, 115, 459, 598, 775, 822, 849, and 1221 of 2018, SLP (Civil) No. 28623 of 2018 and WP (Civil) 37 of 2019] SC judgement dated 25.01.2019)*

The Supreme Court in the case of *Phoenix Arc Pvt. Ltd. Vs. Spade Financial Services Ltd. & Ors. [Civil Appeal No. 2842 of 2020 with 3063 of 2020] SC judgement dated 01.02.2021* held that (a) The collusive commercial arrangements between FCs and the CD would not constitute a 'financial debt'; (b) The objects and purposes of the Code are best served when the CIRP is driven by external creditors, so as to ensure that the CoC is not sabotaged by related parties of the CD. The purpose of excluding a related party of a CD from the CoC is to obviate conflicts of interest; (c) Exclusion under the first proviso to section 21(2) is related not to the debt itself but to the relationship existing between a related party FC and the CD.; and (d) The FC, who in praesenti is not a related party, would not be debarred from being a member of the CoC. However, in case where the related party FC divests itself of its shareholding or ceases to become a related party in a business capacity with the sole intention of participating in the CoC and sabotage the CIRP, it would be in keeping with the object and purpose of the first proviso to section 21(2), to debar the former related party creditor.

Advance amount paid as Security Deposit bearing interest is Financial Debt. NCLT, New Delhi Bench vide its order dated 11th October 2021 in case of *Magicon Impex Pvt. Ltd* observed that, the amount which has been released pursuant to Agreement in the form of Security Deposit and the same is interest bearing, which means it is carrying consideration of time value of money having commercial effect of a borrowing. Therefore, in our view the "debt" claimed is a "Financial Debt" within the definition of Section 5(8)(f) of IBC, 2016.

"Financial Position" in relation to any person, means the financial information of a person as on a certain date [Section 5(9)].

"Information Memorandum" means a memorandum prepared by resolution professional under sub- section (1) of section 29 [Section 5(10)].

"Initiation Date" means the date on which a financial creditor, corporate applicant or operational creditor, as the case may be, makes an application to the Adjudicating Authority for initiating corporate insolvency resolution process or the pre-packaged insolvency resolution proces as the case may be [Section 5(11)].

"Insolvency Commencement Date" means the date of admission of an application for initiating corporate insolvency resolution process by the Adjudicating Authority under sections 7, 9 or section 10, as the case may be [Section 5(12)].

"Insolvency Resolution Process Costs" means –

(a) the amount of any interim finance and the costs incurred in raising such finance;

(b) the fees payable to any person acting as a resolution professional;

(c) any costs incurred by the resolution professional in running the business of the corporate debtor as a going concern;

(d) any costs incurred at the expense of the Government to facilitate the insolvency resolution process; and

(e) any other costs as may be specified by the Board [Section 5(13)].

is incurred towards supply of essential services during the period of moratorium, it may be accounted towards the insolvency resolution process costs. *(Dakshin Gujarat VIJ Company Ltd. Vs. ABG Shipyard Ltd. & Anr. [CA (AT) (Ins.) No. 334 of 2017] NCLAT judgement dated 08.02.2018)*

"Insolvency Resolution Process Period" means the period of one hundred and eighty days beginning from the insolvency commencement date and ending on one hundred and eightieth day [Section 5(14)].

It is always open to the NCLT/NCLAT to exclude certain period for the purpose of counting the total period of 270 days. The grounds include the following: (i) If the CIRP is stayed by a court of law or the NCLT/NCLAT/Supreme Court (ii) If no RP is functioning for one or other reason during the CIRP (iii) The period between the date of order of admission/moratorium is passed and the actual date on which the RP takes charge for completing the CIRP (iv) On hearing a case, if order is reserved by the NCLT/NCLAT/Supreme Court and finally pass order enabling the RP to complete the CIRP (v) If the CIRP is set aside by the NCLAT or order of the NCLAT is reversed by the Supreme Court and CIRP is restored (vi) Any other circumstances which justifies exclusion of certain period. *(Quinn Logistics India Pvt. Ltd. Vs. Mack Soft Tech Pvt. Ltd. & Ors. [CA (AT) (Ins.) No. 185 of 2018] NCLAT judgement dated 08.05.2018)*

"Interim Finance" means any financial debt raised by the resolution professional during the insolvency resolution process period or by the corporate debtor during the pre packaged insolvency resolution process Period, as the case may be, and such other debt as may be notified [Section 5(15)].

> The Ministry of Corporate Affairs vide notification dated 18th March, 2020 notified that a debt raised from the Special Window for Affordable and Middle-Income Housing Investment Fund I, for the purposes of the said clause.
>
> *Explanation*.– For the purposes of this notification, the expression "Special Window for Affordable and Middle-Income Housing Investment Fund I" shall mean the fund sponsored by the Central Government for providing priority debt financing for stalled housing projects, as an alternate investment fund and registered with the Securities and Exchange Board of India, established under sub-section (1) of section 3 of the Securities and Exchange Board of India Act, to provide financing for the completion of stalled housing projects that are in the affordable and middle-income housing sector.

"Liquidation Cost" means any cost incurred by the liquidator during the period of liquidation subject to such regulations, as may be specified by the Board [Section 5(16)].

"Liquidation Commencement Date" means the date on which proceedings for liquidation commence in accordance with section 33 or section 59, as the case may be [Section 5(17)].

"Liquidator" means an insolvency professional appointed as a liquidator in accordance with the provisions of Chapter III or Chapter V of this Part, as the case may be [Section 5(18)].

"Officer" for the purposes of Chapter VI and Chapter VII of this Part, means an officer who is in default, as defined in clause (60) of section 2 of the Companies Act, 2013, or a designated partner as defined in clause (j) of section 2 of the Limited Liability Partnership Act, 2008, as the case may be [Section 5(19)].

"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 [Section 5(20)].

It is clear that an OC who has assigned or legally transferred any operational debt to an FC, the assignee or transferee shall be considered as an OC to the extent of such assignment or legal transfer. *(Cooperative Rabobank U.A. Singapore Branch Vs. Shailendra Ajmera [CA (AT) (Ins.) No. 261 of 2018] NCLAT judgement dated 29.04.2019)*

The workmen of a Company come within the meaning of an OC in terms of section 5(20) r/w section 5(21) of the Code. *(Suresh Narayan Singh Vs. Tayo Rolls Ltd. [CA (AT) (Ins.) No. 112 of 2018] NCLAT judgement dated 26.09.2018)*

An OC means a person to whom an operational debt is owed, and an operational debt under section 5(21) means a claim in respect of provision of goods or services. *(Innoventive Industries Ltd. Vs. ICICI Bank & Anr. [Civil Appeal Nos. 8337-8338 of 2017] SC judgement dated 31.08.2017)*

A Trade Union or Association of workmen/employee does not come within the meaning of OC as no services is rendered by the Workmen's Association/Trade Union to the CD to claim any dues which can be termed to be debt as defined in sub-section (11) of section 3. *(JK Jute Mill Mazdoor Morcha Vs. Juggilal Kamlapat Jute Mills Co. Ltd. [CA (AT) (Ins.) No. 82 of 2017] NCLAT 12.09.2017)*

"Operational Debt" means a claim in respect of the provision of goods or services including employment or a debt in respect of the payment 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 [Section 5(21)].

Operational debt would include a claim in respect of the provision of goods or services, including employment, or a debt in respect of payment of dues arising under any law and payable to the Government or any local authority. *(Swiss Ribbons Pvt. Ltd. & Anr. Vs. Union of India & Ors. [WP (Civil) Nos. 99, 100, 115, 459, 598, 775, 822, 849, and 1221 of 2018, SLP (Civil) No. 28623 of 2018 and WP (Civil) 37 of 2019] SC judgement dated 25.01.2019)*

The property seized by Kolkata Municipal Corporation (KMC) towards recovery of municipal tax dues from CD, can be the subject matter of the CIRP under the Code as the claim of KMC had attained finality and fastened a liability upon the CD, thus constituting an 'operational debt' under section 5(21) of the Code. *(Kolkata Municipal Corporation and Anr. Vs. Union of India and Ors. [WPA No.977 of 2020] HC, Calcutta, judgement dated 29.01.2021)*

Chipsan Aviation Pvt. Ltd. Vs. Punj Llyod Aviation Ltd. [Company Appeal (AT) (Insolvency) No. 261 of 2022] On an assurance from the CD, a sum of Rs. 60 lakh was advanced for aviation related services. The advance payment was reflected in the balance sheet of the CD. However, there was no contract between the parties for providing aviation services. The issue for consideration was whether such the advance paid will fall within the definition of 'operational debt' under the Code. The AA rejected the application holding that advance payment made by OC to the CD does not fall within operational debt. On appeal, the NCLAT observed that the expression 'in respect of' in section 5(21) of the Code has to be interpreted in a broad and purposive manner and held that the advance payment of Rs. 60 lakh was clearly an operational debt.

The Supreme Court in its order dated August 09,2019 in the case of *Pioneer Urban Land and Infrastructure Ltd. v. Union of India,* held that "a debt which arises out of advance payment made to a corporate debtor for supply of goods or services would be considered as an operational debt".

"Personal guarantor" means an individual who is the surety in a contract of guarantee to a corporate debtor [Section 5(22)].

"Personnel" includes the directors, managers, key managerial personnel, designated partners and employees, if any, of the corporate debtor [Section 5(23)].

"Preliminary Information Memorandum" means a memorandum submitted by the corporate debtor under clause (b) of sub-section (1) of section 54G [Section 5(23A)].

"Pre-Packaged Insolvency Commencement Date" means the date of admission of an application for initiating the pre-packaged insolvency resolution process by the Adjudicating Authority under clause (a) of sub-section (4) of section 54C [Section 5(23B)].

"Pre-Packaged Insolvency Resolution Process Costs" means-

(a) the amount of any interim finance and the costs incurred in raising such finance;

(b) the fees payable to any person acting as a resolution professional and any expenses incurred by him for conducting the pre-packaged insolvency resolution process during the pre-packaged insolvency resolution process period, subject to sub-section (6) of section 54F;

(c) any costs incurred by the resolution professional in running the business of the corporate debtor as a going concern pursuant to an order under sub-section (2) of section 54J;

(d) any costs incurred at the expense of the Government to facilitate the prepackaged insolvency resolution process; and

(e) any other costs as may be specified [Section 5(23C)].

"Pre-Packaged Insolvency Resolution Process Period" means the period beginning from the pre-packaged insolvency commencement date and ending on the date on which an order under sub-section (1) of section 54L, or sub-section (1) of section 54N, or sub-section (2) of section 54-O, as the case may be, is passed by the Adjudicating Authority [Section 5(23D)].

"Related Party", in relation to a corporate debtor, means –

(a) a director or partner of the corporate debtor or a relative of a director or partner of the corporate debtor;

(b) a key managerial personnel of the corporate debtor or a relative of a key managerial personnel of the corporate debtor;

(c) a limited liability partnership or a partnership firm in which a director, partner, or manager of the corporate debtor or his relative is a partner;

(d) a private company in which a director, partner or manager of the corporate debtor is a director and holds along with his relatives, more than two per cent. of its share capital;

(e) a public company in which a director, partner or manager of the corporate debtor is a director and holds along with relatives, more than two per cent. of its paid-up share capital;

(f) anybody corporate whose board of directors, managing director or manager, in the ordinary course of business, acts on the advice, directions or instructions of a director, partner or manager of the corporate debtor;

(g) any limited liability partnership or a partnership firm whose partners or employees in the ordinary course of business, acts on the advice, directions or instructions of a director, partner or manager of the corporate debtor;

(h) any person on whose advice, directions or instructions, a director, partner or manager of the corporate debtor is accustomed to act;

(i) a body corporate which is a holding, subsidiary or an associate company of the corporate debtor, or a subsidiary of a holding company to which the corporate debtor is a subsidiary;

(j) any person who controls more than twenty per cent. of voting rights in the corporate debtor on account of ownership or a voting agreement;

(k) any person in whom the corporate debtor controls more than twenty per cent. of voting rights on account of ownership or a voting agreement;

(l) any person who can control the composition of the board of directors or corresponding governing body of the corporate debtor;

(m) any person who is associated with the corporate debtor on account of –

(i) participation in policy making processes of the corporate debtor; or

(ii) having more than two directors in common between the corporate debtor and such person; or

(iii) interchange of managerial personnel between the corporate debtor and such person; or

(iv) provision of essential technical information to, or from, the corporate debtor [Section 5(24)].

"Related Party", in relation to an individual, means –

(a) a person who is a relative of the individual or a relative of the spouse of the individual;

(b) a partner of a limited liability partnership, or a limited liability partnership or a partnership firm, in which the individual is a partner;

(c) a person who is a trustee of a trust in which the beneficiary of the trust includes the individual, or the terms of the trust confers a power on the trustee which may be exercised for the benefit of the individual;

(d) a private company in which the individual is a director and holds along with his relatives, more than two per cent. of its share capital;

(e) a public company in which the individual is a director and holds along with relatives, more than two per cent. of its paid-up share capital;

(f) a body corporate whose board of directors, managing director or manager, in the ordinary course of business, acts on the advice, directions or instructions of the individual;

(g) a limited liability partnership or a partnership firm whose partners or employees in the ordinary course of business, act on the advice, directions or instructions of the individual;

(h) a person on whose advice, directions or instructions, the individual is accustomed to act;

(i) a company, where the individual or the individual along with its related party, own more than fifty per cent. of the share capital of the company or controls the appointment of the board of directors of the company.

Explanation. For the purposes of this clause, –

(a) "relative", with reference to any person, means anyone who is related to another, in the following manner, namely: –

(i) members of a Hindu Undivided Family, (ii) husband, (iii) wife, (iv) father, (v) mother, (vi) son, (vii) daughter, (viii) son's daughter and son, (ix) daughter's daughter and son, (x) grandson's daughter and son, (xi) granddaughter's daughter and son, (xii) brother, (xiii) sister, (xiv) brother's son and daughter, (xv) sister's son and daughter, (xvi) father's father and mother, (xvii) mother's father and mother, (xviii) father's brother and sister, (xix) mother's brother and sister; and

(b) wherever the relation is that of a son, daughter, sister or brother, their spouses shall also be included. [Section 5(24A)}.

In *Swiss Ribbons Pvt. Ltd. & Another Vs. Union of India & Others [(2019) 4 SCC 17],* a constitutional challenge was raised against section 29A(j) (connected parties) read with the definition of related party under the IBC.

The Supreme Court examined the definition of "related party" and observed that persons who act jointly or in concert with others are connected with the business activity of the resolution applicant. Similarly, all the categories of persons mentioned in section 5(24A) (definition of related party to an individual) show that such persons must be "connected" with the resolution applicant within the meaning of section 29A(j). This being the case, the categories of persons who are collectively mentioned as a "relative" need to have a connection with the business activity of the resolution applicant. If this cannot be shown such person cannot be disqualified under section 29A(j). All the categories in this subsection deal with persons, natural as well as artificial, who are connected with the business activity of the resolution applicant. The expressions "related party" and "relative" contained in the definition sections must be read noscitur a sociis (the meaning of an unclear word or phrase should be interpreted within the context it is being used) with the categories of persons mentioned in Explanation I. So read, they would include only persons who are connected with the business activity of the resolution applicant.

"Resolution Applicant" means a person, who individually or jointly with any other person, submits a resolution plan to the resolution professional pursuant to the invitation made under clause (h) of sub- section (2) of section 25 or pursuant to the section 54K, as the case may be [Section 5(25)].

A resolution applicant whose resolution plan stands approved by CoC, cannot be permitted to alter his position to the detriment of various stake holders after pushing out all potential rivals during the bidding process, and the same fraught with disastrous consequences for the CD which may be pushed into liquidation, as the CIRP period may by then be over thereby setting at naught all possibilities of insolvency resolution and protection of a CD, more so, when it is a going concern. *(Kundan Care Products Ltd. Vs. Amit Gupta and Ors. [CA (AT) (Ins.) No. 653 of 2020] NCLAT judgement dated 30.09.2020)*

A successful resolution applicant cannot be permitted to withdraw the approved resolution plan, coupled with the fact in the instant case being the sole RA in the CIRP, which is an MSME and having knowledge of the financial health of the CD as a promoter or as a connected person cannot be permitted to seek revision of the approved plan, on the ground which would not be a material irregularity within the ambit of section 61(3) of the Code.*(Seroco Lighting Industries Pvt. Ltd. Vs. Ravi Kapoor, RP for Arya Filaments Pvt. Ltd. & Ors. [CA (AT) (Ins.) No. 1054 of 2020] NCLAT judgement dated 10.12.2020)*

"Resolution Plan" means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with Part II. It may be noted that a resolution plan may include provision the restructuring of the corporate debtor, insolvency by way of merger, amalgamation and demerger [Section 5(26)].

"Resolution Professional" for the purposes of this Part, means an insolvency professional appointed to conduct the corporate insolvency resolution process or the prepackge insolvency resolution procers, as the case may be and includes an interim resolution professional [Section 5(27)].

"Voting Share" means the share of the voting rights of a single financial creditor in the committee of creditors which is based on the proportion of the financial debt owed to such financial creditor in relation to the financial debt owed by the corporate debtor [Section 5(28)].

Definitions in Section 79 of the Code

Section 79 belongs to Part III of the Code which lays down procedure for insolvency resolution and bankruptcy for **individuals and partnership firms**. Section 79 states that unless the context otherwise requires:

"Adjudicating Authority" means the Debt Recovery Tribunal constituted under sub-section (1) of section 3 of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 [Section 79(1)].

"Associate" of the debtor means –

(a) a person who belongs to the immediate family of the debtor;

(b) a person who is a relative of the debtor or a relative of the spouse of the debtor;

(c) a person who is in partnership with the debtor;

(d) a person who is a spouse or a relative of any person with whom the debtor is in partnership;

(e) a person who is employer of the debtor or employee of the debtor;

(f) a person who is a trustee of a trust in which the beneficiaries of the trust include a debtor, or the terms of the trust confer a power on the trustee which may be exercised for the benefit of the debtor; and

(g) a company, where the debtor or the debtor along with his associates, own more than fifty per cent. of the share capital of the company or control the appointment of the board of directors of the company.

Explanation – For the purposes of this sub-section, "relative", with reference to any person, means anyone who is related to another, if –

(i) they are members of a Hindu Undivided Family;

(ii) one person is related to the other in such manner as may be prescribed [Section 79(2)].

"Bankrupt" means –

(a) a debtor who has been adjudged as bankrupt by a bankruptcy order under section 126;

(b) each of the partners of a firm, where a bankruptcy order under section 126 has been made against a firm; or

(c) any person adjudged as an undischarged insolvent [Section 79(3)].

"Bankruptcy" means the state of being bankrupt [Section 79(4)].

"Bankruptcy Debt" in relation to a bankrupt, means –

(a) any debt owed by him as on the bankruptcy commencement date;

(b) any debt for which he may become liable after bankruptcy commencement date but before his discharge by reason of any transaction entered into before the bankruptcy commencement date; and

(c) any interest which is a part of the debt under section 171 [Section 79(5)].

"Bankruptcy Commencement Date" means the date on which a bankruptcy order is passed by the Adjudicating Authority under section 126 [Section 79(6)].

"Bankruptcy Order" means an order passed by an Adjudicating Authority under section 126 [Section 79(7)].

"Bankruptcy Process" means a process against a debtor under Chapters IV and V of this Part [Section 79(8)].

"Bankruptcy Trustee" means the insolvency professional appointed as a trustee for the estate of the bankrupt under section 125 [Section 79(9)].

"Committee of Creditors" means a committee constituted under section 134; [Section 79(11)].

"Debtor" includes a judgment-debtor [Section 79(12)].

"Discharge Order" means an order passed by the Adjudicating Authority discharging the debtor under sections 92, 119 and section 138, as the case may be [Section 79(13)].

"Excluded Assets" for the purposes of this part includes –

(a) unencumbered tools, books, vehicles and other equipment as are necessary to the debtor or bankrupt for his personal use or for the purpose of his employment, business or vocation;

(b) unencumbered furniture, household equipment and provisions as are necessary for satisfying the basic domestic needs of the bankrupt and his immediate family;

(c) any unencumbered personal ornaments of such value, as may be prescribed, of the debtor or his immediate family which cannot be parted with, in accordance with religious usage;

(d) any unencumbered life insurance policy or pension plan taken in the name of debtor or his immediate family; and

(e) an unencumbered single dwelling unit owned by the debtor of such value as may be prescribed [Section 79(14)].

"Excluded Debt" means –

(a) liability to pay fine imposed by a court or tribunal;

(b) liability to pay damages for negligence, nuisance or breach of a statutory, contractual or other legal obligation;

(c) liability to pay maintenance to any person under any law for the time being in force;

(d) liability in relation to a student loan; and

(e) any other debt as may be prescribed [Section 79(15)].

"Firm" means a body of individuals carrying on business in partnership whether or not registered under section 59 of the Indian Partnership Act, 1932 [Section 79(16)].

"Immediate Family" of the debtor means his spouse, dependent children and dependent parents [Section 79(17)].

"Partnership Debt" means a debt for which all the partners in a firm are jointly liable [Section 79(18)].

"Qualifying Debt" means amount due, which includes interest or any other sum due in respect of the amounts owed under any contract, by the debtor for a liquidated sum either immediately or at certain future time and does not include– (a) an excluded debt; (b) a debt to the extent it is secured; and (c) any debt which has been incurred three months prior to the date of the application for fresh start process [Section 79(19)].

"Repayment Plan" means a plan prepared by the debtor in consultation with the resolution professional under section 105 containing a proposal to the committee of creditors for restructuring of his debts or affairs [Section 79(20)].

"Resolution Professional" means an insolvency professional appointed under this part as a resolution professional for conducting the fresh start process or insolvency resolution process [Section 79(21)].

"Undischarged Bankrupt" means a bankrupt who has not received a discharge order under section 138 [Section 79(22)].

CASE LAWS

1. **The provisions of the IBC override anything contained in any other law in force or any instrument having effect by virtue of such law:** In the matter of *Innoventive Industries Ltd. v. ICICI Bank, the Supreme Court* for the first time explained the paradigm shift in law by virtue of the newly enacted Insolvency and Bankruptcy Code, 2016 which consolidates and amends all the laws relating to the insolvency and bankruptcy process in India.

Facts of the case

ICICI Bank had taken Innoventive Industries Ltd. to NCLT for the recovery of its due as the company had defaulted on loan repayment. The NCLT had given a verdict in favour of the ICICI Bank, which Innoventive Industries challenged in the National Company Law Appellate Tribunal (NCLAT), where it received yet another setback. The company later filed an appeal in the Supreme Court seeking relief under the Maharashtra Relief Undertaking (Special Provisions) Act, 1958 (MRUA), which states that if a company is facing bankruptcy, protection needs to be provided for the employees.

Judgement

The Supreme Court held that the Act is repugnant to the IBC. Under the MRUA, the State Government may take over the management of the undertaking and impose a moratorium in much the same manner as that contained in the IBC. By giving effect to the MRUA, the plan/scheme that may be adopted under the IBC will directly be hindered. There would be a direct clash between moratoriums under the two statutes. The non-obstante clause of the IBC will prevail over the non-obstante clause in the MRUA. On account of the non-obstante clause in the IBC, any right of the CD under any other law cannot come in the way of the IBC.

Further, In the case of *Pr. Commissioner of Income Tax Vs. Monnet Ispat And Energy Ltd. [SLP No. 6483-2018 & other petitions]*, the Supreme Court held that the IBC would override anything inconsistent contained in any other enactment, including the Income Tax Act, 1961.

2. **Enactment of the IBC has marked a quantum change in corporate governance and the rule of law:** *In the case of Arun Kumar Jagatramka vs. Jindal Steel and Power Ltd [CA 9664 of 2019] judgement dated March 15, 2021*, the Supreme Court observed that enactment of the IBC has marked a quantum change in corporate governance and the rule of law. First and foremost, the IBC perceives good corporate governance, respect for and adherence to the rule of law as central to the resolution of corporate insolvencies. Second, the IBC perceives corporate insolvency not as an isolated problem faced by an individual business entities but places it in the context of a framework which is founded on public interest in facilitating economic growth by balancing diverse stakeholder interests. Third, the IBC attributes a primacy to the business decisions taken by creditors acting as a collective body, on the premise that the timely resolution of corporate insolvency is necessary to ensure the growth of credit markets and encourage investment. Fourth, in its diverse provisions, the IBC ensures that the interests of corporate enterprises are not conflated with the interests of their promoters; the economic value of corporate structures is broader in content than the partisan interests of their managements. These salutary objectives of the IBC can be achieved if the integrity of the resolution process is placed at the forefront. Primarily, the IBC is a legislation aimed at re-organization and resolution of insolvencies. Liquidation is a matter of last resort. These objectives can be achieved only through a purposive interpretation which requires courts, while infusing meaning and content to its provisions, to ensure that the problems which beset the earlier regime do not enter through the backdoor through disingenuous stratagems.

3. **The primary focus of the IBC is to ensure the revival and continuation of the corporate debtor:** *In the matter of Gujarat Urja Vikas Nigam Limited Vs. Mr. Amit Gupta & Ors. [Civil Appeal No. 9241 of 2019 Judgment dated 8th March, 2021,* the Hon'ble Supreme Court of India observed that the primary focus of the IBC is to ensure the revival and continuation of the corporate debtor. The interests of the corporate debtor have been bifurcated and separated from the interests of persons in management. The timelines which are prescribed in the IBC are intended to ensure the resuscitation of the corporate debtor. The enactment of the IBC is in significant senses a break from the past. While interpreting the provisions of the IBC, care must be taken to ensure that the regime which Parliament found deficient and which was the basic reason for the enactment of the new legislation is not brought in through the back door by a process of disingenuous legal interpretation. However, this is not to say that the interpretation given to the statutory provisions that existed prior to the enactment IBC is to be rejected in toto. The interpretation given to such statutory provisions that are textually similar to Section 60(5)(c) may be relevant, provided that such interpretation is in tandem with the objective of enacting the IBC, that is, inter alia, avoidance of multiplicity of fora and a timely resolution of the insolvency process.

4. **The foremost and primary objective of the IBC is the reorganization and insolvency resolution of the Corporate Debtor (CD) in a time bound manner:** Hon'ble Supreme Court of India in the matter of *Swiss Ribbons Pvt. Ltd. & Anr. Vs. Union of India & Ors. [WP (Civil) Nos. 99, 100, 115, 459, 598, 775, 822, 849, and 1221 of 2018, SLP (Civil) No. 28623 of 2018 and WP (Civil) 37 of 2019] Judgement dated 25th January, 2019* observed that as is discernible, the Preamble gives an insight into what is sought to be achieved by the Code. The Code is first and foremost, a Code for reorganization and insolvency resolution of corporate debtors. Unless such reorganization is effected in a time-bound manner, the value of the assets of such persons will deplete. Therefore, maximization of value of the assets of such persons so that they are efficiently run as going concerns is another very important objective of the Code. This, in

turn, will promote entrepreneurship as the persons in management of the corporate debtor are removed and replaced by entrepreneurs. When, therefore, a resolution plan takes off and the corporate debtor is brought back into the economic mainstream, it is able to repay its debts, which, in turn, enhances the viability of credit in the hands of banks and financial institutions. Above all, ultimately, the interests of all stakeholders are looked after as the corporate debtor itself becomes a beneficiary of the resolution scheme - workers are paid, the creditors in the long run will be repaid in full, and shareholders/investors are able to maximize their investment. Timely resolution of a corporate debtor who is in the red, by an effective legal framework, would go a long way to support the development of credit markets. Since more investment can be made with funds that have come back into the economy, business then eases up, which leads, overall, to higher economic growth and development of the Indian economy. What is interesting to note is that the Preamble does not, in any manner, refer to liquidation, which is only availed of as a last resort if there is either no resolution plan or the resolution plans submitted are not up to the mark. Even in liquidation, the liquidator can sell the business of the corporate debtor as a going concern.

LESSON ROUND-UP

- The Code applies to companies, partnerships, limited liability partnerships, individuals and any other body which the central government may specify.
- The Insolvency and Bankruptcy Code, 2016 consists of total 255 sections organised in five Parts.
- Sections 3,5 and 79 of the Insolvency and Bankruptcy Code, 2016 define important terms used in the Code.
- The National Company Law Tribunal (NCLT) shall be the Adjudicating Authority with jurisdiction over companies, limited liability entities. Appeals from the order of NCLT shall lie to the National Company Law Appellate Tribunal (NCLAT).
- The Debt Recovery Tribunal (DRT) shall be the Adjudicating Authority with jurisdiction over individuals and partnership firms. Appeals from the order of DRT shall lie to the Debt Recovery Appellate Tribunal (DRAT).
- The Code establishes an Insolvency Regulator (The Insolvency and Bankruptcy Board of India) to exercise regulatory oversight over,
  - Insolvency Professionals;
  - Insolvency Professional Agencies; and
  - Information Utilities.
- An insolvency resolution process can be initiated by either a creditor, or by the debtor, upon an event of default.
- Section 3(19) of the Code defines an 'insolvency professional' as a person enrolled under section 206 with an insolvency professional agency as its member and registered with the Board as an insolvency professional under section 207.
- Section 3(20) of the Code defines 'insolvency professional agency' as any person registered with the Board under section 201 as an insolvency professional agency.
- Section 3(21) of the Code defines an 'information utility' as a person who is registered with the Board as an information utility under section 210.
- The Code proposes to regulate insolvency professionals and insolvency professional agencies. Under Regulator's oversight, these agencies will develop professional standards, codes of ethics and exercise a disciplinary role over errant members leading to the development of a competitive industry for insolvency professionals.
- The Code proposes for Information Utilities which would collect, collate, authenticate and disseminate financial information from listed companies and financial and operational creditors of companies. An individual insolvency data base is also proposed to be setup with the goal of providing information on insolvency status of individuals.

- The Code proposes a swift process and timeline of 180 days for dealing with applications for corporate insolvency resolution. This can be extended for 90 days by the Adjudicating Authority as only one time extension. However, the process shall mandatorily be completed within a period of three hundred and hirty days from the insolvency commencement date.

GLOSSARY

Insolvency and Bankruptcy Board of India (IBBI) : The Insolvency and Bankruptcy Board of India is a unique regulator which regulates a profession as well as processes under the Code. Its role includes overseeing the functioning of insolvency intermediaries i.e., insolvency professionals, insolvency professional agencies and information utilities. The Board is responsible for implementation of the Code that consolidates and amends the laws relating to insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner.

Insolvency Professionals (IPs) : Insolvency Professionals (IPs) to act as intermediary in the insolvency resolution process. Insolvency professionals are a class of regulated but private professionals having minimum standards of professional and ethical conduct. Section 3(19) of the Code defines an “insolvency professional” as a person enrolled under section 206 with an insolvency professional agency as its member and registered with the Board as an insolvency professional under section 207.

Insolvency Professional Agency : Insolvency professional agency as any person registered with the Board under section 201 as an insolvency professional agency. Insolvency Professional Agencies are designated to regulate Insolvency Professionals.

Adjudicating Authority : Adjudicating Authority for insolvency resolution and liquidation for corporate persons means National Company Law Tribunal constituted under section 408 of the Companies Act, 2013.

Information Utility : An information utility as a person who is registered with the Board as an information utility under section 210. The Information Utility collect, collate, authenticate and disseminate financial information.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Briefly explain the meaning of terms ‘insolvency’ and ‘bankruptcy’. Discuss historical developments of insolvency law in India.
2. Discuss the insolvency framework in the United Kingdom and the United States of America.
3. Mentions the reasons that led to the enactment of the Insolvency and Bankruptcy Code, 2016. State the objectives of the Code.
4. What are the salient features of the Insolvency and Bankruptcy Code, 2016?
5. Discuss the institutional framework envisaged under the Insolvency and Bankruptcy Code, 2016 to achieve its objectives.
6. Write a note on the Insolvency and Bankruptcy Board of India (IBBI).
7. Discuss the jurisdiction of the Adjudicating Authorities under the Insolvency and Bankruptcy Board of India (IBBI).
8. Briefly mention the functions and obligations of the Insolvency professionals under the Insolvency and Bankruptcy Board of India (IBBI).
9. What is an information utility (IU) under the Insolvency and Bankruptcy Board of India (IBBI)? State its obligations.
10. Discuss with the help of a case law the overriding provisions of the Code with respect to other laws.

LIST OF FURTHER READINGS
● Insolvency and Bankruptcy Code, 2016 (Bare Act)

OTHER REFERENCES (Including Websites / Video Links)
● https://ibbi.gov.in

Application for Corporate Insolvency Resolution Process

Lesson 15

KEY CONCEPTS

■ Corporate Debtor ■ Financial Creditor ■ Operational Debt ■ Moratorium ■ Resolution Plan ■ Corporate Insolvency Resolution Process ■ Insolvency Professional

Learning Objectives

To understand:

- Concept of initiating CIRP
- Objective of CIRP
- Recommendations of BLRC Report
- Commencement of CIRP
- Sections, Regulations and Rules applicable in making application to initiate CIRP
- Withdrawal of application after admission
- Significance of Moratorium
- Judgements related to the provisions discussed

Lesson Outline

- Historical Background of CIRP
- Introduction
- Persons who may Initiate Corporate Insolvency Resolution Process
- Initiation of corporate insolvency resolution process by financial creditor
- Demand notice and initiation of Insolvency resolution by operational creditor
- Initiation of corporate insolvency resolution process by corporate applicant
- Corporate Debtors against which CIRP cannot be initiated
- Persons not entitled to make application to initiate CIRP
- Withdrawal of application admitted under section 7, 9 or 10 of IBC
- Time-limit for completion of insolvency resolution process
- Declaration of moratorium and public announcement
- Moratorium
- Rules 20, 21, 22, 23, 24 and 26 of Part III of the NCLT Rules, 2016
- Lesson Round-Up
- Test Yourself
- Other References

REGULATORY FRAMEWORK

- The Insolvency and Bankruptcy Code,2016 (Section 6 to section 14 with applicable provisions from other sections)
- The Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016
- The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016

HISTORICAL BACKGROUND OF CORPORATE INSOLVENCY RESOLUTION PROCESS

The Banking Law Reform Committee (BLRC) constituted under the chairmanship of Dr TK Viswnathan presented it's report in two Volume- Volume 1, which is a committee report showing rationale and arguments, and Volume 2 which is a draft law on the Insolvency and Bankruptcy Code.

While laying down framework of the Corporate Insolvency Resolution Process in draft Insolvency and Bankruptcy Code,2016, the report of the Bankruptcy Law Reform Committee (BLRC) Volume I in Rationale and Design of the Insolvency and Bankruptcy Code, 2016 has worded following:

"For some firms, the right answer after default is to take the firm into liquidation. But there may be many situations in which a viable mechanism can be found through which the firm is protected as a going concern. To the extent that this can be done, the costs imposed upon society go down, as liquidation involves the destruction of the organisational capital of the firm."

The Committee proposed following recommendations for advocating rationale of Corporate Insolvency Resolution Process (CIRP):

(i) *Any creditor, whether financial or operational, could initiate CIRP:* Under the Companies Act 2013, the following parties could file an application before NCLT for a declaration that company is sick- (a) the company, (b) any secured creditor, (c) the Central Government, (d) the Reserve Bank of India, (e) State Government, (f) public financial institution, (g) a State level institution, (h) a scheduled bank. Even under the SARFAESI, 2002, debt enforcement rights are available for secured creditors only. However, the Committee proposes that any creditor, whether financial or operational, should be able to initiate the insolvency resolution process (IRP) under the proposed code. It may be noted that operational creditors will include workmen and employees whose past payments are due.

(ii) *Protection for operational creditors in Resolution Plan:* The Committee also recommends that a resolution plan must necessarily provide for certain protections for operational creditors. This will empower the workmen and employees to initiate insolvency proceedings, settle their dues fast and move on to some other job instead of waiting for their dues for years together as is the case under the existing regime.

(iii) *Strategy for CIRP:* The strategy proposed by the Committee runs as follows, when default takes place an Insolvency Resolution Process (IRP) can be initiated and run for as long as 180 days.

(iv) *Role of IRP:* The IRP is overseen by an "Insolvency Professional" (IP) who is given substantial powers. The IP makes sure that assets are not stolen from the company, and initiates a careful check of the transactions of the company for the last two years, to look for illegal diversion of assets. Such diversion of assets would induce criminal charges.

(v) *Applicability of Calm Period:* While the IRP is in process, the law enshrines a "calm period" where creditors stay their claims. This gives a better chance for the firm to survive as a going concern.

(vi) *Time bound CIRP:* The Committee recommended that for the 180 days for which the IRP is in operation, the creditors committee will analyse the company, hear rival proposals, and make up its mind about what has to be done. When 75% of the creditors agree on a revival plan, this plan would be binding on all the remaining creditors. If, in 180 days, no revival plan achieves support of 75% of the creditors, the firm goes into liquidation.

(vii) *One time extension of time limit of 180 days:* In limited circumstances, if 75 % of the creditors committee decides that the complexity of a case requires more time for a resolution plan to be finalised, a one-time extension of the 180 day period for up to 90 days is possible with the prior approval of the adjudicator.

INTRODUCTION

The Preamble of the Code lays down the objective as follows:

"An Act to consolidate and amend the laws relating to reorganisation and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner for maximisation of value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders including alteration in the order of priority of payment of Government dues and to establish an Insolvency and Bankruptcy Board of India, and for matters connected therewith or incidental thereto."

Therefore, the Preamble itself made it clear that the purpose of the Code is to reorganize and resolve the insolvency of corporate persons along with maximization of assets of such corporate persons and not to liquidate it at first instance. Voluntary Liquidation is the only way to liquidate a company having no default.

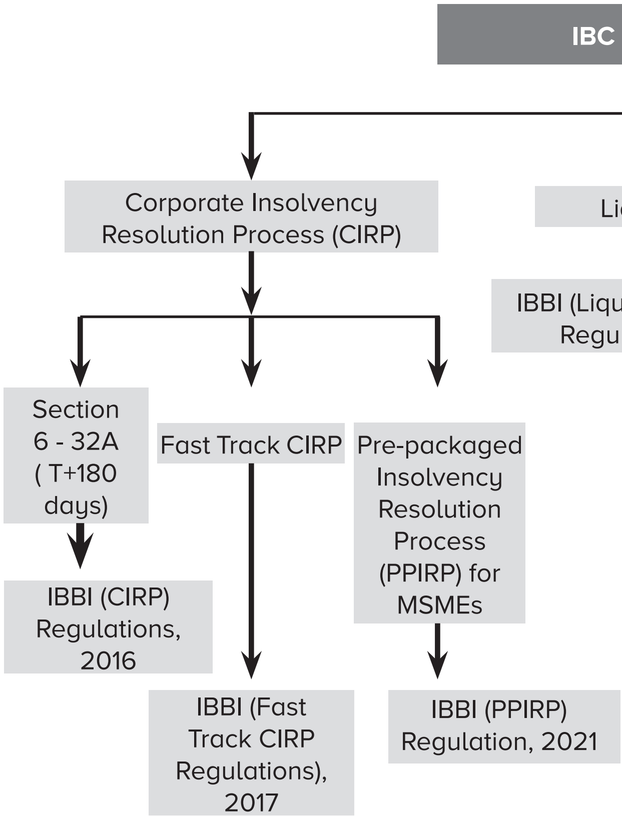
In the case of ***Swiss Ribbons Private Limited and Another Vs. Union of India and Others [(2019) 4 SCC 17]***, the Supreme Court upheld the constitutionality of the IBC and observed that the foremost and primary objective of the IBC is the reorganization and insolvency resolution of the CD in a time-bound manner.

The Code has five parts and Part II of the Insolvency and Bankruptcy Code, 2016 deals with the insolvency resolution and liquidation for corporate persons. Part II is summarized as follows:

THE INSOLVENCY AND BANKRUPTCY CODE, 2016		
PART II ***Insolvency Resolution and Liquidation for Corporate Persons***		
Chapter 1	Preliminary	Sections 4-5
Chapter II	Corporate Insolvency Resolution Process	Sections 6-32A
Chapter III	Liquidation Process	Sections 33-54
Chapter III-A	Pre-Packaged Insolvency Resolution Process	Sections 54A- 54P
Chapter IV	Fast Track Corporate Insolvency Resolution Process	Sections 55- 58
Chapter V	Voluntary Liquidation Of Corporate Persons	Sections 59
Chapter VI	Adjudicating Authority For Corporate Persons	Sections 60- 67A
Chapter VII	Offences and Penalties	Sections 68- 77A

Chapter II of Part II (Sections 6 to 32A) deals with the provisions for reorganization and resolution of insolvency process of Corporate Persons known as Corporate Insolvency Resolution Process (CIRP). CHAPTER IV of Part II (Sections 55- 58) covers Fast Track Corporate Insolvency Resolution Process meant for small companies. Both Chapter II and Chapter IV of Part II are covered here.

The expression "Corporate Insolvency Resolution Process" (CIRP) is not defined in the Insolvency and Bankruptcy Code, 2016. The IBBI (CIRP) Regulations,2016 as well as the Insolvency and Bankruptcy (Application



to Adjudicating Authority) Rules, 2016 defines the expression "corporate insolvency resolution process" in same way. According to Rule 3(1)(b), "corporate insolvency resolution process" means the insolvency resolution process for corporate persons under Chapter II of Part II of the Code.

Section 4 of the Insolvency and Bankruptcy Code, 2016 provides that Part II of the Code shall apply to matters relating to the insolvency and liquidation of corporate debtors where the minimum amount of the default is one lakh rupees. The proviso to section 4 empowers the Central Government to specify, by notification, the minimum amount of default of higher value but it shall not be more than one crore rupees.

Central Government has raised default limit of Corporate Debtor from 1 lakh to 1 crore w.e.f. 24.03.2020. So, CIRP can be initiated only if there is default of minimum Rs 1 crore by corporate debtor.

There were six modes of compulsory winding up of companies under the Companies Act, 1956. With the enactment of IBC,2016, winding up of companies due to their inability to pay debt will be governed by the provisions of the Code, 2016 while remaining will continue to be governed by the Companies Act,2013.

The Code contains the processes for starting and running the Corporate Insolvency Resolution Process (CIRP). To supplement this:

(i) *The Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016:* The Central Government has issued the Application to AA Rules, which detail the process and various steps involved in applying to the AA to initiate the CIRP.

(ii) *The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016* (hereinafter referred as the IBBI(CIRP) Regulations,2026): The IBBI has issued the CIRP Regulations, which detail the process and various steps involved in running a CIRP.

Persons who may Initiate Corporate Insolvency Resolution Process

Who can file application for CIRP?

A financial creditor | Operational Creditor | Corporate Debtor

Section 5(1) defines "Adjudicating Authority", for the purposes of Part II, means National Company Law Tribunal constituted under section 408 of the Companies Act, 2013

Section 6 of the Insolvency and Bankruptcy Code, 2016 provides that where any corporate debtor commits a default, a financial creditor, an operational creditor or the corporate debtor itself may initiate corporate insolvency resolution process in respect of such corporate debtor in the manner as provided under Chapter II of Part II of the Code.

(i) *Default is the mandatory trigger point to initiate CIRP:* Going by the combined reading of section 4 along with section 6 of the Code, CIRP can be initiated against a corporate debtor only if corporate debtor commits a default of Rs. 1(one) crore or more .

> "Default" is defined in section 3(12) of the IBC as non-payment of a debt when the whole or any part or installment of the amount of debt has become due and payable, and is not paid by the debtor or the corporate debtor, as the case may be.
>
> According to section 3(8), a "corporate debtor" means a corporate person who owes a debt to any person

(ii) *Who may initiate CIRP:* In case of a default, the following people are entitled to initiate a corporate insolvency resolution process:

- **A financial creditor**
- **An operational creditor**: According to section 5(20) an "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 or
- **The corporate debtor itself**: The Insolvency and Bankruptcy Code, 2016 permits the corporate debtor itself to initiate the insolvency resolution process once it has defaulted on a debt.

(iii) *Initiation Date:* Section 5 (11) of the Code defines "initiation date" as the date on which a financial creditor, corporate applicant or operational creditor, as the case may be, makes an application to the Adjudicating Authority for initiating corporate insolvency resolution process or pre-packaged insolvency resolution process, as the case may be.

Initiation of corporate insolvency resolution process by financial creditor

Section 7 of the Code lays down the procedure for the initiation of the corporate insolvency resolution process by a financial creditor or two or more financial creditors jointly.

Default of financial debt ≥ Rs 1 crore (Section 4) → Application to initiate CIRP under section 7 → Admission or rejection of application by the Adjudicating Authority

Application to initiate corporate insolvency resolution process: Section 7(1) of the Codes states that who can file application to initiate corporate insolvency resolution process:

- a financial creditor, either by itself or jointly with other financial creditors, or
- any other person on behalf of the financial creditor, as may be notified by the Central Government, may file an application for initiating a corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred in payment of financial debt by the financial creditor.

For the purpose of section 7(1), a default includes a default on a financial debt owed not only to the applicant financial creditor but to any other financial creditor of the corporate debtor.

> According to Section 5(7), a "financial creditor" means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to.

Financial Debt (Sec, 5(8) means a debt along with 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 dematerialised 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 non-recourse basis;
- (f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing;
  - *Explanation*, For the proposes of this sub-clause,
    - (i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and
    - (ii) the expressions, "allottee" and "real estate project" shall have the meanings respectively assigned to them in clauses (d) and (zn) of section 2 of the Real Estate (Regulation and Development) Act, 2016.
- (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;

First proviso to section 7(1) provides that an application for initiating corporate insolvency resolution process against the corporate debtor shall be filed jointly by not less than one hundred of such creditors in the same class or not less than ten per cent of the total number of such creditors in the same class, whichever is less if financial creditors belong to clauses (a) and (b) of sub-section (6A) of section 21.

Section 21(6A) provides for following creditors in clause (a) and (b) as follows:

(a) Where a financial debt is in the form of securities or deposits and the terms of the financial debt provide for appointment of a trustee or agent to act as authorised representative for all the financial creditors

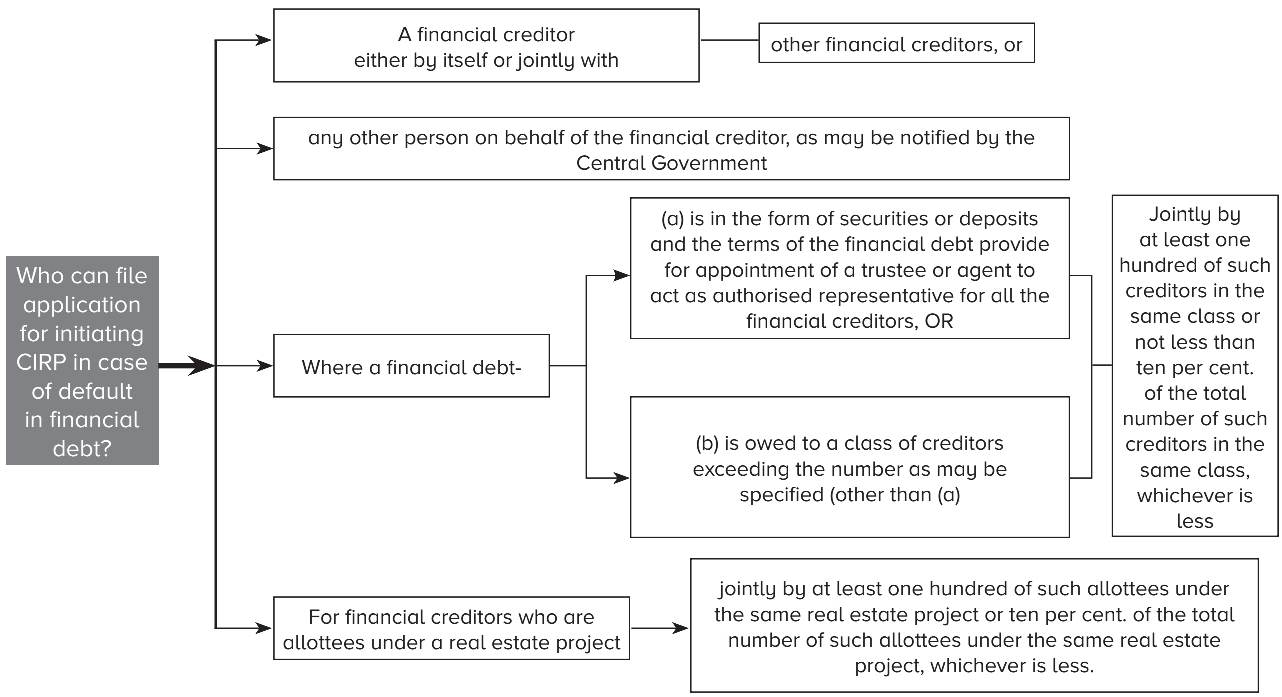
(b) Where a financial debt- is owed to a class of creditors exceeding the number as may be specified (i.e., ten) but do not fall in

- Clause (a) or
- Section 21(6) i.e., where the terms of the financial debt extended as part of a consortium arrangement or syndicated facility do not provide for a single trustee or agent to act for all financial creditors.

> The IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 defines in Regulation 2(1) (aa) "class of creditors" which means a class with at least ten financial creditors under clause (b) of sub-section (6A) of section 21 and the expression, "creditors in a class" shall be construed accordingly.

As explanation to section 5(8) (f) has clarified that any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing and therefore, a financial debt, It is further provided in section 7(1) that an application for initiating corporate insolvency resolution process against the corporate debtor shall be filed jointly by not less than one hundred of such allottees under the same real estate project or not less than ten per cent of the total number of such allottees under the same real estate project, whichever is less.

It is to be noted that applicant shall be allottees under the same real estate project.



Application to be made in prescribed form with prescribed fee:

- Section 7(2) of the Code states *that t*he financial creditor shall make an application under sub-section (1) in such form and manner and accompanied with such fee as may be prescribed.

- *The Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016* spell out the procedural part of making application by financial creditor under section 7 of the Code as follows:

  Application by financial creditor (Rule 4)—

  (1) A financial creditor, either by itself or jointly along with prescribed fee shall make an application for initiating the corporate insolvency resolution process against a corporate debtor under section 7 of the Code in Form 1, accompanied with documents and records required therein and as specified in the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.

  (2) Where the applicant under sub-rule (1) is an assignee or transferee of a financial contract, the application shall be accompanied with a copy of the assignment or transfer agreement and other relevant documentation to demonstrate the assignment or transfer.

  (3) The applicant shall serve a copy of the application to the registered office of the corporate debtor and to the Board, by registered post or speed post or by hand or by electronic means, before filing with the Adjudicating Authority.

  (4) In case the application is made jointly by financial creditors, they may nominate one amongst them to act on their behalf.

Fee payable: The financial creditor should submit the application to the Adjudicating Authority as per the applicable rules/procedures of the relevant Adjudicating Authority, along with prescribed fee of 25,000 Indian rupees in favor of the Pay and Accounts Officer, Ministry of Corporate Affairs, payable in Mumbai, New Delhi, Kolkata, or Chennai.

Documents to be furnished with the application:

- Section 7(3) of the Code provides that the financial creditor shall, along with the application furnish:

  (a) record of the default recorded with the information utility or such other record or evidence of default as may be specified;

  (b) the name of the resolution professional proposed to act as an interim resolution professional; and

  (c) any other information as may be specified by the Board.

- The IBBI (CIRP) Regulations, 2016 provides in Regulation 2A for record or evidence of default by financial creditor. It states that for the purposes of clause (a) of sub-section (3) of section 7 of the Code, the financial creditor may furnish any of the following record or evidence of default, namely: -

  (a) certified copy of entries in the relevant account in the bankers' book as defined in clause (3) of section 2 of the Bankers' Books Evidence Act, 1891 (18 of 1891);

  (b) an order of a court or tribunal that has adjudicated upon the non-payment of a debt, where the period of appeal against such order has expired.

Time frame for ascertaining the existence of default.

- Section 7(4) of the Code provides for the timeline for AA to either accept or reject the application.
- The Adjudicating Authority shall, within **fourteen days** of the receipt of the application under sub-section (2), ascertain the existence of a default from the records of an information utility or on the basis of other evidence furnished by the financial creditor under sub-section (3).
- Provided that if the Adjudicating Authority has not ascertained the existence of default and passed an order under sub-section (5) within such time, it shall record its reasons in writing for the same.

Decision criterion for the Adjudicating Authority is whether default exists or not.

> In the matter of *Surendra Trading Company v. Juggilal Kamlapat Jute Mills Company Limited and Other,* the Supreme Court held that time period of 14 days is directory and not mandatory.

Admission or rejection of application by the Adjudicating Authority:

According to section 7(5), where the Adjudicating Authority is satisfied that –

(a) a default has occurred and the application under sub-section (2) is complete, and there is no disciplinary proceedings pending against the proposed resolution professional, it may, by order, admit such application; or

(b) default has not occurred or the application under sub-section (2) is incomplete or any disciplinary proceeding is pending against the proposed resolution professional, it may, by order, reject such application:

Provided that the Adjudicating Authority shall, before rejecting the application under clause (b) of sub-section (5), give a notice to the applicant to rectify the defect in his application within seven days of receipt of such notice from the Adjudicating Authority.

Insolvency Commencement Date*:* Section 7(6) states that the corporate insolvency resolution process shall commence from the date of admission of the application under sub-section (5).

Section 5(12) of the Code defines "insolvency commencement date" which means the date of admission of an application for initiating corporate insolvency resolution process by the Adjudicating Authority under sections 7, 9 or section 10, as the case may be.

Timeline for communication of order by the Adjudicating Authority*:*

Section 7(7) makes it mandatory for the Adjudicating Authority to communicate-

(a) the order of admission within 7 days of decision of admission of such application under clause (a) of sub-section (5) to the financial creditor and the corporate debtor;

(b) the order of rejection within 7 days of decision of rejection of such application under clause (b) of sub-section (5) to the financial creditor,

FORM 1 to be filed by Financial creditor is divided in five parts detailed as:	
Form 1 **APPLICATION BY FINANCIAL CREDITOR(S) TO INITIATE CORPORATE INSOLVENCY RESOLUTION PROCESS UNDER THE CODE.** (Under section 7 of the Insolvency and Bankruptcy Code, 2016 read with Rule 4 (1) of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016)	
Part-I	PARTICULARS OF APPLICANT (PLEASE PROVIDE FOR EACH FINANCIAL CREDITOR MAKING THE APPLICATION)
Part-II	PARTICULARS OF THE CORPORATE DEBTOR
Part-III	PARTICULARS OF THE PROPOSED INTERIM RESOLUTION PROFESSIONAL
Part - IV	PARTICULARS OF FINANCIAL DEBT
Part-V	PARTICULARS OF FINANCIAL DEBT [DOCUMENTS, RECORDS AND EVIDENCE OF DEFAULT]
Attachment	Copies of all documents referred to in this application.
	Written communication by the proposed interim resolution professional as set out in Form 2.
	Proof that the specified application fee has been paid.
	Where the application is made jointly, the particulars specified in this form shall be furnished in respect of all the joint applicants along with a copy of authorisation to the financial creditor to file and act on this application on behalf of all the applicants.

Practical Questions

Case: There are three financial creditors AM Bank, BN financial institution, CP Bank of XYZ Limited. An application for initiating CIRP has to be made against XYZ Limited as it has made default in repaying debt of AM Bank of Rs 70 Lakhs and BN financial institution of Rs 50 Lakhs. However, there is no default in repayment of debt of CP Bank having outstanding of Rs. 30 Lakhs. Answer the following queries:

Q. Can Corporate Insolvency Resolution Process (CIRP) be initiated against XYZ Limited?

Ans: Yes, CIRP can be initiated against XYZ Limited by the financial creditor as it has committed default in repayment of debt worth Rs. 1.2 crore (70+50 Lakhs) whereas section 4 of the Code provides that CIRP can be initiated against a corporate debtor if it commits default of Rs. 1 crore or more.

Section 7(1) of the Codes states that a financial creditor, either by itself or jointly with other financial creditors, or any other person on behalf of the financial creditor, as may be notified by the Central Government, may file an application for initiating a CIRP against a corporate debtor before the Adjudicating Authority when a default has occurred in payment of financial debt by the financial creditor. For the purpose of section 7(1), a default includes a default on a financial debt owed not only to the applicant financial creditor but to any other financial creditor of the corporate debtor.

Therefore, as joint application is permitted, default of both financial creditors will be clubbed for knowing whether it has committed default in repayment of debt of Rs 1 cr or more.

Q. Can CP Bank initiate CIRP against XYZ Limited?

Ans: Yes, CP Bank can initiate CIRP against XYZ Limited as Explanation to section 7(1) provides that for the purposes of this sub-section, a default includes a default in respect of a financial debt owed not only to the applicant financial creditor but to any other financial creditor of the corporate debtor.

Q. Whether AM Bank and BN financial institution have to file joint application or they may file it individually?

Ans: Pursuant to provisions of section 7(1) of the Code, AM Bank and BN financial institution can file application to initiate CIRP individually or jointly too.

Q. Whether a Power of Attorney holder of Financial Creditor can initiate insolvency proceedings under the Code?

Legal Provision

1. Entry 5 & 6 (Part I) of Form 1 mandates the Financial Creditor to submit name and address of person authorized to submit application. Further, the particulars shall be signed by person authorized to act on behalf of financial creditor at the end.

2. Similar provision is made with regard to application by Operational Creditor and corporate applicant i.e., the application must be signed by a person authorized.

3. Rule 23(1) of NCLT Rules reads as under:

"23. Presentation of petition or appeal – (1) Every petition, application, caveat, interlocutory application, documents and appeal shall be presented in triplicate by the appellant or

applicant or petitioner or respondent, as the case may be, in person or by his duly authorised representative or by an advocate duly appointed in this behalf in the prescribed form with stipulated fee at the filing counter and non-compliance of this may constitute a valid ground to refuse to entertain the same.

In ***Palogix Infrastructure Pvt. Ltd. v. ICICI Bank Ltd. [Company Appeal (AT) (Insol.) No. 30 of 2017]***, NCLAT held that a 'Power of Attorney Holder' is not competent to file an application on behalf of a 'Financial Creditor' or 'Operational Creditor' or 'Corporate Applicant'. NCLAT held that a power of attorney holder is not authorised to present application for CIRP under sections 7, 9 and 10 of the Code. It is only authorised representatives, duly authorised by board resolution, who are eligible to present the same.

Whether NCLT, in exercise of its inherent powers, can convert an application under section 9 of the Code by an operational creditor to an application under section 7 of the Code by a Financial Creditor?
In ***Sanjeev Jain vs. M/s Eternity Infracon Pvt. Ltd. [Company Petition no. (IB) 113(ND)/2017]***, the NCLT observed as under: 16... The Code prescribes stipulated time frame to be followed at every relevant stage of the resolution proceedings. Besides the insolvency resolution process has serious civil consequences, which suggests for a cautious approach strictly in accordance with the procedure prescribed by the Code. 17. ...It is also pertinent to note that the provisions and scope of Section 9 including the applicable rules, forms and procedure are totally distinct and separate from that of Section 7 of the Code. There is no provision in the Code to convert a section 9 application into a section 7 as prayed. On the contrary, the Code provides that applications filed under section 7, 9 or 10 as the case may be, should either be admitted or rejected in accordance with respective provisions.

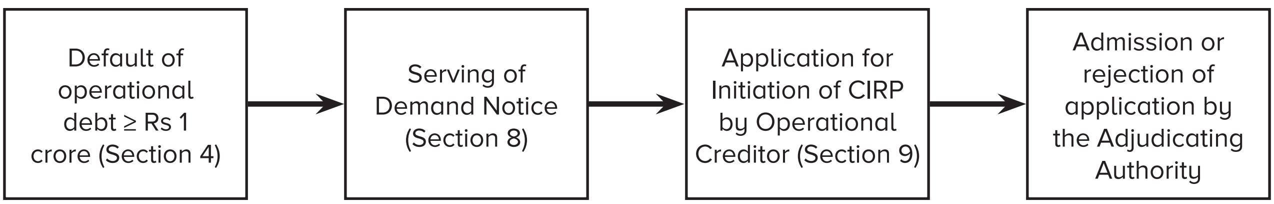
Operational Creditors

An Operational Creditor is defined under section 5(20) of the Code as any person to whom an operational debt is owed (and includes a legal assignee/transferee).

An "operational debt" is defined in section 5(21) as a claim in respect of the provision of goods or services including employment or a debt in respect of the payment 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;

An application to initiate a corporate insolvency resolution process against a corporate debtor may be filed by an operational creditor under section 9 of the Code. However, before filing the application, the operational creditor must serve a demand notice on the corporate debtor under section 8 of the Code.

Insolvency resolution by operational creditor



The rationale for a different procedure in case of operational creditor is based on the premise that the operational debts (such as trade debts, salary or wage claims, and government dues) generally tend to be of smaller amounts (in comparison to financial debts) or are recurring in nature. The possibility of disputed debts in relation to operational creditors is also higher in comparison to financial creditors such as banks and financial institutions.

***Serving of Demand Notice* (Section 8)**

- *Demand notice or copy of invoice demanding payment of the debt*: Section 8(1) of IBC states that an operational creditor may, on the occurrence of a default, deliver a demand notice of unpaid operational debtor copy of an invoice demanding payment of the amount involved in the default to the corporate debtor in such form and manner as may be prescribed.
- Explanation to section 8 of the Code states that for the purposes of this section, a "demand notice" means a notice served by an operational creditor to the corporate debtor demanding payment of the operational debt in respect of which the default has occurred.
- *The Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016:* Rule 5 of these rules prescribes Form in which demand notice or copy of invoice demanding payment shall be served and the manner in which it shall be served as follows:

Demand notice by operational creditor (Rule 5)—

(1) An operational creditor shall deliver to the corporate debtor, the following documents, namely. -

(a) a demand notice in Form 3; or

(b) a copy of an invoice attached with a notice in Form 4.

(2) The demand notice or the copy of the invoice demanding payment referred to in sub-section (2) of section 8 of the Code, may be delivered to the corporate debtor,

(a) at the registered office by hand, registered post or speed post with acknowledgement due; or

(b) by electronic mail service to a whole-time director or designated partner or key managerial personnel, if any, of the corporate debtor.

(3) A copy of demand notice or invoice demanding payment served under this rule by an operational creditor shall also be filed with an information utility, if any.

In most cases, the demand notice is delivered through registered post/hand delivery, or via an email. Acknowledgment/proof of delivery of the demand notice must be provided to the Adjudicating Authority as part of the application by the operational creditor under section 9 of the Code.

The important particulars of FORM 3 and FORM 4 are emphasized as follows:

<table>
<tr><td colspan="3">FORM 3
FORM OF DEMAND NOTICE / INVOICE DEMANDING PAYMENT UNDER THE INSOLVENCY AND BANKRUPTCY CODE, 2016
(Under rule 5 (1)(a) of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016)</td></tr>
<tr><td colspan="3">1. It has to be stated specifically that this letter is a demand notice/invoice demanding payment of an unpaid operational debt due from [name of corporate debtor].</td></tr>
<tr><td colspan="3">2. PARTICULARS OF OPERATIONAL DEBT has to be clearly stated in terms of
● total amount of debt due,
● transactions in terms of which debt is due and the date it fell due,
● amount claimed to be in default and the date of default,
● details of security if any,
● details of retention of title, if any,
● Provision of Law, Contract or other Document under which Debt has become due.</td></tr>
<tr><td colspan="3">Other contents of Information to be stated in FORM 3</td></tr>
<tr><td rowspan="3">Operational Creditor has to specifically ask Corporate Debtor to provide proof of pendency of pre-existing dispute or payment of debt, if it has been paid already.</td><td colspan="2">If you dispute the existence or amount of unpaid operational debt (in default) please provide the undersigned, within ten days of the receipt of this letter, of the pendency of the suit or arbitration proceedings in relation to such dispute filed before the receipt of this letter/notice.</td></tr>
<tr><td rowspan="2">If you believe that the debt has been repaid before the receipt of this letter, please demonstrate such repayment by sending to us, within ten days of receipt of this letter, the following:</td><td>a) an attested copy of the record of electronic transfer of the unpaid amount from the bank account of the corporate debtor; or</td></tr>
<tr><td>b) an attested copy of any record that [name of the operational creditor] has received the payment.</td></tr>
</table>

Attachment	The workings for computation of default in tabular form
	Copy of a certificate of registration of charge issued by the registrar of companies (if the corporate debtor is a company)
	Record of default with the information utility (if any)
Operational Creditor has to attach confirmation from Information Utility for no record of dispute with it, if applicable.	The undersigned, hereby, attaches a certificate from an information utility confirming that no record of a dispute raised in relation to the relevant operational debt has been filed by any person at any information utility. (if applicable)
It has to be a demand notice specifically asking for Unconditional repayment in full within 10 days with declaration that if payment not made in time, Operational Creditor shall initiate corporate insolvency resolution process.	The undersigned request you to unconditionally repay the unpaid operational debt (in default) in full within ten days from the receipt of this letter failing which we shall initiate a corporate insolvency resolution process in respect of [name of corporate debtor.

Form 4 **(See clause (b) of sub-rule (1) of rule 5)** **FORM OF NOTICE WITH WHICH INVOICE DEMANDING PAYMENT IS TO BE ATTACHED** **(Under Rule 5 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016)**
[Name of operational creditor], hereby provides notice for repayment of the unpaid amount of INR [insert amount] that is in default as reflected in the invoice attached to this notice.
In the event you do not repay the debt due to us within ten days of receipt of this notice, we may file an application before the Adjudicating Authority for initiating a corporate insolvency resolution process under section 9 of the Code.
FORM 4 has to be sent with invoice and it is mandatory to quantify debt defaulted as well an intimation of initiating CIRP if corporate debtor fails to repay within 10 days of receipt of this notice.

Existence of dispute or payment of debt

- Section 8(2) of the Code mandates the corporate debtor to bring to the notice of the operational creditor, within a period of ten days of the receipt of the demand notice or copy of the invoice mentioned in sub-section (1)–
  - (a) existence of a dispute, if any, or record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute;
  - (b) the payment of unpaid operational debt-
    - (i) by sending an attested copy of the record of electronic transfer of the unpaid amount from the bank account of the corporate debtor; or
    - (ii) by sending an attested copy of record that the operational creditor has encashed a cheque issued by the corporate debtor.

> Section 5(6) of the Code defines dispute as "dispute" includes a suit or arbitration proceedings relating to–
>
> (a) the existence of the amount of debt;
>
> (b) the quality of goods or service; or
>
> (c) the breach of a representation or warranty.

Application for Initiation of Corporate Insolvency Resolution Process by Operational Creditor (Section 9)

- The Insolvency and Bankruptcy Code ,2016 (Section 9): (i) *Application to initiate CIRP by Operational Creditor:* After the expiry of the period of ten days from the date of delivery of the notice or invoice demanding payment under sub-section (1) of section 8, if the operational creditor does not receive payment from the corporate debtor or notice of the dispute under sub-section (2) of section 8, the operational creditor may file an application before the Adjudicating Authority for initiating a corporate insolvency resolution process in such form and manner and accompanied with such fee , as may be prescribed.

- *The Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016:* Rule 6 of the Rules prescribes that:

  (1) An operational creditor, shall make an application for initiating the corporate insolvency resolution process against a corporate debtor under section 9 of the Code in **Form 5**, accompanied with documents and records required therein and as specified in the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.

  (2) The applicant under sub-rule (1) shall serve a copy of the application to the registered office of the corporate debtor and to the Board, by registered post or speed post or by hand or by electronic means, before filing with the Adjudicating Authority.

The Form 5 is divided in five parts, each providing for the submission of the following particulars:

Form 5 **APPLICATION BY OPERATIONAL CREDITOR TO INITIATE CORPORATE INSOLVENCY RESOLUTION PROCESS UNDER THE CODE.** (Under rule 6 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016)	
Part – I	PARTICULARS OF APPLICANT
Part – II	PARTICULARS OF CORPORATE DEBTOR
Part-III	PARTICULARS OF THE PROPOSED INTERIM RESOLUTION PROFESSIONAL [IF PROPOSED]
Part-IV	PARTICULARS OF OPERATIONAL DEBT
Part-V	PARTICULARS OF OPERATIONAL DEBT [DOCUMENTS, RECORDS AND EVIDENCE OF DEFAULT]
Note:	Where workmen/employees are operational creditors, the application may be made either in an individual capacity or in a joint capacity by one of them who is duly authorised for the purpose.

Documents to be submitted with the application:

- *The Insolvency and Bankruptcy Code ,2016 (Section 9):* As per section 9 (3) of the IBC, the Operational Creditor shall, along with the application, furnish:

  (a) a copy of the demand notice delivered by the operational creditor to the corporate debtor;

  (b) an affidavit to the effect that there is no notice given by the corporate debtor relating to a dispute in the unpaid operational debt (that is, no notice under section 8(2) of the IBC);

  (c) a copy of a certificate from financial institutions maintaining accounts of the operational creditor confirming that there is no payment of an unpaid operational debt by the corporate debtor, if available;

(d) a copy of any record with an Information Utility (IU) confirming that there has been no payment of an unpaid operational debt by the corporate debtor, if available;

(e) any other proof confirming that there has been no payment of the unpaid operational debt by the corporate debtor or such other information as may be prescribed;

- *The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (Regulations 2B):* Record or evidence of transaction, debt and default by operational creditor (Regulation 2B): The operational creditor shall, alongwith application under section 9, furnish copies of relevant extracts of Form GSTR-1 and Form GSTR-3B filed under the provisions of the relevant laws relating to Goods and Services Tax and the copy of e-way bill wherever applicable:

  Provided that provisions of this regulation shall not apply to those operational creditors who do not require registration and to those goods and services which are not covered under any law relating to Goods and Services Tax.

- *The Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016:* Form 5 to be furnished pursuant to Rule 6 prescribes following annexure to be filed along with it:

Annex	1. Copy of the invoice / demand notice as in Form 3 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 served on the corporate debtor. 2. Copies of all documents referred to in this application. 3. Copy of the relevant accounts from the banks/financial institutions maintaining accounts of the operational creditor confirming that there is no payment of the relevant unpaid operational debt by the operational debtor, if available. 4. Affidavit in support of the application in accordance with the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016. 5. Written communication by the proposed interim resolution professional as set out in Form 2 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016. [WHERE APPLICABLE] 6. Proof that the specified application fee has been paid.

The application should be submitted by the operational creditor to the Adjudicating Authority (AA) complying with the applicable rules/procedures of the relevant AA, along with a demand draft of 2,000 Indian rupees in favor of the Pay and Accounts Officer, Ministry of Corporate Affairs, payable in Mumbai, New Delhi, Kolkata, or Chennai.

(iii) Recommending name of Interim Resolution Professional is discretionary for Operational Creditor:

Section 9(4) provides that an operational creditor initiating a corporate insolvency resolution process under this section, may propose a resolution professional to act as an interim resolution professional.

If not proposed, the Adjudicating Authority will appoint an interim resolution professional, usually from the panel formed by the IBBI.

Macquarie Bank Limited Vs. Shilpi Cable Technologies Ltd. [(2018) 2SCC 674]

In this case, the Supreme Court held that

- A certificate from the financial institution maintaining accounts of an operational creditor (as provided for in section 9(3) of the IBC) is not mandatory for triggering a CIRP of the corporate debtor. The debt and default can be proved by other documents as well.
- An authorized agent or a lawyer acting on behalf of a client can issue a demand notice under section 8(2) of the IBC.
- Section 9(4) of the IBC states that an operational creditor may propose an insolvency professional to act as an Interim Resolution Professional (IRP). If not proposed, the Adjudicating Authority will appoint an IRP, usually from the panel formed by the IBBI.

Query: Whether the Principal and Interest amounts can be clubbed together to reach the minimum threshold of Rs. 1 Crore for operational debt as stipulated under Section 4 of IBC, 2016?
NCLT Chandigarh Bench in the matter of ***M/s. Wanbury Ltd. Vs. M/s. Panacea Biotech Ltd. in CP No. 8/2016 dated 18.04.2017*** held that – "There is a marked difference between the definition of the term 'financial debt' and the 'operational debt'. Under Section 5(8) the term 'financial debt' means a debt along with interest, if any, which is disbursed against the consideration for the time value of money and that is an inclusive definition. In the definition of the term 'operational debt' under section 5(21) the word 'interest' has not been mentioned..." In the light of the above decision, it was held by NCLT, New Delhi Bench in *CBRE South Asia Private Limited vs. M/s. United Concepts and Solutions Private Limited, (IB)-797(ND)2021*, that the Interest amount cannot be clubbed with the principal amount of operational debt to arrive at the minimum threshold of Rs.1 Crore for complying with the provision of Section 4 of IBC, 2016.

Whether two or more operational creditors can file a joint application under section 9 of the Code?
In ***Uttam Galva Steels Limited vs. DF Deutsche Forfait AG & Anr. [Company Appeal (AT) (Insolvency) 39 of 2017], decided on 28th July, 2017***, an application was filed by two Operational Creditors namely M/s DF Deutsche Forfait AG ("Deutsche") and Misr Bank Europe GmbH ("Misr Bank") against Uttam Galva Steels Limited, Corporate Debtor ("Uttam Galva") stating that the Corporate Debtor had defaulted in making payment of an amount payable towards 20,000 tons of prime steel billets supplied by German Company named AIC Handels GmbH ("AIC Handels"). The debt, running to the tune of around Rs. 110 crores, was initially assigned by AIC Handels to Deutsche by entering into a discount agreement, thereafter Deutsche, in turn, subsequently assigned a part of this debt to Misr Bank. This is how the application came to be filed by above two Operational Creditors. The application was accepted by NCLT and CIRP was initiated against Uttam Galva. In appeal before NCLAT, a contention was raised by Uttam Galva that the joint application filed two Operational Creditors was not maintainable. NCLAT, upon perusal of definition of section 9 and section 7 of the Code, came to the conclusion that since the language used in section 9 of the Code is different from section 7 of the Code, two or more operational creditors cannot file a joint application under section 9 of Code. NCLAT noted that in section 7 of Code, it is specifically written that a Financial Creditor can file application either by 'itself or jointly with other financial creditors', whereas, such phrase is not used in section 9 of Code.

Admission or rejection of application by Adjudicating Authority (AA)

Section 9(5) provides the conditions subject to which the Adjudicating Authority shall, within fourteen days of the receipt of the application under sub-section (2), by an order, admit or reject the application.

Clause (i) provides that AA shall admit the application and communicate such decision to the operational creditor and the corporate debtor if, -

(a) the application made under sub-section (2) is complete;

(b) there is no payment of the unpaid operational debt;

(c) the invoice or notice for payment to the corporate debtor has been delivered by the operational creditor;

(d) no notice of dispute has been received by the operational creditor or there is no record of dispute in the information utility; and

(e) there is no disciplinary proceeding pending against any resolution professional proposed under sub-section (4), if any.

Clause (ii) provides that Adjudicating Authority shall reject the application and communicate such decision to the operational creditor and the corporate debtor, if –

(a) the application made under sub-section (2) is incomplete;

(b) there has been payment of the unpaid operational debt;

(c) the creditor has not delivered the invoice or notice for payment to the corporate debtor;

(d) notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility; or

(e) any disciplinary proceeding is pending against any proposed resolution professional:

It is provided that Adjudicating Authority shall, before rejecting an application under sub-clause (a) of clause (ii), give a notice to the applicant to rectify the defect in his application within seven days of the date of receipt of such notice from the adjudicating Authority.

Decision of admission or rejection of application shall be communicated to both operational creditor and corporate debtor.

In ***Mobilox Innovations Pvt. Ltd. Vs. Kirusa Software Pvt. Limited [(2018) 1 SCC 353]***, the Supreme Court undertook a detailed analysis of the provisions relating to applications by an operational creditor (OC) under section 9 of the IBC and laid down the following principles:

When examining an application under section 9 of the IBC, the NCLT will have to determine:

i. whether there is an operational debt exceeding Rs 100,000;

ii. whether the documentary evidence furnished with the application demonstrates that the debt is due and has not yet been paid;

iii. whether there are any disputes between the parties over the debt, or a record of pendency of any suit or arbitration proceeding filed before the receipt of the demand notice in relation to the dispute.

If any of the above conditions are not satisfied, the operational creditor's application will be rejected by the Adjudicating Authority. Any "notice of dispute" issued by the corporate detbor under section 8(2) of the IBC must bring to the notice of the operational creditor the "existence of a dispute," or the fact that a suit or arbitration proceedings relating to a dispute is pending between the parties. What is important is that the dispute must predate the receipt of the demand notice. The definition of "dispute" in section 5(6) is inclusive. It must relate to one of the three sub-clauses of section 5(6)–(a) the existence of the amount of debt, (b) the quality of goods or service, or (c) the breach of a representation or warranty, either directly or indirectly.

The difference between initiating CIRP by financial creditor and operational Creditor was laid down by Apex Court in ***Innoventive Industries Ltd. Vs. ICICI Bank & Another [(2018) 1 SCC 407]***

The first application to be filed under section 7 of the IBC was by ICICI Bank, financial creditor (the FC) against Innoventive Industries Limited, corporate debtor (the CD). The application was admitted by the Mumbai bench of the Adjudicating Authority (AA). The directors of the CD appealed against the admission order. The NCLAT upheld the order passed by the AA. The directors then appealed to the Supreme Court. The Supreme Court observed that since the application filed by the financial creditor was the very first application that had been moved under the IBC, it was necessary to deliver a detailed judgment so that all courts and tribunals would take notice of a paradigm shift in the law. The Supreme Court noted that entrenched managements are no longer allowed to continue in management if they cannot pay their debts and went on to examine various aspects of the IBC, especially section 7.

The Supreme Court held that:

- A financial creditor can trigger section 7(1) of the IBC for default of a financial debt owed by the corporate debtor to any financial creditor. It need not be a debt owed to the financial creditor who is the applicant.

- Under section 8 of the IBC, a dispute that existed before the receipt of a demand notice/invoice by the corporate debtor will make the application of an operational creditor inadmissible. On the other hand, under section 7, the moment the AA is satisfied that a default has occurred, the application of the financial creditor must be admitted unless it is incomplete, in which case it may give notice to the applicant to rectify the errors within seven days of receiving a notice from the Adjudicating Authority.
- The concept of "default" under the IBC is very wide. It is simply a non-payment of debt that has become due and includes non-payment of even a part of it. Even non-payment of a disputed financial debt when due would constitute a default under the IBC. In other words, so long as the debt is due it does not matter if it is disputed.

In ***Swiss Ribbons Private Limited and Another Vs. Union of India and Others [(2019) 4 SCC 17]***, the Supreme Court held that a review of the definition of "financial creditor" and "financial debt" makes it clear that a financial debt is a debt together with any interest that is disbursed against the consideration for the time value of money.

It may further be money that is borrowed or raised in any of the manners prescribed in section 5(8) or otherwise, as section 5(8) provides an inclusive definition. On the other hand, an "operational debt" would include a claim for the provision of goods or services, including employment, or a debt in respect of payment of dues arising under any law, and payable to the government or any local authority.

The court further observed that most financial creditors, particularly banks and financial institutions, are secured creditors whereas most operational creditors are unsecured—payments for goods and services as well as payments to workers not being secured by mortgaged documents and the like. The distinction between secured and unsecured creditors has been made since the earliest of the Companies Acts was passed both in the United Kingdom and in this country. Moreover, the nature of the loan agreements with financial creditors differs from contracts with operational creditors for supplying goods and services. Financial creditors generally lend finance on a term loan or for working capital that enables the corporate debtor to set up or operate its business. On the other hand, contracts with operational creditors relate to the supply of goods and services in the operation of the business. Financial contracts generally involve large sums of money. In contrast, the dues of operational contracts are generally lower. In the running of a business, operational creditors can be many as opposed to financial creditors. In addition, financial creditors have specified repayment schedules, and defaults entitle financial creditors to recall a loan in totality. Contracts with operational creditors do not have such stipulations. Also, the forum in which dispute resolution takes place is completely different. Contracts with operational creditors can and do have arbitration clauses where dispute resolution is done privately. The court observed that operational debts also tend to be recurring in nature and the possibility of genuine disputes in the case of operational debts is much higher compared to financial debts.

The court held that, most importantly, financial creditors are, from the very beginning, involved with assessing the viability of the corporate debtor. They can and do engage in restructuring the loan as well as reorganizing the corporate debtor's business when there is financial stress. These are steps that operational creditor do not and cannot take. Thus, to preserve the corporate debtor as a going concern, while ensuring maximum recovery for all creditors, the IBC needs to distinguish between financial creditors and operational creditors. The difference directly relates to the IBC's objectives.

Other requisites in filing application u/s 7 or 9:

Submission of information along with application. The financial creditor or operational creditor shall, while filing application under section 7 or 9, as the case may be, also furnish details of his/ its— (a) Permanent Account Number; and (b) Email-ID.

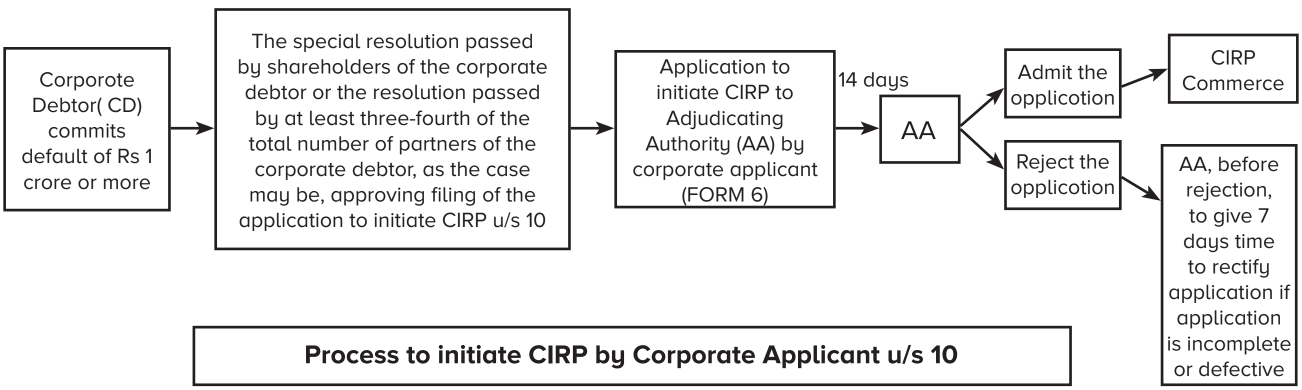
Details of debt, default and limitation in respect of applications under section 7 or section 9.

While filing an application under section 7 or 9, the financial creditor or the operational creditor, as the case may be, shall also submit along with evidence, chronology of the debt and default including the date when the debt became due, date of default, dates of part payments, if any, date of last acknowledgment of debt and the limitation applicable.

The Insolvency and Bankruptcy Board of India (Information Utilities) Regulations, 2017

- As per regulation 20 of the Insolvency and Bankruptcy Board of India (Information Utilities) Regulations, 2017 ("IU Regulations"), a creditor needs to submit financial information to the IU in Form C of the schedule. The documents to be uploaded as evidence for 'debt'/ or 'default of debt', have been specified by the Board in Form C.
- Vide notification dated 14th June, 2022, Sub-regulation (1A) has been inserted in the Regulation 20 which makes it mandatory for the creditor to file the information of default, with the information utility before filing an application to initiate corporate insolvency resolution process under section 7 or 9, as the case may be and the information utility shall process the information for the purpose of issuing record of default in accordance with Regulation 21.
- Sub-regulation (4) of Regulation 21 provides that after recording the status of information of default under sub-regulation (3), the information utility shall communicate the status of authentication in physical or electronic form of the relevant colour, indicating whether default is authenticated or disputed, as the case may be, by issuing a record of default in Form D of the Schedule, to the registered users who are-
  (a) creditors of the debtor who has defaulted in payment of a debt;
  (b) parties and sureties, if any, to the debt in respect of which the information of default has been received.

Initiation of corporate insolvency resolution process by corporate applicant (Section 10)



Process to initiate CIRP by Corporate Applicant u/s 10

Section 10 of the Code provides an option to the corporate debtor to voluntary initiate process of corporate insolvency resolution in case of default. So, it is not necessary that only financial or operational creditors come forward to opt for IBC to resolve insolvency of corporate debtor and run it as going concern but corporate debtor itself can be applicant to initiate it's own CIRP.

A corporate applicant is defined in section 5(5) of the IBC as

(a) corporate debtor; or

(b) a member or partner of the corporate debtor who is authorised to make an application for the corporate insolvency resolution process or the pre-packaged insolvency resolution process, as the case may be, under the constitutional document of the corporate debtor; or

(c) an individual who is in charge of managing the operations and resources of the corporate debtor; or

(d) a person who has the control, and supervision over the financial affairs of the corporate debtor.

Section 5(4) of the Code defines "constitutional document", in relation to a corporate person, as includes articles of association, memorandum of association of a company and incorporation document of a Limited Liability Partnership.

1. **Application to initiate corporate insolvency resolution process:**

   Section 10(1) of IBC, 2016: Where a corporate debtor has committed a default, a corporate applicant thereof may file an application for initiating corporate insolvency resolution process with the Adjudicating Authority.

2. **Form, Manner and Fee of Application: The** application shall be filed in such form, containing such particulars and in such manner and accompanied with such fee as may be prescribed.

The Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016: Rule 7 prescribes form and manner of application by corporate applicant. —

(1) A corporate applicant, shall make an application for initiating the corporate insolvency resolution process against a corporate debtor under section 10 of the Code in Form 6, accompanied with documents and records required therein and as specified in the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.

(2) The applicant under sub-rule (1) shall serve a copy of the application to the Board by registered post or speed post or by hand or by electronic means, before filing with the Adjudicating Authority.

- The application should be submitted by the corporate applicant to the AA along with a demand draft of 25,000 Indian rupees favoring the Pay and Accounts Officer, Ministry of Corporate Affairs, payable in Mumbai, New Delhi, Kolkata, or Chennai.

FORM 6

APPLICATION BY CORPORATE APPLICANT TO INITIATE CORPORATE INSOLVENCY RESOLUTION PROCESS UNDER THE CODE.

(Under rule 7 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016)

Form 6 is divided into three parts, each providing for the submission of the following particulars:

Part-I	**PARTICULARS OF THE CORPORATE APPLICANT-**	Details of all directors, promoters, and partners; the date of incorporation, nominal and paid-up share capital; and details of the authorized representative, along with details of the CD.
Part II	**Particulars of the proposed IRP—**	Details such as the name, address, email address, and registration number of the proposed IRP
Part III	**Particulars of the financial or operational debt-** [CREDITOR WISE, AS APPLICABLE]	Details of the financial or operational creditors, the total amount of debt along with the date(s) when the debts were incurred, particulars of the security amount claimed to be in default, and the date on which the default occurred.

3. **Information/Documents to be furnished with the application:**

   Section 10(3) of IBC, 2016: The corporate applicant shall, along with the application, furnish-

(a) the information relating to its books of account and such other documents for such period as may be specified;

(b) the information relating to the resolution professional proposed to be appointed as an interim resolution professional; and

(c) the special resolution passed by shareholders of the corporate debtor or the resolution passed by at least three-fourth of the total number of partners of the corporate debtor, as the case may be, approving filing of the application.

4. Timeline for admission or rejection of application:

***Section 10(4) of the Code states that** t*he Adjudicating Authority shall, within a period of **fourteen days** of the receipt of the application, by an order-

(a) admit the application, if it is complete and no disciplinary proceeding is pending against the proposed resolution professional; or

(b) reject the application, if it is incomplete or any disciplinary proceeding is pending against the proposed resolution professional.

Provided that Adjudicating Authority shall, before rejecting an application, give a notice to the applicant to rectify the defects in his application within seven days from the date of receipt of such notice from the Adjudicating Authority.

5. Commencement of CIRP

Section 10(5) of the Code provides that the corporate insolvency resolution process shall commence from the date of admission of the application under sub-section (4) of this section.

In ***M/s. Unigreen Global Private Limited Vs. Punjab National Bank and Others [Company Appeal (AT) (Insolvency) No. 81 of 2017]***, the NCLAT examined the scope of discretion available to an Adjudicating Authority in admitting or rejecting a section 10 application. The NCLAT held that the Adjudicating Authority must admit an application filed by a Corporate Debtor to initiate a CIRP if it is satisfied that:

- the default has occurred
- the application is complete, and
- the Corporate Debtor is not barred under section 11 of the IBC.

Facts unrelated to or beyond the requirement of the IBC or the forms prescribed cannot amount to suppression of facts and cannot be looked at by the AA for denying admission.

Intimation to Information Utility

IBBI vide Circular No. IBBI/IU/51/2022 dated 15th June 2022 decided to forward all the applications received for initiating insolvency to the Information Utility (IU) and, the IU is required to (a) inform other creditors of the CD by sharing the application; (b) issue notice to the applicant, requiring it to file 'information of default' as per IU Regulations; and (c) process the 'information of default' for the purpose of issuing ROD as per the IU.

Fraudulent or Malicious Initiation of Proceedings

While evaluating whether to initiate a corporate insolvency resolution process, the applicant(s) should be aware of the potential impact of section 65 of the IBC, which deals with fraudulent or malicious initiation of proceedings. This provision says that if any person initiates a corporate insolvency resolution process or liquidation process fraudulently, or with malicious intent, for any purpose other than the resolution of insolvency, or liquidation, the

Adjudicating Authority may impose on him/her a penalty which shall not be less than one lakh rupees, but may extend to one crore rupees..

Applicability of the Limitation Act

Section 238A was inserted in the IBC through the Insolvency and Bankruptcy (Amendment) Ordinance 2018 (later replaced by the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018), to make the provisions of the Limitation Act, 1963, apply to proceedings or appeals before the Adjudicating Authority, the NCLAT, the Debt Recovery Tribunal, and the Debt Recovery Appellate Tribunal.

Thus, applications under sections 7, 9, or 10 cannot be admitted for time-barred debts.

In ***B.K. Educational Services Private Limited Vs. Parag Gupta and Associates [(2019) 11 SCC 633]***, the Supreme Court observed that the intention of lawmakers, from the very beginning, was to apply the Limitation Act, 1963, to the NCLT and the NCLAT while deciding applications filed under section 7 and section 9 of the IBC and appeals. The relevant section of the Limitation Act is section 137. No doubt, the right to sue accrues when a default occurs. But if the default has occurred more than three years before the date of filing the application, it would be barred by section 137, except in cases where the delay can be condoned under section 5 of the Limitation Act. It also held that section 238A of the Code should apply the provisions of the Limitation Act, "as far as may be." Therefore, where periods of limitation have been laid down in the IBC, they will apply notwithstanding anything to the contrary contained in the Limitation Act.

In ***Dena Bank (Now Bank of Baroda) Vs. C. Shivakumar Reddy & Anr. 2021 SCC Online SC 543***, Supreme Court held that entries in books of accounts and/or Balance sheets of a Corporate Debtor would amount to an acknowledgment under Section 18 of the Limitation Act.

Placing reliance upon same, the NCLT, New Delhi Bench, while adjudicating an application filed under section 9 of Insolvency and Bankruptcy Code, 2016 ("IBC, 2016") in *M/s SKC Infratech Pvt. Ltd vs M/s EOS Hospitality Pvt. Ltd.* has reiterated that entries made in the Balance Sheet amounts to acknowledgement of debt as per section 18 of Limitation Act, 1963.

In ***Babulal Vardharji Gurjar Vs. Veer Gurjar Aluminium Industries Private Limited & Another [Civil Appeal No. 6347 of 2019]***, the Supreme Court examined the limitation period for filing section 7 applications and observed:

The period of limitation for an application to initiate a corporate insolvency resolution process under section 7 of the IBC is governed by article 137 of the Limitation Act and is, therefore, three years from the date when the right to apply accrues.

The right to apply under the IBC accrues on the date when the default occurs. If the default had occurred over three years prior to the date of filing the application, the application would be time-barred, save and except in those cases where, on facts, the delay in filing may be condoned.

An application under section 7 of the IBC is not for enforcing mortgage liability and article 62 of the Limitation Act does not apply to this application.

The date of the IBC's coming into force on 01.12.2016 is irrelevant to the triggering of any limitation period for the purposes of the IBC.

In this case, the court observed that the Financial Creditor never made any arguments other than stating the date of default as "08.07.2011" in the application. Therefore, no case for extending the period of limitation is available to be examined. In other words, even if section 18 of the Limitation Act – (which allows the period of limitation to be extended if the defaulter had acknowledged the debt) – and the principles thereof were applicable, they would not apply to the application under consideration, looking at the averment made in the application regarding default and for want of any other averment in regard to acknowledgement. The court annulled the insolvency proceedings, holding that because the application of the financial creditor is barred by limitation, no proceedings undertaken after the order of admission could be of any effect.

Excluded Categories

The corporate person which are excluded from IBC falls in two categories:

1. Against which CIRP cannot be initiated

2. Persons not entitled to make application (Section 11)

Against which Corporate Insolvency Resolution Process cannot be initiated:

Corporate Insolvency Resolution Process can be initiated against a corporate debtor. A corporate debtor is defined in section 3(8) of the Code as a corporate person who owes a debt to any person. A "corporate person" is defined in section 3(7) to mean

- a company under the Companies Act, 2013,
- an LLP under the Limited Liability Partnership Act, 2008, or
- any other person incorporated with limited liability under any law in force at the time excluding financial service providers.

Therefore, a financial service provider is not a corporate debtor for the purposes of the Code and, consequently, a Corporate Insolvency Resolution Process against a financial service provider cannot be initiated under section 7, 9, or 10 of the IBC.

A "financial service provider" is defined in section 3(17) of the IBC as a person authorized and registered by a financial sector regulator to provide financial services. The terms "financial services" and "financial sector regulator" are defined in section 3(15) and section 3(18) respectively.

Section 239 of the Code entrust upon the Central Government power to make rules, by notification, carrying out the provisions of this Code. Without prejudice to the generality of the provisions of sub-section (1), the Central Government may make rules for any of the following matters, namely:

"(zk) the manner of conducting insolvency and liquidation proceedings under section 227;"

Section 227 of the IBC empowers the Central Government, in consultation with the appropriate financial sector regulators, to notify financial service providers or categories of financial service providers about their insolvency and liquidation proceedings, which may be conducted under the IBC with such modifications and in such manner as may be prescribed. Pursuant to its powers, the MCA introduced and notified the Insolvency and Bankruptcy (Insolvency and Liquidation Proceedings of Financial Service Providers and Application to Adjudicating Authority) Rules, 2019.

The Financial Service Provider Rules empower the government to commence the Corporate Insolvency Resolution Process in terms of the IBC against financial service providers, in consultation with the appropriate financial sector regulator as prescribed by the law. In terms of the notification dated November 18, 2019, issued by the MCA, the Financial Service Provider Rules would apply to non-banking finance companies (which include housing finance companies) with asset size of Rs.500 crore or more, as per last audited balance sheet with the RBI as the appropriate financial service regulator.

Further, the MCA, in its notification dated January 30, 2020 notified the manner of dealing with the third-party assets in custody or possession of such financial service provider.

Dewan Housing Financial Corporation is the first financial service provider to come under the ambit of the IBC in the matter of ***RBI Vs. Dewan Housing Financial Corporation in C.P. (IB)-4258/MB/2019***. The RBI, in its capacity as appropriate regulator, in terms of rule 5 of the Financial Service Provider Rules, initiated the CIRP against Dewan Housing Financial Corporation. It was admitted by the NCLT, Mumbai bench, on December 3, 2019.

In ***Hindustan Construction Company Limited & Another Vs. Union of India & Others [WP (Civil) No. 1074/2019*** with other Civil Appeals], a CIRP was sought to be initiated against the National Highway Authority of India. The Supreme Court held that the National Highway Authority of India is a statutory body that functions as an extended limb of the Central Government and performs governmental functions that cannot be taken over by an RP under the IBC or by any other corporate body. Nor can such authority ultimately be wound up under the IBC. For all these reasons, it is not possible to either read in or read down the definition of "corporate person" in section 3(7) of the IBC.

Persons not entitled to make application (Section 11)

Section 11 of the Code states that certain persons are not entitled to make applications for initiating a Corporate Insolvency Resolution Process. These are:

a) a corporate debtor already undergoing a corporate insolvency resolution process or a pre-packaged insolvency resolution process; or

(aa) a financial creditor or an operational creditor of a corporate debtor undergoing a pre-packaged insolvency resolution process; or

(b) a corporate debtor having completed corporate insolvency resolution process twelve months preceding the date of making of the application; or

(ba) a corporate debtor in respect of whom a resolution plan has been approved under Chapter III-A, twelve months preceding the date of making of the application; or

(c) a corporate debtor or a financial creditor who has violated any of the terms of resolution plan which was approved twelve months before the date of making of an application under this Chapter; or

(d) a corporate debtor in respect of whom a liquidation order has been made.

Explanation I. - For the purposes of this section, a corporate debtor includes a corporate applicant in respect of such corporate debtor.

Explanation II.- For the purposes of this section, it is hereby clarified that nothing in this section shall prevent a corporate debtor referred to in clauses (a) to (d) from initiating corporate insolvency resolution process against another corporate debtor.

The Insolvency and Bankruptcy Code (Amendment) Ordinance, 2019 (later replaced by the Insolvency and Bankruptcy Code (Amendment) Act, 2020, has added Explanation II to the IBC that a corporate debtor may initiate insolvency proceedings against another corporate debtor for the debts owed to it. The explanation allows a corporate debtor to initiate CIRP against its corporate debtor by virtue of them now being a creditor. The amendment has sought to clarify the ambiguous and unsettled position of the law.

Timeline for admission or rejection of Application filed to initiate Corporate Insolvency Resolution Process, whether mandatory or directory

In all cases where an application to initiate a CIRP is filed, the IBC provides that the Adjudicating Authority (AA) should admit it within 14 days of receiving the application. The AA can reject such an application on the grounds mentioned in the respective sections 7,9 or 10, as may be applicable. However, if AA reject such an application on ground of being incomplete, the Adjudicating Authority shall, before rejecting such application, give a notice to the applicant to rectify the defects in his application within seven days from the date of receipt of such notice from the Adjudicating Authority.

Now, question arises whether this timeline of 14 days or 7 days is mandatory or discretionary for Adjudicating Authority.

M/s. Surendra Trading Company Vs. M/s. Juggilal Kampat Jute Mills Company Ltd. and Others [(2017) 16 SCC 143]

The question for consideration before the Supreme Court was whether the period of seven days to rectify errors was mandatory or a guideline (directory).

The appeal arose from an order of the NCLAT that held that the period of 14 days for admitting/rejecting the application under sections 7, 9, and 10 was directory and the period of seven days given to the applicant for rectifying errors was mandatory.

The Supreme Court upheld the NCLAT's view on 14 days for admission/rejection being directory and also held that there was no reason to make the proviso (that is, seven days for rectifying errors) mandatory. It held that the proviso is directory in nature; however, it also considered that there may be cases where:

(a) applicants or their counsel may not remove the objections in time, or

(b) frivolous applications may be filed with ulterior/oblique motives and kept pending without any removal of errors.

Hence, the Supreme Court, while interpreting the provisions to be directory in nature, held that the applicant/counsel is required to submit, in writing, why the removal of objections could not be completed within the stated seven days. If the court/tribunal is satisfied with the reasons given, it will entertain the application on merit; if not, the court/tribunal will have the right to dismiss it.

Time-limit for completion of insolvency resolution process (Section 12)

Thus the 14-day period given to the AA to admit or reject an application to initiate a Corporate Insolvency Resolution Process as well as 7 days period for rectification of defects is not mandatory.

Opportunity of Being Heard to Corporate Debtor

Before admitting a Corporate Insolvency Resolution Process application in respect of a Corporate Debtor, the Corporate Debtor must be given an opportunity to be heard.

Rules 4(3), 6(2), and 7(2) of the Application to Adjudicating Authority Rules mandate that the applicant (Financial Creditor, Operational Creditor, and Corporate Applicant, respectively) shall serve a copy of the application to the registered office of the corporate debtor and to the IBBI, by registered post or speed post or by hand or by electronic means, before filing with the Adjudicating Authority.

In practice, however, a prior service is made to the Corporate Debtor because the relevant registry of the NCLT may not accept filings any other way. Further, once the application is submitted to the Adjudicating Authority, the acknowledged copy of it should be served on the Corporate Debtor. The AA then allocates a company petition number to it. Thereafter, the application comes up for hearing before the Adjudicating Authority.

The relevant NCLT registry allocates a date and a courtroom number for the matter when it receives the covering letter. The matter is then listed for hearing by the Adjudicating Authority. If the Adjudicating Authority decides that the matter should be heard, it issues a notice to the Corporate Debtor. The copy of the application is served again on the Corporate Debtor when the Adjudicating Authority issues the notice. If the Corporate Debtor does not appear before the Adjudicating Authority, the Adjudicating Authority may require the filing of a service affidavit before it (showing evidence of service to the Corporate Debtor. Such practices are adopted to ensure that the Corporate Debtor is provided enough opportunity of being heard if it wishes to oppose the application for admission under the IBC.

Withdrawal of application admitted under section 7, 9 or 10 (Section 12A)

There are three phases in which application could be sought to be withdrawn by applicant:

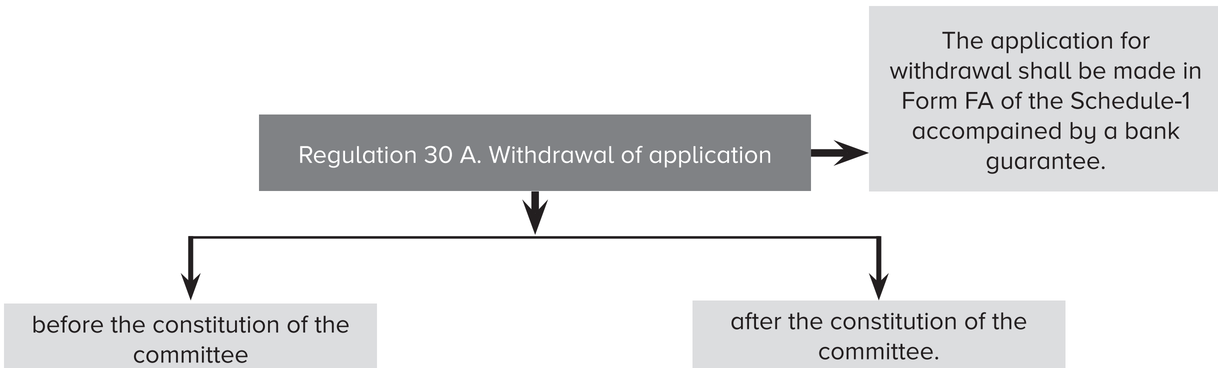
(i) *Case I: Before admission of application by Adjudicating Authority:* Rule 8 of the *Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016* provides for withdrawal of application as—The Adjudicating Authority may permit withdrawal of the application made under rules 4, 6 or 7, as the case may be, on a request made by the applicant before its admission.

(ii) *Case II:* After admission of application but before constitution of Committee of Creditors.

(iii) *Case III*: After constitution of Committee of Creditors.

Once an application for a CIRP is admitted by the Adjudicating Authority, it can be withdrawn under section 12A of the IBC read with Regulation 30A of the CIRP Regulations. The provisions of both are summarized below:

Section 12 A of the Code provides that the Adjudicating Authority may allow the withdrawal of application admitted under section 7 or section 9 or section 10, on an application made by the applicant with the approval of ninety per cent voting share of the committee of creditors, in such manner as may be specified.



Regulation 30A of the CIRP Regulations specifies the manner for such withdrawal after admission as follows:

Particulars	**Provisions where an application for withdrawal is made before the constitution of the committee**	**Provisions where an application for withdrawal is made after the constitution of the committee**
1. Through whom applicant can apply	the interim resolution professional	• the interim resolution professional; or • the resolution professional, as the case may be. In this case if application is made after the issue of invitation for expression of interest under regulation 36A, the applicant shall state the reasons justifying withdrawal after issue of such invitation.
2. Bank Guarantee to be given (Regulation 30A(2))	(a) towards estimated expenses incurred on or by the interim resolution professional for purposes of regulation 33, till the date of filing of the application before the constitution of the committee	(b) towards estimated expenses incurred for purposes of clauses (aa), (ab), (c) and (d) of regulation 31, till the date of filing of the application after the constitution of the committee.
3. Time period for submitting application to AA	By the interim resolution professional on behalf of the applicant **within three days of its receipt.**	• The committee shall consider the application, within seven days of its receipt. • If application is approved by COC with 90% voting share, the resolution professional shall submit such application along with the approval of the committee, **to the AA on behalf of the applicant, within three days of such approval.**

4. AA may approve or reject the application. If AA approves withdrawal	**Actions required:** 1. The applicant shall deposit an amount, towards the actual expenses incurred for the purposes referred to in clause (a) or clause (b) of sub-regulation (2) till the date of approval by the Adjudicating Authority, 2. The amount of deposit shall be determined by the interim resolution professional or resolution professional, as the case may be. **3. The applicant shall deposit the amount within three days of such approval, in the bank account of the corporate debtor.** 4. If applicant fails to deposit the amount in three days of approval, the bank guarantee received under sub-regulation (2) shall be invoked, without prejudice to any other action permissible against the applicant under the Code.

In ***Swiss Ribbons Private Limited and Another Vs. Union of India and Others [(2019) 4 SCC 17]***, the Supreme Court held that the provision allowing an application to be withdrawn before an invitation for Expression of Interests is issued is directory and not mandatory. In exceptional cases, withdrawal may also be allowed after the invitation for Expression of Interests has been issued. The main precondition for withdrawal is that 90 percent of the Committee of Creditor's members have to agree to it.

Time-limit for completion of insolvency resolution process (Section 12)

Time-limit for completion of CIRP by Adjudicating Authority (Section 12)

180 days from the date of admission of the application to initiate such

+

One extension maximum days time of 90

→

- On an application filed by resolution professional,
- On the authority of a resolution passed at a meeting of the committee of creditors by a vote of 66% of the voting shares.
- If Adjudicating Authority is satisfied that the subject matter of the case is such that CIRP cannot be completed within 180 days

The corporate insolvency resolution process starts on the date the application is admitted. This is taken as the insolvency commencement date.

- Completion of CIRP in 180 days: Section 12(1) states that subject to sub-section (2), the corporate insolvency resolution process shall be completed within a period of one hundred and eighty days from the date of admission of the application to initiate such process.
- Application to file for extension beyond 180 days: Section (2) states that the resolution professional shall file an application to the Adjudicating Authority to extend the period of the corporate insolvency resolution process beyond one hundred and eighty days, if instructed to do so by a resolution passed at a meeting of the committee of creditors by a vote of sixty-six per cent of the voting shares.
- One time Extension by the Adjudicating Authority of maximum 90 days: Section 12 (3) states that on receipt of an application under sub-section (2), if the Adjudicating Authority is satisfied that the subject matter of the case is such that corporate insolvency resolution process cannot be completed within one hundred and eighty days, it may by order extend the duration of such process beyond one hundred and eighty days by such further period as it thinks fit, but not exceeding ninety days:

Proviso to sub-section (3) clarifies that any extension of the period of corporate insolvency resolution process under this section shall not be granted more than once.

It is further provided that the corporate insolvency resolution process shall mandatorily be completed within a period of three hundred and thirty days from the insolvency commencement date, including any extension of the period of corporate insolvency resolution process granted under this section and the time taken in legal proceedings in relation to such resolution process of the corporate debtor.

Regulation 40 of CIRP Regulations, 2016: It lays down similar provisions as follows:

Extension of the corporate insolvency resolution process period.

(1) The committee may instruct the resolution professional to make an application to the Adjudicating Authority under section 12 to extend the insolvency resolution process period.

(2) The resolution professional shall, on receiving an instruction from the committee under this Regulation, make an application to the Adjudicating Authority for such extension.

CoC of Essar Steel India Limited Vs. Satish Kumar Gupta [(2019) SCC Online SC 1478]

In this case, the Supreme Court examined the constitutionality of the amendment made in section 12(3) of the IBC (which provided that the corporate insolvency resolution process must mandatorily be completed within 330 days). While leaving the provision otherwise intact, it struck down the word "mandatorily" as being manifestly arbitrary under Article 14, as well as placing an excessive and unreasonable restriction on the litigant's right to carry on business under Article 19(1) (g) of the Constitution. The court held that the effect of this declaration is that ordinarily the corporate resolution process of the corporate debtor must be completed within the outer limit of 330 days from the insolvency commencement date, including extensions and the time taken in legal proceedings.

However, on the facts of a given case, if it can be shown to the Adjudicating Authority and/or the NCLAT that only a short period is needed beyond the 330 days to complete the corporate insolvency resolution process; that it would be in the interest of all stakeholders for the corporate debtor to be put back on its feet instead of being liquidated; and that the time taken in legal proceedings is largely due to factors that cannot be ascribed to the litigants before the Adjudicating Authority and/or the NCLAT, the delay or a large part thereof being attributable to the tardy process of the AA and/or the NCLAT itself, the Adjudicating Authority and/ or the NCLAT may extend the time beyond 330 days. The general rule is that 330 days is the outer limit within which resolution of the stressed assets of the corporate debtor must take place. Beyond this period, the corporate debtor is to be liquidated.

Timelines within the Corporate Insolvency Resolution Process

The IBC and the IBBI (Corporate Insolvency Resolution Process) Regulations,2016 detail a timeline for each step to be taken by various participants in the CIRP. Regulation 40A of CIRP Regulations,2016 lays down model time-line for corporate insolvency resolution process in tablular form on the assumption that the interim resolution professional is appointed on the date of commencement of the process and the time available is hundred and eighty days :

[Section / Regulation	Description of Activity	Norm	Latest Timeline
Section 16(1)	Commencement of CIRP and appointment of IRP	....	T
Regulation 6(1)	Public announcement inviting claims	Within 3 Days of Appointment of IRP	T+3
Section 15(1)(c) / Regulations 6(2)(c) and 12 (1)	Submission of claims	For 14 Days from Appointment of IRP	T+14

[Section / Regulation	Description of Activity	Norm	Latest Timeline
Regulation 12(2)	Submission of claims	Up to 90th day of commencement	T+90
Regulation 13(1)	Verification of claims received under regulation 12(1)	Within 7 days from the receipt of the claim	T+21
	Verification of claims received under regulation 12(2)		T+97
Section 21(6A) (b) / Regulation 16A	Application for appointment of AR	Within 2 days from verification of claims received under regulation 12(1)	T+23
Regulation 17(1)	Report certifying constitution of CoC		T+23
Section 22(1) / Regulation 19(2)	1st meeting of the CoC	Within 7 days of filing of the report certifying constitution of the CoC, but with five days' notice	T+30
Section 22(2)	Resolution to appoint RP by the CoC	In the first meeting of the CoC	T+30
Section 16(5)	Appointment of RP	On approval by the AA	………..
Regulation 17(3)	IRP performs the functions of RP till the RP is appointed.	If RP is not appointed by 40th day of commencement	T+40
Regulation 27	Appointment of valuer	Within 7 days of appointment of RP, but not later than 47th day of commencement	T+47
Section 12(A) / Regulation 30A	Submission of application for withdrawal of application admitted	Before issue of EoI	W
	CoC to dispose of the application	Within 7 days of its receipt or 7 days of constitution of CoC, whichever is later.	W+7
	Filing application of withdrawal, if approved by CoC with 90% majority voting, by RP to AA	Within 3 days of approval by CoC	W+10
Regulation 35A	RP to form an opinion on preferential and other transactions	Within 75 days of the commencement	T+75
	RP to make a determination on preferential and other transactions	Within 115 days of commencement	T+115
	RP to file applications to AA for appropriate relief	Within 130 days of commencement	T+130
Regulation 36 (1)	Submission of IM to CoC	Within 95 days of commencement	T+95
Regulation 36A	Publish Form G	Within 60 days of commencement	T+60
	Invitation of EoI		
	Submission of EoI	At least 15 days from issue of EoI (Assume 15 days)	T+75
	Provisional List of RAs by RP	Within 10 days from the last day of receipt of EoI	T+85

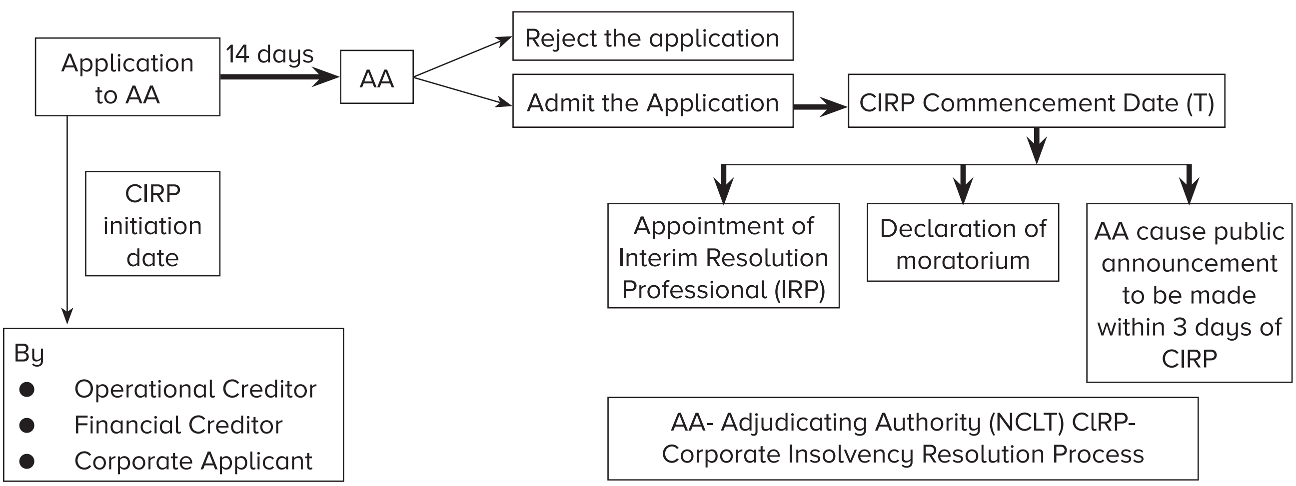
[Section / Regulation	Description of Activity	Norm	Latest Timeline
	Submission of objections to provisional list	For 5 days from the date of provisional list	T+90
	Final List of RAs by RP	Within 10 days of the receipt of objections	T+100
Regulation 36B	Issue of RFRP, including Evaluation Matrix and IM	Within 5 days of the issue of the final list	T+105
	Receipt of Resolution Plans	At least 30 days from issue of RFRP (Assume 30 days)	T+135
Regulation 39(4)	Submission of CoC approved Resolution Plan to AA	As soon as approved by the CoC	T+165
Section 31(1)	Approval of resolution plan by AA		T+180

Terms used in Table:

- RP –Resolution Professional
- AA-Adjudicating Authority
- CoC-Committee of Creditors
- IRP-Interim Resolution Professional
- IM- Information Memorandum
- RAs- Resolution Applicants
- EOI-Expression of Interest
- RFRP- Request For Resolution Plan
- IM- Information Memorandum
- AR-Authorised Representative
- CIRP-Corporate Insolvency Resolution Process.

In ***ArcelorMittal India Private Limited vs. Satish Kumar Gupta and Others [2018 (13) SCALE]***, the Supreme Court referred to regulation 40A of the CIRP Regulations and observed that "it is of utmost importance for all authorities concerned to follow this model timeline as closely as possible."

Declaration of moratorium and public announcement



The IBC has shifted the "debtor in possession" regime to a "creditor in control" model for corporate debtors undergoing Corporate Insolvency Resolution Process (CIRP). This control is exercised through an Interim Resolution Professional (and later the Resolution Professional). From the insolvency commencement date (ICD), the powers of the Board of Directors or the partners of the corporate debtor are suspended and are exercised by the Interim Resolution Professional. Similarly, the management of the corporate debtor vests in the Interim Resolution Professional (and later the Resolution Professional). This continues for the entire CIRP period, that is, from the insolvency commencement date (ICD) till the Adjudicating Authority (AA) passes an order for resolution (that is, an order approving the resolution plan) or liquidation of the corporate debtor.

The Interim Resolution Professional constitutes the Committee of Creditors based on claims submitted by the creditors pursuant to Public Announcement, which can then decide to either continue the Interim Resolution Professional as the Resolution Professional or replace him with another insolvency professional as the Resolution Professional.

On the insolvency commencement date, a "moratorium" in respect of the corporate debtor and its assets is declared, which continues for the entire CIRP period. During this time, the IRP (and later the RP) runs the CD as a going concern and fulfills various duties under the IBC and CIRP Regulations, under the overall supervision of the Committee of Creditors.

(i) *Section 13 IBC,2016:* Section 13 of the Code specifies three actions that the NCLT shall take after an application for initiating the corporate insolvency resolution process has been admitted.

According to section 13 of IBC,2016:

(1) The Adjudicating Authority, after admission of the application under section 7 or section 9 or section 10, shall, by an order –

(a) declare a moratorium for the purposes referred to in section 14;

(b) cause a public announcement of the initiation of corporate insolvency resolution process and call for the submission of claims under section 15; and

(c) appoint an interim resolution professional in the manner as laid down in section.

(2) The public announcement referred to in clause (b) of sub-section (1) shall be made immediately after the appointment of the interim resolution professional.

Moratorium

The Bankruptcy Law Reforms Committee recommends that a provision relating to a "calm period" be introduced in the IBC so that all efforts are focused on resolution. The moratorium provisions are framed in the IBC to ensure that the corporate debtor is not burdened with additional stress. The Bankruptcy Law Reforms Committee, in its report, recommended two phases of resolution, upon commencement of the corporate insolvency resolution process.

(a) A serious effort be made to evaluate the viability of the debt during a "calm period" where the creditors' interests are preserved, without affecting the running of the corporate debtor's business. This is possible only when a moratorium is imposed on all recovery actions against the corporate debtor, so that an insolvency professional can manage and operate the company effectively.

(b) If the investigations into the viability of the company do not result in a solution that can be implemented, the corporate debtor may be considered unviable and the matter may proceed to a liquidation, which is regarded as the last resort. The Committee of creditors and the resolution professional should make every effort to maximize the value of the corporate debtor and balance the interest of all stakeholders.

Section 14 of the Code details the moratorium protection given to the corporate debtor. The entire period of corporate insolvency resolution professional is covered under this moratorium, during which all suits, legal proceedings, and recovery actions against the corporate debtor are held in abeyance to give time to the corporate debtor to resolve its status. Section 14 is reproduced below:

(1) Prohibitory order by the Adjudicating Authority: Subject to provisions of sub-sections (2) and (3), on the insolvency commencement date, the Adjudicating Authority shall by order declare moratorium for prohibiting all of the following, namely: -

(a) the institution of suits or continuation of pending suits or proceedings against the corporate debtor including execution of any judgement, decree or order in any court of law, tribunal, arbitration panel or other authority;

(b) transferring, encumbering, alienating or disposing off by the corporate debtor any of its assets or any legal right or beneficial interest therein;

(c) any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect of its property including any action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;

(d) the recovery of any property by an owner or lessor where such property is occupied by or in the possession of the corporate debtor.

Explanation to sub-section (1) provides for non-termination of license, quota or any other amenities provided by government authority or sectoral regulator subject to payment of current dues arising due to their use during CIRP as:

'For the purposes of this sub-section, it is hereby clarified that notwithstanding anything contained in any other law for the time being in force, a licence, permit, registration, quota, concession, clearance or a similar grant or right given by the Central Government, State Government, local authority, sectoral regulator or any other authority constituted under any other law for the time being in force, shall not be suspended or terminated on the grounds of insolvency, subject to the condition that there is no default in payment of current dues arising for the use or continuation of the license, permit, registration, quota, concession, clearances or a similar grant or right during the moratorium period;

(The explanation does not bar termination of such a license (or similar item) on grounds other than insolvency. Such a safeguard in terms of non-termination of licenses and permits and continued supply of critical goods and services has been provided to protect and preserve the value of the corporate debtor and manage its operations as a going concern.)

Case Laws related to section 14(1)(a)

In ***Alchemist Asset Reconstruction Company Limited Vs. Hotel Gaudavan Private Limited [(2018) 16 SCC 94]***, the Supreme Court affirmed that once a moratorium is imposed under the IBC, any proceeding initiated against the corporate debtor is non-est (does not exist) in law.

Powers of High Court under Article 226 and of Supreme Court under Article 32 of the Constitution are not affected by Moratorium: ***In Canara Bank Vs. Deccan Chronicle Holdings Limited [Company Appeal (AT) (Insolvency) No. 147 of 2017]***, the NCLAT held that the moratorium will not affect any proceedings initiated or pending before the Supreme Court under Article 32 of the Constitution of India or where an order is passed under Article 136. Further, it will not affect the powers of any High Court under Article 226 of the Constitution.

Proceeding in moratorium do not include prosecution: *In* ***Mr. Ajay Kumar Bishnoi Vs. M/s Tap Engineering and Other [Criminal Original Petition No. 34996 of 2019]***, the corporate debtor underwent insolvency resolution while a complaint was pending under section 138 of the Negotiable Instruments Act, 1881. Further, during this time, a resolution plan for the corporate debtor was approved with a change in management and control. The Managing Director (MD) of the erstwhile corporate debtor sought to quash the prosecution under section 138 in view of the approval of the resolution plan. The High Court confirmed that the moratorium under section 14 of the IBC prohibits proceedings, but such proceedings do not include prosecution.

Moratorium does not apply to criminal proceedings: In the matter of ***Varrsana Ispat Limited Vs. Deputy Director, Directorate of Enforcement [Company Appeal (AT) (Insolvency) No. 493 of 2018]***, the Resolution Professional (RP) had sought de-attachment of properties attached with the Directorate of Enforcement under the Prevention of Money Laundering Act, 2002, a considerable time prior to the initiation of corporate insolvency resolution process. The NCLAT had held that section 14 of the IBC is not applicable to the criminal proceeding or any penal action taken pursuant to the criminal proceeding or any act having the essence of crime or crime proceedings.

The Supreme Court also upheld the order passed by the NCLAT ***[Varrsana Ispat Limited Vs. Deputy Director, Directorate of Enforcement, Civil Appeal No. 5546 of 2019]***. While the bar under IBC is automatic, practically the IRPs/RPs may need to file an application before various forums where proceedings against the corporate debtor is continuing, bringing to their attention the commencement of CIRP and the moratorium declared by the AA under section 14 of the IBC, and requesting the relevant forums to pass an order staying proceedings.

Moratorium also applies on the Regulatory Authorities: In the matter of ***Ms. Anju Agarwal Resolution Professional For Shree Bhawani Paper Mills Ltd. Vs Bombay Stock 19 Exchange & Ors.***, the NCLAT observed that Section 28A of the SEBI Act, 1992 being inconsistent with Section 14 of IBC, it held that Section 14 of IBC will prevail over Section 28A of the SEBI Act, 1992 and SEBI cannot recover any amount including the penalty from the CD. The 'Bombay Stock Exchange' cannot suspend trading of shares of CD for the same reason.

Penalty imposed by Regulator may be claimed as Operational Creditor but cannot be recovered during the Resolution Process: In *the matter of* ***Maharashtra Seamless Ltd. Vs. Shri Padmanabhan Venkatesh & Ors.*** , the NCLAT held that the statutory dues i.e. the dues to Central Government or the State Government arising under any law for the time being in force and payable come within the meaning of 'Operational Debt'. If penalty is imposed or amount is payable to the 'Securities Exchange Board of India' in such case, it may claim as an 'Operational Creditor' but cannot recover the same during the 'Resolution Process'.

Under section 14(1)(b) and (c), the bar is only in respect of the Corporate Debtor and its assets. It follows that property not owned by the Corporate Debtor would not come under the protective umbrella of section 14 unless the property is occupied by or in possession of the Corporate Debtor (in which case, its recovery would be prohibited under section 14(1) (d) of the IBC).

Case laws related to section 14(1)(d)

In the matter of ***Rajendra K. Bhutta Vs. Maharashtra Housing and Area Development Authority (MHADA) and 17 Another***, the Supreme Court held that Section 14(1)(d) of the IBC, when it speaks about recovery of property "occupied", does not refer to rights or interests created in property but only actual physical occupation of the property:

In ***M/s Embassy Property Developments Pvt. Ltd. Vs. State of Karnataka and Others [2019 SCC Online SC 1542]***, one of the issues before the Supreme Court was whether the AA had the power under the IBC to review the order passed by the Government of Karnataka during the moratorium period, rejecting the auto-extension of a mining lease granted by it to the Corporate Debtor. The Supreme Court observed, among other things, that the moratorium under section 14 did not impact the right of the government to refuse extension of the lease. It observed that the purpose of section 14 was to preserve the status quo and not to create a new right. Even section 14(1)(d), which prohibits, during the period of moratorium, the recovery of any property by the owner/ lessor will not go to the rescue of the corporate debtor since what is prohibited is only right not to be dispossessed, but not the right to have renewal of the lease of such property. It was further observed that this right not to be dispossessed will have nothing to do with the rights conferred by a mining lease especially on government land. It was noted that what was granted to the Corporate Debtor was not an exclusive possession of the land in question so as to enable the RP to invoke section 14(1)(d) of the IBC.

(2) Supply of essential goods or service:

Following spirit of the "calm period" and running the corporate debtor as going concern during "calm period" as envisaged in BLRC report, sub-section 2 of section 14 mandates that the supply of essential goods or services to the corporate debtor as may be specified shall not be terminated or suspended or interrupted during moratorium period.

Subsection 2A was added after section 14(1)(2) by way of the Insolvency and Bankruptcy Code (Amendment) Act, 2020, to the effect that where the interim resolution professional or the resolution professional considers the supply of goods or services critical to protect and preserve the value of the corporate debtor and manage the operations of such corporate debtor as a going concern, then the supply of such goods or services shall not be terminated, suspended, or interrupted during the period of moratorium, except where such corporate debtor has not paid dues arising from such supply during the moratorium period or in such circumstances as may be specified.

This Amendment has vested discretion in IRP or RP to consider whether particular goods or services are essential or not and if according to them, they are essential and then their supply cannot be terminated provided the corporate debtor pays current dues in respect of the same during the moratorium period.

Regulation 32 of *the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016* defines Essential Supplies as follows:

Essential supplies: The essential goods and services referred to in section 14(2) shall mean-

(1) electricity;

(2) water;

(3) telecommunication services; and

(4) information technology services,

But the condition is that above (4) shall be treated as Essential Supplies only to the extent these are not a direct input to the output produced or supplied by the corporate debtor. Illustration-Water supplied to a corporate debtor will be essential supplies for drinking and sanitation purposes, and not for generation of hydro-electricity.

In ***Dakshin Gujarat VIJ Company Ltd. Vs. M/s. ABG Shipyard Ltd. and Another [Company Appeal (AT) (Insolvency) No. 334 of 2017]***,

The question that came before the NCLAT was whether the moratorium under section 14 of the IBC will cover the current charges payable by the corporate detbor for supply of such services as water and electricity.

The NCLAT held that:

- There is no prohibition or bar imposed on the payment of current charges for essential services. Such payment is not covered by the order of the moratorium.
- The law does not stipulate that essential goods, including water and electricity, should be supplied free of charge until the moratorium is ended. The amount paid for these services by the RP shall be part of the CIRP cost. The RP was directed to pay current charges for the supply of electricity during the moratorium.

(3) Exceptions to Moratorium

Section 14(3) of the Code provides exceptions to applicability of moratorium. It states that the provisions of sub-section (1) shall not apply to —

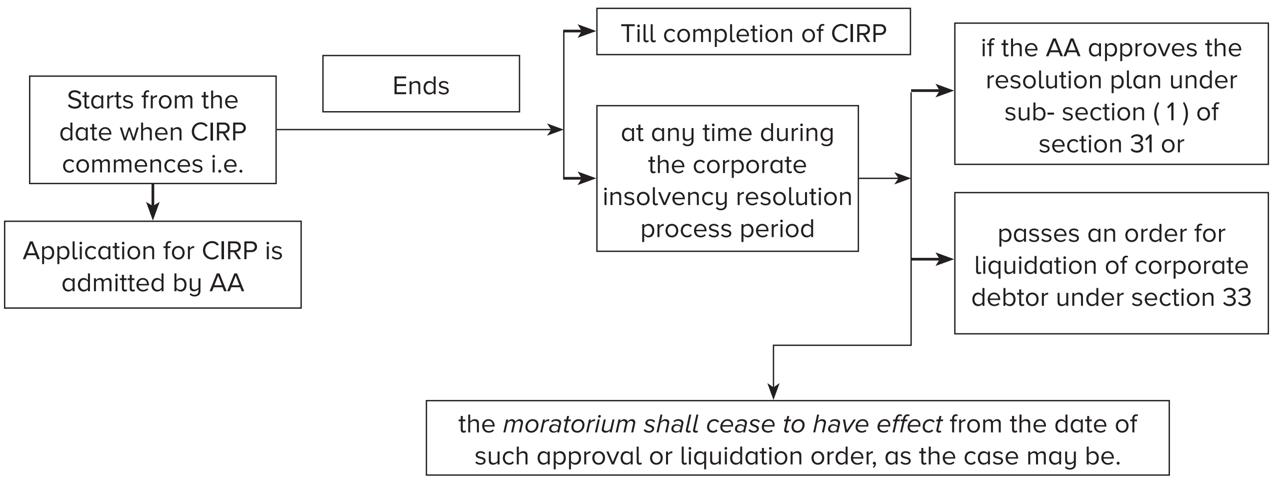
(a) such transactions, agreements or other arrangement as may be notified by the Central Government in consultation with any financial sector regulator or any other authority;

(b) a surety in a contract of guarantee to a corporate debtor.

(Under the Insolvency and Bankruptcy Code,2016 the surety is denied the right to subrogation)

In ***State Bank of India Vs. Ramkrishnan [Civil Appeal Nos. 3595 & 4553 of 2018, (2018) 17 SCC 394]***, the Supreme Court held that section 14 did not apply to the personal guarantor of the corporate debtor but only to the corporate debtor. The court held that in a contract of guarantee, the liability of surety and that of principal debtor is coextensive and hence, the creditor can proceed against assets of either the principal debtor or the surety, or both, in no particular order.

(4) Duration of Moratorium



Sub-section (4) of section 14 of the Code provides that the order of moratorium shall have effect from the date of such order till the completion of the corporate insolvency resolution process:

Proviso to sub-section (4) specifies the situations when CIRP comes to an end before statutory time period of CIRP mentioned under IBC (180/270/330 days) expires that where at any time during the corporate insolvency resolution process period, if the Adjudicating Authority

- approves the resolution plan under sub-section (1) of section 31 or
- passes an order for liquidation of corporate debtor under section 33,

the moratorium shall cease to have effect from the date of such approval or liquidation order, as the case may be.

Punishment for Contravention of Moratorium

Section 74 (1) & (2) of the Code provides for punishment for contravention of moratorium as follows:

Section of the Code	Who violates the provisions of section 14	Who shall be liable for punishment	Punishment
74(1)	the corporate debtor or any of its officer	any such officer who knowingly or wilfully committed or authorised or permitted such contravention	• Imprisonment: Minimum three years to maximum five years, • Fine: Minimum Rs 1 Lakh to maximum three lakh rupees, or • Both.

74(2)	any creditor	any person who knowingly and wilfully authorised or permitted such contravention by a creditor	● Imprisonment: Minimum one years to maximum five years, ● Fine: Minimum Rs one Lakh to maximum one crore rupees, or ● Both.

Filing of Application and Application Fee

Rule 10 of the *Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 provides for the rules to be followed for filing application to initiate CIRP as follows:*

(1) Till such time the rules of procedure for conduct of proceedings under the Code are notified, the application made under sub-section (1) of section 7, sub-section (1) of section 9 or sub-section (1) of section 10 of the Code shall be filed before the Adjudicating Authority in accordance with rules 20, 21, 22, 23, 24 and 26 of Part III of the National Company Law Tribunal Rules, 2016.

(2) An applicant under these rules shall immediately after becoming aware, notify the Adjudicating Authority of any winding-up petition presented against the corporate debtor.

(3) The application shall be accompanied by such fee as specified in the Schedule.

(4) The application and accompanying documents shall be filed in electronic form, as and when such facility is made available and as prescribed by the Adjudicating Authority:

Provided that till such facility is made available, the applicant may submit the accompanying documents, and wherever they are bulky, in electronic form, in scanned, legible portable document format in a data storage device such as a compact disc or a USB flash drive acceptable to the Adjudicating Authority.

Rules 20, 21, 22, 23, 24 and 26 of the National Company Law Tribunal Rules, 2016

Procedure for filing petition: Rule 20 lays down procedure for filing petition with NCLT-

(1) Every appeal or petition or application or caveat petition or objection or counter presented to the Tribunal shall be in English and in case it is in some other Indian language, it shall be accompanied by a copy translated in English and shall be fairly and legibly type written, lithographed or printed in double spacing on one side of standard petition paper with an inner margin of about four centimeter width on top and with a right margin of 2.5. cm, and left margin of 5 cm, duly paginated, indexed and stitched together in paper book form.

(2) The cause title shall state "Before the National Company Law Tribunal" and shall specify the Bench to which it is presented and also set out the proceedings or order of the authority against which it is preferred.

(3) Appeal or petition or application or counter or objections shall be divided into paragraphs and shall be numbered consecutively and each paragraph shall contain as nearly as may be, a separate fact or allegation or point.

(4) Where Saka or other dates are used, corresponding dates of Gregorian Calendar shall also be given.

(5) Full name, parentage, age, description of each party and address and in case a party sues or being sued in a representative character, shall also be set out at the beginning of the appeal or petition or application and need not be repeated in the subsequent proceedings in the same appeal or petition or application.

(6) The names of parties shall be numbered consecutively and a separate line should be allotted to the name and description of each party.

(7) These numbers shall not be changed and in the event of the death of a party during the pendency of the appeal or petition or matter, his legal heirs or representative, as the case may be, if more than one shall be shown by sub-numbers.

(8) Where fresh parties are brought in, they may be numbered consecutively in the particular category, in which they are brought in.

(9) Every proceeding shall state immediately after the cause title the provision of law under which it is preferred.

Particulars to be set out in the address for service - Rule 21 lays provisions for the address for service:

The address for service of summons shall be filed with every appeal or petition or application or caveat on behalf of a party and shall as far as possible contain the following items namely: -

(a) the name of the road, street, lane and Municipal Division or Ward, Municipal Door and other number of the house;

(b) the name of the town or village;

(c) the post office, postal district and PIN Code, and

(d) any other particulars necessary to locate and identify the addressee such as fax number, mobile number, valid e-mail address, if any.

Initiating alteration- Rule 22 specifies that –

"Every interlineations, eraser or correction or deletion in any appeal or petition or application or document shall be initiated by the party or his authorised representative presenting it."

Presentation of petition or appeal

Rule 23 prescribes the manner of filing petition with NCLT:

(1) Every petition, application, caveat, interlocutory application, documents and appeal shall be presented in triplicate by the appellant or applicant or petitioner or respondent, as the case may be, in person or by his duly authorised representative or by an advocate duly appointed in this behalf in the prescribed form with stipulated fee at the filing counter and non-compliance of this may constitute a valid ground to refuse to entertain the same.

(2) Every petition or application or appeal may be accompanied by documents duly certified by the authorised representative or advocate filing the petition or application or appeal duly verified from the originals.

(3) All the documents filed in the Tribunal shall be accompanied by an index in triplicate containing their details and the amount of fee paid thereon.

(4) Sufficient number of copies of the appeal or petition or application shall also be filed for service on the opposite party as prescribed under these rules.

(5) In the pending matters, all applications shall be presented after serving copies thereof in advance on the opposite side or his authorised representative.

(6) The processing fee prescribed by these rules, with required number of envelopes of sufficient size and notice forms shall be filled alongwith memorandum of appeal.

Number of copies to be filed (Rule 24)

The appellant or petitioner or applicant or respondent shall file three authenticated copies of appeal or petition or application or counter or objections, as the case may be, and shall deliver one copy to each of the opposite party.

Endorsement and Verification (Rule 26)

(1) At the foot of every petition or appeal or pleading there shall appear the name and signature of the authorised representative.

(2) Every petition or appeal shall be signed and verified by the party concerned in the manner provided by these rules.

The National Company Law Appellate Tribunal (Chennai Bench) in a significant ruling in the matter of ***Nirej Vadakkedathu Paul & Ors Vs Sunstar Hotels & Estate Private Limited and Mcdowell Holdings Ltd (Company Appeal (AT) (CH) (Ins) No. 142/2022)*** dealt with the issue of objection by group of shareholders (which included some Foreign Portfolio Investors) of corporate debtor against which corporate insolvency resolution process (CIRP) has been initiated by the NCLT (Adjudicating Authority/AA) under section 7 of the I&B Code, 2016.

NCLAT Findings:

The NCLAT after going through the factual matrix of the case primarily decided the following two issues: - (a) Whether the shareholder of the 'Corporate Debtor' has any locus in Section 7 application filed by the 'Financial Creditor? (b) Whether the shareholders can make payment to satisfy financial debt of financial creditor in order to take away the 'Corporate Debtor' from the clutches of the 'Corporate Insolvency Resolution Process?

The NCLAT having regard to the provision under I&B Code, 2016 held that

- The shareholders have no 'locus' once an application under Section 7 of the I &B Code,2016 filed by a Financial Creditor is accepted and CIRP is initiated by the Adjudicating Authority.
- Once debt and default is established before the Adjudicating Authority, there is no law which allows a shareholder of a corporate debtor to challenge the initiation of corporate insolvency resolution process of the corporate debtor.
- The NCLAT further held that shareholders cannot be aggrieved merely by the admission of the corporate debtor into the corporate insolvency resolution process since such objection may render the object of I &B Code,2016 redundant since any shareholder of a corporate debtor against which insolvency proceedings have been initiated can seek to maintain a derivative action and question and sabotage a valid CIRP initiated by the Adjudicating Authority. A shareholder is technically an investor who owns limited investment in the company to the extent of share capital subscribed by him.
- The NCLAT relied on its judgment in the case of *Anant Kajare Vs Eknath Aher & Anr CA (AT) (Insolvency) No.296 of 2017* wherein it has been held that since appellant is an investor therefore it cannot claim to be an aggrieved person for preferring an appeal against the order passed by the Adjudicating Authority. However, the NCLAT held that an investor is entitled to file its claim before the Insolvency Resolution Professional.
- The NCLAT further held that in an appeal filed under section 61 of the I &B Code, no direction can be given to any party to the settlement (particularly to a third party) to perform certain duties to ensure settlement between other parties.
- Similarly, on the issue of settling of claims of the Financial Creditor by a third party, the NCLAT held that there is no law which allows a third party to settle claims of the Financial Creditor on behalf of the corporate debtor more so without the consent of the corporate debtor and in the teeth of opposition by the Financial Creditor.

Source: ICSIIIP Insolvency and Bankruptcy Journal March 2023

Supreme Court of India: Case title: ***Sabarmati Gas Limited vs. Shah Alloys Limited Case no.: Civil Appeal No. 1669 of 2020 Decision Date: 4th January, 2023***

Facts:

- The respondent, for its manufacturing needs, required commercial supply of natural gas. To facilitate the same the appellant and the respondent entered into a Gas Sales Agreement (GSA) whereby and where under the appellant was obligated to supply natural gas.
- On later stage the Respondent defaulted in the payment and made only partial irregular payments.
- Meanwhile, the respondent approached BIFR to get it declared as a 'sick unit' and for recommendation of a plan for its rehabilitation, in terms of the provisions under SICA.
- After the enactment of IBC, the Appellant issued a demand notice, under Section 8 of the IBC, 2016 demanding payment of operational debt. Respondent gave a reply to the aforesaid demand notice stating that there was shortfall in supply of natural gas and it caused huge loss due to the disconnection of gas supply. Therefore, Respondent declined the liability to pay the amount demanded.
- Thereafter, an application was fi led by under section 9 of Insolvency and Bankruptcy Code, 2016 (IBC) by Operational Creditor (Sabarmati Gas Limited) seeking initiation of Corporate Insolvency Resolution Process (CIRP) of Shah Alloys Limited.
- The said application was dismissed by the NCLT on the grounds of being barred by limitation and existence of a 'pre-existing dispute' between the appellant and the respondent. In the preset case, while the proceedings under SICA were pending, Insolvency & Bankruptcy Code came into effect, which repealed SICA. The Appellant could not have resorted to any legal proceedings to enforce its rights.
- The Hon'ble Supreme Court interpreted the provision related to limitation of time that section 238A of IBC renders the provision of Limitation Act applicable to the computation of the period of limitation in regard to proceedings before the NCLT.
- Decision in the case of *B.K. Educational Services Private Limited* was referred by the Hon'ble Supreme Court , that the period of limitation is three years from the right to apply accrues but the delay is condonable on sufficient grounds as provided under Section 5 of the Limitation Act.
- Sufficient cause is the cause for which a party could not be blamed. As such, in the absence of provisions for exclusion of the period of suspension of legal proceedings, the same can be excluded and is sufficient cause for condoning the delay under Section 5 of the Limitation Act.
- Hon'ble Court held that question of condonation of delay is not considered it will result in injustice as the party was statutorily prevented from initiating action against the industrial company concerned. Moreover, for an application filed under section 7 or 9 of IBC, the date of coming into force of IBC i.e., 01.12.2016 would not form the trigger point of limitation and the period of limitation for an application for initiating of CIRP under Section 9, IBC would be three years from the date when the right to apply accrues as provided by Article 137 of the Limitation Act.
- Furthermore, the Hon'ble Supreme Court concluded that there was a pre-existing dispute between the parties.

In the case of *Vishal Chelani & Ors. vs. Debashis Nanda (Civil Appeal No. 3806 of 2023)* the issue before Hon'ble Supreme Court was whether there could be different treatment of allottees in the resolution plan for the one who had invoked RERA and of others who did not approach RERA?

Hon'ble Apex Court while setting aside the order of NCLAT held that allottees who approached RERA were FCs under explanation to section 5(8)(f) of the Code. It was observed that per se there can be no distinction between different classes of FC for the purposes of drawing a resolution plan. Such a distinction is artificial and amounts to hyper classification, is thus contradictory to Article 14 of the Indian Constitution. It further observed that 'to treat a particular segment of that class differently for the purposes of another enactment, on the ground that one or some of them had elected to take back the deposits together with such interest as ordered by the competent authority, would be highly inequitable.

LESSON ROUND-UP

- The IBC regime provides that if a corporate debtor defaults on paying a debt, an application may be made to the jurisdictional AA by a creditor of the corporate debtor or by the corporate debtor itself to initiate a corporate insolvency resolution process (CIRP). Once a corporate insolvency resolution process starts, every attempt is made to resolve and reorganize the insolvency of corporate debtor.
- The insolvency of corporate debtor may get "resolved"—when a resolution plan for the corporate debtor is approved by the requisite majority (66%) of the committee of creditors of the corporate debtor and the plan is then approved by the Adjudicating Authority by way of an order passed under section 31 of the IBC.
- The corporate debtor does not get resolved through the CIRP—for instance, if no resolution plan is received or approved for the corporate debtor, or if the committee of creditors, prior to receiving any resolution plan takes a decision to liquidate the CD. The non-resolution of insolvency through a CIRP would lead to an order passed by the Adjudicating Authority under section 33 of the IBC to liquidate the corporate debtor, thereby starting the liquidation process.
- Hence, every CIRP, will lead to either an order of approval of the resolution plan by the Adjudicating Authority or an order of liquidation of the corporate debtor. It should be kept in mind that the primary aim of the IBC is to revive and save the corporate debtor (that is, to resolve). Only once the CIRP fails does the liquidation follow.
- Whenever an application is filed by any creditor or even corporate applicant to initiate CIRP against Corporate Debtor, Application to the Adjudicating Authority Rules states that the applicant shall dispatch forthwith, a copy of the application filed with the Adjudicating Authority, by registered post or speed post to the Board (i.e. IBBI) and registered office of the corporate debtor.
- Recommending name of Interim Resolution Professional: It is mandatory to recommend name of Interim Resolution Professional if applicant initiating CIRP is financial creditor or corporate debtor but is optional for Operational Creditor.
- An important distinction between the application filed by a financial creditor and an operational creditor is that in the case of the latter, the Adjudicating Authority admits the application only if demand notice has been served on the corporate debtor to make payment within 10 days of notice and there is no dispute regarding the existence of the debt.
- The Adjudicating Authority shall, within 14 days of receipt of application, either admit or reject the application filed to initiate CIRP. Though, Supreme Court has held that this timeline is directory and not mandatory.
- The corporate insolvency resolution process shall be completed within a period of one hundred and eighty days from the date of admission of the application to initiate such process. However, one time extension of maximum 90 days may be granted by the Adjudicating Authority on an application filed by the Resolution Professional provided it is approved by 66% voting by the members of the Committee of Creditors of the Corporate Debtor. It is further provided that the corporate insolvency resolution process shall mandatorily be completed within a period of three hundred and thirty days from the insolvency commencement date, including any extension of the period of corporate insolvency resolution process granted under this section and the time taken in legal proceedings in relation to such resolution process of the corporate debtor.
- The Adjudicating Authority, after admission of the application under section 7 or section 9 or section 10, shall, by an order –(a) declare a moratorium for the purposes referred to in section 14; (b) cause a public announcement of the initiation of corporate insolvency resolution process and call for the submission of claims under section 15; and (c) appoint an interim resolution professional in the manner as laid down in section.

- Section 14 of the Code details the moratorium protection given to the corporate debtor. The entire period of corporate insolvency resolution professional is covered under this moratorium, during which all suits, legal proceedings, and recovery actions against the corporate debtor are held in abeyance to give time to the corporate debtor to resolve its status.
- Rules 20, 21, 22, 23, 24 and 26 of Part III of the National Company Law Tribunal Rules, 2016 are applicable for filing application to initiate CIRP before the Adjudicating Authority (NCLT).

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. What is the form and manner of filing application to initiate corporate insolvency resolution process under section 7 of IBC, 2016?
2. Whether the insolvency resolution proceedings under the Code can be initiated, in view of pendency of proceedings before Debt Recovery Tribunal and invocation of Section 13(4) of the SARFAESI Act?
3. Whether insolvency proceedings can be initiated against financial service providers under the provisions of the Insolvency and Bankruptcy Code, 2016?
4. What is the duration of Corporate Insolvency Resolution Process under the Insolvency and Bankruptcy Code, 2016?
5. Explain "moratorium" in accordance with the prohibitory provisions of IBC, 2016?

OTHER REFERENCES

- IBBI 2019 Handbook- Understanding the IBC
- Pronouncements under the Insolvency and Bankruptcy Code, 2016: Issue Analysis, ICSIIPA.

Role, Functions and Duties of Insolvency Professional, Interim Resolution Professional and Resolution Professional

Lesson 16

KEY CONCEPTS

■ Insolvency Professional ■ Interim Resolution Professional ■ Resolution Professional ■ Committee of Creditors ■ Code & Conduct

Learning Objectives

To Understand

- Appointment of Interim Resolution Professional
- Appointment of Resolution Professional
- Resolution Professional
- Management of Affairs of Corporate Debtor
- Meeting of Committee of Creditors
- Duties of Resolution Professional

Lesson Outline

- Introduction
- Provisions of the Insolvency and Bankruptcy Code, 2016 relating to Resolution Professional & Interim Resolution Professional
- Role of Insolvency Profession as an Authorised Representative under the Code
- The IBBI (Insolvency Professionals) Regulations, 2016
- Public Announcement
- Code of Conduct of Insolvency Professional
- Duties and Powers of Interim Resolution Professional/ Resolution Professional
- Professional fee
- Case Laws
- Lesson Round-Up
- Test Yourself
- Other References (Including Websites / Video Links)

REGULATORY FRAMEWORK

- The Insolvency and Bankruptcy Code 2016
- The IBBI (Insolvency Professionals) Regulations, 2016
- The IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016
- The IBBI (Model Bye- Laws and Governing Board of Insolvency Professional Agencies), 2016

INTRODUCTION

The Banking Law Reform Committee (BLRC) Report- Volume 1, Rationale for the Code elaborated the significance of role of Insolvency Professional as follows:

Insolvency professionals play a vital role in the insolvency and bankruptcy resolution process as envisaged by the Committee. As mentioned in the report -insolvency and bankruptcy resolution under the Code will proceed in two phases, for registered entities as well as for individuals.

- The first phase of the insolvency and bankruptcy process is the period of insolvency resolution during which insolvency is assessed and a solution is reached within a stipulated time period.
- In case a solution is not reached within the specified time limit, the second phase of the process begins wherein the entity is declared bankrupt. At this point a registered entity enters into Liquidation whereas an individual enters into bankruptcy resolution.

This entire insolvency and bankruptcy process is managed by a regulated and licensed professional namely the Insolvency Professional or an IP, appointed by the adjudicator. In an insolvency and bankruptcy resolution process driven by the law, there are judicial decisions being taken by the adjudicator. But there are also checks and accounting as well as conduct of due process that are carried out by the IPs. Insolvency professionals form a crucial pillar upon which rests the effective, timely functioning as well as credibility of the entire edifice of the insolvency and bankruptcy resolution process.

An IP may hold any of the following roles under the Code:

1. Resolution professional (RP) to resolve insolvency for a firm or an individual;
2. Bankruptcy Trustee in an individual bankruptcy process;
3. Liquidator in a firm liquidation process.

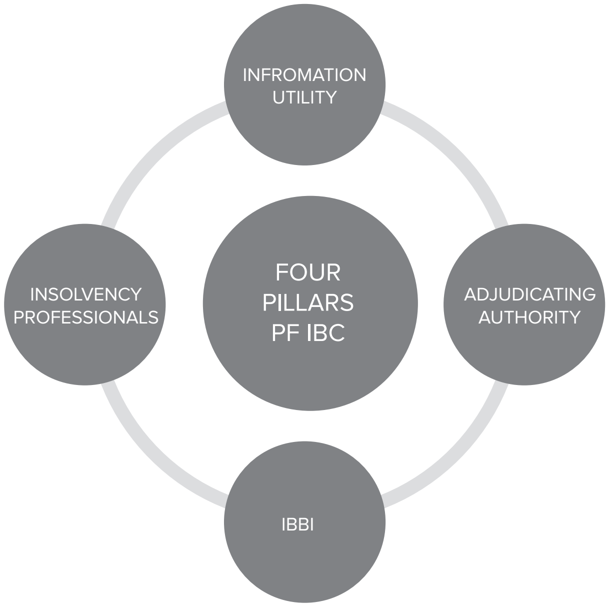
In administering the resolution outcomes, the role of the IP encompasses a wide range of functions, which include adhering to procedure of the law, as well as accounting and finance related functions. The latter include the identification of the assets and liabilities of the defaulting debtor, its management during the insolvency proceedings if it is an enterprise, preparation of the resolution proposal, implementation of the solution for individual resolution, the construction, negotiation and mediation of deals as well as distribution of the realisation proceeds under bankruptcy resolution. In performing these tasks, an IP acts as an agent of the adjudicator. In a way the adjudicator depends on the specialized skills and expertise of the IPs to carry out these tasks in an efficient and professional manner.

The REPORT also describes the mandates for the IPs and delineate a framework for regulating IPs as follows:

In the case of insolvency resolution, a failure of the process may result from two main sources: collusion between the parties involved and poor quality of execution of the process itself. Hence, it is important that the professionals responsible for implementing the insolvency resolution process adhere to certain minimum standards so as to prevent failures of the process and enhance credibility of the system as a whole.

In India today, there are professionals and intermediaries that offer services to resolve financial distress of both registered entities as well as individuals. These include lawyers, accountants and auditors, valuers and specialist resolution managers. However, given the critical role that the Code envisages for these entities in the resolution process, the Committee believes that the Board should set minimum standards for the selection of these professionals, along with their licensing, appointment, functioning and conduct under the Code.

To this end, the Code empowers the Board to lay down the minimum professional standards and the code of conduct to be followed to by IPs at each stage of the insolvency and bankruptcy resolution process.



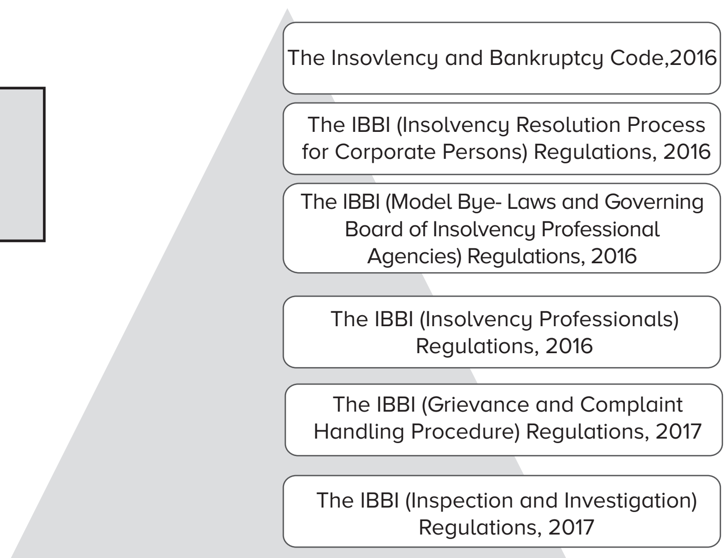
- Out of the four pillars of IBC,2016, the first pillar of the IBC's institutional infrastructure is insolvency professionals (IPs).
- An IP is one of the most important components of the IBC ecosystem.
- An IP is a regulated and licensed professional, responsible for managing and overseeing the CIRP and/or the liquidation process of the CD, and the resolution and bankruptcy process for partnerships and individuals.
- IPs form a crucial pillar on which the entire edifice of the insolvency and bankruptcy process rests.
- The Disciplinary Committee set up by the IBBI and the Insolvency Professional Agencies also play a crucial role in ensuring that the IPs adhere to ethical standards and the Code of Conduct.

The IBC gives various powers to IPs, while subjecting them to regulatory and judicial oversight. The first level of regulatory oversight of an IP is provided by the insolvency professional agency (IPA) with which the IP is registered. To support IPs, the concept of an insolvency professional entity (IPE), a regulated service provider supporting IPs, is also recognized.

IPs are aided in the insolvency resolution, liquidation, and bankruptcy process by information utilities (IUs), which form the second pillar of the institutional infrastructure. The IUs are regulated and licensed repositories of information relating to the CD. IUs collect, collate, authenticate, and disseminate financial information to be used in insolvency resolution, liquidation, and bankruptcy proceedings.

The judicial oversight of IPs is provided by adjudicating authorities (AAs), the third pillar of the IBC's institutional infrastructure. The AAs are specialized tribunals tasked with ensuring that the insolvency resolution, liquidation, and bankruptcy process is being performed as per the IBC and its related rules and regulations.

Regulatory framework for Insolvency Professionals



An IP is defined in section 3(19) of the IBC as a person enrolled under section 206 with an IPA as a member and registered with the IBBI as an IP under section 207.

Only an IP can be appointed under the IBC as	- an interim resolution professional (IRP), - a resolution professional (RP), - a liquidator, or - a bankruptcy trustee.

The AA appoints an IRP or an RP to run the CIRP of a CD, and a liquidator to run the liquidation process. A bankruptcy trustee runs the insolvency and bankruptcy process for partnerships and individuals. Hence, the IP—acting as an IRP, RP, liquidator, or bankruptcy trustee—is the foundation of the IBC.

ROLE OF INSOLVENCY PROFESSIONALS	
As an Interim Resolution Professional (IRP)	Chapter II (Part II of the Code)- Insolvency Resolution Process of Corporate Persons
	Chapter IV (Part II of the Code)- Fast track corporation insolvency resolution process
As a Resolution Professional	Chapter II (Part II of the Code)- Insolvency Resolution Process of Corporate Persons
	Chapter III-A (Part II of the Code) Pre-Packaged Insolvency Resolution Process
	Chapter IV (Part II of the Code)- Fast track corporation Insolvency resolution process
As a Liquidator	Chapter III (Part II of the Code)- Liquidation Process of corporate persons
	Chapter V (Part II of the Code)- Voluntary Liquidation Process of corporate
As a Bankruptcy Trustee	PART III of the Code-Insolvency Resolution And Bankruptcy For Individuals And Partnership Firms

In the corporate insolvency resolution process, the insolvency professional runs the debtor's business during the moratorium period, verifies the claims of the creditors and constitutes a creditor's committee and helps the committee of creditors in arriving at a consensus for the revival and rehabilitation of the corporate debtor's business. In liquidation, the insolvency professional acts as a liquidator and in case of individual and partnership insolvency resolution, he performs the role of bankruptcy trustee.

The Resolution Professional (RP) holds a central position in conducting the CIRP and his role is vital to the efficient operation of the resolution process. The RP acts as a bridge between the debtor and the creditor and plays a significant role in aligning the interests of the CD with those of the creditors. The RP is appointed as an officer of the AA to conduct the resolution process and is vested with various statutory duties and powers. It is the RP who communicates with AA on behalf of CoC.

Definitions in the Insolvency and Bankruptcy Code, 2016:

Section 3(19): "Insolvency Professional" means a person enrolled under section 206 with an insolvency professional agency as its member and registered with the Board as an insolvency professional under section 207.

Section 5(18): "Liquidator" means an insolvency professional appointed as a liquidator in accordance with the provisions of Chapter III or Chapter V of Part II, as the case may be.

Section 5(27): "Resolution Professional", for the purposes of Part II, means an insolvency professional appointed to conduct the corporate insolvency resolution process and includes an interim-resolution professional.

Section 79(9): "Bankruptcy Trustee" means the insolvency professional appointed as a trustee for the estate of the bankrupt under section 125.

Section 79(21): "Resolution Professional" means an insolvency professional appointed under Part III as a resolution professional for conducting the fresh start process or insolvency resolution process.

An IP is a person who is enrolled with an IPA as a member and registered with the IBBI after qualifying Limited Insolvency Examination. Any eligible person having the required experience and qualifications including a chartered accountant, cost accountant, company secretary, advocate, managerial person can seek registration with an IPA and IBBI after meeting the requirements of the regime.

Thus, an IP is a crucial pillar responsible for the effective, timely and credible functioning of the entire edifice of the insolvency and bankruptcy resolution process. In administering the resolution outcomes, the role of the IP encompasses a wide range of functions, which include adhering to procedure of the law, as well as general management and finance related functions.

The IP is required to adhere to a strict code of conduct while performing his obligations under the Code and also ensuring there are adequate procedures and policies laid down and implemented by his team deployed on any ongoing CIRP.

Part IV of the Code lays down Regulation of Insolvency Professionals, Agencies and Information Utilities. Chapter IV of Part IV deals with registration, functions and obligations of Insolvency Professionals.

The Code has provided for a two-tier regulation of IPs: -

(i) The first-tier regulation of IPs is steered by the IPAs who administer the registration of IPs and promote and supervise their continuous development.

(ii) The second-tier regulation is steered by the IBBI which maintains a panel of IPs who have no disciplinary proceedings pending or against them and who hold Authorisation for Assignment or consented for assignments.

This saves judicial time in appointments. Thus, an IP is a crucial pillar responsible for the effective, timely and credible functioning of the entire edifice of the insolvency and bankruptcy resolution process. In administering the resolution outcomes, the role of the IP encompasses a wide range of functions, which include adhering to procedure of the law, as well as general management and finance related functions.

The IP is required to adhere to a strict code of conduct while performing his obligations under the Code and also ensuring there are adequate procedures and policies laid down and implemented by his team deployed on any ongoing CIRP.

ELIGIBILITY FOR RESOLUTION PROFESSIONAL UNDER THE IBBI (INSOLVENCY RESOLUTION PROCESS FOR CORPORATE PERSONS) REGULATIONS, 2016

Regulation 3(1) lays down the criterion for a person who can be appointed as an interim resolution professional or resolution professional as follows:

(1) An insolvency professional shall be eligible to be appointed as an interim resolution professional or a resolution professional, as the case may be, for a corporate insolvency resolution process of a corporate debtor if he, and all partners and directors of the insolvency professional entity of which he is a partner or director, are independent of the corporate debtor.

Explanation is provided to determine when a person shall be considered independent of the corporate debtor i.e. if he:

(a) is eligible to be appointed as an independent director on the board of the corporate debtor under section 149 of the Companies Act, 2013 , where the corporate debtor is a company;

(b) is not a related party of the corporate debtor; or

(c) is not an employee or proprietor or a partner:

(i) of a firm of auditors or secretarial auditors in practice or cost auditors of the corporate debtor; or

(ii) of a legal or a consulting firm, that has or had any transaction with the corporate debtor amounting to five per cent or more of the gross turnover of such firm, in the last three financial years.

(1A) Where the committee decides to appoint the interim resolution professional as resolution professional or replace the interim resolution professional under section 22 or replace the resolution professional under section 27, it shall obtain the written consent of the proposed resolution professional in Form AA of the Schedule-I .

(2) An interim resolution professional or a resolution professional, as the case may be, shall make disclosures at the time of his appointment and thereafter in accordance with the Code of Conduct.

(3) An interim resolution professional or a resolution professional, who is a director or a partner of an insolvency professional entity, shall not continue as the interim resolution professional or resolution professional, as the case may be, in a corporate insolvency resolution process, if the insolvency professional entity or any other partner or director of such insolvency professional entity represents any other stakeholder in that corporate insolvency resolution process.

RELATED PROVISIONS UNDER IBC

Appointment and Tenure of Interim Resolution Professional (IRP)

Section 16 of the Code provides for the Appointment and Tenure of Interim Resolution Professional (IRP) as follows –

(1) *Who appoints IRP:* The Adjudicating Authority shall appoint an interim resolution professional on the insolvency commencement date.

(2) *Appointment of IRP in case of application made by financial creditor or corporate applicant:* Where the application for corporate insolvency resolution process is made by a financial creditor or the corporate debtor, as the case may be, the resolution professional, as proposed respectively in the application under section 7 or section 10, shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.

(3) *Appointment of IRP in case in case of application made by operational creditor*: Where the application for corporate insolvency resolution process is made by an operational creditor and-

(a) no proposal for an interim resolution professional is made, the Adjudicating Authority shall make a reference to the Board for the recommendation of an insolvency professional who may act as an interim resolution professional;

(b) a proposal for an interim resolution professional is made under sub-section (4) of section 9, the resolution professional as proposed, shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.

(4) *Recommendation by the Board:* The Board shall, within ten days of the receipt of a reference from the Adjudicating Authority under sub-section (3), recommend the name of an insolvency professional to the Adjudicating Authority against whom no disciplinary proceedings are pending.

(5) *Term of IRP:* The term of the interim resolution professional shall continue till the date of appointment of the resolution professional under section 22.

Rule 9 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 provides for submission of written consent of insolvency professional whose name is recommended for appointment as an Interim Resolution Professional (IRP) while filing application to initiate CIRP under section 7, 9 or 10 of the Code. It states that:

(1) The applicant, wherever he is required to propose or proposes to appoint an insolvency resolution professional, shall obtain a written communication in Form 2 from the insolvency professional for appointment as an interim resolution professional and enclose it with the application made under rules 4, 6 or 7, as the case may be.

(2) The application under sub-rule (1) shall be accompanied by a certificate confirming the eligibility of the proposed insolvency professional for appointment as a resolution professional in accordance

with the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.

Management of Affairs of Corporate Debtor By Interim Resolution Professional

Section 17 of the Code provides for the management of affairs of corporate debtor by interim resolution professional i.e., powers and duties of IRP after appointment, as follows:

(1) From the date of appointment of the interim resolution professional, -

(a) the management of the affairs of the corporate debtor shall vest in the interim resolution professional;

(b) the powers of the board of directors or the partners of the corporate debtor, as the case may be, shall stand suspended and be exercised by the interim resolution professional;

(c) the officers and managers of the corporate debtor shall report to the interim resolution professional and provide access to such documents and records of the corporate debtor as may be required by the interim resolution professional;

(d) the financial institutions maintaining accounts of the corporate debtor shall act on the instructions of the interim resolution professional in relation to such accounts and furnish all information relating to the corporate debtor available with them to the interim resolution professional.

(2) The interim resolution professional vested with the management of the corporate debtor, shall-

(a) act and execute in the name and on behalf of the corporate debtor all deeds, receipts, and other documents, if any;

(b) take such actions, in the manner and subject to such restrictions, as may be specified by the Board;

(c) have the authority to access the electronic records of corporate debtor from information utility having financial information of the corporate debtor;

(d) have the authority to access the books of account, records and other relevant documents of corporate debtor available with government authorities, statutory auditors, accountants and such other persons as may be specified; and

(e) be responsible for complying with the requirements under any law for the time being in force on behalf of the corporate debtor.

In the case of *Pooja Menghani vs. Insolvency and Bankruptcy Board of India & Anr* , judgement dated November 20, 2023, Hon'ble High Court of Delhi inter alia observed that Section 17 of the IBC which deals with management of affairs of corporate debtor by interim resolution professional stipulates that from the date of appointment of the interim resolution professional, the management of the affairs of the corporate debtor shall vest in the interim resolution professional and the powers of the board of directors or the partners of the corporate debtor shall stand suspended and will be exercised by the interim resolution professional. It also stipulates that the officers and managers of the corporate debtor shall report to the interim resolution professional and provide access to such documents and records of the corporate debtor as may be required by the interim resolution professional. It also stipulates that the financial institutions maintaining accounts of the corporate debtor shall act on the instructions of the interim resolution professional in relation to such accounts and furnish all information relating to the corporate debtor available with them to the interim resolution professional.

Section 18 of the Code enumerates "Duties of interim resolution professional. According to it, the interim resolution professional shall perform the following duties, namely: -

(a) collect all information relating to the assets, finances and operations of the corporate debtor for determining the financial position of the corporate debtor, including information relating to –

(i) business operations for the previous two years;

(ii) financial and operational payments for the previous two years;

(iii) list of assets and liabilities as on the initiation date; and

(iv) such other matters as may be specified.

(b) receive and collate all the claims submitted by creditors to him, pursuant to the public announcement made under sections 13 and 15;

(c) constitute a committee of creditors;

(d) monitor the assets of the corporate debtor and manage its operations until a resolution professional is appointed by the committee of creditors;

(e) file information collected with the information utility, if necessary; and

(f) take control and custody of any asset over which the corporate debtor has ownership rights as recorded in the balance sheet of the corporate debtor, or with information utility or the depository of securities or any other registry that records the ownership of assets including –

(i) assets over which the corporate debtor has ownership rights which may be located in a foreign country;

(ii) assets that may or may not be in possession of the corporate debtor;

(iii) tangible assets, whether movable or immovable;

(iv) intangible assets including intellectual property;

(v) securities including shares held in any subsidiary of the corporate debtor, financial instruments, insurance policies;

(vi) assets subject to the determination of ownership by a court or authority;

(g) to perform such other duties as may be specified by the Board

Explanation. – For the purposes of this section, the term “assets” shall not include the following, namely: -

(a) assets owned by a third party in possession of the corporate debtor held under trust or under contractual arrangements including bailment;

(b) assets of any Indian or foreign subsidiary of the corporate debtor; and

(c) such other assets as may be notified by the Central Government in consultation with any financial sector regulator.

Personnel to Extend Co-operation to Interim Resolution Professional

Section 19 of the Code requires personnel to extend co-operation to interim resolution professional.

(1) The personnel of the corporate debtor, its promoters or any other person associated with the management of the corporate debtor shall extend all assistance and cooperation to the interim resolution professional as may be required by him in managing the affairs of the corporate debtor.

(2) Where any personnel of the corporate debtor, its promoter or any other person required to assist or cooperate with the interim resolution professional does not assist or cooperate, the interim resolution professional may make an application to the Adjudicating Authority for necessary directions.

(3) The Adjudicating Authority, on receiving an application under sub-section (2), shall by an order, direct such personnel or other person to comply with the instructions of the resolution professional and to cooperate with him in collection of information and management of the corporate debtor.

Management of Operations of Corporate Debtor as Going Concern

Section 20 of the Code mandates IRP to run management of operations of corporate debtor as going concern.

(1) The interim resolution professional shall make every endeavour to protect and preserve the value of the property of the corporate debtor and manage the operations of the corporate debtor as a going concern.

(2) For the purposes of sub-section (1), the interim resolution professional shall have the authority-

(a) to appoint accountants, legal or other professionals as may be necessary;

(b) to enter into contracts on behalf of the corporate debtor or to amend or modify the contracts or transactions which were entered into before the commencement of corporate insolvency resolution process;

(c) to raise interim finance provided that no security interest shall be created over any encumbered property of the corporate debtor without the prior consent of the creditors whose debt is secured over such encumbered property. It is provided that no prior consent of the creditor shall be required where the value of such property is not less than the amount equivalent to twice the amount of the debt;

(d) to issue instructions to personnel of the corporate debtor as may be necessary for keeping the corporate debtor as a going concern; and

(e) to take all such actions as are necessary to keep the corporate debtor as a going concern.

Section 5(15) of the Code defines "interim finance" which means any financial debt raised by the resolution professional during the insolvency resolution process period or by the corporate debtor during the pre-packaged insolvency resolution process period, as the case may be[and such other debt as may be notified.

Section 21 of the Code imposes duty on IRP to constitute "Committee of creditors – It states that the interim resolution professional (IRP) shall after collation of all claims received against the corporate debtor and determination of the financial position of the corporate debtor, constitute a committee of creditors.

If required by the committee of creditors at any time during the corporate insolvency resolution process, the resolution professional shall make available any financial information so required within a period of seven days of such requisition.

Appointment of resolution professional. – Section 22 of the Code provides for the appointment of resolution professional in the first meeting of the committee of creditors (CoC) in following ways:

(i) *When CoC resolves to appoint IRP as resolution professional or replace IRP by another resolution professional:* The committee of creditors, may, in the first meeting, by a majority vote of not less than sixty-six per cent. of the voting share of the financial creditors, either resolve to appoint the interim resolution professional as a resolution professional or to replace the interim resolution professional by another resolution professional.

(ii) *When CoC resolves to continue IRP as resolution professional: S*ubject to a written consent from **the interim resolution professional in the specified form**, it shall communicate its decision to the interim resolution professional, the corporate debtor and the Adjudicating Authority.

(iii) *When CoC resolves to replace the interim resolution professional:* It shall file an application before the Adjudicating Authority for the appointment of the proposed resolution professional along with a written consent from the proposed resolution professional in the specified form.

(iv) *Forwarding name of new proposed RP to the AA:* The Adjudicating Authority shall forward the name of the resolution professional proposed to replace IRP to the Board for its confirmation and shall make such appointment after confirmation by the Board.

(v) *IRP to continue as RP:* Where the Board does not confirm the name of the proposed resolution professional within ten days of the receipt of the name of the proposed resolution professional, the Adjudicating Authority shall, by order, direct the interim resolution professional to continue to function as the resolution professional until such time as the Board confirms the appointment of the proposed resolution professional

Resolution Professional to Conduct Corporate Insolvency Resolution Process

Section 23 of the Code provides for that subject to section 27, the resolution professional shall conduct the entire corporate insolvency resolution process and manage the operations of the corporate debtor during the corporate insolvency resolution process period:

It further provides that the resolution professional shall continue to manage the operations of the corporate debtor after the expiry of the corporate insolvency resolution process period, until an order approving the resolution plan under sub-section (1) of section 31 or appointing a liquidator under section 34 is passed by the Adjudicating Authority.

The section also states that the resolution professional shall exercise powers and perform duties as are vested or conferred on the interim resolution professional under this Chapter.

It also requires the interim resolution professional to provide all the information, documents and records pertaining to the corporate debtor in his possession and knowledge to the resolution professional in case of any appointment of a resolution professional in lieu of interim resolution professional by committee of creditors under sub-sections (4) of section 22,

Meeting of Committee of Creditors

Section 24 of the Code provides that all meetings of the committee of creditors shall be conducted by the resolution professional. Sub-section (3) provides that the resolution professional shall give notice of each meeting of the committee of creditors to

(a) members of committee of creditors, including the authorised representatives referred to in sub-sections (6) and (6A) of section 21 and sub-section (5);

(b) members of the suspended Board of Directors or the partners of the corporate persons, as the case may be;

(c) operational creditors or their representatives if the amount of their aggregate dues is not less than ten per cent. of the debt.

It also casts a duty on the resolution professional that he shall determine the voting share to be assigned to each creditor in the manner specified by the Board.

Duties of Resolution Professional

Section 25 of the Code lists out the mandatory duties of resolution professional as follows:

(1) It shall be the duty of the resolution professional to preserve and protect the assets of the corporate debtor, including the continued business operations of the corporate debtor.

(2) For the purposes of sub-section (1), the resolution professional shall undertake the following actions, namely: -

- (a) take immediate custody and control of all the assets of the corporate debtor, including the business records of the corporate debtor;
- (b) represent and act on behalf of the corporate debtor with third parties, exercise rights for the benefit of the corporate debtor in judicial, quasi-judicial or arbitration proceedings;
- (c) raise interim finances subject to the approval of the committee of creditors under section 28;
- (d) appoint accountants, legal or other professionals in the manner as specified by Board;

(e) maintain an updated list of claims;

(f) convene and attend all meetings of the committee of creditors;

(g) prepare the information memorandum in accordance with section 29;

(h) invite prospective resolution applicants, who fulfil such criteria as may be laid down by him with the approval of committee of creditors, having regard to the complexity and scale of operations of the business of the corporate debtor and such other conditions as may be specified by the Board, to submit a resolution plan or plans.

(i) present all resolution plans at the meetings of the committee of creditors;

(j) file application for avoidance of transactions in accordance with Chapter III, if any; and (k) such other actions as may be specified by the Board.

Regulation 3A of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 provides for assistance and cooperation by the personnel of the corporate debtor as follows:

(1) *Duty to take custody and control:* The interim resolution professional or resolution professional, as the case may be, shall take custody and control as specified under this regulation from the personnel of the corporate debtor,its promoters or any other person associated with the management of the corporate debtor as the case may be, of the following:-

(a) **the records of information** relating to the assets, finances and operations of the corporate debtor referred in clause (a) of section 18 and such other information required under regulation 36;

(b) **the assets recorded in the balance sheet** of the corporate debtor or in any other records referred in clause (f) of section 18.

(2) *Obligation of personnel/promoter etc. to provide list of assets and records while handing over their custody and control:* The personnel of the corporate debtor, its promoters or any other person associated with the management of the corporate debtor shall provide to the interim resolution professional or resolution professional, as the case may be**, a list of assets and records** while handing over their custody and control, and the interim resolution professional or resolution professional may, after taking such custody and control, if deemed necessary, identify person(s) in whose possession these assets and records will be held.

(3) *Duty of IRP/RP to prepare list of assets and records:* Where any asset or record has not been handed over or the list has not been provided under sub-regulation (2), the interim resolution professional or resolution professional, as the case may be, shall himself prepare a list of assets and records while taking custody and control of assets and records, and the interim resolution professional or resolution professional may, after taking such custody and control, if deemed necessary, identify person(s) in whose possession these assets and records will be held.

(4) *Signing of list of assets and records:* Each list of assets and records under sub-regulation (2) and (3) shall be signed by the parties present and by at least two individuals who have witnessed the act of taking control and custody of such assets and records.

(5) *Requisition by IRP/RP for information required under the Code but not handed over:* The interim resolution professional or resolution professional, as the case may be, shall requisition from the personnel of the corporate debtor, its promoters or any other person associated with the management of the corporate debtor as the case maybe, the information relating to the assets, finances and operations of the corporate debtor referred in clause (a) of section 18 and such information required under regulation 36 which were required to be maintained by the corporate debtor but have not yet been handed over.

(6) *Requisition by IRP/RP for assets in records but not handed over:* The interim resolution professional or resolution professional, as the case may be, shall requisition from the personnel of the corporate debtor, its promoters or any other person associated with the management of the corporate debtor as the case maybe, the assets which are recorded in the balance sheet or in any other records referred in clause (f) of section 18 and whose custody has not been handed over.

(7) An application made under sub-section (2) of section 19 in respect of failure to provide any asset or record as requisitioned under the Code and this regulation, shall show presence of such asset or record in the notice of requisition and absence of such asset or record in the list of assets and records taken in control and custody under sub-regulation (2) and (3).

Regulation 4 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 provides for right of Interim Resolution Professional (IRP)/Resolution Professional as follows:

(1) Access to Books: Without prejudice to section 17(2)(d), the interim resolution professional or the resolution professional, as the case may be, may access the books of account, records and other relevant documents and information, to the extent relevant for discharging his duties under the Code, of the corporate debtor held with- (a) depositories of securities; (b) professional advisors of the corporate debtor; (c) information utilities; (d) other registries that records the ownership of assets; (e) members, promoters, partners, board of directors and joint venture partners of the corporate debtor; and (f) contractual counterparties of the corporate debtor.

(2) Duty of the personnel to provide information to IRP/RP: The personnel of the corporate debtor, its promoters or any other person associated with the management of the corporate debtor shall provide the information within such time and in such format as sought by the interim resolution professional or the resolution professional, as the case may be.

The IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 provides for following duties of IRP/Resolution Professional:

4B. Disclosure of change in name and address of corporate debtor: Where a corporate debtor has changed its name or registered office address during the period of two years preceding the insolvency commencement date, the interim resolution professional or resolution professional, as the case may be, shall disclose all the former name(s) and registered office address(es) so changed along with the current name and registered office address in every communication, record, proceeding or any other document.

4C. Process e-mail: (1) The interim resolution professional shall open an email account and use it for all correspondences with stakeholders and in the event of his replacement by a resolution professional, shall handover the credentials of the email to him. (2) The resolution professional shall, in case of his replacement with another resolution professional or a liquidator, hand over the credentials of the email to the other resolution professional or the liquidator, as the case may be.

4D. **Operating separate bank account for each real estate project:** Where the corporate debtor has any real estate project, the interim resolution professional or the resolution professional, as the case may be, shall operate a separate bank account for each real estate project.

Replacement of Resolution Professional by Committee of Creditors

Section 27 of the Code lays down provisions for replacement of resolution professional by CoC during CIRP:

(1) Where, at any time during the corporate insolvency resolution process, the committee or creditors is of the opinion that a resolution professional appointed under section 22 is required to be replaced, it may replace him with another resolution professional in the manner provided under this section.

(2) The committee of creditors may, at a meeting, by a vote of sixty-six per cent of voting shares, resolve to replace the resolution professional appointed under section 22 with another resolution professional, subject to a written consent from the proposed resolution professional in the specified form.

(3) The committee of creditors shall forward the name of the insolvency professional proposed by them to the Adjudicating Authority.

(4) The Adjudicating Authority shall forward the name of the proposed resolution professional to the Board for its confirmation and a resolution professional shall be appointed in the same manner as laid down in section 16.

(5) Where any disciplinary proceedings are pending against the proposed resolution professional under sub-section (3), the resolution professional appointed under section 22 shall continue till the appointment of another resolution professional under this section.

Preparation of Information Memorandum

Resolution Professional to prepare information memorandum: Section 29(1) of the Code states that the resolution professional shall prepare an information memorandum in such form and manner containing such relevant information as may be specified by the Board for formulating a resolution plan.

Section 5(10) defines "information memorandum" which means a memorandum prepared by resolution professional under sub-section (1) of section 29.

Duty of the creditor to provide information to IRP/RP: Regulation 4(3) of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 casts duty on the creditor that he/they shall provide to the interim resolution professional or resolution professional, as the case may be, the information in respect of assets and liabilities of the corporate debtor from the last valuation report, stock statement, receivables statement, inspection reports of properties, audit report, stock audit report, title search report, technical officers report, bank account statement and such other information which shall assist the interim resolution professional or the resolution professional in preparing the information memorandum, getting valuation determined and in conducting the corporate insolvency resolution process.

Resolution Professional to provide access of relevant information to the resolution applicant: Section 29 (2) states that the resolution professional shall provide to the resolution applicant access to all relevant information in physical and electronic form, provided such resolution applicant undertakes- (a) to comply with provisions of law for the time being in force relating to confidentiality and insider trading; (b) to protect any intellectual property of the corporate debtor it may have access to; and (c) not to share relevant information with third parties unless clauses (a) and (b) of this sub-section are complied with.

Explanation. – For the purposes of this section, "relevant information" means the information required by the resolution applicant to make the resolution plan for the corporate debtor, which shall include the financial position of the corporate debtor, all information related to disputes by or against the corporate debtor and any other matter pertaining to the corporate debtor as may be specified

Submission of resolution plan. – Section 30(2) of the Code states that it is the duty of the resolution professional to confirm that each resolution plan –

(a) provides for the payment of insolvency resolution process costs in a manner specified by the Board in priority to the payment of other debts of the corporate debtor;

(b) provides for the payment of debts of operational creditors and financial creditors, who do not vote in favour of the resolution plan in the manner specified in the section.

Submission of resolution professional to CoC: Section 30(3) provides that the resolution professional shall present to the committee of creditors for its approval such resolution plans which confirm the conditions referred to in sub-section (2).

Duty of the resolution professional to submit approved resolution plan to AA: According to section 30(6), the resolution professional shall submit the resolution plan as approved by the committee of creditors to the Adjudicating Authority.

> ***Protection of action taken in good faith**. - Section 233 of the Code provides, "No suit, prosecution or other legal proceeding shall lie against an insolvency professional or liquidator for anything which is in done or intended to be done in good faith under this Code or the rules or regulations made thereunder."*

Enrolled and Registered Persons to act as Insolvency Professionals

Section 206 of the Code makes it mandatory for a person before rendering his services as insolvency professional under this Code

(i) to be enrolled as a member of an insolvency professional agency; and

(ii) registered with the Board.

i.e. both the conditions should be complied with before renderinng services as an Insolvency Professional.

Registration of insolvency professionals

Section 207(1) of the Code provides that to become an Insolvency Professional (IP), an individual shall first enroll with an Insolvency Professional Agency (IPA) as a member, and then register with the IBBI within such time, manner and after payment of fee as may be specified by the regulations.

Sub-section (2) of section 207 (2) vests in the Board power to specify the categories of professionals or persons possessing such qualifications and experience in the field of finance, law, management, insolvency or such other field, as it deems fit.

Functions and obligations of insolvency professionals

Section 208 of the Code prescribes functions and obligations of insolvency professionals:

(1) Where any insolvency resolution, fresh start, liquidation or bankruptcy process has been initiated, it shall be the function of an insolvency professional to take such actions as may be necessary, in the following matters, namely: –

(a) a fresh start order process under Chapter II of Part III;

(b) individual insolvency resolution process under Chapter III of Part III;

(c) corporate insolvency resolution process under Chapter II of Part II;

(ca) pre-packaged insolvency resolution process under Chapter III-A of Part II;

(d) individual bankruptcy process under Chapter IV of Part III; and

(e) liquidation of a corporate debtor firm under Chapter III of Part II.

(1A) Where the name of the insolvency professional proposed to be appointed as a resolution professional, is approved under clause (e) of sub-section (2) of section 54A, it shall be the function of such insolvency professional to take such actions as may be necessary to perform his functions and duties prior to the initiation of the pre-packaged insolvency resolution process under Chapter III-A of Part II.

(2) Every insolvency professional shall abide by the following code of conduct: –

(a) to take reasonable care and diligence while performing his duties;

(b) to comply with all requirements and terms and conditions specified in the bye-laws of the insolvency professional agency of which he is a member;

(c) to allow the insolvency professional agency to inspect his records;

(d) to submit a copy of the records of every proceeding before the Adjudicating Authority to the Board as well as to the insolvency professional agency of which he is a member; and

(e) to perform his functions in such manner and subject to such conditions as may be specified.

INSOLVENCY AND BANKRUPTCY BOARD OF INDIA (INSOLVENCY PROFESSIONALS) REGULATIONS, 2016

In exercise of the powers conferred by sections 196, 207 and 208 read with section 240 of the Insolvency and Bankruptcy Code, 2016, the Board has made the Regulations hereinafter called as the "IBBI (Insolvency Professionals) Regulations, 2016." These regulations came into force with effect from 29th November 2016.

The IBBI (Insolvency Professionals) Regulations, 2016 makes provisions for the examination and registration of Insolvency Professionals with the Insolvency and Bankruptcy Board of India. These regulations also make provisions for the disciplinary proceedings against the insolvency professional as well as prescribes the code of conduct for insolvency professionals. There are two schedules provided in the Regulation:-

(i) FIRST SCHEDULE [Regulation 7(2)(h)]: It provides for Code of Conduct for Insolvency Professionals.

(ii) SECOND SCHEDULE: It provides for the FORMS applicable w.r.t. Insolvency Professionals.

THE CODE OF CONDUCT

FIRST SCHEDULE [Under Regulation 7(2)(h)] - CODE OF CONDUCT FOR INSOLVENCY PROFESSIONALS

1. Integrity and Objectivity	2. Independence and impartiality	3. Professional competence
4. Representation of correct facts and correcting misapprehensions.	5. Timeliness.	6. Information management
7. Confidentiality	8. Occupation, employability and restrictions	9. Remuneration and costs
	10. Gifts and hospitality	

Regulation 7(2) of the IP Regulations provides that the registration of an IP is subject to the conditions that the IP shall:

A) at all times abide by the code, rules, regulations, and guidelines thereunder and the bye-laws of the IPA with which he is enrolled;

The First Schedule of the Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016 provides for the Code of Conduct for Insolvency Professionals to ensure best practices in the profession of Insolvency Professionals.

The code of conduct is explained as follows:

Integrity and Objectivity

Integrity and Objectivity are among the fundamental principles of ethics for Insolvency Professionals (IP). As per the First Schedule of the IP Regulations:

1. An Insolvency Professional (IP) must maintain integrity by being honest and straight forward in all professional relationships.

   Integrity envisages being straightforward and honest in all professional and business relationships. It implies fair dealing and truthfulness. The most important attribute of a professional for which he is accountable is integrity in character and conduct. Integrity, reputation and character are also pre-requisites for being considered as 'fit and proper' for registration as IP under regulation 4 of the IP Regulations. A profession is only as good as its members. Thus, it is necessary to ensure that a person with clean hands only can enter this profession to manage the operation of the corporate debtor and conduct the insolvency resolution process.

   Objectivity requires IP not to compromise professional or business judgements because of bias, coercion, conflict of interest or undue influence of others, whether directly or indirectly. The IP must visibly demonstrate his impartiality and lack of bias by

   - being transparent in all his interactions and decisions,
   - being collaborative and consultative with all participants of the Committee of Creditors, and
   - ensuring that all decisions are arrived at by active consensus and are not bull-dozed by a dominant participant or by the IP himself.

2. An Insolvency Professional (IP) must not misrepresent any facts or situations and should refrain from being involved in any action that would bring disrepute to the profession.

3. An Insolvency Professional (IP) must act with objectivity in its professional dealings by ensuring that his decisions are made without the presence of any bias, conflict of interest, coercion, or undue influence of any party, whether directly connected to the insolvency proceedings or not.

3A. An insolvency professional must disclose the details of any conflict of interests to the stakeholders, whenever he comes across such conflict of interest during an assignment.

   This is required to avoid a threat to compliance with objectivity or other fundamental principles of the Code of Conduct. Timely disclosure of any conflict whether identified prior to appointment or during the performance of duties under the appointment to all stakeholders is critical. This might also require consent from Committee of Creditors to continue the appointment.

4. An insolvency professional appointed as an interim resolution professional, resolution professional, liquidator, or bankruptcy trustee should not itself acquire, directly or indirectly, any of the assets of the debtor, nor knowingly permit any relative to do so.

In ***Asset Reconstruction company Ltd. vs. Shivam Water Treaters Pvt Ltd, CP(IB) 1882/MB/2018, 16.01.2019***, NCLT, Mumbai Bench vide its order dated 2nd Jan, 2019 had clarified that IRP is acting as a Court Officer and any hindrance in the work of CIRP will amount to contempt of Court. The NCLT directed the promoter/ director, officials and auditor the Corporate Debtor Company to fully co-operate the RP in the completion of CIRP.

Further, in the aforesaid matter, the NCLT ordered that Police assistance to be given to the Resolution Professional so that the RP can take full control of the company without any interference from Ex-Director's or his officials. The Police Commissioner, Ahmadabad is directed to provide police assistance to RP and his team, so that the Resolution Professional can take control of the entire unit.

In ***Sanjay Kumar Ruia Vs. Catholic Syrian Bank Ltd. & Anr, Company Appeal (AT) (Insolvency) No. 876 of 2019, 11.09.2019***, NCLAT, New Delhi remitted the matter to the Liquidator, in view of the fact that liquidation proceeding has already been started. Hon'ble NCLAT further held that if the amount based on bills and ledger have been approved by the Committee of Creditors, the Liquidator cannot reject, the same being the 'resolution cost' and not claim of any creditor.

Hon'ble NCLAT disposed off the appeal and made it clear that the fee of the Resolution Professional and the cost incurred by Resolution Professional, will be treated as 'resolution cost'. Further, allowed the Liquidator to determine the claim under Section 40 of the Code. Once the amount is shown as 'fees' and 'resolution cost' the same to be paid in terms of Section 53 of the Code.

In ***BMW India Financial Services Private Limited v. SK Wheels Private Limited, MA NO. 2319/2019 in C.P. (IB) 4301/2018, 16.10.2019*** Hon'ble NCLT held:

"15. It is trite law that this tribunal has been provided with vast powers under section 60 (5) of the Code. Therefore, based on the above this bench is of the view that the actions or rather inaction on the part of the Resolution Professional in not taking a decision with respect to the claim of the Applicant is an abuse of the powers given to him under the code and contrary to justice and public policy. His actions are nothing more but an abuse of his dominant position.

18. This kind of injustice carried out by the Resolution Professional herein is completely unacceptable. The landowner is just not entitled to receive the license fee but also, he has to right to receive the possession of the said premises. The tenancy rights automatically get terminated, the moment default in payment of rent is committed."

In ***Ruchita Modi v. Mrs. Kanchan Ostwal & Anr, Company Appeal (AT) (Ins) No.1000 of 2019, 15.11.2019***, Hon'ble NCLAT held:

"As the IRP is functioning since 18th September, 2019 on admission of Section 9 Application, we compute the fees of IRP @ Rs.1,50,000/-. The IRP would be entitled to also recover CIRP costs as may have been incurred. The Appellant – for CD undertakes to contact IRP and pay fees as above and CIRP costs as may have been incurred by the IRP in 3 weeks, after deducting amount already received by IRP under the Impugned Order. In case IRP has any difficulty regarding CIRP costs, he would be entitled to move the Adjudicating Authority and the Appellant will be bound to pay the CIRP costs concerned, as may be directed by Adjudicating Authority."

Hon'ble NCLAT vide its order dated 04.11.2019 set aside the impugned order dated 18th September, 2019 passed by NCLT, Jaipur bench for initiation of CIRP and disposed of application u/s 9 of the code as withdrawn. Further, NCLAT also directed that if there is default in payment in terms of the settlement, it will be open for the Operational Creditor to move to the Appellate Tribunal for recall of this Order and to revive the CIRP process against the CD"

Independence and Impartiality

5. An insolvency professional must maintain complete independence in its professional relationships and should conduct the insolvency resolution, liquidation or bankruptcy process, as the case may be, independent of external influences.
6. In cases where the insolvency professional is dealing with assets of a debtor during liquidation or bankruptcy process, he must ensure that he or his relatives do not knowingly acquire any such assets, whether directly or indirectly unless it is shown that there was no impairment of objectivity, independence or impartiality in the liquidation or bankruptcy process and the approval of the Board has been obtained in the matter.
7. An insolvency professional shall not take up an assignment under the Code if he, any of his relatives, any of the partners or directors of the insolvency professional entity of which he is a partner or director, or the insolvency professional entity of which he is a partner or director is not independent, in terms of the Regulations related to the processes under the Code, in relation to the corporate person/ debtor and its related parties.
8. An insolvency professional shall disclose the existence of any pecuniary or personal relationship with any of the stakeholders entitled to distribution under sections 53 or 178 of the Code, and the concerned corporate person/ debtor as soon as he becomes aware of it, by making a declaration of the same to the applicant, committee of creditors, and the person proposing appointment, as applicable.

8A. An insolvency professional shall disclose as to whether he was an employee of or has been in the panel of any financial creditor of the corporate debtor, to the committee of creditors and to the insolvency professional agency of which he is a professional member and the agency shall publish such disclosure on its website.

8B. An insolvency professional shall disclose its relationship, if any, with the corporate debtor, other professionals engaged by it, financial creditors, interim finance providers, and prospective resolution applicants to the insolvency professional agency of which he is a member, within the time specified hereunder.

Relationship of the insolvency professional with	Disclosure to be made within three days of
(1)	(2)
Corporate debtor	his appointment.
Registered valuers / accountants/ legal professionals/ other professionals appointed by him	appointment of the professionals.
Financial creditors	the constitution of committee of creditors.
Interim finance providers	the agreement with the interim finance provider.
Prospective resolution applicants	the supply of information memorandum to the prospective resolution applicant.
If relationship with any of the above, comes to notice or arises subsequently	of such notice or arising

8C. An insolvency professional shall ensure disclosure of the relationship, if any, of the other professionals engaged by it with itself, the corporate debtor, the financial creditor, the interim finance provider, if any, and the prospective resolution applicant, to the insolvency professional agency of which he is a member, within the time specified as under:

Relationship of the other professional with	Disclosure to be made within three days of
(1)	(2)
Insolvency professional	the appointment of the other professional.
Corporate debtor	the appointment of the other professional.
Financial creditors	constitution of committee of creditors.
Interim finance providers	the agreement with the interim finance provider or three days of the appointment of the other professional, whichever is later.
Prospective resolution applicants	the supply of information memorandum to the prospective resolution applicant or three days of the appointment of the other professional, whichever is later.
If relationship with any of the above, comes to notice or arises subsequently	of such notice or arising.

Explanation: For the purposes of clause 8B and 8C above, 'relationship' shall mean any one or more of the following four kinds of relationships at any time or during the three years preceding the appointment of other professionals:

Kind of relationship	Nature of relationship
(1)	(2)
A	Where the insolvency professional or the other professional, as the case may be, has derived 5% or more of his / its gross revenue in a year from professional services to the related party.
B	Where the insolvency professional or the other professional, as the case may be, is a shareholder, director, key managerial personnel or partner of the related party.
C	Where a relative (spouse, parents, parents of spouse, sibling of self and spouse, and children) of the insolvency professional or the other professional, as the case may be, has a relationship of kind A or B with the related party.
D	Where the insolvency professional or the other professional, asthe case may be, is a partner or director of a company, firm or LLP, such as, an insolvency professional entity or registered valuer, the relationship of kind A, B or C of every partner or director of such company, firm or LLP with the related party.

8D. An insolvency professional shall ensure timely and correct disclosures by it, and other professionals appointed by it and shall provide a confirmation to the insolvency professional agency of which he is a professional member to the effect that the appointment, if any, of every other professional has been made at arms' length relationship.

9. An insolvency professional shall not influence the decision or the work of the committee of creditors or debtor, or other stakeholders under the Code, so as to make any undue or unlawful gains for itself or its related parties, or cause any undue preference for any other persons for undue or unlawful gains and shall not adopt any illegal or improper means to achieve any mala fide objectives.

In the case of ***State Bank of India Vs. M/s. Metenere Ltd., C.P. No.IB-639(PB)/2018*** *a*n appeal was preferred by State Bank of India, financial creditor against the order of Hon'ble NCLT wherein it was observed that there is an apprehension of bias against the appointment of proposed Interim Resolution Professional, as he was ex-employee of financial creditor and has been drawing pension from the financial creditor. Therefore, Hon'ble NCLT directed financial creditor to substitute name of Interim Resolution Professional.

Hon'ble NCLAT held that:

"the Adjudicating Authority was perfectly justified in seeking substitution of Mr. Shailesh Verma to ensure that the 'Corporate Insolvency Resolution Process' was conducted in a fair and unbiased manner. This is notwithstanding the fact that Mr. Shailesh Verma was not disqualified or ineligible to act as an 'Interim Resolution Professional'. Viewed thus, we find no legal flaw in the impugned order which is free from any legal infirmity and has to be upheld. It goes without saying that the Appellant- 'Financial Creditor' should not have been aggrieved of the impugned order as the same did not cause any prejudice to it."

The Disciplinary Committee of IBBI vide an order dated November, 2019 found that an Insolvency Professional:

- Failed to make disclosures with respect to appointment of an LLP (in which he was a partner) as an IPE contravening the directions under the Circular issued by IBBI;
- Allowed charging fee of Rs. 12,09,90,185/- payable to lender's legal counsel as an IRPC and abdicated his authority in favour of CoC. He paid expenses of third party from CD and included in IRPC. He deliberately in connivance with some stakeholders squandered the assets (money) for unlawful purpose;
- Shared the fee, which can be paid only to an individual acting as an IP, with an LLP (in which he was a partner) against the provisions of the Code and the Regulations.

The Disciplinary Committee of IBBI observed that there was understanding between CoC and RP to contravene a law and willingness to remedy the situation only if they are caught. Thus, the RP has deliberately compromised his independence. The Disciplinary Committee Imposed penalty of ten percent of the RP's fee and Directed the RP to make good the loss by securing reimbursement and deposit the amount of Rs. 12,09,90,185/- in the account of Corporate Debtor.

Professional competence

10. An insolvency professional must maintain and upgrade his professional knowledge and skills to render competent professional service.

> Insolvency professionals play the role of regulator's 'eyes and ears' into the workings of the assignments and thus shoulder immense responsibility and are accountable not only to the immediate user of their services but also to a wider stakeholder group, including regulators and the society as a whole.

Surrender of certificate of registration.

Regulation 10A providing for surrender of certificate of registration by an Insolvency Professional as follows:

- An insolvency professional may surrender its certificate of registration by making a request to the Board, in writing along with the certificate of registration in original.
- If the Board is satisfied, it may accept the request for surrender of certificate of registration within thirty days of its receipt and upon acceptance, the registration of such insolvency professional shall stand cancelled.
- On and from the date of cancellation of certificate of registration, the concerned person shall not represent itself to be a holder of the certificate for carrying out the activity for which such certificate had been granted.

Representation of correct facts and correcting misapprehensions.

11. An insolvency professional must inform such persons under the Code as may be required, of a misapprehension or wrongful consideration of a fact of which he becomes aware, as soon as may be practicable.
12. An insolvency professional must not conceal any material information or knowingly make a misleading statement to the Board, the Adjudicating Authority or any stakeholder, as applicable.

    During the corporate insolvency resolution process (CIRP) either on the own analysis of the resolution professional (RP) or on the forensic audit report submitted by the forensic auditor, the RP may become aware of any misapprehension or wrongful consideration of any fact. In that case, as per the code of conduct, the RP is expected to duly inform the same to the concerned stakeholder. Also, while disseminating information to stakeholders like CoC, Resolution Applicant, IBBI etc. the RP shall not conceal any material information or make any misleading statements. As an Officer of the Court, the RP is expected to be unbiased and diligent.

Timeliness

13. An insolvency professional must adhere to the time limits prescribed in the Code and the rules, regulations and guidelines thereunder for insolvency resolution, liquidation or bankruptcy process, as the case may be, and must carefully plan its actions, and promptly communicate with all stakeholders involved for the timely discharge of its duties.
14. An insolvency professional must not act with mala fide or be negligent while performing its functions and duties under the Code.

    Bye-law 13 of the Model Bye-laws of an IPA, as specified by the IBBI under Schedule to Insolvency and Bankruptcy Board of India (Model Bye-Laws and Governing Board of Insolvency Professional Agencies) Regulations, 2016, states that an IP must perform duties as quickly and efficiently as reasonable, subject to the timelines under the Code

In the matter of ***M/s. Surendra Trading Company V. M/s. Juggilal Kamlapat Jute Mills Company Limited and Others, Civil Appeal No. 8400 of 2017***, the Hon'ble Supreme Court held that the timelines provided in sections 7, 9 and 10 of the Code, for deciding a matter within 14 days as well as the time to remove a defect within 7 days, are directory and not mandatory.

In the matter of ***Committee of Creditors of Essar Steel India Limited V. Satish Kumar Gupta & Ors, Civil Appeal No. 8766-67 of 2019***, the Hon'ble Supreme Court held that "ordinarily the time taken in CIRP must be completed within the time limit of 330 days from the insolvency commencement date, including the time taken in litigation process. However, in few cases where it can be shown to the Adjudicating Authority and/or Appellate Tribunal under the Code that only a short time is left in completion of corporate insolvency resolution process beyond 330 days, and it would be interest of all stakeholders that the corporate debtor be put back on its feet instead of being sent into liquidation and that the time taken in legal proceedings is largely due to factors owing to which the fault cannot be ascribed to the litigants before the Adjudicating Authority and/or Appellate Tribunal, the delay or a large part thereof being attributable to the tardy process of the Adjudicating Authority and/ or the Appellate Tribunal itself, it may be open in such cases for the Adjudicating Authority and/or Appellate Tribunal to extend time beyond 330 days."

Information management

15. An insolvency professional must make efforts to ensure that all communication to the stakeholders, whether in the form of notices, reports, updates, directions, or clarifications, is made well in advance and in a manner which is simple, clear, and easily understood by the recipients.

15A. An insolvency professional shall prominently state in all its communications to a stakeholder, its (i) name, (ii) address, (iii) e-mail, (iv) registration number and (v) validity of authorisation for assignment, if any, issued by the insolvency professional agency of which he is a member.

16. An insolvency professional must ensure that he maintains written contemporaneous records for any decision taken, the reasons for taking the decision, and the information and evidence in support of such decision. This shall be maintained so as to sufficiently enable a reasonable person to take a view on the appropriateness of its decisions and actions.

17. An insolvency professional must not make any private communication with any of the stakeholders unless required by the Code, rules, regulations and guidelines thereunder, or orders of the Adjudicating Authority.

18. An insolvency professional must appear, co-operate and be available for inspections and investigations carried out by the Board, any person authorised by the Board or the insolvency professional agency with which he is enrolled.

19. An insolvency professional must provide all information and records as may be required by the Board or the insolvency professional agency with which he is enrolled.

20. An insolvency professional must be available and provide information for any periodic study, research and audit conducted by the Board.

Confidentiality

21. An insolvency professional must ensure that confidentiality of the information relating to the insolvency resolution process, liquidation or bankruptcy process, as the case may be, is maintained at all times. However, this shall not prevent it from disclosing any information with the consent of the relevant parties or required by law.

In the matter of ***Rajputana Properties Pvt. Ltd. Vs. Ultra Tech Cement Ltd. & Ors.***, NCLAT vide its order dated 15th May 2018 held that the Resolution Professional is required to examine whether resolution plan confirm the provisions as mentioned therein but he cannot disclose it to any other person including Resolution Applicant(s), who has submitted the resolution plan. The resolution plan submitted by one or other Resolution Applicant being confidential cannot be disclosed to any competitor Resolution Applicant nor any opinion can be taken or objection can be called for from other Resolution Applicants with regard to one or other resolution plan.

In ***Re.: Vijay Kumar Jain Vs Standard Chartered Bank & Ors Civil Appeal No. 8430-2018 Order dated 31.01.2019,*** Hon'ble Supreme Court *inter alia* observed that - "It is clear that the resolution professional can take an undertaking from members of the erstwhile Board of Directors, as has been taken in the facts of the present case, to maintain confidentiality. The source of this power is Regulation 7(2)(h) of the Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulations, 2016, read with paragraph 21 of the First Schedule thereto. This can be in the form of a non-disclosure agreement in which the resolution professional can be indemnified in case information is not kept strictly confidential."

"The resolution professional does not seek information at a meeting of the committee of creditors, which is what Section 24 is all about. The resolution professional only seeks information from the erstwhile Board of Directors under Section 29 before preparing an information memorandum, which then includes the financial position of the corporate debtor and information relating to disputes by or against the corporate debtor etc."

Occupation, employability and restrictions

22. An insolvency professional must refrain from accepting too many assignments, if he is unlikely to be able to devote adequate time to each of his assignments.

    Clarification (Inserted by Notification No. IBBI/2021-22/GN/REG077, dated 22nd July, 2021 (w.e.f. 21.07.2021).: An insolvency professional may, at any point of time, not have more than ten assignments as resolution professional in corporate insolvency resolution process, of which not more than three shall have admitted claims exceeding one thousand crore rupees each.

22A. *Resignation by an Insolvency Professional:* An insolvency professional may resign from the assignment, subject to the recommendation of the committee of creditors in a corporate insolvency resolution process, consultation committee in liquidation process, the debtor or the creditor in the insolvency resolution process of personal guarantor to the corporate debtor, as the case may be, and the approval of the Adjudicating Authority. It is further explained that the insolvency professional shall continue to discharge his duties, functions and responsibilities till the approval of resignation by the Adjudicating Authority.

23. An insolvency professional must not engage in any employment when he holds a valid authorisation for assignment or when he is undertaking an assignment.

23A. Where an insolvency professional has conducted a corporate insolvency resolution process, he and his relatives shall not accept any employment, other than an employment secured through open competitive recruitment, with, or render professional services, other than services under the Code, to a creditor having more than ten percent voting power, the successful resolution applicant, the corporate debtor or any of their related parties, until a period of one year has elapsed from the date of his cessation from such process.

23B. An insolvency professional shall not engage or appoint any of his relatives or related parties, for or in connection with any work relating to any of his assignment.

    For the purposes of this clause, the insolvency professional which is an insolvency professional entity may engage or appoint its partners or directors, as the case may be, for or in connection with any work relating to any of its assignment other than work related to valuation and audit of the debtor.

23C. An insolvency professional shall not provide any service for or in connection with the assignment which is being undertaken by any of his relatives or related parties.

    Explanation.- For the purpose of clauses 23A to 23C, "related party" shall have the same meaning as assigned to it in clause (24A) of section 5, but does not include an insolvency professional entity of which the insolvency professional is a partner or director.

For the purposes of this clause, the insolvency professional which is an insolvency professional entity may provide any service, other than service related to valuation and audit, for or in connection with the assignment which is being undertaken by any of its partners or directors, as the case may be.

24. An insolvency professional must not conduct business which in the opinion of the Board is inconsistent with the reputation of the profession.

In the matter of ***IDBI Bank Ltd. v. Lanco Infratech Ltd, C.P.(IB)No. 111/7/HDB/2017,*** the Hon'ble NCLT Hyderabad Bench in its order dated 7th August, 2017 stated that "Therefore, we agreed with the submissions of the respondents considering his previous three assignments to large companies and the current corporate debtor itself is a large company we are of the prima facie view that the proposed IRP would not find sufficient time to act as IRP for the respondent company."

In the matter of ***Anil Goel v. LML Ltd., C P No. (IB) 55/ALD/2007 with CA No.73/2018***, the Hon'ble NCLT Allahabad Bench in its order dated 23rd March, 2018 stated that "......He is also appointed the Liquidator in another two matters..."

"In the case in hand, the Resolution Profession Process was to be completed within the extended period of CIRP, by dated 25.02.2018. But the Resolution Professional failed to submit the progress report/ the resolution plan within the statutory period i.e. 270 days. The Resolution Professional has filed this application on 19.03.2018, after the issuance of notice by order of this Tribunal dated 13.03.2018 for submission of progress report/ Resolution Plan against him. The RP was also directed to remain present in the Court in person on 19.03.2018. The above act of the RP shows that he was not careful in following the timeline prescribed under the Insolvency and Bankruptcy Code."

Remuneration and costs

25. An insolvency professional must provide services for remuneration which is charged in a transparent manner, is a reasonable reflection of the work necessarily and properly undertaken, and is not inconsistent with the applicable regulations.

25A. An insolvency professional shall disclose the fee payable to it, the fee payable to the insolvency professional entity, and the fee payable to professionals engaged by it to the insolvency professional agency of which he is a professional member and the agency shall publish such disclosure on its website.

25B. An insolvency professional shall raise bills or invoices in its name towards its fees, and such fees shall be paid to it through banking channel.

25C. An insolvency professional shall ensure that the insolvency professional entity or the professional engaged by it raises bills or invoices in their own name towards their fees, and such fees shall be paid to them through banking channel.

26. An insolvency professional shall not accept any fees or charges other than those which are disclosed to and approved by the persons fixing its remuneration.

26A. An insolvency professional shall not accept /share any fees or charges from any professional and/or support service provider who are appointed under the processes.

27. An insolvency professional shall disclose all costs towards the insolvency resolution process costs, liquidation costs, or costs of the bankruptcy process, as applicable, to all relevant stakeholders, and must endeavour to ensure that such costs are not unreasonable.

27A. An insolvency professional shall, while undertaking assignment or conducting processes, exercise reasonable care and diligence and take all necessary steps to ensure that the corporate person complies with the applicable laws.

27B. An insolvency professional shall not include any amount towards any loss, including penalty, if any, in the insolvency resolution process cost or liquidation cost, incurred on account of non-compliance of any provision of the laws applicable on the corporate person while conducting the insolvency resolution process, fast track insolvency resolution process, liquidation process or voluntary liquidation process, under the Code.

In ***Anurag Nirbhaya Vs. Anuj Maheshwari & Ors, Order dated 14.10.2019, NCLT***, IRP claimed Rs. 12 Lakhs for the first month and Rs. 11 Lakhs per month for the period of rest of the two and half months and he was paid Rs. 6 Lakhs for the total period of three and half months. The AA observed that the exorbitant fee has been claimed by the IRP and stated that generally they allow fee @ Rs. 1 Lakh per month to the professionals.

In ***Punjab National Bank Vs. Divyajyoti Sponge Iron Pvt. Ltd NCLT, Order dated 13.03.2018***, the AA took notice of fixation of exaggerated insolvency resolution cost, inclusive of fixation of fee of RP in a lump sum manner by the CoC without applying its mind as regards to the fate of CD, the volume, nature and complexity of CIRP. It is observed that it is time to have legitimate guidelines or regulation in this regard so as to safeguard and to ensure the prospects and revival of a dying CD not be at the highest cost which canned be affordable by the CD. It hoped that IBBI would frame necessary regulations/guidelines for fixation of fees and resolution cost by a RP.

An IP should not charge abnormally high fee in relation to the services: The Disciplinary Committee of IBBI found that an IP attempted to charge abnormally high fee in relation to the services. Besides, he acted malafide by seeking increase of his fee after approval of fee by the AA and displayed professional incompetence by using stale information for decision making. He, then IRP signed the term sheet with the applicant, who is not legally competent to appoint RP or fix his fee, and thereby attempted to deprive the CoC of its legitimate right to appoint a RP of its choice and fix his fee. The Disciplinary Committee suspended the registration of the IP for two years, directed the IP to undergo the pre-registration educational course and work for at least six months as an intern with a senior insolvency professional, at any time during the period of suspension.

Fee paid to the professionals appointed on the direction of CoC should not be included as IRPC: The Disciplinary Committee of IBBI observed that Despite the IBBI Circular dated 12.06.2018 clearly stating that Insolvency Resolution Process Cost (IRPC) shall not include any expense incurred by a member of CoC or a professional engaged by them, the RP charged the fee of lender's legal counsel from the Insolvency Resolution Process Cost. Resolution Professional, on the direction of COC, finalized the appointment of a Professional to conduct second forensic audit. The fees should have been borne by the CoC members themselves but the same was included as IRPC. The Disciplinary Committee suspended the registration of IP for six months, directed to secure reimbursement of the amount which was paid to lender's legal counsel and professional for conducting second forensic audit and charged to IRPC.

Gifts and hospitality

28. An insolvency professional, or his relative must not accept gifts or hospitality which undermines or affects his independence as an insolvency professional.

29. An insolvency professional shall not offer gifts or hospitality or a financial or any other advantage to a public servant or any other person, intending to obtain or retain work for himself, or to obtain or retain an advantage in the conduct of profession for himself.

CASE LAWS

In the case of *Pooja Menghani vs. Insolvency and Bankruptcy Board of India & Anr,* judgement dated November 20, 2023, Hon'ble High Court of Delhi inter alia observed that an Insolvency Professional performs very important functions in the insolvency resolution process of a company. An Insolvency Professional virtually takes over the company during the period it goes through the insolvency resolution process. An Insolvency Professional in fact becomes the heart and brain of the company under the insolvency resolution process and a person having slightest of disqualification cannot be permitted to be appointed as an Insolvency Professional otherwise the entire purpose of the IBC will get vitiated.

In ***Re: V Nagarajan Vs. SKS Ispat and Power Ltd.& Ors, Civil Appeal No. 3327 of 2020 order dated 22.10.2021***, Hon'ble Supreme Court inter alia observed that "The Resolution Professional is responsible for ensuring the timeliness of the process and has to file several forms, as detailed under Regulation 40B, and explain all delays that occur in the intervening period, when filing the final Form H upon submitting a successful resolution plan under Section 30 of the IBC.

In ***Re.: Sandeep Khaitan, Resolution Professional for National Plywood Industries Ltd. Vs. JSVM Plywood Industries Ltd. & Anr. Criminal Appeal No.447 of 2021 Order dated 22.04.2021***, Supreme Court *inter alia* observed that "With the appointment of Committee of Creditors, a Resolution Professional is to be appointed. The Resolution Professional is thereafter to conduct the resolution process and manage the operations. Section 23 (2) makes it clear that his power is the same as the powers of the Interim Resolution Professional. Undoubtedly, the Resolution Professional is bound to seek prior approval of the Committee of Creditors in matters covered by Section 28."

"The IRP/RP must take a decision guided purely by the object of the IBC and the provisions and the factual matrix."

"The role of the insolvency professional is neatly carved out. From the date of admission of application and the appointment of Interim Resolution Professional, the management of the affairs of the Corporate Debtor is to vest in the Interim Resolution Professional. With such appointment, the powers of the Board of Directors or the partners of the Corporate Debtor as the case may be are to stand suspended. Section 17 further declares that the powers of the Board of Directors or partners are to be exercised by the Interim Resolution Professional. The financial institutions are to act on the instructions of the Interim Resolution Professional. Section 14 is emphatic, subject to the provisions of sub section (2) and (3). The impact of the moratorium includes prohibition of transferring, encumbering, alienating or disposing of by the Corporate Debtor of any of its assets."

In ***Re.: Manish Kumar Vs. Union of India & Anr., Writ Petition (C) No.26 of 2020 with other writ petitions order dated 19.01.2021***, Hon'ble Supreme Court *inter alia* observed that "The resolution professional has to examine each resolution plan received by him on the basis of the invitation made by the resolution professional under Section 25(h) and ascertain whether the plan is in conformity with the various criteria mentioned in Section 30(2) of the Code."

"The IRP may or may not continue as the Resolution Professional (RP) but a RP is, undoubtedly, to be appointed under the scheme of the Code. The management passes into the hands of the RP. Thereafter, depending upon the receipt of the Resolution Plan and its acceptability to the Committee of Creditors and finally the approval by the Adjudicating Authority of the Resolution Plan, which is approved by the Committee of Creditors, depends the Resolution of the Insolvency."

"In short, the show is run by the Resolution Professional, subject to the control of the Committee of Creditors."

In ***Re.: Arcelor Mittal India Private Limited Vs Satish Kumar Gupta & Ors. Civil Appeal Nos. 9402-9405 -2018, Order dated 04.10.2018***, Hon'ble Supreme Court *inter alia* observed as:

"However, it must not be forgotten that a Resolution Professional is only to "examine" and "confirm" that each resolution plan conforms to what is provided by Section 30(2)."

"A conspectus of all these provisions would show that the Resolution Professional is required to examine that the resolution plan submitted by various applicants is complete in all respects, before submitting it to the Committee of Creditors."

"The Resolution Professional is not required to take any decision, but merely to ensure that the resolution plans submitted are complete in all respects before they are placed before the Committee of Creditors, who may or may not approve it. The fact that the Resolution Professional is also to confirm that a resolution plan does not contravene any of the provisions of law for the time-being in force, including Section 29A of the Code, only means that his prima facie opinion is to be given to the Committee of Creditors that a law has or has not been contravened."

"Section 30(2)(e) does not empower the Resolution Professional to "decide" whether the resolution plan does or does not contravene the provisions of law."

"Thus, the importance of the Resolution Professional is to ensure that a resolution plan is complete in all respects, and to conduct a due diligence in order to report to the Committee of Creditors whether or not it is in order."

"Even though it is not necessary for the Resolution Professional to give reasons while submitting a resolution plan to the Committee of Creditors, it would be in the fitness of things if he appends the due diligence report carried out by him with respect to each of the resolution plans under consideration, and to state briefly as to why it does or does not conform to the law."

LESSON ROUND-UP

- The significance of role of Insolvency Professional has been summed up in the BLRC Report, Volume 1-Rationale for the Code.
- Regulatory framework for Insolvency Professionals is governed by(i) the IBC,2016 (ii) the IBBI(CIRP) Regulations,2016 (iii)the IBBI (IP) Regulations,2016 (iv) the IBBI (Model Bye- Laws and Governing Board of Insolvency Professional Agencies) Regulations, 2016 (v) The IBBI (Grievance and Complaint Handling Procedure) Regulations, 2017 (vi)The IBBI (Inspection and Investigation) Regulations, 2017.
- The Resolution Professional (RP) holds a central position in conducting the CIRP and his role is vital to the efficient operation of the resolution process. The RP acts as a bridge between the debtor and the creditor and plays a significant role in aligning the interests of the CD with those of the creditors. The RP is appointed as an officer of the AA to conduct the resolution process and is vested with various statutory duties and powers. It is the RP who communicates with AA on behalf of CoC.
- An IP is a person who is enrolled with an IPA as a member and registered with the IBBI after qualifying Limited Insolvency Examination. Any eligible person having the required experience and qualifications including a chartered accountant, cost accountant, company secretary, advocate, managerial person can seek registration with an IPA and IBBI after meeting the requirements of the regime.
- The Code has provided for a two-tier regulation of IPs: - (i)The first-tier regulation of IPs is steered by the IPAs who administer the registration of IPs and promote and supervise their continuous development (ii)The second-tier regulation is steered by the IBBI which maintains a panel of IPs who have no disciplinary proceedings pending or against them and who hold Authorisation for Assignment or consented for assignments.
- An insolvency professional shall be eligible to be appointed as an interim resolution professional or a resolution professional, as the case may be, for a corporate insolvency resolution process of a corporate debtor if he, and all partners and directors of the insolvency professional entity of which he is a partner or director, are independent of the corporate debtor.
- The name of the insolvency professional proposed to be appointed as IRP is mandatory in case application to initiate CIRP is filed by financial creditor and corporate applicant while the same is optional for operational creditor. AA appoints the proposed insolvency professional as IRP only if Board confirms that there are no disciplinary proceedings pending against that insolvency professional.
- The management of CD is vested in IRP from the date of his appointment and then in RP.
- Duties and powers of the IRP and RP are well defined in the regulatory framework governing Insolvency Professional as stated above. It includes duty to constitute CoC, conduct meetings of the CoC, run CD as a going concern etc.
- The regulatory framework of IP also cast obligation on personnel of CD and creditors to extend full co-operation and give all requisite information to IRP/RP to facilitate him to conduct CIRP.
- CoC is vested with power to appoint same IRP as RP in its first meeting or to replace IRP with another RP as well as to replace RP during the tenure of CIRP.
- First Schedule of the IBBI (IP) Regulations, 2016 lays down Code of Conduct for Insolvency Professionals.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).

1. What is the eligibility criterion for an individual to become Insolvency Professional?
2. Who is liable to pay fee to IRP in case of non-cooperation by creditors as well as Operational creditor (applicant on whose application CIRP was initiated) leading to failure to constitute Committee of Creditors and thereby leading to application u/s 60 by IRP for termination of CIRP, seeking his discharge from duties as IRP and reimbursement of costs for duties performed? Decide with reference to case.
3. State the role of Disciplinary Committee constituted by IBBI under the Code?
4. State the provision of surrender of authorization for assignment by an Insolvency Professional?
5. Discuss the duties of Resolution Professional under the IBC.

REFERENCES

- IBBI Handbook on IP
- IBBI 2019 Handbook
- IBBI Newsletter Jan-March 2023
- ICSIIP Journal Feb 2023

Resolution Strategies

Lesson 17

KEY CONCEPTS

■ Corporate Restructuring ■ External Restructuring ■ Internal Restructuring ■ Debt Restructuring ■ Equity Restructuring ■ Slump sale

Learning Objectives

To understand:

- Concept of Debt Restructuring
- Concept of Equity Restructuring
- Acquisition in liquidation

Lesson Outline

- Introduction
- Debt Restructuring
- Equity Restructuring
- Acquisition in liquidation - sale of assets as a going concern
- Case laws
- Lesson Round Up
- Test Yourself
- List of Further Readings
- Other References (Including Websites / Video Links)

REGULATORY FRAMEWORK

- Section 30(2) of the Insolvency and Bankruptcy Code, 2016
- Regulation 37 & 38 of Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016
- Regulation 32 to 40 of Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016

INTRODUCTION

The legislative framework in India for insolvency and bankruptcy proceedings provides for a wide range of resolution measures, viz. re-organisation by way of a merger or amalgamation, acquisition of control and change of management, demerger, slump sale and reconstruction or financial, capital and business/ operational restructuring and as such a resolution strategy may consist of one or more of such measures and/or any measure other than the said measures. Failure to reach an understanding/resolution with the creditors under the Code could lead to liquidation of the corporate debtor.

Part II of the Insolvency and Bankruptcy Code, 2016 deals with the insolvency resolution and liquidation for corporate persons. Section 4 of the Insolvency and Bankruptcy Code, 2016 provides that Part II of the Code shall apply to matters relating to the insolvency and liquidation of corporate debtors where the minimum amount of the default is **one crore rupees**.

Part II of the Insolvency and Bankruptcy Code, 2016 lays down the following two independent stages:

(i) Corporate Insolvency Resolution Process [Sections 4 and 6 to 32]; and

(ii) Liquidation [Sections 33 to 54] and Voluntary Liquidation [Section 59]

Chapter II of Part II deals with corporate insolvency resolution process while Chapter III together with Chapter V of Part II governs the liquidation process for corporate persons.

The procedure for restructuring encompasses schemes of mergers, amalgamations, demergers, transfer/ sale of assets, restructuring of capital by way of cancellation/ delisting or any other modification in share capital, and restructuring of debts by ways of satisfaction or modification of security charge/ interest as suggested in Regulation 37 of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (CIRP Regulations) by way of which the liabilities of the distressed companies can be restructured and the state of insolvency can be resolved. In the event of initiation of a Corporate Insolvency Resolution Process against the Corporate Debtor under IBC 2016, the Resolution Professional shall invite resolution plans from the prospective resolution applicants, subject to the compliance of the conditions as laid down under Section 30(2) of the IBC, 2016 read with Regulation 38 of the CIRP regulations.

Issuance of securities of corporate debtor in exchange for claims/ interests (of the creditors) can be used as a tool for restructuring in the resolution plans which has also been duly recognized/provided for in restructurings suggested under Regulation 37 of the CIRP regulations that may be submitted by the resolution applicants to the Resolution Professional for onward consent of the Committee of Creditors and thereafter the approval of the adjudicating authority. The same is done to bring the debt to a sustainable level either by waiver of excess debt or conversion into equity, or a combination of both.

Apart from the above, the Asset Reconstruction Companies (ARCs) set-up under the provisions of SARFAESI Act, 2002 may also acquire the debts of the corporate debtor from the lending banks/ Financial Institutions (FIs) and subsequently restructure the same in post discussions and arrangement with the corporate debtor.

The provisions of SARFAESI Act, 2002 also empower the lenders/ARCs to effect a change in management as a restructuring mechanism which can be achieved by applying to become resolution applicant or partnering with resolution applicant.

The SARFAESI Act,2002 established ARCs as organizations for banks and other financial entities to sell distressed financial assets. Prior to SARFAESI Act, ARCs were not allowed to engage in any activities other than securitization or asset reconstruction without RBI approval. However, the RBI has permitted ARCs with a minimal net owned fund of INR 1000 crores to serve as resolution applicant under the provisions of the IBC, 2016, via its circular dated October 11, 2022 on "Review of Regulatory Framework for Asset Reconstruction Companies ". However, after five years from the date the Adjudicating Authority under the IBC approved the resolution plan, the ARCs shall not have any major influence or control over the corporate debtor with regard to a particular CIRP. The ARCs shall not be permitted to file any new resolution plans under IBC, either as a resolution applicant or a resolution co-applicant, in the event that this condition is not complied with.

Nonetheless, a resolution applicant shall opt for corporate restructuring in the CD (which might be mix of different methods of operational and financial restructuring) to revive it and improve its further financial performance. The Code has not specifically defined measures of restructuring for the resolution however the resolution applicant may introduce the required measures as per the situation of the corporate debtor.

CORPORATE RESTRUCTURING

Corporate restructuring is an inorganic business strategy where one or more aspects of a business are redesigned to improve commercial efficiency, manage competition effectively, drive faster pace of growth, ensure effective utilization of resources, and fulfilment of stakeholders' expectations. It serves different purposes for different companies at different points of time and may take up various forms.

Restructuring typically occurs to address challenges or it can be driven by the necessity to make financial adjustments to its assets and liabilities. Mergers, amalgamations, demergers, or reconstruction of capital structure are various forms of corporate restructuring exercises. The purpose of each of these restructuring exercises may be different but each of these exercises attempts to bring in more efficiency in the system so that the distress can be addressed.

The Insolvency and Bankruptcy Board of India ('IBBI') has made the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 to regulate the insolvency resolution Process for Corporate Persons. Corporate restructuring process in India under Insolvency and Bankruptcy Code, 2016. Regulation 37 of CIRP regulations provides that:

A resolution plan shall provide for the measures, as may be necessary, for insolvency resolution of the corporate debtor for maximization of value of its assets including but not limited to the following:

(a) transfer of all or part of the assets of the corporate debtor to one or more persons;

(b) sale of all or part of the assets whether subject to any security interest or not;

(ba) restructuring of the corporate debtor, by way of merger, amalgamation and demerger;

(c) the substantial acquisition of shares of the corporate debtor, or the merger or consolidation of the corporate debtor with one or more persons;

(ca) cancellation or delisting of any shares of the corporate debtor, if applicable;

(d) satisfaction or modification of any security interest;

(e) curing or waiving of any breach of the terms of any debt due from the corporate debtor;

(f) reduction in the amount payable to the creditors;

(g) extension of a maturity date or a change in interest rate or other terms of a debt due from the corporate debtor;

(h) amendment of the constitutional documents of the corporate debtor;

(i) issuance of securities of the corporate debtor, for cash, property, securities, or in exchange for claims or interests, or other appropriate purpose;

(j) change in portfolio of goods or services produced or rendered by the corporate debtor;

(k) change in technology used by the corporate debtor;

(l) obtaining necessary approvals from the Central and State Governments and other authorities;

(m) sale of one or more assets of corporate debtor to one or more successful resolution applicants submitting resolution plans for such assets; and manner of dealing with remaining assets.

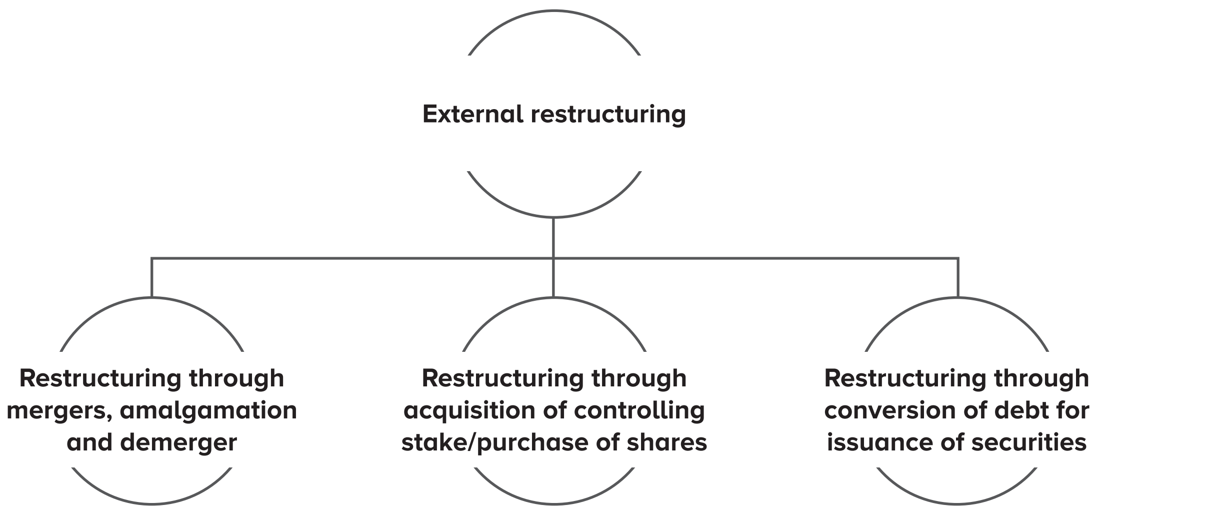
Corporate restructuring may be broadly categorized as follows:

Internal restructuring | **External restructuring**

These categories are briefly explained below.

1. External restructuring

It consist of merger and amalgamation of one company with another or demerger of one or more undertakings of a company into another company, acquisition of controlling stake in a company through purchase of majority stake in it, conversion of debt into equity, etc. The same are briefly explained hereunder.



(i) Restructuring through mergers, amalgamation and demerger

A company is merged, amalgamated or demerged to achieve improvement in efficiency in operational and financial performance of the company. In the insolvency proceedings of a corporate debtor, the resolution plan may provide for merger, forward or reverse of the corporate debtor with the resolution applicant (company) or any of its group companies to maximize the utilization of the assets of the corporate debtor. Similarly, the resolution applicant may provide to demerge one or more units of the corporate debtor to gain operational and financial efficiency.

In case of mergers/amalgamations or demergers, the consideration is in the form of equity shares in the merged/transferee entity, which are issued to the shareholders of the merging/ transferor company based on the share exchange ratio determined on the basis of valuation of equity shares of each company. The funds available in the transferee company or its cash flow for the period after the merger/ amalgamation or demerger is used for meeting capital expenditure and working capital requirements of the entity which has merged or transferred and for resolving the debt of the said entity. In addition, the entity, which has merged, gets the benefit of resources of the transferee company including its brands, goodwill, managerial inputs, technology, funds, expert manpower, etc. and the same helps it to improve its profitability. The restructuring through mergers /amalgamation and demerger may, in addition, require financial and operational restructuring, in order to make an effective resolution of the insolvency of the transferor entity.

In ***Edelweiss Asset Reconstruction Company Ltd. Vs. Synergies Dooray Automotive Ltd. & Ors.,*** NCLAT (New Delhi Bench) held that merger and amalgamation of the companies can be proposed in the Resolution Plan. IBC,2016 is a Code by itself and Section 238 of IBC,2016 provides over riding effect of it over the provisions of the other Acts. Therefore, the arguments of the Appellant that merger and amalgamation of the companies cannot be proposed in the 'Resolution Plan' is violative of clause (e) of sub-section (2) of Section 30 cannot be upheld.

(ii) Restructuring through acquisition of controlling stake/ purchase of shares

The resolution applicant may, through a resolution plan, acquire the controlling stake in the corporate debtor by either reducing or cancelling its existing paid up share capital and recapitalizing it by infusing further equity capital. Alternatively the resolution applicant may acquire the existing equity share capital of the company partly or fully by making payment of some nominal consideration to the shareholders of the Corporate debtor and for meeting the requirement of funds of the Corporate debtor, the resolution applicant may infuse the funds partly in equity or partly in the form of debt or fully in the form of debt only. The management of the corporate debtor including its board is also changed by the resolution applicant by appointing his nominee directors on the board and by appointing other key managerial personnel.

(iii) Restructuring through conversion of debt for issuance of securities

It can be understood that the insolvency of a corporate debtor is mainly due to default in its debt, whether financial debt or operational debt, where it could not fulfill its repayment obligation. The Resolution applicant on the basis of the assessment of the corporate debtor, may propose the conversion of debt of the corporate debtor into securities of the Corporate debtor issued in favor of the creditors, thereby, changing the nature and terms of the debt. The said securities may be in the form of equity share, preference share or debentures/ bonds. As a result of the said restructuring, the existing debt of the Corporate debtor is reduced to a sustainable level by conversion of the same into equity and by waiving substantial part of the unsustainable debt.

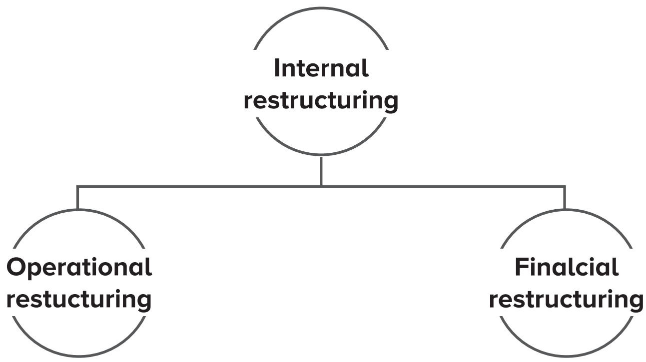
> The same kind of restructuring was used in acquisition of Bhushan Steel limited (after acquisition by Tata Group, it is named as Tata Steel BSl Limited, ("TBSL") by resolution applicant Bamnipal Steel Limited (subsidiary of Tata Steel limited). Pursuant to the Resolution Plan, Bamnipal Steel Limited subscribed to 72.65% of the equity share capital of TBSL for an aggregate amount of Rs.158.89 crore and provided additional funds aggregating to Rs.35,073.69 crore to TBSL by way of debt/ convertible debt, which were utilized to repay the dues of the Corporate debtor.

2. Internal restructuring

The same kind of restructuring was used in acquisition of Bhushan Steel limited (after acquisition by Tata Group, it is named as Tata Steel BSl Limited, ("TBSL") by resolution applicant Bamnipal Steel Limited (subsidiary of Tata Steel limited). Pursuant to the Resolution Plan, Bamnipal Steel Limited subscribed to 72.65% of the equity share capital of TBSL for an aggregate amount of Rs.158.89 crore and provided additional funds aggregating to Rs.35,073.69 crore to TBSL by way of debt/convertible debt, which were utilized to repay the dues of the Corporate debtor.

These two restructurings can be used simultaneously as required to resolve the insolvency of a corporate debtor. Following explanation can derive the need of the two restructurings in the resolution of the corporate debtor:

In the insolvency proceedings, the restructuring of corporate debtor is achieved through approval of the Resolution Plan by the adjudicating authority subsequent to the approval by its Committee of the Creditors. The resolution plan should opt for restructuring required for the corporate debtor depending upon various factors of the corporate debtor such as nature and size of business, industry, market size and situation, the financial creditors, internal policies, business relationship with the vendors and customers, applicable laws, etc. A resolution applicant is required to analyse all these factors and prepare/ formulate the resolution plan containing the appropriate restructuring strategies to take over the corporate debtor and to resolve its insolvency. As mentioned in earlier sections, the Regulation 37 of CIRP Regulations briefly lays down the external as wellas internal restructuring strategies that may be opted by the resolution applicants. The internal restructuring includes operational and financial restructuring. These are discussed in detail as follows:



(i) Operational restructuring

Operational Restructuring involves improving the operational efficiency of the corporate debtor so as to increase its business receipts and profitability. It may consist of creation of new departments to serve growing markets or downsizing or eliminating departments to conserve overheads. A company may undertake restructuring to focus on a particular market segment leveraging its core competencies or may undertake restructuring to make the organization lean and efficient. This type of restructuring affects employees and involves layoffs or collaboration with third parties to upgrade skills and technical know- how.

In the corporate insolvency resolution process of the corporate debtor, the resolution applicant is advised to present their strategy backed by a business plan where the Operational restructuring to be introduced by it (resolution applicant) to resolve the insolvency state of the corporate debtor. Regulation 37 also suggests different methods of the Operational restructuring to bring out the efficiency of the corporate debtor. Operational restructuring in the corporate debtor undergoing corporate insolvency resolution process may be made through change in portfolio of goods or services produced or rendered by it, change in technology used by it or introducing any other changes in the operational structure as may be required.

Additionally, the Regulation 38 of CIRP Regulations also advocates a detailed business plan where Regulation 38(3), provides for the following:

> *"A resolution plan shall demonstrate that –*
>
> *(a) it addresses the cause of default;*
>
> *(b) it is feasible and viable;*
>
> *(c) it has provisions for its effective implementation;*
>
> *(d) it has provisions for approvals required and the timeline for the same; and*
>
> *(e) the resolution applicant has the capability to implement the resolution plan".*

It clarifies that the Resolution Plan in itself should be complete in every aspect by detailing Corporate restructuring including operational restructuring as required, to resolve the insolvency of the corporate debtor. It is, thus, an essential element of the resolution Plan to provide for the future way forward for the working of the corporate debtor.

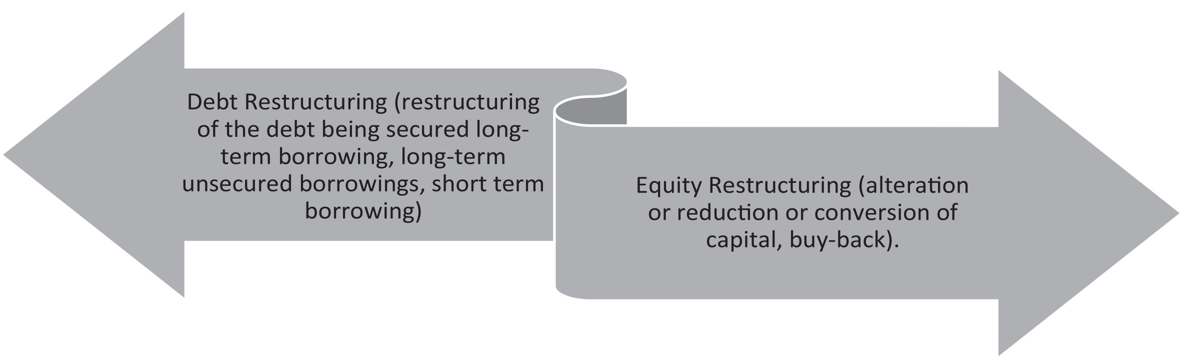
(ii) Financial restructuring

Financial restructuring is the process of reorganizing the financial structure, which primarily comprises of equity capital and debt capital. There may be several reasons (financial and non-financial) that trigger the need for financial restructuring. Financial restructuring is undertaken either because of compulsion (to recover from financial distress) or as part of company's financial strategy to achieve better financial performance.

Financial restructuring is done for various business reasons such as to overcome poor financial performance, to gain market share, or to seize emerging market opportunities. Financial restructuring undertaken to recover from financial distress involves negotiations with various stakeholders such as banks, financial institutions, creditors in order to reduce liabilities.

Corporate financial restructuring involves a considerable change in the company's financial structure and is undertaken for various business reasons such as:					
To overcome poor financial performance by reduction of debt and interest cost	To address external competition	To regain market share	To seize emerging market opportunities	To seize emerging market opportunities	Development of core competencie

The two components of financial restructuring are:



DEBT RESTRUCTURING

Debt restructuring is the process of reorganizing the whole debt capital of the company in negotiation with bankers, creditors, vendors to the terms to favor in improving the financial performance of the company. Debt capital of the company includes secured long term borrowing, unsecured long- term borrowing, and short term borrowings. Debt restructuring involves a reduction of debt and an extension of payment term or change in terms and conditions. Debt restructuring is more commonly used as a financial tool than compared to equity restructuring.

The resolution plan provides for restructuring of debt of the corporate debtor by different ways which include payment of their dues. These are briefly detailed as follows:

> Restructuring includes alteration of (a) repayment period, (b) repayable amount, (c) the amount of instalments, (d) rate of interest; rollover of credit facilities, sanction of additional credit facility, enhancement of existing credit limits, compromise settlements etc.

(a) Modification in payment period, where the resolution applicant may propose for partial upfront/ immediate payment of the claims of the financial creditors and balance in a period that is acceptable to them. Presently, the financial creditors depending upon the situation of the corporate debtor may agree for such restructuring however, it is desirable by Financial Creditors to get most of the payment upfront as their dues had not been paid/ honored by the corporate debtor for long which led to the initiation of the CIRP.

(b) Conversion of the debt in some other instrument where the resolution applicant proposes to convert the debt or part of debt in equity or some other instruments such as redeemable debentures/ preference shares or optional convertible debentures/ preference shares etc. this restructuring may provide the corporate debtor with a feasible and viable manner to honor its obligations and it may provide the financial creditors with a safer and faster way to get the payment of their dues. In case of insolvent companies, however, the lenders may not be interested in converting the entire amount of their debt into equity and that they insist for the payment of the settlement amount over a very short period of time say from three months to one year and in addition to the said payment, they may agree for accepting some percentage of restructured equity share capital of the Corporate debtor, so that in case the Corporate Debtor revives and starts making profits, they may offload their equity and compensate them for the loss /sacrifice they have made while settling with the Corporate Debtor.

(c) Waiver of part of the principal, interest or other charges where the resolution applicant proposes for waiver for outstanding principal, interest and other charges, which in his opinion is not sustainable. The resolution applicant proposes to pay the agreed settlement amount after waivers as above said over a short period of time and in addition accept some percentage of the restructured equity capital of the Corporate debtor.

(d) Modification in security of the secured financial creditors of the corporate debtor can also be used to restructure the debt to resolve its insolvency. The securities may be offered to be disposed off/released to discharge the entire or part of the claims of the financial creditors. The resolution applicant may bring in another financial partner/ investor for infusion of funds whiles the some or the total securities held by the Financial Creditors may be released in the favor of the new investor.

(e) Modification in credit limits may also be introduced through resolution plan where the fund based and non-fund based credit facilities are restructured and the credit limits are modified based on the actual requirement of the corporate debtor post resolution. Continuation of the credit limits, however, depends upon the creditworthiness of the resolution applicant.

(f) Restructuring of secured long-term borrowings – it is undertaken for reducing the cost of capital, improving liquidity and increasing the cash flow and is effected by making the modifications, conversion etc. as stated above.

(g) Restructuring of unsecured long-term borrowing – it depends on the type of borrowing which can be in form of public deposits, private loans (unsecured), unsecured bonds or debentures. Here also, objective is to reduce the interest cost, synchronization of the cash inflow and outflow by changing existing dues and /or the repayment period etc. The said restructuring also involves modification conversion etc. as stated above.

(h) Restructuring of short-term borrowings – these borrowings are restructured by converting some part of them as long term, reducing interest rate and /or existing dues and also by renegotiating the existing terms.

Until recently, there had been several debt restructuring mechanisms such as framework for revitalizing distressed assets, Corporate debt restructuring Scheme (CDR), the Joint lenders' Forum (JLF), Flexible Structuring of existing long term Project loans, Strategic debt restructuring Scheme (SDR), Change in Ownership outside SDR, and Scheme for Sustainable Structuring of Stressed Assets (S4A). These schemes, based on various circulars and guidelines issued by the Reserve Bank of India (RBI), were used as a tool for restructuring the debt of a Corporate Debtor.

In order to harmonise and simplify the framework for the resolution of stressed assets, the Reserve Bank of India (RBI), vide a circular dated 07.06.2019 has withdrawn these schemes. The Joint Lenders' Forum (JLF), an institutional mechanism for resolution of stressed accounts, also stands discontinued. Therefore, before initiating insolvency proceedings against the corporate debtor, the banks/ financial institutions are required to recourse the formal restructuring as per the guidelines issued in the circular by RBI on 07.06.2019. The framework as provided by the RBI through circular issued on 07.06.2019; provides the procedure for debt restructuring of the company to resolve the distress situation.

EQUITY RESTRUCTURING

Equity restructuring involves reorganization of equity capital. Under the provisions of the Code, the equity restructuring can be brought out by various ways, which is generally part of the greater corporate restructuring process, operational or financial or both. The same includes the following:

- Alteration of share capital
- Reduction of share capital
- Buy-back of shares

Alteration of share capital Legal Provisions:

- Section 61 to 64 read with Section 13 and 14 of the Companies Act, 2013
- Companies (Share Capital and Debentures) Rules, 2014.
- National Company Law Tribunal Rules, 2016.

Reduction of share capital Legal Provisions:

- Section 66 of the Companies Act, 2013
- Rule 2 to 6 of the National Company Law Tribunal (Procedure for Reduction of Share Capital of Company) Rules, 2016
- SEBI (LODR) Regulations, 2015.

Buy-Back Legal Provisions:

- Section 68 to 70 of the Companies Act, 2013
- Rule 17 of Companies (Share Capital and Debentures) Rules, 2014.
- Securities and Exchange Board of India (Buyback of Securities) Regulations, 2018.

The strategies for restructuring can be used jointly or independently depending upon the operational and financial assessment by the resolution applicant and negotiation with the CoC. The restructuring strategies of mergers/ amalgamations/ demergers, etc. are mostly used for the purposes of corporate restructuring and have rarely been employed as a tool for debt restructuring. It may also be noted that the schemes of mergers, amalgamations and demergers may be approved by CoC and thereafter by Adjudicating Authority (NCLT).

CASE LAW

The acquisition of Bhushan Steel Ltd (BSL) for Rs. 35,200 crore by Bamnipal Steel Ltd (BNL), a subsidiary of Tata Steel Ltd. in May 2018, has been the first major case of acquisition of a major stressed asset under the insolvency and Bankruptcy Code. BNL completed the acquisition of controlling stake of 72.65 per cent in BSL in accordance with the approved resolution plan under the Corporate insolvency resolution Process (CIRP) of the IBC. Tata Steel has paid Rs.35,200 crore in cash to acquire Bhushan Steel. It would pay another Rs.1,200 crore over next 12 months to operational creditors.

ACQUISITION UNDER THE CODE: EXEMPTION FROM SEBI TAKEOVER CODE

- The provision is envisaged to boost acquisitions of such companies.
- The acquisition of Bhushan Steel Ltd. by Tata Steel Ltd., acquisition of Electrosteel Steels Ltd. by Vedanta resources ltd., acquisition of Monnet Iispat & energy ltd. by JSW Steel ltd. under IiBC were exempted from the open offer requirements.
- The acquirers of distressed companies are not under the obligation to make an open offer. The relaxation is granted with an intention to ease the additional burden on the acquirer from infusing an additional capital pursuant to acquiring the stake in the company. Moreover, in majority of the distressed companies under CIRP or where process is over, the dues of even the secured creditors have not been paid in full and as a result the liquidation value in respect of equity shareholders is Nil.

The promoters of BSL approached the National Company Law Appellate Tribunal (NCLAT) over issue of ineligibility of Tata Steel to acquire BSL. L&T, an operational creditor also approached the Hon'ble NCLAT over issue of unfair distribution of settlement amount for its claim under the provisions of IBC, 2016.

NCLAT upheld the acquisition of Bhushan Steel, rejecting allegations of its ineligibility by the promoters of the company. The NCLAT also rejected the claims of L&T, an operational creditor of Bhushan Steel Ltd, opposing Tata Steel's resolution plan seeking a higher priority in debt settlement.

The NCLAT said that Tata Steel UK, a foreign subsidiary of Tata Steel, which was fined by an English Court in February 2018 under UK Act, had a provision of 'imprisonment for a term not exceeding twelve months, or a fine, or both'. While, the provision in section 29A(d) of the Code, which deals with eligibility, stipulates "has been convicted for any offence punishable with imprisonment for two years or more", cannot be equated with Section 33(1)(a) of the U.K Act, said NCLAT. Section 29A of the IBC mandates that a person convicted for any offence punishable with imprisonment for two years or more is ineligible for submitting a resolution plan.

Over the claims of L&T, which had supplied goods and machineries over Rs.900 crore, NCLAT said that Tata Steel's resolution plan was fair towards operational creditors of Bhushan Steel which has a total demand of Rs.1,422 crore. The NCLAT observed that the company has allotted Rs.1,200 crore for them and L&T plea for a higher priority could not be accepted.

Moreover, it also declined the plea of the promoters family, contending Tata Steel's Resolution Plan' was illegal as it purports to transfer shares' of the 'preference shareholders' of Bhushan Steel without their consent for a fixed consideration of Rs.100 as against Rs.2,269 crore.

RESOLUTION MEASURES UNDER THE INSOLVENCY AND BANKRUPTCY CODE, 2016

As stated earlier, the Insolvency and Bankruptcy Code, 2016 read with Regulation 37 of CIRP Regulations provides for various measures to resolve the insolvency of the corporate debtor. These measures are detailed as follows:

- ***Transfer of all or part of the assets of the corporate debtor to one or more persons***

  The resolution applicant may acquire part of the assets and may opt to transfer some assets to one or more persons in order to fetch a better value towards the resolution of the corporate debtor. The consideration towards the said assets is utilized to repay the dues of corporate debtor to its creditors.

- ***Sale of all or part of the assets whether subject to any security interest or not***

  The resolution applicant, as its resolution strategy, may provide for sale of the assets of the Corporate Debtor in full or in part whether subject to any security interest or not. For example, if the Corporate Debtor holds assets which may be subject to the security interest and which may bring benefit to the Corporate Debtor on their sale (through sale of all or part of assets), the resolution applicant may provide for sale of such assets and provide for settlement of debt of the Corporate Debtor or infusion for improvement of operations of the Corporate Debtor or for activity of any other similar nature through the funds as realized from sale of such assets.

- ***Restructuring of the corporate debtor, by way of merger, amalgamation and demerger***

  As discussed earlier, the Resolution Plan may also provide for merger/amalgamation/demerger or combination of such arrangements in order to resolve the Corporate Debtor, as best suited to it.

- ***The substantial acquisition of shares of the corporate debtor, or the merger or consolidation of the corporate debtor with one or more persons***

  The resolution applicant may provide for the substantial acquisition of the shares of the Corporate Debtor or the merger or consolidation with one or more persons as may be beneficial to the corporate debtor to fetch the maximized value of its assets and resolve the state of insolvency. The prohibition set out under the proviso to Regulation 3(2) of the takeover regulations, which restricts an acquirer from acquiring shares or voting rights in a target company, resulting in aggregate shareholding of the acquirer, along with persons acting in concert, exceeding the maximum permissible non-public shareholding of 75%, will not be applicable to an acquirer acquiring shares pursuant to a resolution plan approved under Section 31 of the Code.

  > The following sub-regulation (2a) was added to regulation 10 of Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 vide Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) (Second Amendment) regulations, 2020 on 22nd June, 2020 which states the following:
  >
  > *"(2a) any acquisition of shares or voting rights or control of the target company by way of preferential issue in compliance with regulation 164a of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 shall be exempt from the obligation to make an open offer under sub-regulation (1) of regulation 3 and regulation 4."*

- ***Cancellation or delisting of any shares of the corporate debtor, if applicable***

  Equity restructuring by cancellation or reduction or delisting of shares of the corporate debtor may be quite useful in resolution of the corporate debtor as the same may save the RA from time consuming transfer procedures and other problems. Moreover, the delisting procedure under the SEBI (Delisting of Equity Shares) Regulations 2009 will no longer apply to any delisting of equity shares pursuant to a resolution plan approved under Section 31 of the Code, if the resolution plan satisfies the following conditions:

- **the plan sets out a specific delisting procedure; or**

- **the plan provides an exit option to existing public shareholders at a price specified in the plan which shall not be less than the liquidation value determined under regulation 35 of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, and;**

- **further, if the promoters are provided with the opportunity of exiting under the plan at a price, then the delisting should be at a price not less than the price at which the promoters are provided exit.**

- ***Satisfaction or modification of any security interest***

  The resolution applicant may also satisfy or modify any of the security interest(s) as held by the Financial Creditor(s) as part of the debt restructuring.

- ***Curing or waiving of any breach of the terms of any debt due from the corporate debtor:***

  The Corporate Debtor may suffer from breach(es) of terms of the debt owed by it to the creditors which may play a vital role in the process of its acquisition by the resolution applicant. Thus, the resolution applicant in order to acquire the Corporate Debtor free from past breaches, non-compliances which may create problems in the future, as per its due diligence, may provide for cure of such breach(es) or may provide for waiver of such breach(es).

- ***Reduction in the amount payable to the creditors***

  The resolution applicant as part of the debt restructuring may provide for settlement of the debt of the creditors at a price lower than their dues/ claims since the payment of the entire dues/claims of the creditors may not be feasible and viable for the resolution applicant in order to acquire the Corporate Debtor and resolve its insolvency.

- ***Extension of a maturity date or a change in interest rate or other terms of a debt due from the corporate debtor***

  The debt restructuring, as designed/ formulated by the resolution applicant for the Corporate Debtor (as a part of the Resolution Plan), may provide for the extension of maturity date or change in the interest rate or other terms of the debt due from the Corporate Debtor.

- ***Amendment of the constitutional documents of the corporate debtor***

  Resolution applicant, as part of the corporate restructuring may require the amendments in terms of the constitutional documents of the corporate debtor, Memorandum of Association and Articles of the Association which inter-alia other things, define the powers and duties of the members and Board of directors of the Company. The amendments of the constitutional documents of the corporate debtor can aid the resolution applicant in process of acquisition of the Corporate debtor and implementation of the Resolution Plan effectively.

- ***Issuance of securities of the corporate debtor, for cash, property, securities, or in exchange for claims or interests, or other appropriate purpose***

  The Resolution Plan by the resolution applicant may provide for the issuance of the securities including shares or debentures of the Corporate debtor in lieu of cash, property, securities or in exchange for the claims/ interests or other appropriate purpose. The resolution applicant may provide for issuance of securities of the Corporate debtor to itself for the funds it might bring in, for the property it might bring in and may provide for issuance of the securities to creditors in conversion of their debt/ claims in full or in part as consideration to them or for any other appropriate purpose as may be beneficial or helpful in resolution of the Corporate debtor.

- ***Change in portfolio of goods or services produced or rendered by the corporate debtor***

  For operational/ organizational restructuring, the resolution applicant may provide for change in portfolio of goods or services produced or rendered by the corporate debtor which may or may not be part of its current portfolio.

- ***Change in technology used by the corporate debtor***

  The resolution applicant may provide for the change in technology or process used by the corporate debtor for the resolution of insolvency of the Corporate debtor as there may be case that the Corporate Debtor may be suffering from obsolete technologies or process.

- ***Obtaining necessary approvals from the Central and State Governments and other authorities***

  The resolution applicant, if required, would provide for obtaining the necessary approvals (on basis of current processes/ goods/ services of the corporate debtor or on the basis of the future operational processes/goods/ services of the Corporate debtor as required under the resolution Plan) from the Central and State Government and other authorities.

- ***Sale of one or more assets of corporate debtor to one or more successful resolution applicants submitting resolution plans for such assets; and manner of dealing with remaining assets***

  It has been noted that some Corporate Debtors have assets in both functional and non-functional locations across the country. The Resolution Applicant who are interested in the functional asset or the asset in one location/business are not interested in the others in such circumstances. It is also observed that the Resolution Applicant is unwilling to implement a resolution plan because the extra investment demand for the non-functional asset or the assets in other locations/businesses becomes too high. CIRP Regulations also allow CoC to explore resolutions of part assets/ businesses by allowing submission of different resolution plans for these part assets/ businesses.

ACQUISITION OF CORPORATE DEBTOR UNDER LIQUIDATION THROUGH SALE OF ASSETS AS A GOING CONCERN

Regulation 32A of IBBI (Liquidation Process) Regulations, 2016

In common usage, a "going concern" sale occurs on a "as is, where is" basis and covers all of the company's assets, liabilities, properties, and business. According to the IBBI (Liquidation) Regulations, 2016 the liquidator may consider selling the CD or its company as a going concern based on recommendations from the CoC or Stakeholder Consultation Committee. According to Section 53 of the Code, the Liquidator will use the sale profits to pay off the CD's debts. It is outlined in Regulation 32A of the IBBI (Liquidation) Regulations, 2016, how and when CD will be sold as a going concern during the bankruptcy process.

Regulation 32A states as follows:

1. Where the committee of creditors has recommended sale under clause (e) or (f) of regulation 32 or where the liquidator is of the opinion that sale under clause (e) or (f) of regulation 32 shall

maximise the value of the corporate debtor, he shall endeavour to first sell under the said clauses.

2. For the purpose of sale under sub-regulation (1), the group of assets and liabilities of the corporate debtor, as identified by the committee of creditors under sub-regulation (2) of regulation 39C of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 shall be sold as a going concern.

3. Where the committee of creditors has not identified the assets and liabilities under sub-regulation (2) of Regulation 39C of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, the liquidator shall identify and group the assets and liabilities to be sold as a going concern, in consultation with the consultation committee.

4. If the liquidator is unable to sell the corporate debtor or its business under clause (e) or (f) of regulation 32 within ninety days from the liquidation commencement date, he shall proceed to sell the assets of the corporate debtor under clauses (a) to (d) of regulation 32.

Chapter VI (comprising regulations 32 to 40) of the **IBBI (Liquidation Process) Regulations, 2016** makes the following provisions for the realization of assets. The IBBI had inserted Regulation 32A in the **IBBI (Liquidation Process) Regulations, 2016** to provide for methods for sale of assets as a going concern as a resolution measure for the CD.

Can Liquidator sell the corporate debtor as going concern even after 90 day period prescribed under the Code?

As per Regulation 32A(4), if the liquidator is unable to sell the corporate debtor or its business under clause (e) or (f) of regulation 32 within ninety days from the liquidation commencement date, he shall proceed to sell the assets of the corporate debtor under clauses (a) to (d) of regulation 32.

Regulation 32 of liquidation regulations provides as below: The liquidator may sell:

a) an asset on a standalone basis;

b) the assets in a slump sale;

c) a set of assets collectively;

d) the assets in parcels;

e) the corporate debtor as a going concern; or

f) the business(s) of the corporate debtor as a going concern

Provided that where an asset is subject to security interest, it shall not be sold under any of the clauses (a) to (f) unless the security interest therein has been relinquished to the liquidation estate.

In ***Dr. Devaiah Pagidipati v. Southern Online Bio Technologies Limited,*** NCLT Hyderabad held that sale of assets of Corporate Debtor undergoing liquidation as a going concern does not require NCLT approval under IBC. However, given the lacuna in the IBC framework on measures that can be adopted in case of such sale, NCLT order may be needed to effectuate the sale of CD as a going concern and for claiming certain reliefs and concessions. Without granting additional reliefs that are essential and required to operate the company as an ongoing concern, the simple purchase of the unit as a going concern is useless. To put it another way, buying the business/assets of business as a going business without giving the applicant the reliefs defeats the purpose of doing so.

In ***M/s. Visisth Services Limited, v. S. V. Ramani,& Ors.,*** NCLAT held that Regulation 32 A of the IBBI (Liquidation Process) Regulations, 2016 provides that Sale as a 'Going Concern' means sale of assets as well as liabilities and not assets sans liabilities. It means sale of both assets and liabilities, if it is stated on 'as is where is basis.

In ***Bank of Baroda v. Topworth Pipes & Tubes Pvt. Ltd,*** NCLT held that successful bidder may not be held liable for any past liabilities of the Corporate Debtor prior to the effective date including liabilities arising in enquiries, investigations, assessments, claims, litigations, arbitrations or other judicial, regulatory, administrative proceedings in relation to or in connection with the Corporate Debtor during sale of corporate debtor as going concern during liquidation.

What is the mode of sale provided to Liquidator?

As per Regulation 33 of the IBBI (Liquidation Process) Regulations, 2016, the liquidator shall ordinarily sell the assets of the corporate debtor through an auction in the manner specified in Schedule I. The liquidator may sell the assets of the corporate debtor by means of private sale in the manner specified in Schedule I when-

(a) the asset is perishable;

(b) the asset is likely to deteriorate in value significantly if not sold immediately;

(c) the asset is sold at a price higher than the reserve price of a failed auction; or

(d) the prior permission of the Adjudicating Authority has been obtained for such sale:

Provided that the liquidator shall not sell the assets, without prior permission of the Adjudicating Authority, by way of private sale to-

(a) a related party of the corporate debtor;

(b) his related party; or

(c) any professional appointed by him.

The liquidator shall not proceed with the sale of an asset if he has reason to believe that there is any collusion between the buyers, or the corporate debtor's related parties and buyers, or the creditors and the buyer, and shall submit a report to the Adjudicating Authority in this regard, seeking appropriate orders against the colluding parties.

In ***Alchemist Asset Reconstruction Co. Ltd. Vs. Moser Baer India Ltd. [CA-769(PB)/2019 in C.P. No. IB-378(PB)/2017] NCLT, New Delhi order dt. 16.07.2019***

It was stated that the proper interpretation on clauses (a) and(b) of the regulation 33 of Liquidation Process Regulations would be that a liquidator is entitled to sell the assets without requirement of prior permission after reaching the conclusion that the assets are perishable and it is likely to deteriorate significantly in value if not sold immediately. Otherwise, the purpose of Regulation would be defeated if time is required to be spent in filing an application and taking permission, because the assets which are perishable may not remain available for sale and perish or it may deteriorate significantly in value, if not sold immediately.

In ***MRG Estates LLP Vs. Akash Shinghal, Liquidator, Amira Pure Foods Pvt. Ltd. &Ors. [W.P.(C) 10023/2020] HC, New Delhi order dt. 15.12.2020***

The HC directed IBBI to consider the petition as a representation on the issue of adoption of Swiss Challenge method as a form of an auction under the Liquidation Process Regulations.

CONTENTS OF ASSET REPORT

As per Regulation 36 of the IBBI (Liquidation Process) Regulations, 2016, On sale of an asset, the liquidator shall prepare an asset sale report in respect of said asset, to be enclosed with the Progress Reports, containing –

- the realized value;
- cost of realization, if any;
- the manner and mode of sale;
- if the value realized is less than the value in the asset memorandum, the reasons for the same;
- the person to whom the sale is made; and
- any other details of the sale.

When shall the liquidator distribute the proceeds from realization to the stakeholders?

As per Regulation 42 of the IBBI (Liquidation Process) Regulations, 2016, the liquidator shall not commence distribution before the list of stakeholders and the asset memorandum has been filed with the Adjudicating Authority. The liquidator shall distribute the proceeds from realization within ninety days from the receipt of the amount to the stakeholders. Further the insolvency resolution process costs, if any, and the liquidation costs shall be deducted before such distribution is made.

CASE LAWS

In the matter of ***Y. Shivram Prasad & Ors. v. S. Dhanapal & Ors***, the NCLAT passed the impugned order of liquidation as Committee of Creditors did not find any resolution plan viable and feasible. The promoters submitted that they should have been given an opportunity to settle the dues. While rejecting the said submission, the NCLAT clarified that settlement can be made only at three stages, i.e., before admission, before constitution of CoC and in terms of section 12A of the Code and such stages were over in this instant matter. It, however, observed that during the liquidation process, it is necessary to take steps for revival and continuance of the Corporate debtor by protecting it from its management and from a death by liquidation.

Wherein this appellate tribunal having noticed the decision of the Hon'ble Supreme Court in ***"Swiss Ribbon Pvt. Ltd. & Anr. v. Union of India & Ors. (Supra) and "Meghal Homes Pvt. Ltd."*** observed and referring to the matter of "Swiss Ribbon Pvt. Ltd. & Anr. v. Union of India & Ors. (Supra) where Hon'ble Supreme Court observed that "What is interesting to note is that the Preamble does not, in any manner, refer to liquidation, which is only availed of as a last resort if there is either no resolution plan or the resolution plans submitted are not up to the mark. Even in liquidation, the liquidator can sell the business of the corporate debtor as a going concern" and NCLAT in its matter further held that "in view of the provision of Section 230 and the decision of the Hon'ble Supreme Court in 'Meghal Homes Pvt. ltd.' and 'Swiss Ribbons Pvt. Ltd.', we direct the 'liquidator' to proceed in accordance with law. He will verify claims of all the creditors; take into custody and control of all the assets, property, effects and actionable claims of the 'corporate debtor', carry on the business of the 'corporate debtor' for its beneficial liquidation, etc. as prescribed under Section 35 of the Code. If the members or the 'Corporate debtor' or the 'creditors' or a class of creditors like 'Financial Creditor' or 'Operational Creditor' approach the company through the liquidator for compromise or arrangement by making proposal of payment to all the creditor(s), the liquidator on behalf of the company will move an application under Section 230 of the Companies Act, 2013 before the adjudicating authority i.e. National Company Law Tribunal, Chennai Bench, in terms of the observations as made in above. On failure, as observed above, steps should be taken for outright sale of the 'Corporate debtor' so as to enable the employees to continue".

In the matter of ***Edelweiss Asset Reconstruction Company Ltd. v. Bharati Defence and Infrastructure Ltd.***, the Resolution Professional (RP) filed an application seeking approval of the resolution plan submitted by an resolution applicant, who is a Financial Creditor with 82.7% voting share in the CoC. The plan provided that the resolution applicant will sell the Corporate debtor in two years. NCLT, Mumbai Bench noted that the plan does not give due consideration to the interest of all stakeholders, seeks several exemptions, and contains a lot of uncertainties and speculations. It provides for generation of income from ongoing operations and no upfront money is brought in by the resolution applicant. The NCLT Bench also noted that the resolution applicant has proposed to hold majority equity in the Corporate debtor, run its operations, enhance its value and over a period endeavour to find a suitable investor/buyer for the same.

Relying on the judgment in the matter of Binani Industries Limited, the NCLT Bench observed: *".....resolution plan is for insolvency resolution of the Corporate Debtor as a going concern and not for the addition of value and intended to sale the corporate debtor"*. It observed that resolution applicant is essentially extending the CIRP period to find an investor, which is not the intention of the legislature. It further observed: *"if the ultimate object in the resolution plan is to sell the company, then it can be achieved by sale as a going concern during the liquidation process". Accordingly, it rejected the resolution plan and ordered for liquidation.*

LESSON ROUND-UP

- Corporate restructuring may be broadly categorized as external restructuring and internal restructuring. External restructuring consists of mergers, amalgamation, acquisition of controlling stake, conversion of debt into equity and internal restructuring consists of operational and financial restructuring.
- The two components of financial restructuring are debt restructuring (restructuring of the secured long-term borrowing, long-term unsecured borrowings, short-term borrowing) and equity restructuring (alteration or reduction of capital, buy-back).
- Debt restructuring is the process of reorganizing the whole debt capital of the company in negotiation with bankers, creditors, vendors. Debt restructuring involves a reduction of debt and an extension of payment terms or change in terms and conditions.

- Regulation 37 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 provides that a resolution plan shall provide for the measures, as may be necessary, for insolvency resolution of the corporate debtor for maximization of value of its assets.
- Equity restructuring involves reorganization of equity capital, which includes alteration of share capital, reduction of share capital and buy-back of shares.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions is not to be submitted for evaluation)

1. Discuss the resolution strategies available for insolvency resolution of the corporate debtor under the Insolvency and Bankruptcy Code, 2016.
2. Mention the advantages and disadvantages of debt restructuring and equity restructuring.
3. Mention the measures that a resolution plan shall provide for insolvency resolution of the corporate debtor for maximization of value of its assets under Regulation 37 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.

LIST OF FURTHER READINGS

- Insolvency and Bankruptcy Code, 2016 and rules made thereunder.
- Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016
- Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016

OTHER REFERENCES (Including Websites / Video Links)

- https://ibbi.gov.in/en
- https://ibbi.gov.in/en/publication/study-materials
- https://www.mca.gov.in/content/mca/global/en/home.html
- https://ibbi.gov.in/uploads/publication/6adaf64e3d3221399cfcda795de38a23.pdf

Convening and Conduct of Meetings of Committee of Creditors

Lesson 18

KEY CONCEPTS

■ Claim ■ Financial Creditor ■ Related Party ■ Financial Sector Regulator ■ Voting Share ■ Committee of Creditors ■ Types of Committees of Creditors ■ Authorised Representaive

Learning Objectives

To understand:

- Committee of Creditors
- Meetings of Committee of Creditors
- Representation of the Financial Creditors
- Video conferencing or other audio and visual means
- Voting and Approval by the Committee
- Commercial Wisdom of Committee of Creditors

Lesson Outline

- Introduction
- Meeting of Committee of Creditors
- Right of Committee of Creditors to replace Resolution Professional
- Approval of Resolution Plan by Committee of Creditors
- Application to extend time period of Corporate Insolvency Resolution Process
- Commercial wisdom of committee of creditors
- Role and Responsibilities of Authorised Representative of financial creditor
- Case Law
- Lesson Round-Up
- Test Yourself
- References

REGULATORY FRAMEWORK

- The Insolvency and Bankruptcy Code,2016
- The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016

INTRODUCTION

The Banking Law Reforms Committee (BLRC) has laid special emphasis upon the "rights of creditors" under the Code. In its 2015 Report, the BLRC has stated the following;

> *"... When default takes place, control is supposed to transfer to the creditors; equity owners have no say."*

The BLRC thus recognized the positional weakness of creditors under the prevalent bankruptcy regime, and thus developed a "creditor-in-control" model under the Code. According to this model, the management of the corporate debtor's affairs shall vest absolutely in the hands of the creditors in the event of financial distress. Likewise, the Hon'ble Supreme Court, *in Innoventive Industries v. Union of India*, upheld the intention of the BLRC and observed that;

> *"... the most significant change being, that when a company defaults on its debt, control of the company should shift to creditors rather than the management who was retaining control after the default."*

The committee of creditors is the most important business decision-making body in every corporate insolvency resolution process. It exercises its commercial wisdom and plays a fundamental role in the turnaround and restructuring of the corporate debtor within the timelines set down by the IBC. Most importantly, the Committee of Creditors is vested with the responsibility to assess the viability of the Corporate Debtor and determine the manner in which its distress is to be resolved.

The Committee of Creditors is uniquely positioned to support and facilitate the discharge of duties by the Resolution Professional. Members of the Committee of Creditors support and help the Resolution Professional in maximizing the value of the assets of the Corporate Debtor by discharging their own duties with alacrity.

In ***Municipal Corporation of Greater Mumbai (MCGM) Vs. Abhilash Lal and Others [(2019) SCC Online SC 1479]***, the Supreme Court observed that-

The Interim Resolution Professional selected by the NCLT has to constitute a Committee of Creditors comprising all the financial creditors of the corporate debtor. This provision is aimed at creditors adopting a collective approach toward insolvency resolution instead of proceeding individually. Key decisions of the process and the resolution plan are approved by the Committee of Creditors if it is satisfied that the provisions of the most acceptable plan would ensure that their dues are cleared.

The creditor-in-control approach of the corporate insolvency resolution process (CIRP) while strengthening the creditors' rights puts the financial creditors (FCs) in a unique position visà-vis other stakeholder. The FCs are decision makers, the decisions, however, are ought to be made representing interest of all other stakeholders and are not on the basis of their own qualified interests. The Code hence places them in a position of 'trust' and hence the power vested in the CoC has to be exercised with caution, reason and fairness. The CoC is a creation of statute (Numetal Ltd. v. Satish Kumar Gupta & Anr.) Its powers and duties are provided in the Code making it a statutory institution and it discharges a public function. It is designed (and expected to act) as a responsible, empowered and accountable institution and shall not be guided by anti-common interests.

The significance of creditor is apparent from the fact that the corporate insolvency resolution process under the Code can be initiated by a creditor (financial or operational). Section 18(c) of the Code states that it is mandatory for Interim Resolution Professional to constitute Committee of Creditors i.e. the Interim Resolution Professional shall........... (c) constitute a committee of creditors; It is further provided in sub-section (d) that Interim Resolution Professional shall monitor the assets of the corporate debtor and manage its operations until a resolution professional is appointed by the committee of creditors.

All decisions during CIRP from appointment of Resolution professional to actions required to run the corporate debtor as a going concern and achieve objective of maximization of value as envisaged in Preamble of Code are vested in the Committee of Creditors from the first day of its meeting. Section 12A of the Code provides for withdrawal of application admitted under section 7, 9 or 10 subject to approval of Committee of Creditors by 90% voting. It provides that the Adjudicating Authority may allow the withdrawal of application admitted under section 7 or section 9 or section 10, on an application made by the applicant with the approval of ninety per cent voting share of the committee of creditors, in such manner as may be specified.

The committee of creditors is composed of financial creditors of the corporate debtor as the financial creditors have the capability to assess the commercial viability of the corporate debtor and are willing to modify the terms of the debt contracts in negotiations between the creditors and the corporate debtor.

Operational creditors, on the other hand, are not equipped to decide on matters relating to commercial viability of the corporate debtor, nor are they generally willing to take the risk of restructuring their debts in order to ensure the management of operations of corporate debtor a going concern.

Hon'ble Supreme Court has in the matter of ***Swiss Ribbon Pvt. Ltd. & Anr. Vs. Union of India & Ors. (date of judgment 25.01.2019)*** held that the classification under IBC between financial creditors and operational creditors is based on an intelligible criteria and is neither discriminatory nor arbitratory nor violative of Article 14 of Constitution of India;

The Code clearly details the duties of CoC without ambiguity. Given the complex and dynamic nature of businesses, the role of CoC is a difficult one. However, the Code has empowered the CoC with the services of a capable and trained Resolution Professional (RP) to conduct the process under its guidance. The role of the CoC in helping keep the corporate debtor as a going concern and in assessing viability of the business is crucial to the entire insolvency process in search of liquidation remote solutions. The CoC is at a vantage position to decide on meeting the needs of the company to remain as a going concern including raising interim finance. The CoC also decides on what and how expenses are to be made and approve the process cost. It also decides the professional fees for the services of the Insolvency Professional (IP) it chooses to conduct the process. In addition, the CoC makes the decision to retain or replace the Insolvency Professional. Assessing viability of the business is done by the CoC at two levels; one an ex-post analysis of financial position of the debtor's business when the insolvency proceeding is initiated, to understand the reasons for insolvency; and two an ex-ante evaluation of the feasibility and viability of a resolution plan in addressing the cause of insolvency and putting the CD back in business in a sustainable manner. Such assessment forms the basis for the identification of criteria that prospective resolution applicants (RAs) have to meet and construction of the evaluation matrix on which resolution plans are evaluated. The CoC carries out its functions through its meetings and these meetings are a sacred ritual. Recognising the need for sanctity of these meetings, the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (CIRP Regulations) provides, in detail, the manner in which these have to be conducted.

Important Definitions

Creditor means any person to whom a debt is owed and includes

- a financial creditor,
- an operational creditor,
- a secured creditor,
- an unsecured creditor; and
- a decree-holder {section 3 (10)}

Section 3 (30) "secured creditor" means a creditor in favour of whom security interest is created;

Section 5(7) "financial creditor" means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to;

Section 5 (20) "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;

Section 3(11) of the Code defines "debt" which means a liability or obligation in respect of a claim which is due from any person and includes a financial debt and operational debt;

"Operational Debt" means a claim in respect of the provision of goods or services including employment or a debt in respect of the payment 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; { Section 5(21)}

"Financial debt" means a debt alongwith interest, if any, which is disbursed against the consideration for the time value of money. {Section 5 (8)}

Section 5 (8) "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 dematerialised 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 non-recourse basis;

(f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing;

(i) any amount raised from an allottee under a real estate project shall be deemed to be an amount 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;

Home Buyers to be considered as ......Financial Creditors

The Supreme Court in the case of ***Pioneer Urban Land & Infrastructure Ltd. & Anr. vs. Union of India & Ors.,*** *upheld the* constitutional validity of the introduction of home buyers as "financial creditors" to the IBC, made by the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018, enabling home buyers to trigger IBC against the real estate developer.

Claim

Section 21 of the Code states that the Interim Resolution Professional shall constitute a committee of creditors after collation of all claims received against the corporate debtor and determination of the financial position of the corporate debtor. Section 18 of the Code enumerates mandatory duties of the Interim Resolution Professional which include that the Interim Resolution Professional shall receive and collate all the claims submitted by creditors to him, pursuant to the public announcement made under sections 13 and 15; and constitute a committee of creditors; So, claim is the first step to be determined to constitute committee of creditors.

Claim is defined in section 3(6) of the Code as

(a) a right to payment, whether or not such right is reduced to judgment, fixed, disputed, undisputed, legal, equitable, secured, or unsecured;

(b) right to remedy for breach of contract under any law for the time being in force, if such breach gives rise to a right to payment, whether or not such right is reduced to judgment, fixed, matured, unmatured, disputed, undisputed, secured or unsecure.

The IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 provides procedure for holding first meeting of Committee of Creditors as follows:

An insolvency professional shall make a public announcement immediately on his appointment as an interim resolution professional (IRP) i.e. within three days of his appointment. {Regulation 6(1)}

The public announcement shall state where claim forms can be downloaded or obtained from, as the case may be, provide the last date for submission of proofs of claim, which shall be fourteen days from the date of appointment of the interim resolution professional. {Regulation 6(2)}

The interim resolution professional or the resolution professional, as the case may be, shall verify every claim, as on the insolvency commencement date, within seven days from the last date of the receipt of the claims, and thereupon maintain a list of creditors containing names of creditors along with the amount claimed by them, the amount of their claims admitted and the security interest, if any, in respect of such claims, and update it. {(Regulation 13(1))}

The interim resolution professional shall file a report certifying constitution of the committee to the Adjudicating Authority within two days of the verification of claims received under subregulation (1) of regulation 12.. {Regulation 17(1)}

The interim resolution professional shall hold the first meeting of the committee within seven days of filing the report under this regulation. {Regulation 17(2)}

Committee of Creditors

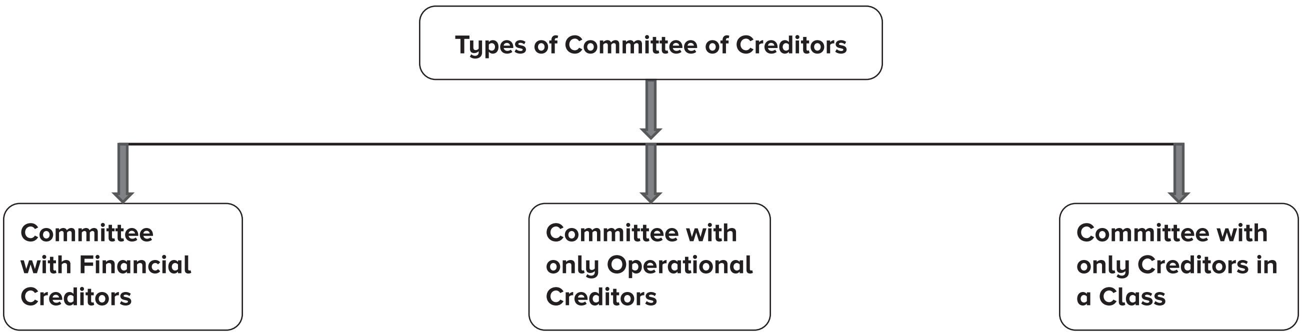
Regulation 2 (1) (d) of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 defines "committee" which means a committee of creditors established under section 21;

Who shall constitute Committee of Creditors (CoC)

(i) The Interim Resolution Professional shall constitute a committee of creditors after collation of all claims received against the corporate debtor and determination of the financial position of the corporate debtor. (Section 21(1)).

(ii) Regulation 13 of the IBBI (Corporate Insolvency Resolution Process) Regulations states that the Interim Resolution Professional or the Resolution Professional, as the case may be, shall verify every claim, as on the insolvency commencement date, within seven days from the last date of the receipt of the claims, and thereupon maintain a list of creditors containing names of creditors along with the amount claimed by them, the amount of their claims admitted and the security interest, if any, in respect of such claims, and update it. The list of creditors shall be presented at the first meeting of Committee of Creditors.

Composition of Committee of Creditors



- The committee of creditors shall comprise all financial creditors of the corporate debtor. (Section 21(2))
- Both secured and unsecured financial creditors are members of Committee of Creditors.

Composition of Committee of Creditors where there is no financial creditor.

- It is provided that where a corporate debtor does not have any financial creditors, the committee of creditors shall be constituted and shall comprise of such persons to exercise such functions in such manner as may be specified. (Section 21(8)).
- **Committee with only operational creditors (Regulation 16 of the IBBI (Corporate Insolvency Resolution Process) Regulations, 2016):** Regulation 16 provides that where the corporate debtor has no financial debt or where all financial creditors are related parties of the corporate debtor, the committee shall consist of members as under –

  (a) eighteen largest operational creditors by value:
  Provided that if the number of operational creditors is less than eighteen, the committee shall include all such operational creditors,

  (b) one representative elected by all workmen other than those workmen included under subclause (a); and

(c) one representative elected by all employee other than those employee included under subclause (a).

Status of Financial Creditor, if related party to the Corporate Debtor: First proviso to section 21(2) provides that a financial creditor or the authorised representative of the financial creditor, if it is a related party of the corporate debtor, shall not have any **right of representation, participation or voting** in a meeting of the committee of creditors.

- **Committee with only creditors in a class** (**Regulation 16B of the the IBBI (Corporate Insolvency Resolution Process) Regulations,2016):** Where the corporate debtor has only creditors in a class and no other financial creditor eligible to join the committee, the committee shall consist of only the authorised representative(s).

According to section 5(24), a **"related party",** in relation to a corporate debtor, means-

(a) a director or partner of the corporate debtor or a relative of a director or partner of the corporate debtor;

(b) key managerial personnel of the corporate debtor or a relative of key managerial personnel of the corporate debtor;

(c) a limited liability partnership or a partnership firm in which a director, partner, or manager of the corporate debtor or his relative is a partner;

(d) a private company in which a director, partner or manager of the corporate debtor is a director and holds alongwith his relatives, more than two per cent of its share capital;

(e) a public company in which a director, partner or manager of the corporate debtor is a director and holds alongwith relatives, more than two per cent of its paid-up share capital;

(f) anybody corporate whose board of directors, managing director or manager, in the ordinary course of business, acts on the advice, directions or instructions of a director, partner or manager of the corporate debtor;

(g) any limited liability partnership or a partnership firm whose partners or employees in the ordinary course of business, acts on the advice, directions or instructions of a director, partner or manager of the corporate debtor;

(h) any person on whose advice, directions or instructions, a director, partner or manager of the corporate debtor is accustomed to act;

(i) a body corporate which is a holding, subsidiary or an associate company of the corporate debtor, or a subsidiary of a holding company to which the corporate debtor is a subsidiary;

(j) any person who controls more than twenty per cent. of voting rights in the corporate debtor on account of ownership or a voting agreement;

(k) any person in whom the corporate debtor controls more than twenty per cent. of voting rights on account of ownership or a voting agreement;

(l) any person who can control the composition of the board of directors or corresponding governing body of the corporate debtor;

(m) any person who is associated with the corporate debtor on account of-

  (i) participation in policy making processes of the corporate debtor; or

  (ii) having more than two directors in common between the corporate debtor and such person; or

  (iii) interchange of managerial personnel between the corporate debtor and such person; or

  (iv) provision of essential technical information to, or from, the corporate debtor.

In the matter of *'Phoenix Arc Private Limited Vs. Spade Financial Services Limited & Ors.',* the Supreme Court elucidates the two way relationship in related parties that *"The definition describes a commutative relationship, meaning that X can be a related party of Y, if either X is related to Y, or Y is related to X. The definition of 'related party' under the IBC is significantly broad. The intention of the legislature in adopting such a broad definition was to capture all kinds of inter-relationships between the financial creditor and the corporate debtor."*

The Insolvency and Bankruptcy Code (Second Amendment) Act, 2018 also added second proviso to section 21(2) which clarified that the first proviso shall not apply to a financial creditor, regulated by a financial sector regulator, if it is a related party of the corporate debtor solely on account of conversion or substitution of debt into **equity shares** or instruments convertible into equity shares, or completion of such transactions as may be prescribed, **prior to the insolvency commencement date**. The Insolvency and Bankruptcy Code (Amendment) Ordinance, 2019 added the words "or completion of such transactions as may be prescribed" in the said section, thus, widening the condition in which a financial creditor would not be considered to be a related party.

According to section 3(18) of the Code, a **"financial sector regulator"** means an authority or body constituted under any law for the time being in force to regulate services or transactions of financial sector and includes the Reserve Bank of India, the Securities and Exchange Board of India, the Insurance Regulatory and Development Authority of India, the Pension Fund Regulatory Authority and such other regulatory authorities as may be notified by the Central Government.

Whether the relatedness of the related party could merely have existed in the past or whether they must continue in *praesenti* i.e. at the present time?

The Supreme Court in the matter of ***'Phoenix Arc Private Limited Vs. Spade Financial Services Limited & Ors.',*** clarified that while the default rule under the first proviso to Section 21(2) is that only those financial creditors that are related parties in *praesenti* would be debarred from the Committee, those related party financial creditors that cease to be related parties in order to circumvent the exclusion under the first proviso to Section 21(2), should also be considered as being coveredby the exclusion thereunder. Thus, relatedness of related parties at the present time would be considered for exclusion from the Committee, in addition, any parties that were related in the past and cease to be related parties at present in order to become a member of the Comimittee must also be considered for exclusion from the Committee.

Representation of the Financial Creditor

1. **Consortium:** Section 21(6) of the Code provides

Where the terms of the financial debt extended as part of a consortium arrangement or syndicated facility provide for a single trustee or agent to act for all financial creditors, each financial creditor may-	(a) authorise the trustee or agent to act on his behalf in the committee of creditors to the extent of his voting share;
	(b) represent himself in the committee of creditors to the extent of his voting share;
	(c) appoint an insolvency professional (other than the resolution professional) at his own cost to represent himself in the committee of creditors to the extent of his voting share; or
	(d) exercise his right to vote to the extent of his voting share with one or more financial creditors jointly or severally.

2. **Class of Creditors (Section 21(6A):** To address the challenges of representing certain types of FCs. The section envisages three types of representatives for FCs:

Where a financial debt	*Authorised Representative to act on behalf of financial creditors:*
(a) is in the form of securities or deposits and the terms of the financial debt provide for appointment of a trustee or agent to act as authorised representative for all the financial creditors,	such trustee or agent shall act on behalf of such financial creditors;
(b) If a financial debt is owed to a class of creditors exceeding a specified number (other than that described above, or covered under section 21(6)), the Interim Resolution Professional shall make an application to the Adjudicating Authority along with the list of all financial creditors, containing the name of an insolvency professional, other than the Interim Resolution Professional, to act as their authorised representative	Such Authorised representative shall be appointed by the Adjudicating Authority prior to the first meeting of the committee of creditors;
(c) is represented by a guardian, executor or administrator,	such person shall act as authorised representative on behalf of such financial creditors.

Such AR shall attend the meetings of the Committee of Creditors and vote on behalf of each financial creditor to the extent of his voting share. The remuneration payable to the authorised representative-

(i) under clauses (a) and (c) of sub-section (6A), if any, shall be as per the terms of the financial debt or the relevant documentation; and

(ii) under clause (b) of sub-section (6A) shall be as specified which shall be form part of the insolvency resolution process costs. (Section 21(6B)).

3. *Appointment of Authorised Representative by individual creditor* {Section 24(5)}: Subject to sub-sections (6), (6A) and (6B) of section 21, any creditor who is a member of the committee of creditors may appoint an insolvency professional other than the resolution professional to represent such creditor in a meeting of the committee of creditors along with responsibility of paying fee to such insolvency professional.

Role and Responsibilities of Authorised Representatives (AR)

ARs are the agents/trustees of the creditors/class of creditors they represent and must act in accordance with their instructions. The role, responsibilities, and rights of the AR (under section 21(6), section 21(6A), or section 24(5)) are set out in section 25A of the IBC, which was inserted by way of the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018.

(i) *Section 25A provides that authorized representative shall have*

- the right to participate and vote in meetings of the Committee of Creditors on behalf of the financial creditors he represents in accordance with the prior voting instructions of such financial creditors obtained through physical or electronic means;
- the duty to circulate the agenda and minutes of the Committee of Creditors meeting to the financial creditors he represents;
- the duty to not act against the interests of the financial creditors he represents and always act in accordance with their prior instructions;
- the duty to file with the Committee of Creditors any voting instructions received by way of physical or electronic means from the financial creditors he represents;

- the duty to ensure that the appropriate voting instructions of the financial creditors he represents are correctly recorded by the Interim Resolution Professional or Resolution Professional.

(ii) *Regulation 16A of the IBBI (Corporate Insolvency Resolution Process) Regulations,2016):* Regulation 16A provides for selection, duties and rights of Authorised Representative as follows:

(1) *Selection of Authorised Representative:* The Interim Resolution Professional shall select the insolvency professional, who is the choice of the highest number of financial creditors in the class in Form CA received with proof, on or before the last date mentioned in the public announcement, to act as the authorised representative of the creditors of the respective class. But this does not apply to the choice for an insolvency professional to act as authorised representative in Form CA received after time provided in public announcement.

(2) *Application to AA for appointment of Authorised Representative:* The Interim Resolution Professional shall apply to the Adjudicating Authority for appointment of the authorised representatives selected under sub-regulation (1) within two days of the verification of claims received under sub-regulation (1) of regulation 12.

(3) *Delay in appointment of authorised representative:* Any delay in appointment of the authorised representative for any class of creditors shall not affect the validity of any decision taken by the committee.

(3A) *Replacement of AR (Regulation (3A):* The financial creditors in the class, representing not less than ten per cent. voting share may seek replacement of the authorised representative with an insolvency professional of their choice by making a request to the interim resolution professional or resolution professional who shall circulate such request to the creditors in that class and announce a voting window open for at least twenty-four hours.

(4) *Information and means of communication to be provided to Authorised Representative:*

- The Interim Resolution Professional shall provide the list of creditors in each class to the respective authorised representative appointed by the Adjudicating Authority.
- The Interim Resolution Professional or the resolution professional, as the case may be, shall provide an updated list of creditors in each class to the respective authorised representative as and when the list is updated.

  Clarification: The authorised representative shall have no role in receipt or verification of claims of creditors of the class he represents.
- The Interim Resolution Professional or the resolution professional, as the case may be, shall provide electronic means of communication between the authorised representative and the creditors in the class.

(5) *Voting share of a creditor in a class:*

The voting share of a creditor in a class shall be in proportion to the financial debt which includes an **interest at the rate of eight per cent per annum** unless a different rate has been agreed to between the parties.

(6) *Fee payable to Authorised Representative:*

- The authorised representative of creditors in a class shall be entitled to receive fee for every meeting of the committee attended by him in the following manner, namely: -

Number of creditors in the class	Fee per meeting of the committee (Rs.)
10-100	30,000
101-1000	40,000
More than 1000	50,000

The authorised representative shall be entitled to receive fee for every meeting of the class of creditors convened by him in the following manner, namely: -

Number of creditors in the class	Fee per meeting of creditors in class with authorised representative (Rs.)
10-100	10,000
101-1000	12,000
More than 1000	15,000

Fee of AR to be part of IRP cost: The payment of fee to authorised representative shall be part of insolvency resolution process cost in respect of two meeting with the creditors he represents corresponding to a meeting of the committee of creditors.

Approval of fee of AR: The fee for any additional meeting beyond two meetings corresponding to a meeting of the committee of creditors shall be part of insolvency resolution process cost subject to approval of committee of creditors.

(7) *Duty of Authorised Representative:*

- The authorised representative shall circulate the agenda to creditors in a class, and may seek their preliminary views on any item in the agenda to enable him to effectively participate in the meeting of the committee.
- The creditors shall have a time window of at least twelve hours to submit their preliminary views, and the said window opens at least twenty-four hours after the authorised representative seeks preliminary views.
- Such preliminary views shall not be considered as voting instructions by the creditors.

(8) The duties of Authorised Representative shall : -

(a) assist the creditors in a class he represents in understanding the discussions and considerations of the committee meetings and facilitate informed decision-making;

(b) review the contents of minutes prepared by the resolution professional and provide his comments to the resolution professional, if any;

(c) help the creditors in a class he represents during the consultations made by the resolution professional to prepare a strategy for marketing of the assets of the corporate debtor in terms of sub-regulation (1) of regulation 36C

(d) work in collaboration with the creditors in a class he represents to enhance the marketability of the assets of the corporate debtor in terms of sub-regulation (3) of regulation 36C;

(e) assist the creditors in a class he represents in evaluating the resolution plans submitted by resolution applicants;

(f) ensure that the creditors in a class he represents have access to any information or documents required to form an opinion on issues discussed in the committee meetings;

(g) update regularly the creditors in a class he represents on the progress of the corporate insolvency resolution process;

(h) make suggestions for modifications of the resolution plan as may be required by the creditors in class he represents;

(i) record proceedings and prepare the minutes of the meeting with the creditors in a class he represents; (The provisions regarding minutes of meetings in this regulation shall apply mutatis mutandis to class meetings) and

(j) act as a representative for the creditors in a class he represents in representations before the Adjudicating Authority, National Company Law Appellate Tribunal, and other regulatory authorities.

The creditors in a class may propose any additional responsibility upon the authorised representative in relation to the representation of their interest in the committee.

Meeting of Committee of Creditors

Section 24 of the Code along with the IBBI ((Insolvency Resolution Process for Corporate Persons) Regulations, 2016 lays down legal provisions w.r.t. conduct of the meeting of the Committee of Creditors as follows:

First Meeting of Committee of Creditors: The first meeting of the committee of creditors shall be held within seven days of the constitution of the committee of creditors by Interim Resolution Professional.

Place of meeting of Committee of Creditors: The members of the committee of creditors may meet in person or by such electronic means as may be specified. (Section 24 (1))

Who shall conduct meeting of the Committee of Creditors:

- All meetings of the committee of creditors shall be conducted by the resolution professional. (Section 24 (2)).
- Regulation 18 provides for meetings of the committee (Corporate Insolvency Resolution Process Regulations,2016):

  1. A resolution professional shall convene a meeting of the committee before lapse of thirty days from the last meeting. It is provided that the committee may decide to extend the interval between such meetings subject to the condition that there shall be at least one meeting in each quarter.
  2. A resolution professional may convene a meeting of the committee as and when he considers necessary.
  3. A resolution professional may convene a meeting, if he considers it necessary, on a request received from members of the committee and shall convene a meeting if the same is made by members of the committee representing at least thirty three per cent of the voting rights.

     It is further explained that for the purposes of sub- regulation (2) it is clarified that meeting (s) may be convened under this sub-regulation till the resolution plan is approved under sub-section (1) of section 31 or order for liquidation is passed under section 33 and decide on matters which do not affect the resolution plan submitted before the Adjudicating Authority.
  4. A resolution professional may place a proposal received from members of the committee in a meeting, if he considers it necessary and shall place the proposal if the same is made by members of the committee representing at least thirty three per cent of the voting rights.

Notice of meeting of Committee of Creditors

(i) To whom notice is to be served:

- Section 24(3) provides that the resolution professional shall give notice of each meeting of the committee of creditors to-

  (a) members of committee of creditors, including the authorised representatives referred to in sub-sections (6) and (6A) of section 21 and sub-section (5);

  (b) members of the suspended Board of Directors or the partners of the corporate persons, as the case may be;

  (c) operational creditors or their representatives if the amount of their aggregate dues is not less than ten per cent of the debt.

- Section 24(4) provides that while the directors, partners, and one representative of the OC, as referred to in subsection (3), may attend the meetings of the committee of creditors, they shall not have any right to vote in such meetings. In addition, their absence shall not invalidate the proceedings of the meetings.

CASE LAWS

In ***Vijay Kumar Jain Vs. Standard Chartered Bank & Others [(2019) SCC Online SC 103],*** the Supreme Court held that resolution plans need to be provided to members of the suspended board of directors of the corporate debtor, as they have a right to participate in the meetings of the committee of creditors. It was observed that a combined reading of the IBC and the Corporate Insolvency Resolution Process Regulations leads to the conclusion that members of the suspended board of directors, being vitally interested in resolution plans that may be discussed at meetings of the committee of creditors, must be given a copy of such plans as part of the documents that have to be furnished along with the notice of such meetings.

In ***Consolidated Engineering Company & Another Vs. Golden Jubilee Hotels Pvt. Ltd. [Company Appeal (AT) (Insolvency) No. 501 of 2018],*** the NCLAT held that the AA has rightly held that 10 percent of total debt for the purpose of representation in the committee of creditors is to be calculated on the basis of the claim as collated and noticed by the RP. It cannot be based on the amount claimed by all the operational creditors until it is verified and compared. If the claim of operational creditors on verification is found to be less than 10 percent, the operational creditors have no right to claim representation in the meeting of the committee of creditors.

(ii) Notice period:

Regulation 19 of the Corporate Insolvency Resolution Process Regulations provide for notice period of meeting of committee of creditors as follows:

- *Minimum 5 days' notice period*: Subject to this Regulation, a meeting of the committee shall be called by giving not less than five days' notice in writing to every participant, at the address it has provided to the Interim Resolution Professional or the resolution professional, as the case may be, and such notice may be sent by hand delivery, or by post but in any event, be served on every participant by electronic means in accordance with Regulation 20.
- *Notice period of 24 hrs/48 hrs:* The committee may reduce the notice period from five days to such other period of not less than twenty-four hours, as it deems fit. It is provided that the committee may reduce the period to such other period of not less than forty-eight hours if there is any authorised representative.

"Participant" means a person entitled to attend a meeting of the committee under section 24 or any other person authorised by the committee to attend the meeting; (Regulation 2(1) (l) of Corporate Insolvency Resolution Process Regulations)

(iii) Service of notice by electronic means

Regulation 20 of the Corporate Insolvency Resolution Process Regulations states: -

- A notice by electronic means may be sent to the participants through e-mail as a text or as an attachment to e-mail or as a notification providing electronic link or Uniform Resource Locator for accessing such notice.
- The subject line in e-mail shall state the name of the corporate debtor, the place, if any, the time and the date on which the meeting is scheduled.
- If notice is sent in the form of a non-editable attachment to an e-mail, such attachment shall be in the Portable Document Format or in a non-editable format together with a 'link or instructions' for recipient for downloading relevant version of the software.

- When notice or notifications of availability of notice are sent by an e-mail, the resolution professional shall ensure that it uses a system which produces confirmation of the total number of recipients e-mailed and a record of each recipient to whom the notice has been sent and copy of such record and any notices of any failed transmissions and subsequent re-sending shall be retained as "proof of sending".
- The obligation of the resolution professional shall be satisfied when he transmits the e-mail and he shall not be held responsible for a failure in transmission beyond its control.
- The notice made available on the electronic link or Uniform Resource Locator shall be readable, and the recipient should be able to obtain and retain copies and the resolution professional shall give the complete Uniform Resource Locator or address of the website and full details of how to access the document or information.
- If a participant, other than a member of the committee, fails to provide or update the relevant e-mail address to the resolution professional, the non-receipt of such notice by such participant of any meeting shall not invalidate the decisions taken at such meeting.

(iv) Contents of the notice for meeting.

Regulation 21 of Corporate Insolvency Resolution Process Regulations provides for the content of notice of meeting of Committee of Creditors as follows:

(1) The notice shall inform the participants of the venue, the time and date of the meeting and of the option available to them to participate through video conferencing or other audio and visual means, and shall also provide all the necessary information to enable participation through video conferencing or other audio and visual means.

(2) The notice of the meeting shall provide that a participant may attend and vote in the meeting either in person or through an authorised representative. It is provided that such participant shall inform the resolution professional, in advance of the meeting, of the identity of the authorised representative who will attend and vote at the meeting on its behalf.

"Video conferencing or other audio and visual means" means such audio and visual facility which enables the participants in a meeting to communicate concurrently with one another and to participate effectively in the meeting. (Regulation 2(1) (p) of Corporate Insolvency Resolution Process Regulations)

(3) The notice of the meeting shall contain the following	(i) a list of the matters to be discussed at the meeting;
	(ii) a list of the issues to be voted upon at the meeting; and
	(iii) copies of all documents relevant to the matters to be discussed and the issues to be voted upon at the meeting.
(4) The notice of the meeting shall-	a) state the process and manner for voting by electronic means and the time schedule, including the time period during which the votes may be cast:
	b) provide the login ID and the details of a facility for generating password and for keeping security and casting of vote in a secure manner; and
	c) provide contact details of the person who will address the queries connected with the electronic voting.

Quorum at the Meeting

Regulation 22 of the Corporate Insolvency Resolution Process Regulations states that

- *Quorum for the meeting:* A meeting of the committee shall be quorate if members of the committee representing at least thirty three percent of the voting rights are present either in person or by video conferencing or other audio and visual means. It is also provided that the committee may modify the percentage of voting rights required for quorum in respect of any future meetings of the committee.

- *Meeting adjourned for want of quorum:* Where a meeting of the committee could not be held for want of quorum, unless the committee has previously decided otherwise, the meeting shall automatically stand adjourned at the same time and place on the next day.
- *Quorum at the adjourned meeting:* In the event a meeting of the committee is adjourned for want of quorum, the adjourned meeting shall quorate with the members of the committee attending the meeting.

Participation through Video Conferencing

Regulation 23 of Corporate Insolvency Resolution Process Regulations provides for participation of the members of Committee of Creditors through video conferencing by laying down essentials of contents of notice and duties of RP in this regard as follows:

(i) *Notice to provide option to attend meeting through video conferencing:* The notice convening the meetings of the committee shall provide the participants an option to attend the meeting through video conferencing or other audio and visual means in accordance with this Regulation.

(ii) *Duties of the Resolution Professional:*

- The resolution professional shall make necessary arrangements to ensure uninterrupted and clear video or audio and visual connection.
- The resolution professional shall take due and reasonable care:

  (a) to safeguard the integrity of the meeting by ensuring sufficient security and identification procedures;

  (b) to ensure availability of proper video conferencing or other audio and visual equipment or facilities for providing transmission of the communications for effective participation of the participants at the meeting;

  (c) to record proceedings and prepare the minutes of the meeting;

  (d) to store for safekeeping and marking the physical recording(s) or other electronic recording mechanism as part of the records of the corporate debtor;

  (e) to ensure that no person other than the intended participants attends or has access to the proceedings of the meeting through video conferencing or other audio and visual means; and

  (f) to ensure that participants attending the meeting through audio and visual means are able to hear and see, if applicable, the other participants clearly during the course of the meeting. It is provided that the persons, who are differently abled, may make request to the resolution professional to allow a person to accompany him at the meeting.

(iii) *Deemed Venue of the meeting:* Where a meeting is conducted through video conferencing or other audio and visual means, the scheduled venue of the meeting as set forth in the notice convening the meeting, which shall be in India, shall be deemed to be the place of the said meeting and all recordings of the proceedings at the meeting shall be deemed to be made at such place.

Conduct of the Meetings

Regulation 24 of the Corporate Insolvency Resolution Process Regulations states that

- *Chairman of the meeting: T*he resolution professional shall act as the chairman of the committee of creditors' meeting.
- *Attendance at the commencement of the meeting:*

<table>
<tr><td rowspan="6">At the commencement of a meeting, the resolution professional shall take a roll call when every participant attending through video conferencing or other audio and visual means shall state, for the record, the following,-</td><td>(a)</td><td>his name;</td></tr>
<tr><td>(b)</td><td>whether he is attending in the capacity of a member of the committee or any other participant;</td></tr>
<tr><td>(c)</td><td>whether he is representing a member or group of members;</td></tr>
<tr><td>(d)</td><td>the location from where he is participating;</td></tr>
<tr><td>(e)</td><td>that he has received the agenda and all the relevant material for the meeting; and</td></tr>
<tr><td>(f)</td><td>that no one other than him is attending or has access to the proceedings of the meeting at the location of that person.</td></tr>
</table>

- *Confirmation of quorum:* After the roll call, the resolution professional shall inform the participants of the names of all persons who are present for the meeting and confirm if the required quorum is complete.

- *Quorum throughout the meeting:* The resolution professional shall ensure that the required quorum is present throughout the meeting.

- *Restricted access to the meeting:* From the commencement of the meeting till its conclusion, no person other than the participants and any other person whose presence is required by the resolution professional shall be allowed access to the place where meeting is held or to the video conferencing or other audio and visual facility, without the permission of the resolution professional.

Voting by the Committee

The Committee of Creditors as a collective body takes decisions by members voting on a particular item/matter. Each member of the Committee of Creditors has a voting share in the Committee of Creditors. Voting by the Committee is governed by the following provisions:

(i) *Voting right of creditor in Committee of Creditors:* Each creditor shall vote in accordance with the voting share assigned to him based on the financial debts owed to such creditor. [Section 24 (6)]

> Section 5 (28) "voting share" means the share of the voting rights of a single financial creditor in the committee of creditors which is based on the proportion of the financial debt owed to such financial creditor in relation to the financial debt owed by the corporate debtor.

(ii) *Who shall determine voting right:* The resolution professional shall determine the voting share to be assigned to each creditor in the manner specified by the Board. [Section 24 (7)].

Voting share in case of joint/consortium Loan: Subject to sub-sections (6) and (6A), where the corporate debtor owes financial debts to two or more financial creditors as part of a consortium or agreement, each such financial creditor shall be part of the committee of creditors and their voting share shall be determined on the basis of the financial debts owed to them. [Section 21(3)]

Same person is operational as well as financial creditor: Where any person is a financial creditor as well as an operational creditor, - (a) such person shall be a financial creditor to the extent of the financial debt owed by the corporate debtor, and shall be included in the committee of creditors, with voting share proportionate to the extent of financial debts owed to such creditor; (b) such person shall be considered to be an operational creditor to the extent of the operational debt owed by the corporate debtor to such creditor. [Section 21(4)]

Assignment of operational debt to financial creditor: Where an operational creditor has assigned or legally transferred any operational debt to a financial creditor, the assignee or transferee shall be considered as an operational creditor to the extent of such assignment or legal transfer. [Section 21(5)]

Right to attend meeting of committee of creditors but not vote: Following persons have only right to attend meeting of committee of creditors but not vote:

(a) Section 24 (4)	The directors, partners and one representative of operational creditors, as referred to in sub-section (3), may attend the meetings of committee of creditors, but shall not have any right to vote in such meetings.	It is also provided that the absence of any such director, partner or representative of operational creditors, as the case may be, shall not invalidate proceedings of such meeting.
(b) First proviso of Section 21(2)	a financial creditor or the authorised representative of the financial creditor referred to in sub-section (6) or sub-section (6A) or sub-section (5) of section 24, if it is a related party of the corporate debtor, shall not have any right of representation, participation or voting in a meeting of the committee of creditors:	It is further provided that the first proviso shall not apply to a financial creditor, regulated by a financial sector regulator, if it is a related party of the corporate debtor solely on account of conversion or substitution of debt into equity shares or instruments convertible into equity shares or completion of such transactions as may be prescribed, prior to the insolvency commencement date.

Voting by Authorised Representative

As far as voting by an authorised representative is concerned, section 25A(3) provides that if the authorised representative represents several financial creditors, he shall cast his vote on behalf of each financial creditor in accordance with instructions received from each financial creditor, to the extent of his voting share. If any financial creditor does not give prior instructions through physical or electronic means, the authorised representative shall abstain from voting on behalf of these creditors.

However, the voting provision of creditors in a class is different from voting by other financial creditors. By the Insolvency and Bankruptcy Code (Amendment) Act, 2019, sub-clause 3A was inserted in section 25A to overcome a peculiar situation where the committee of creditors comprised a substantial number (or only) of creditors in a class (primarily home buyers). It was noticed that in these cases, the total voting share being polled by home buyers was very small (since they were scattered all over the country and not organized), thereby creating a deadlock in decision making as the requisite voting majorities were not being obtained. Hence, the newly inserted provision provides that an authorised representative under section 21(6A) (that is, an AR of creditors in a class) shall cast his vote on behalf of all the financial creditors he represents in accordance with the decision taken by a vote of more than 50 percent of the voting share of the financial creditors he represents who have cast their vote. Further, it is provided that for a vote to be cast in respect of a withdrawal application under section 12A of the IBC, the financial creditors shall cast his vote in accordance with the provisions of section 25A(3) of the IBC.

Voting Procedures

The voting procedures for the Committee of Creditors are detailed in regulation 25 of the Corporate Insolvency Resolution Process Regulations which provides that-

(i) Mandatory actions to be considered in meeting: The actions listed in section 28(1) shall be considered in meetings of the committee.

Prior Approval of committee of creditors for certain actions. -

- *Actions to be approved by Committee of Creditors:* Sub-section (1)of section 28 has overriding effect as it start with “ Notwithstanding anything contained in any other law for the time being in force...................". It provides that the resolution professional, during the corporate insolvency resolution process, shall not take any of the following actions without the prior approval of the committee of creditors namely: -

- *Prior Approval of Committee of Creditors***:** The resolution professional shall convene a meeting of the committee of creditors and seek the vote of the creditors prior to taking any of the actions under sub-section (1).(Section 28 (2)).
- *Approval by Committee of Creditors:* No action under sub-section (1) shall be approved by the committee of creditors unless approved by a vote of sixty-six per cent of the voting shares. (Section 28 (3))

Raise any interim finance in excess of the amount as may be decided by the committee of creditors in their meeting.	Create any security interest over the assets of the corporate debtor.	Change the capital structure of the corporate debtor, including by way of issuance of additional securities, creating a new class of securities or buying back or redemption of issued securities in case the corporate debtor is a company.	Record any change in the ownership interest of the corporate debtor.
Give instructions to financial institutions maintaining accounts of the corporate debtor for a debit transaction from any such accounts in excess of the amount as may be decided by the committee of creditors in their meeting.	Undertake any related party transaction.	Amend any constitutional documents of the corporate debtor.	Delegate its authority to any other person.
Dispose of or permit the disposal of shares of any shareholder of the corporate debtor or their nominees to third parties.	Make any change in the management of the corporate debtor or its subsidiary.	Transfer rights or financial debts or operational debts under material contracts otherwise than in the ordinary course of business.	Make changes in the appointment or terms of contract of such personnel as specified by the committee of creditors.

Make changes in the appointment or terms of contract of statutory auditors or internal auditors of the corporate debtor.

- *Consequence of action without approval:* Where any action under sub-section (1) is taken by the resolution professional without seeking the approval of the committee of creditors in the manner as required in this section, such action shall be void. (Section 28 (4))
- *Action against RP:* The committee of creditors may report the actions of the resolution professional under sub-section (4) to the Board for taking necessary actions against him under this Code. (Section 28 (5)).

(ii) **Other actions:** Any action other than those listed in section 28(1) requiring approval of the committee may be considered in meetings of the committee.

(iii) **Voting of members:** The resolution professional shall take a vote of the members of the committee present in the meeting, on any item listed for voting after discussion on the same.

(iv) **Announcement of decision by Resolution Professional**: At the conclusion of a vote at the meeting, the resolution professional shall announce the decision taken on items along with the names of the members of the committee who voted for or against the decision, or abstained from voting.

In the case of *K. Shashidhar,* the Supreme Court read Regulation 25(5) of the CIRP Regulations and with Section 30(4) of the Code and concluded as follows;

"For approval of the resolution plan, the "percent of voting share of the financial creditors" approving vis à vis dissenting is required to be reckoned. It is ***not on the basis of members present and voting*** *as such. At any rate, the approving votes must fulfil the threshold percent of voting share of the financial creditors."*

Therefore, the Hon'ble Supreme Court has **rejected** the principle of "*present and voting"* for the calculation of votes and has interpreted Regulation 25(5) to also cover members who may be absent for a given meeting. Moreover, Regulation 25(5) of the CIRP Regulations provides that where a member remains absent for meeting, he shall nonetheless have the opportunity to review the Minutes of the Meeting and cast his/her vote via electronic means.

(v) Minutes of the meeting of Committee of Creditors

- Regulation 24 of Corporate Insolvency Resolution Process Regulations provides for the duty of resolution professional to prepare minutes of each meeting of committee of creditors and circulate the same as follows:
  - *Disclosure in minutes:* The resolution professional shall ensure that minutes are made in relation to each meeting of the committee and such minutes shall disclose the particulars of the participants who attended the meeting in person, through video conferencing, or other audio and visual means.
  - *Circulation of minutes:* The resolution professional shall circulate the minutes of the meeting to all participants by electronic means within forty eight hours of the said meeting.
- *Regulation 25 of Corporate Insolvency Resolution Process Regulations provide for the manner of circulation of minutes as follows:*

  The resolution professional shall-

  (a) circulate the minutes of the meeting by electronic means to all members of the committee and the authorised representative, if any, within forty-eight hours of the conclusion of the meeting; and

  (b) seek a vote of the members who did not vote at the meeting on the matters listed for voting, by electronic voting system in accordance with regulation 26 where the voting shall be kept open, from the circulation of the minutes, for such time as decided by the committee which shall not be less than twenty-four hours and shall not exceed seven days.

  Provided that on a request for extension made by a creditor, the voting window shall be extended in increments of twenty-four hours period. It is further provided that the resolution professional shall not extend the voting window where the matters listed for voting have already received the requisite majority vote and one extension has been given after the receipt of requisite majority vote.
- *Circulation of minutes by the authorised representative (Regulation 25(6):* The authorised representative shall circulate the minutes of the meeting received under Regulation 25(5) to creditors in a class and announce the voting window at least twenty-four hours before the window opens for voting instructions and keep the voting window open for at least twelve hours.

(vi) Voting by electronic means: Regulation 26 provides for the procedure for voting by electronic means in the following manner:

1. - The resolution professional shall provide each member of the committee the means to exercise its vote by either electronic means or through electronic voting system in accordance with the provisions of this Regulation.
2. - At the end of the voting period, the voting portal shall forthwith be blocked.
3. - At the conclusion of a vote held under this Regulation, the resolution professional shall announce and make a written record of the summary of the decision taken on a relevant agenda item along with the names of the members of the committee who voted for or against the decision, or abstained from voting.
4. - The resolution professional shall circulate a copy of the record made under sub-regulation (4) to all participants by electronic means within twenty four hours of the conclusion of the voting.

- It is further explained- For the purposes of these Regulations-

a) the expressions "voting by electronic means" or "electronic voting system" means	a "secured system" based process of display of electronic ballots, recording of votes of the members of the committee and the number of votes polled in favour or against, such that the voting exercised by way of electronic means gets registered and counted in an electronic registry in a centralized server with adequate cyber security;
b) the expression "secured system" means computer hardware, software, and procedure that	(i) are reasonably secure from unauthorized access and misuse;
	(ii) provide a reasonable level of reliability and correct operation
	(iii) are reasonably suited to perform the intended functions; and
	(iv) adhere to generally accepted security procedures.

Duties of resolution professional. – Section 25 (2) of the Code states that the resolution professional shall (e) maintain an updated list of claims (f) convene and attend all meetings of the committee of creditors; (i) present all resolution plans at the meetings of the committee of creditors.

(vii) Decision by Committee of Creditors*:* Save as otherwise provided in this Code, all decisions of the committee of creditors shall be taken by a vote of not less than fifty-one per cent of voting share of the financial creditors.

(viii) Right of Committee of Creditors to require information from RP: The committee of creditors shall have the right to require the resolution professional to furnish any financial information in relation to the corporate debtor at any time during the corporate insolvency resolution process which shall be furnished within a period of seven days of such requisition. [Section 21 (9&10)].

The Resolution Professional (RP) shall submit all resolution plans that comply with the provisions of the Code to the committee

The committee shall:
(a) evaluate the resolution plans as per evaluation matrix;
(b) record its deliberations on the feasibility and viability of each resolution plan; and
(c) vote on all such resolution plans simultaneously.

Where only one resolution plan is put to vote, it shall be considered approved if it receives requisite votes.

Where two or more resolution plans are put to vote simultaneously, the resolution plan, which receives the highest votes, but not less than requisite votes shall be considered as approved.

Where two or more resolution plans receive equal votes, but not less than requisite votes, the committee shall approve any one of them, as per the tie-breaker formula announced before voting.

Where none of the resolution plans receives requisite votes, the committee shall again vote on the resolution plan that received the highest votes, subject to the timelines under the Code.

The RP shall endeavour to submit the resolution plan approved by the committee to the Adjudicating at least 15 days before the maximum period for completion of CIRP.

(ix) Voting rights of members of Committee consisting of operational creditors: A member of the committee formed under this Regulation shall have voting rights in proportion of the debt due to such creditor or debt represented by such representative, as the case may be, to the total debt.

Explanation – For the purposes of voting by Operational Credtiros-'total debt' is the sum of		
(a) the amount of debt due to the creditors listed in subregulation 2(a);	(b) the amount of the aggregate debt due to workmen under subregulation 2(b); and	(c) the amount of the aggregate debt due to employees under subregulation 2(c).

A member of the committee formed under this Regulation shall have voting rights in proportion of the debt due to such creditor or debt represented by such representative, as the case may be, to the total debt.

Right of Committee of Creditors to replace Resolution Professional

Where, at any time during the corporate insolvency resolution process, the committee of creditors is of the opinion that a resolution professional appointed under section 22 is required to be replaced, it may resolve to replace him with another resolution professional at a meeting, by a vote of sixty-six per cent of voting shares, subject to a written consent from the proposed resolution professional in the specified form. The committee of creditors shall forward the name of the insolvency professional proposed by them to the Adjudicating Authority. **(Section 27)**

CASE LAWS

Is it necessary for CoC to give reason for replacement of IRP/RP?

Punjab National Bank Vs. Mr. Kirah Shah, Interim Resolution Professional of ORG Informatics Ltd. [CA (AT) (Ins) No. 749/2019]

In the impugned order, the AA noted that the application does not explain why the Interim Resolution Professional was replaced. Immediately after the first meeting of the Committee of Creditors, it is supposed to prefer an application under section 22, which was not done in this case. On appeal, the NCLAT held that the Committee of Creditors is not required to record any reason for replacing the RP that may otherwise call for proceedings against such Resolution Professional. Having decided to remove the Resolution Professional with 88 percent of the voting share, the Committee of Creditors was not open to the AA interfering with such decision, till it is shown that the decision of the Committee of Creditors is perverse or without jurisdiction.

Can CoC replace RP in any of its meeting without recording reason for the same?

Bank of India Vs. M/s Nithin Nutritions Pvt. Ltd. [Company Appeal (AT) (Insolvency) No. 497 of 2020 (with connected appeals)]

In the third Committee of Creditors meeting, the Interim Resolution Professional was replaced by another person as the RP. The appellant had filed an application before the AA for confirmation of the RP's appointment. The AA rejected the application on the basis that the Committee of Creditors's decision was taken in its third meeting (and not the first meeting, as prescribed in the IBC) and no reasons were given for not adopting the resolution to replace the Interim Resolution Professional in the first meeting.

In the appeal against the AA's order, the NCLAT observed that neither section 22 nor section 27 of the IBC requires the Committee of Creditors to give any reasons. The reason is that the relationship between the RP and the Committee of Creditors is that of confidence. If there is loss of confidence and the RP continues in the role, the corporate debtor would be put to loss because of the bad relationship between the Interim Resolution Professional/RP and the Committee of Creditors. The NCLAT further noted that initially section 16 of the IBC specified a 30-day term for the Interim Resolution Professional. This provision was substituted with effect from June 6, 2018, and now the term of the Interim Resolution Professional shall continue till the date of appointment of the RP under section 22. It also referred to regulation 17 of the Corporate Insolvency Resolution Process Regulations and observed that the Interim Resolution Professional continues as such by performing the functions of an RP from day 40. Considering these provisions, the NCLAT held that the Committee of Creditors has the requisite powers to propose changing the Interim Resolution Professional even in meeting/s subsequent to the first one and there is no requirement that they should give particular reasons for the change.

Approval of Resolution Plan by Committee of Creditors

The Code has provided the Committee with exclusive access to negotiations and also the final hand in dealing with business decisions. Thereby, the Committee of Creditors is also endowed with the mammoth responsibility of evaluating resolution plans and thereafter voting and approving the best resolution plan.

Regulation 39 of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 lays down the provisions of the approval of the resolution plan by the committee.

(i) *Approval of resolution plan by Committee of Creditors:* The committee of creditors may approve a resolution plan by a vote of **not less than sixty-six per cent of voting share of the financial creditors,** after considering its feasibility and viability, the manner of distribution proposed, which may take into account the order of priority amongst creditors as laid down in sub-section (1) of section 53, including the priority and value of the security interest of a secured creditor and such other requirements as may be specified by the Board. [Section 30(4)].

(ii) *A Resolution Applicant to attend meeting of Committee of Creditors:* The resolution applicant may attend the meeting of the committee of creditors in which the resolution plan of the applicant is considered but the resolution applicant shall not have a right to vote at the meeting of the committee of creditors unless such resolution applicant is also a financial creditor. [Section 30(5)].

APPLICATION TO EXTEND TIME PERIOD OF CORPORATE INSOLVENCY RESOLUTION PROCESS/ FAST TRACK CORPORATE INSOLVENCY RESOLUTION PROCESS

If Corporate Insolvency Resolution Process or Fast Track Corporate Insolvency Resolution Process couldn't be completed in 180 days/90 days respectively, an application for extension of time limit has to be made to the Adjudicating Authority which needs **approval by a resolution passed at a meeting of Committee of Creditors as follows:**

(i) Extension of *Time-limit for completion of insolvency resolution process beyond 180 days:* The resolution professional shall file an application to the Adjudicating Authority to extend the period of the corporate insolvency resolution process beyond one hundred and eighty days, if instructed to do so by a resolution passed at a meeting of the committee of creditors by a vote of sixty-six per cent. of the voting shares. [Section 12(2)].

(ii) *Extension of Time-limit for completion of fast track corporate insolvency resolution process.* - The resolution professional shall file an application to the Adjudicating Authority to extend the period of the fast track corporate insolvency resolution process beyond ninety days if instructed to do so by a resolution passed at a meeting of the committee of creditors and supported by a vote of seventy-five percent of the voting share. [Section 56 (2)].

It is clarified in Regulation 40 that the resolution professional shall continue to discharge his responsibilities under the corporate insolvency resolution process, till the application for extension is decided by the Adjudicating Authority.

Commercial Wisdom of Committee of Creditors

The Code places the CoC in control of the insolvency process. The courts have subsequently sanctified the decision-making power of the CoC. CoC's decision with requisite voting share in relation to the resolution plan is sacrosanct. The approved plan as stamped by the court is binding on all stakeholders including the dissenting creditors. The choice of resolution plan has been placed under the ambit of the 'commercial wisdom' of the CoC and is unchallenged. The courts have reiterated the primacy of the CoC's commercial wisdom on several occasions and restrained from interfering with its decision or commenting on the plan on merit.

CASE LAWS

The significance of "Commercial wisdom of Committee of Creditors" was discussed in details by Supreme Court in the case of ***Committee of Creditors of Essar Steel India Ltd. V. Satish Kumar Gupta & Ors (2019)*** where the Apex Court held that-

- At the outset it is important to be noted that the legislature in their wisdom under the provisions of the Insolvency and Bankruptcy Code, 2016 (Code) have left the decision-making in respect of commercial matters completely in the domain of the Committee of Creditors.
- In fact even the Bankruptcy Law Reforms Committee report (which formed the basis for the enactment of the Code) specifically notes the deliberate scheme of the Code, where the law does not prescribe any particular manner of insolvency resolution and leaves this commercial decision making process to the Committee Of Creditors without the interference of the legislature as well as judiciary. The Committee of Creditors does not act in any fiduciary capacity to any group of creditors. On the contrary, it is to take a business decision based upon ground realities by a majority, which then binds all stakeholders, including dissentient creditors.
- The NCLAT judgment which substitutes its wisdom for the commercial wisdom of the Committee of Creditors and which also directs the admission of a number of claims which was done by the

resolution applicant, without prejudice to its right to appeal against the aforesaid judgment, must therefore be set aside.

- It is always open to the Committee Of Creditors to adjudge the commercial wisdom of the resolution plan while approving it. As pointed out by the Supreme Court in ***K. Sashidhar vs Indian Overseas Bank & Ors.*** (Civil Appeal No. 10673 of 2018), such commercial decision of the Committee Of Creditors is not subject to appeal under the Code.
- The Hon'ble Apex Court specifically ruled that the NCLT must limit its judicial review to the parameters outlined in Section 30 (2) of IBC, while the NCLAT must adhere to the guidelines set forth in Section 32 in conjunction with Section 61(3) of the IBC.
- The NCLT and NCLAT must never interfere with a commercial decision made by the majority of the Committee of Creditors.

The Supreme Court passed its order in the case *of* ***K. Sashidhar v. Indian Overseas Bank & Ors. (Civil Appeal No. 10673 of 2018)*** wherein the SC, inter alia, has held that

- the National Company Law Tribunal ("**NCLT**") and the National Company Law Appellate Tribunal ("**NCLAT**") have no jurisdiction and authority to analyse or evaluate the commercial decisions taken by the committee of creditors ("**Committee of Creditors**").
- Non recording of reasons for approving or rejecting the resolution plan by the concerned financial creditors during the voting in the meeting of Committee of Creditors, would not render the final collective decision of Committee of Creditors nullity per se.
- Concededly, if the objection to the resolution plan is on account of infraction of ground(s) specified in section 30(2) and 61(3), that must be specifically and expressly raised at the relevant time. For the approval of resolution plan by the Committee of Creditors can be challenged on those grounds.
- However, if the opposition to the proposed resolution plan is purely a commercial or business decision, the same, being non-justiciable is not open to challenge before the Adjudicating Authority (NCLT) or for that matter the Appellate Authority (NCLAT). If so, non-recording of any reason for taking such commercial decision will be of no avail.
- The Hon'ble National Company Law Appellate Tribunal has held that the Committee of Creditors has the discretion to approve any resolution plan and its decision to approve the same cannot be interfered with by the Adjudicating Authority or the Appellate Authority, except for in terms of Section 31(1) to examine compliance of Section 30(2) read with relevant regulations. *(Ref:Kannan Tiruvengandram Vs. M.K. Shah Exports Ltd. & Ors. in and Darshak Enterprise Pvt. Ltd. and Ors. v. Chhaparia Industries Pvt. Ltd. and Ors. E.)*

In ***Kalpraj Dharamshi and Another v. Kotak Investment Advisors Limited and Another, 2021 SC,*** the Hon'ble Supreme Court, has reiterated that the legislative scheme, as interpreted by various decisions of this Court, is unambiguous and the commercial wisdom of Committee of Creditors is not to be interfered with, excepting the limited scope as provided under Sections 30 and 31 of the I&B Code.

In ***Vallal Rck vs M/S Siva Industries And Holdings ... on 3 June, 2022,*** Supreme Court held that this Court has consistently held that the commercial wisdom of the Committee of Creditors has been given paramount status without any judicial intervention for ensuring completion of the stated processes within the timelines prescribed by the IBC. It has been held that there is an intrinsic assumption, that financial creditors are fully informed about the viability of the corporate debtor and feasibility of the proposed resolution plan. They act on the basis of thorough examination of the proposed resolution plan and assessment made by their team of experts. Neither the learned NCLT nor the learned NCLAT were justified in not giving due weightage to the commercial wisdom of Committee of Creditors.

Therefore, supremacy of commercial wisdom of Committee of Creditors has been held persistently by the Apex Court since the inception of the Code.

Jindal Stainless Ltd. v. Mr. Shailendra Ajmera, Resolution Professional of Mittal Corp Ltd. & Ors. Case no.: Comp. App. (AT) (Ins.) No. 1058 of 2022 Decision Date: January 18, 2023, *National Company Law Appellate Tribunal, Delhi:*

Facts:

1. Mittal Corp Limited (Corporate Debtor) was admitted into Corporate Insolvency Resolution Process on 10.11.2021 by the Adjudicating Authority.

2. The Resolution Applicants were communicated the rules of Challenge Process and gave their unconditional acceptance to the same.

3. All the Resolution Applicants were notifi ed that the signed and compliance Resolution Plan must be submitted by 18.07.2022. Jindal Stainless Ltd., Shyam Sel and Power Ltd. along with two other resolution applicants submitted their amended Resolution Plans by 18.07.2022.

4. An application for consideration of amended resolution plans was also filed with the Adjudicating Authority.

Issue:

Can decision of CoC to vote on a resolution modified in given timeline and refuse to consider other modified after time stipulated for same be questioned?

Held:

1. Taking note of Regulation 39 (1A) of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, the regulation has been brought in place to enable the Committee of Creditors to negotiate with all the Resolution Applicants by one alternative mechanism to find out the best resolution plan.

2. Clause 7 of the Challenge Process clearly contemplates that after conclusion of the Challenge Process, the eligible Resolution Applicants shall not revise their bid/commercial offer. It is relevant to note that Challenge Process also reserves the unconditional right of the Committee of Creditors to cancel/ modify/ withdraw/ abandon/ amend the process of the Challenge Process at any stage. The approval of the plan submitted in Corporate Insolvency Resolution Process is in the domain of the Committee of Creditors. Under Regulation 39 of the Corporate Insolvency Resolution Process Regulations, the committee is entitled to record its deliberation and vote on such resolution plan simultaneously.

3. There can be no fetter on the power of the Committee of Creditors to cancel or modify any negotiation with the Resolution Applicant including a Challenge Process but it is the wisdom of the Committee of Creditors to take a decision in that regard. Committee of Creditors, in the facts of the present case, did not take any decision to disregard the Challenge Process, rather it decided to vote on the plan.

4. It is well settled that the timeline in the IBC has its salutary value, and it was the wisdom of the Committee of Creditors which decided to vote on the Resolution Plan after completion of Challenge Process and not to proceed to take any further negotiation or further modification of the plan, that decision ought not to have been interfered with.

5. The decision of Committee of Creditors to vote on the Resolution Plan after completion of Challenge Process and not to further accept any modification of the plan, should not be interfered with. The Application was filed by Shyam Sel and Power Ltd. on 07.08.2022, when Committee of Creditors had already resolved the vote on all the plans and voting had also commenced w.e.f. 07.08.2022.

Source: ICSIIIP Quarterly Newsletter

In the case of ***Vishal Chelani & Ors. vs. Debashis Nanda [Civil Appeal No. 3806 of 2023]***, the issue before Supreme Court was whether there could be different treatment of allotees in the resolution plan for the one who had invoked RERA and of others who did not approach RERA?

Hon'ble Supreme Court in its order dated October 06, 2023, inter alia observed that the Resolution Professional's view appears to be that once an allottee seeks remedies under RERA, and opts for return of money in terms of the order made in her favour, it is not open for her to be treated in the class of home buyer. This Court is unpersuaded by the submission. It is only home buyers that can approach and seek remedies under RERA – no others. In such circumstances, to treat a particular segment of that class differently for the purposes of another enactment, on the ground that one or some of them had elected to take back the deposits together with such interest as ordered by the competent authority, would be highly inequitable. As held in Mr. *Natwar Agrawal (HUF) vs. Ms. Ssakash Developers & Builders Pvt. Ltd.* by the Mumbai Bench of National Company Law Tribunal the underlying claim of an aggrieved party is crystallized in the form of a Court order or decree. That does not alter or disturb the status of the concerned party - in the present case of allottees as financial creditors. Furthermore, Section 238 of the IBC contains a non obstante clause which gives overriding effect to its provisions. Consequently, its provisions acquire primacy, and cannot be read as subordinate to the RERA Act. In any case, the distinction made by the R.P. is artificial; it amounts to "hyper classification" and falls afoul of Article 14. Such an interpretation cannot therefore, be countenanced.

The impugned order of NCLAT set aside by the Supreme Court and Hon'ble Apex Court ordered that the appellants are declared as financial creditors within the meaning of Section 5(8)(f) (Explanation) and entitled to be treated as such along with other home buyers/financial creditors for the purposes of the resolution plan which is awaiting final decision before the adjudicating authority.

LESSON ROUND-UP

- The committee of creditors is the most important business decision-making body in every corporate insolvency resolution process.
- The Code has shifted the control from debtor to creditor in taking decision with respect to a corporate debtor undergoing insolvency resolution process.
- Section 18 and Section 21 of the Code, obligate the Interim Resolution Professional to constitute the Committee of Creditors, after the collation of the proof of claims. As per sub-section (2) of Section 21, the Committee shall comprise "all financial creditors of the corporate debtor".
- The committee of creditors is composed of financial creditors of the corporate debtor as the financial creditors have the capability to assess the commercial viability of the corporate debtor and are willing to modify the terms of the debt contracts in negotiations between the creditors and the corporate debtor.
- Regulation 16 of the Insolvency & Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (CIRP Regulations), provides that CoC shall consists of operational creditors where the corporate debtor has (i) no financial debt; or (ii) where all financial creditors are related parties and this Committee shall consist of (a) eighteen largest operational creditors by value; (b) one representative of workmen; and (c) one representative of employees of the corporate debtor.
- The CoC carries out its functions through its meetings. The IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (CIRP Regulations) provides in detail, the manner in which these meetings have to be conducted.
- The meetings are convened and chaired by the RP in his/her capacity as Interim Resolution Professional (IRP) or RP, as the case may be.
- The notice should be shared with all its members- the unrelated financial creditors including the authorised representative of a class of creditors; members of the suspended Board of Directors or Partners of the corporate debtor and operational creditors (OCs) or their representatives if their aggregate dues is not less than 10% of the debt. The notice can be shared electronically also.

- Quorum of at least 33% of the voting rights are present either in person or by video conferencing or other audio and visual means is required for conduct of a meeting.
- The CoC exercises its power of decision making through the process of voting.
- The Code provides that the thresholds for general decision making in the CoC should not be less than 51%.
- Instances involving significant actions that impact the working of the CD or the CIRP inter alia include raising of interim finance; creating security interest on assets of the CD; change in ownership or capital structure; amend constitutional documents of the CD; change management of the CD or its subsidiary; appointment of statutory auditor or internal auditor and replacement of a RP require a higher threshold of 66%. Where the CoC decides to accept the applicants' request for withdrawal which has the effect of terminating the CIRP midway requires a still higher threshold of 90%.
- CoC is the decision-making body in the CIRP. The Code and the courts have left a wide ambit of commercial and business decisions to the CoC.
- The Hon'ble Supreme Court (SC) reiterated in its judgement in the *K. Sashidhar v. Indian Overseas Bank & Ors* that the commercial wisdom of CoC has been given paramount status without any judicial intervention for ensuring completion of the stated processes within the timelines prescribed... the legislature has consciously not provided any ground to challenge the "commercial wisdom" of the individual financial creditors or their collective decision before the adjudicating authority. That is made non-justiciable.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1 Define financial debt under the provisions of the Code.

2 List out the procedure till conduct of first meeting of Committee of Creditors by Interim Resolution Professional according to IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.

3 What is the constitution of Committee of Creditors with operational creditors only?

4 What should be the quorum at the meeting of Committee of Creditors?

5 Explain "Commercial Wisdom of Committee of Creditors" with reference to decided case laws.

REFERENCES

- IBBI Handbook 2019
- IBBI quarterly newsletter
- ICSIIIP Journal
- Promoting common good amidst anti-common behaviour of stakeholders: Role of Committee of Creditors, Sudhaker Shukla and Kokila Jayaram

Preparation & Approval of Resolution Plan

Lesson 19

KEY CONCEPTS

■ Resolution Plan ■ Resolution Applicant ■ Connected Person ■ Relevant Information ■ Financial Entity ■ Expression of Interest ■ Request for resolution plans (RFRP) ■ Performance security ■ Evaluation Matrix

Learning Objectives

To understand:

- Meaning of Resolution Plan & Resolution Applicant
- Expression of Interest
- Request for Resolution Plans
- Contents of a Resolution Plan
- Approval of Resolution Plan

Lesson Outline

- BLRC Report on Resolution Plan
- Meaning of Resolution Plan and Resolution Applicant
- Appointment of Registered Valuer
- Persons not eligible to be resolution applicant (Section 29A)
- The Process of Inviting and Submitting Resolution Plans
- Invitation for Expressions of Interest
- Request for resolution plans (RFRP)
- Strategy for marketing of assets of the corporate debtor
- Resolution plan
- The Evaluation Matrix
- Submission of resolution plan
- Approval of resolution plan by CoC
- Approval of resolution plan by AA
- Appeal
- Liability for prior offences, etc.
- Case Laws
- Lesson Round-Up
- Test Yourself
- References

REGULATORY FRAMEWORK

- Section 5(25) & 5(26) of the Insolvency and Bankruptcy Code, 2016
- Section 29A of the Insolvency and Bankruptcy Code, 2016
- Section 30 to 32A of the Insolvency and Bankruptcy Code, 2016
- The Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 (hereinafter referred as CIRP Regulations)

INTRODUCTION

The Banking Law Reform Committee (BLRC) Report- Volume 1, Rationale for the Code has stated following with respect to *obtaining the resolution to insolvency in the insolvency resolution process.*

The Committee is of the opinion that there should be freedom permitted to the overall market to propose solutions on keeping the entity as a going concern. Since the manner and the type of possible solutions are specific to the time and environment in which the insolvency becomes visible, it is expected to evolve over time, and with the development of the market. The Code will be open to all forms of solutions for keeping the entity going without prejudice, within the rest of the constraints of the IRP. Therefore, how the insolvency is to be resolved will not be prescribed in the Code.

There are three aspects of this process that the Code does state.

The first is that the process of obtaining solutions is provided with all information as can be reasonably expected at the time, is transparent and is time-bound.

The second is that any proposed solution must explicitly account for the IRP costs and the liabilities of the operational creditors within a reasonable period from the approval of the solution if it is approved.

The Committee argues that there must be a counterbalance to operational creditors not having a vote on the creditors committee. Thus, they concluded that the dues of the operational creditors must have priority in being paid as an explicit part of the proposed solution. This must be ensured by the RP in evaluating a proposal before bringing it to the creditors committee.

The third is that any solution that is presented must recognise restrictions and requirements from related laws. This holds particularly for corporate actions, which have provisions in Act governing the form of the given entity. For example, if the entity is a listed firm and the solution involves a merger of the entity with another, the solution must include awareness of the rules and regulations governing the merger of firms under Companies Act 2013, and SEBI (Substantial Acquisition of Shares and Takeover) Regulations if the firm is listed on an exchange.

The choice of the solution to keep the entity as a going concern will be voted on by the creditors committee. There are no constraints on the proposals that the Resolution Professional can present to the creditors committee. Other than the majority vote of the creditors committee, the Resolution Professional needs to confirm to the Adjudicator that the final solution complies with three additional requirements. The first is that the solution must explicitly require the repayment of any interim finance and costs of the insolvency resolution process will be paid in priority to other payments. Secondly, the plan must explicitly include payment to all creditors not on the creditors committee, within a reasonable period after the solution is implemented. Lastly, the plan should comply with existing laws governing the actions of the entity while implementing the solutions.

Meaning of Resolution Plan and Resolution Applicant

The Insolvency and Bankruptcy Code, 2016 (Code) aims at resolving the woes of insolvent companies through the corporate insolvency resolution process (CIRP), wherein the assets or business of the corporate debtor are transferred as a going concern to the most eligible party approved by the Committee of Creditors. Such an eligible party is willing to take up the management of the Corporate Debtor as well as to service its debts. The parties that are willing to take over the corporate debtor are called resolution applicants and they participate in the CIRP by submitting a document called a resolution plan. It is a comprehensive document which covers, inter alia, overview of the eligible party, how does the party plan to take over the corporate debtor, debt repayment schedule etc. The resolution plans are first analysed by the resolution professional to ensure that they meet the conditions prescribed under the Code, pursuant to which, they are placed before the committee of creditors for their discussion, evaluation and approval. The resolution plan, so approved by the committee and scoring the highest points, is then filed by the resolution professional with the Adjudicating Authority.

In ***Binani Industries Limited Vs. Bank of Baroda, Company Appeal (AT) (Insolvency) No. 82 of 2018,*** the NCLAT observed that the objective of the IBC is Resolution. The Purpose of Resolution is for maximization of value of assets of the Corporate Debtor (CD) and thereby for all creditors. It is not maximization of value for a 'stakeholder' or 'a set of stakeholders' such as Creditors and to promote entrepreneurship, availability of credit and balance the interests. The first order objective is "resolution". The second order objective is "maximization of value of assets" of the CD and the third order objective is "promoting entrepreneurship, availability of credit and balancing the interests". This order of objectives is sacrosanct.

Significance of resolution is highlighted by Supreme Court in ***Swiss Ribbons Pvt. Ltd. & Another Vs. UoI & Others [WP (Civil) No. 99/2018*** with connected matters where the preamble does not refer to liquidation, which is only pursued as a last resort if there is either no resolution plan or the resolution plans submitted are not up to the mark.

RESOLUTION PLAN:

According to section 5(26), a 'resolution plan' means a plan proposed by resolution applicant for insolvency resolution of the corporate debtor as a going concern in accordance with Part II".

Explanation- For removal of doubts, it is clarified that are solution plan may include provisions for the restructuring of the corporate debtor, including by way of merger, amalgamation and demerger.

RESOLUTION APPLICANT:

As per Section 5(25) of the Code "resolution applicant" means a person, who individually or jointly with any other person, submits are solution plan to the resolution professional pursuant to the invitation made under clause (h) of sub-section (2) of section 25 or pursuant to section 54K, as the case may be.

Appointment of Registered Valuer

A key objective of the IBC is maximization of the value of assets of the corporate debtor and consequently value for its stakeholders. A critical element toward achieving this objective is transparent and credible determination of the value of the assets to facilitate comparison and informed decision making by the Committee of Creditors.

In ***Maharashtra Seamless Limited Vs. Padmanabhan Venkatesh and Others [Civil Appeal No. 4242 of 2019, 2020 SCC Online SC 67],*** the Supreme Court observed that it appears that the aim of prescribing such valuation process is to help the committee of creditors make a decision on a resolution plan properly. The CIRP Regulations assign the valuation responsibility to registered valuers. By way of a circular dated October 17, 2018, the IBBI has directed that every valuation required under the IBC or any of the regulations made thereunder is required to be conducted by a registered valuer, that is, a valuer registered with the IBBI under the Companies (Registered Valuers and Valuation) Rules, 2017. Further, with effect from February 1, 2019, no insolvency professional (IP) shall appoint a person other than a registered valuer to conduct any such valuation. By way of another circular, dated August 13, 2019, the IBBI has reiterated that appointing any person, other than a registered valuer, on or after February 1, 2019, to conduct such valuation is illegal and payment, whether as a fee or otherwise, to such person shall not form part of the insolvency resolution process costs or liquidation cost.

Appointment of Registered Valuer: Regulation 27, Chapter VIII of CIRP Regulations provides for appointment of registered valuer as: (1) The resolution professional shall, within seven days of his appointment but not later than forty-seventh day from the insolvency commencement date, appoint two registered valuers to determine the fair value and the liquidation value of the corporate debtor in accordance with regulation 35.	Regulation 2(1) (hb) of CIRP Regulations: **"Fair value"** means the estimated realizable value of the assets of the corporate debtor, if they were to be exchanged on the insolvency commencement date between a willing buyer and a willing seller in an arm's length transaction, after proper marketing and where the parties had acted knowledgeably, prudently and without compulsion. Regulation 2(1) (k) of CIRP Regulations: "Liquidation value" means the estimated realizable value of the assets of the corporate debtor, if the corporate debtor were to be liquidated on the insolvency commencement date.

As per regulation 2(1)(m), "Registered valuer" means a person registered as such in accordance with the Companies Act, 2013, and rules made thereunder.

Who shall not be appointed as Registered Valuer by Resolution Professional: Regulation 27(3) of CIRP Regulations,2016 provides that the resolution professional, as the case may be, shall appoint a professional under this regulation on an arm's length basis following an objective and transparent process, provided that the following persons shall not be appointed, namely: -

(a) a relative of the resolution professional;

(b) a related party of the corporate debtor;

(c) an auditor of the corporate debtor at any time during the period of five years preceding the insolvency commencement date;

(d) a partner or director of the insolvency professional entity of which the resolution professional is a partner or director.

Regulation 35 provides for determining the fair value and liquidation value of the corporate debtor as follows:

(1) Fair value and liquidation value shall be determined in the following manner: -

(a) the two registered valuers appointed under regulation 27 shall submit to the resolution professional an estimate of the fair value and of the liquidation value computed in accordance with internationally accepted valuation standards, after physical verification of the inventory and fixed assets of the corporate debtor;

(b) if the two estimates of a value in an asset class are significantly different, or on receipt of a proposal to appoint a third registered valuer from the committee of creditors, the resolution professional may appoint a third registered valuer for an asset class for submitting an estimate of the value computed in the manner provided in clause (a).

(c) the average of the two closest estimates of a value shall be considered the fair value or the liquidation value, as the case may be.

Explanation. - For the purpose of clause (b),

(i) "Asset class" means the definition provided under the Companies (Registered Valuers and Valuation) Rules, 2017;

(ii) "Significantly different" means a difference **of twenty-five per cent** in liquidation value under an asset class and the same shall be calculated as (L1-L2)/L1,

where, L1= higher valuation of liquidation value L2= lower valuation of liquidation value.

Duty of RP w.r.t. confidentiality of fair value and liquidation value so determined: After the receipt of resolution plans in accordance with the Code and these regulations, the resolution professional shall provide the fair value, the liquidation value and valuation reports to every member of the committee in electronic form, on receiving an undertaking from the member to the effect that such member shall maintain confidentiality of the fair value, the liquidation value and valuation reports and shall not use the information contained in the valuation reports to cause an undue gain or undue loss to itself or any other person and comply with the requirements under sub-section (2) of section 29. The resolution professional and registered valuers shall maintain confidentiality of the fair value and the liquidation value.

Persons not Eligible to be Resolution Applicant (Section 29A)

The Insolvency and Bankruptcy Code (Amendment) Act, 2018 had inserted a new section 29A, which declares certain persons ineligible to be a resolution applicant and prohibits such persons from submitting are solution plan.

Ineligibility during the resolution process and liquidation

(As laid down in the matter of ***'Arun Kumar Jagatramka. Vs. Jindal Steel and Power Ltd. & Anr')***

The birth of section 29A is an event attributable to the experience which was gained from the actual working of the provisions of the statute since it was published in the Gazette of India on 28 May 2016.

Section 29A has been construed to be a crucial link in ensuring that the objects of the IBC are not defeated by allowing "ineligible persons", including but not confined to those in the management who have run the company aground, to return in the new avatar of resolution applicants.

The values which animate Section 29A continue to provide sustenance to the rationale underlying the exclusion of the same category of persons from the process of liquidation involving the sale of assets, by virtue of the provisions of section 35(1)(f).

The purpose of the ineligibility under Section 29A is to achieve a sustainable revival and to ensure that a person who is the cause of the problem either by a design or a default cannot be a part of the process of solution.

A person shall not be eligible to submit a resolution plan, if such person, or any other person acting jointly or in concert with such person—

(a) is an undischarged insolvent;

(b) is a wilful defaulter in accordance with the guidelines of the Reserve Bank of India issued under the Banking Regulation Act, 1949;

(c) at the time of submission of the resolution plan has an account, or an account of a corporate debtor under the management or control of such person or of whom such person is a promoter, classified as non-performing asset in accordance with the guidelines of the Reserve Bank of India issued under the Banking Regulation Act, 1949 or the guidelines of a financial sector regulator issued under any other law for the time being in force, and at least a period of one year has lapsed from the date of such classification till the date of commencement of the corporate insolvency resolution process of the corporate debtor.

It is provided that the person shall be eligible to submit a resolution plan if such person makes payment of all overdue amounts with interest thereon and charges relating to non-performing asset accounts before submission of resolution plan.

Further proviso is an exception to clause (c) which states that nothing in this clause shall apply to a resolution applicant where such applicant is a financial entity and is not a related party to the corporate debtor.

Explanation I.- For the purposes of this proviso, the expression "related party" shall not include a financial entity, regulated by a financial sector regulator, if it is a financial creditor of the corporate debtor and is a related party of the corporate debtor solely on account of conversion or substitution of debt into equity shares or instruments convertible into equity shares or completion of such transactions as may be prescribed], prior to the insolvency commencement date.	*Non applicability of ineligibility criterion of clause (c):* *Explanation II.*— For the purposes of this clause, where a resolution applicant has an account, or an account of a corporate debtor under the management or control of such person or of whom such person is a promoter, classified as non-performing asset and such account was acquired pursuant to a prior resolution plan approved under this Code, then, the provisions of this clause shall not apply to such resolution applicant for a period of three years from the date of approval of such resolution plan by the Adjudicating Authority under this Code.

(d) has been convicted for any offence punishable with imprisonment –

(i) for two years or more under any Act specified under the Twelfth Schedule; or

(ii) for seven years or more under any law for the time being in force: Provided that this clause shall not apply to a person after the expiry of a period of two years from the date of his release from imprisonment.

Provided further that this clause shall not apply in relation to a connected person referred to in clause(iii) of Explanation I;

(e) is disqualified to act as a director under the Companies Act, 2013:

Provided that this clause shall not apply in relation to a connected person referred to in clause (iii) of Explanation I;

(f) is prohibited by the Securities and Exchange Board of India from trading in securities or accessing the securities markets;

(g) has been a promoter or in the management or control of a corporate debtor in which a preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction has taken place and in respect of which an order has been made by the Adjudicating Authority under this Code.

Exception:

It is provided that this clause shall not apply if a preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction has taken place prior to the acquisition of the corporate debtor by the resolution applicant pursuant to a resolution plan approved under this Code or pursuant to a scheme or plan approved by a financial sector regulator or a court, and such resolution applicant has not otherwise contributed to the preferential transaction, undervalued transaction, extortionate credit transaction or fraudulent transaction.

(h) has executed a guarantee in favour of a creditor in respect of a corporate debtor against which an application for insolvency resolution made by such creditor has been admitted under this Code and such guarantee has been invoked by the creditor and remains unpaid in full or part;	It may be noted that pursuant to Section 240A (1) of the Code, notwithstanding anything to the contrary contained in this Code, the provisions of clauses (c) and (h) of section 29A shall not apply to the resolution applicant in respect of corporate insolvency resolution process or pre-packaged insolvency resolution process of any micro, small and medium enterprises.

In the case of ***Saravana Global Holdings Ltd. & Another Vs. Bafna Pharmaceuticals Ltd. & Others [Civil Appeal No(s). 5344/2019],*** the Supreme Court upheld the order of the NCLAT, which had held that the CD is an MSME and the promoters are not ineligible in terms of section 29A of the IBC. Therefore, it is not necessary for the CoC to find out whether the resolution applicant is ineligible in terms of section 29A or not. *(Source: IBBI Handbook 2019)*

(i) is subject to any disability, corresponding to clauses (a) to (h), under any law in a jurisdiction outside India; or

(j) has a connected person not eligible under clauses (a) to (i).

Explanation 5 — For the purposes of this clause, the expression "connected person" means—	(i) any person who is the promoter or in the management or control of the resolution applicant; or (ii) any person who shall be the promoter or in management or control of the business of the corporate debtor during the implementation of the resolution plan; or (iii) the holding company, subsidiary company, associate company or related party of a person referred to in clauses (i) and (ii) except where such resolution applicant is a financial entity and is not a related party of the corporate debtor.

Provided further that the expression "related party" shall not include a financial entity, regulated by a financial sector regulator, if it is a financial creditor of the corporate debtor and is a related party of the corporate debtor solely on account of conversion or substitution of debt into equity shares or instruments convertible into equity shares or completion of such transactions as may be prescribed, prior to the insolvency commencement date.

Explanation II—For the purposes of this section, "financial entity" shall mean the following entities which meet such criteria or conditions as the Central Government may, in consultation with the financial sector regulator, notify in this behalf, namely: —	(a) a scheduled bank; (b) any entity regulated by a foreign central bank or a securities market regulator or other financial sector regulator of a jurisdiction outside India which jurisdiction is compliant with the Financial Action Task Force Standards and is a signatory to the International Organisation of Securities Commissions Multilateral Memorandum of Understanding; (c) any investment vehicle, registered foreign institutional investor, registered foreign portfolio investor or a foreign venture capital investor, where the terms shall have the meaning assigned to them in regulation 2 of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2017 made under the Foreign Exchange Management Act, 1999; (d) an asset reconstruction company register with the Reserve Bank of India under section 3 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002; (e) an Alternate Investment Fund registered with Securities and Exchange Board of India; (f) such categories of persons as may be notified by the Central Government.

In ***Arcelormittal India Private Limited Vs. Satish Kumar Gupta & Others [(2019) 2 SCC 1],*** the Supreme Court delved into the interpretation of section 29A of the IBC and held that the stage at which ineligibility in section

29A(c) attaches is when the resolution plan is submitted by a resolution applicant and not from the insolvency commencement date (or any other anterior point in time). The ineligibility under section 29A(c) can only be removed if the person submitting the plan pays all overdue amounts with interest thereon and charges relating to the non-performing asset in question before submitting a resolution plan. On the other hand, the ineligibility under section 29A(g) cannot be cured by paying off the debts of the corporate debtor. Persons in erstwhile management or control of the corporate debtor can become eligible to submit a resolution plan for the corporate debtor by paying off the debts of the company only if they are not disqualified under section 29A(g).

In ***Swiss Ribbons Pvt. Ltd. & Another Vs. Union of India & Others [(2019) 4 SCC 17],*** the Supreme Court examined the definition of "related party" and observed that persons who act jointly or in concert with others are connected with the business activity of the resolution applicant. Similarly, all the categories of persons mentioned in section 5(24A) (definition of related party to an individual) show that such persons must be "connected" with the resolution applicant within the meaning of section 29A(j). This being the case, the categories of persons who are collectively mentioned as a "relative" need to have a connection with the business activity of the resolution applicant. If this cannot be shown such person cannot be disqualified under section 29A(j). All the categories in this subsection deal with persons, natural as well as artificial, who are connected with the business activity of the resolution applicant. The expressions "related party" and "relative" contained in the definition sections must be read noscitur a sociis (the meaning of an unclear word or phrase should be interpreted within the context it is being used) with the categories of persons mentioned in Explanation I. So read, they would include only persons who are connected with the business activity of the resolution applicant.

The Supreme Court found that Explanation I make it clear that if a person is otherwise covered as a "connected person," this provision also covers a person who is in management or control of the business of the CD during the implementation of a resolution plan. Therefore, any such person is not indeterminate at all, but is someone who is in the saddle of the business of the CD, either at an anterior point in time or during implementation of the resolution plan. With this, the constitutionality of section 29A(j) was upheld.

The Process of Inviting and Submitting Resolution Plans

A key duty of the RP under section 25(2)(h) of the IBC is to invite prospective resolution applicants (PRAs), who fulfil such criteria as may be laid down by him with the approval of committee of creditors, having regard to the complexity and scale of operations of the business of the corporate debtor and such other conditions as may be specified by the Board, to submit a resolution plan or plans.

The details pertaining to the steps for inviting, submitting, evaluating, and approving the resolution plan (and timelines in relation to them) are detailed in the CIRP Regulations.

Below is a summary of the timelines for a resolution plan as provided in the CIRP Regulations, all of which are explained in detail thereafter:

Regulation	Action	Timeline
Reg 36A (1)	Publish brief particulars of the invitation for expression of interest in Form G of the Schedule-I.	Not later than sixtieth day from the insolvency commencement date, from interested and eligible prospective resolution applicants to submit resolution plans. Clarification: The resolution professional after the approval of the committee may invite a resolution plan for each real estate project or group of projects of the corporate debtor.
Reg 36A (3)	Last date for submission of expression of interest.	Not less than fifteen days from the date of issue of detailed invitation.
Reg 36A (10)	RP to issue a provisional list of eligible prospective resolution applicants.	Within ten days of the last date for submission of expression of interest.
Reg 36A (11)	Objection for inclusion or exclusion of a prospective RA in the provisional list.	Within five days from the date of issue of the provisional list.

Reg 36A (12)	Issue of final list of prospective resolution applicants (PRAs).	Within ten days of the last date for receipt of objections, to the committee.
Reg 36B (1)	Issue of information memorandum, evaluation matrix and a request for resolution plans.	Within five days of the date of issue of the provisional list.
Reg 36B (3)	Submission of resolution plans to the RP.	Minimum of 30 days from the date of issue of the request for resolution plans.

1. Invitation for Expression of Interest (EOI) (Regulation 36A)

An EOI is not a resolution plan but a statement by a prospective resolution applicant (PRA) indicating its interest in presenting a resolution plan for the corporate debtor. The CIRP Regulations envisage that a PRA should first submit an EOI for the corporate debtor. Only after it fulfills certain prescribed conditions and provides certain undertakings, is it given access to the Information Memorandum (IM) and relevant information. Based on the information, it can submit the resolution plan for the corporate debtor. The process for inviting and submitting the EOIs is detailed in regulation 36A of the CIRP Regulations. Broadly, the process is as follows:

(i) *Publication of EOI in Form G of Schedule-I*

Form G contains basic information about the CD, timelines for submitting the EOI, eligibility criteria, and timelines for the CIRP starting from the submission of the EOI, details of the RP, and other relevant information.

Timeline for publication: The resolution professional shall publish brief particulars of the invitation for expression of interest in Form G of the Schedule-I at the earliest, not later than sixtieth day from the insolvency commencement date, from interested and eligible prospective resolution applicants to submit resolution plans. Hence, even before the issuance of Form G, the eligibility criteria should have been drafted by the resolution professional. *{Regulation 36A(1)}*

Regulation 36A (2):

The resolution professional shall publish Form G

(i) in one English and one regional language newspaper with wide circulation at the location of the registered office and principal office, if any, of the corporate debtor and any other location where in the opinion of the resolution professional, the corporate debtor conducts material business operations;

(ii) on the website, if any, of the corporate debtor;

(iii) on the website, if any, designated by the Board for the purpose; and

(iv) in any other manner as may be decided by the committee.

Mandatory contents of Form G:

The Form G in the Schedule-I shall -

(a) state where the detailed invitation for expression of interest can be downloaded or obtained from, as the case may be; and

(b) provide the last date for submission of expression of interest which shall not be less than fifteen days from the date of issue of detailed invitation. *{Regulation 36A (3)}*

(ii) *Detailed invitation for EOIs*

{Regulation 36A (4)}

The detailed invitation referred to in sub-regulation (3) shall-

(a) specifies the criteria for prospective resolution applicants, as approved by the committee in accordance with clause (h) of sub-section (2) of section 25;

(b) state the ineligibility norms under section 29A to the extent applicable for prospective resolution applicants;

(c) provide such basic information about the corporate debtor as may be required by a prospective resolution applicant for expression of interest; and

(d) not require payment of any fee or any non-refundable deposit for submission of expression of interest.

(iii) *Modification in EoI:* Any modification in the invitation for expression of interest may be made in the manner as the initial invitation for expression of interest was made but it is provided that such modification shall not be made more than once. *{Regulation 36A(4A)}*

(iv) *Submission of EoI:* A prospective resolution applicant, who meet the requirements of the invitation for expression of interest, may submit expression of interest within the time specified in the invitation under clause (b) of sub-regulation (3). *{Regulation 36A(5)}*

(v) *Delay EoI to be rejected:* The expression of interest received after the time specified in the invitation under clause (b) of sub-regulation (3) shall be rejected. *{Regulation 36A(6)}*

(vi) Documents accompanying EoI:

An expression of interest shall be unconditional and be accompanied by- {Regulation 36A(7)}

(a) an undertaking by the prospective resolution applicant that it meets the criteria specified by the committee under clause (h) of sub-section (2) of section 25;

(b) relevant records in evidence of meeting the criteria under clause (a);

(c) an undertaking by the prospective resolution applicant that it does not suffer from any ineligibility under section 29A to the extent applicable;

(d) relevant information and records to enable an assessment of ineligibility under clause (c);

(e) an undertaking by the prospective resolution applicant that it shall intimate the resolution professional forthwith if it becomes ineligible at any time during the corporate insolvency resolution process;

(f) an undertaking by the prospective resolution applicant that every information and records provided in expression of interest is true and correct and discovery of any false information or record at any time will render the applicant ineligible to submit resolution plan, forfeit any refundable deposit, and attract penal action under the Code; and (g) an undertaking by the prospective resolution applicant to the effect that it shall maintain confidentiality of the information and shall not use such information to cause an undue gain or undue loss to itself or any other person and comply with the requirements under sub-section (2) of section 29.

(vii) *Due Diligence by RP:* The resolution professional shall conduct due diligence based on the material on record in order to san tisfy that the prospective resolution applicant complies with-

(a) the provisions of clause (h) of sub-section (2) of section 25;

(b) the applicable provisions of section 29A, and

(c) other requirements, as specified in the invitation for expression of interest. *{Regulation 36A (8)}*

(viii) *Right of RP to seek clarification or additional information:* The resolution professional may seek any clarification or additional information or document from the prospective resolution applicant for conducting due diligence under sub-regulation (8). *{Regulation 36A (9)}*

(ix) *Issue of Provisional List of eligible prospective resolution applicants:* The resolution professional shall issue a provisional list of eligible prospective resolution applicants within ten days of the last date for submission of expression of interest to the committee and to all prospective resolution applicants who submitted the expression of interest. *{Regulation 36A (10)}*

(x) *Objection for inclusion or exclusion of a prospective RA in the provisional list:* Any objection to inclusion or exclusion of a prospective resolution applicant (RA) in the provisional list referred to in sub-regulation (10) may be made with supporting documents within five days from the date of issue of the provisional list. *{Regulation 36A (11)}*

(xi) *Issue of final list of PRAs:* On considering the objections received under sub-regulation (11), the resolution professional shall issue the final list of prospective resolution applicants (PRAs) within ten days of the last date for receipt of objections, to the committee. *{Regulation 36A (12)}*

2. Request For Resolution Plans (RFRP) (Regulation 36B)

Once the process of receiving and considering EOIs is complete, the RP needs to start the process of requesting resolution plans. This process is detailed in regulation 36B of the CIRP Regulations, which deals with the request for resolution plans (RFRP) (sometimes referred as a process note) and other incidental matters.

(i) *Issue of information memorandum, evaluation matrix and a request for resolution plans:*

The resolution professional shall, within five days of the date of issue of the final list under regulation 36A(12), issue the information memorandum, evaluation matrix and a request for resolution plans to every resolution applicant in the final list:

Provided that where such documents are available, the same may also be provided to every prospective resolution applicant in the provisional list. {(Regulation 36B (1)}

(ii) *RFRP mandatory contents:* The request for resolution plans shall detail each step in the process, and the manner and purposes of interaction between the resolution professional and the prospective resolution applicant, along with corresponding timelines. [Regulation 36B(2)]

(iii) *Time to submit resolution plan:* The request for resolution plans shall allow prospective resolution applicants a minimum of thirty days to submit the resolution plan(s). [Regulation 36B (3)]

(iv) *RFRP not to require non-refundable deposit:* The request for resolution plans shall not require any non-refundable deposit for submission of or along with resolution plan. {(Regulation 36B(4)} Both the EOI and the RFRP provisions refer to a “non-refundable deposit.” In practice, especially at the stage of submitting the resolution plan, the RFRP would require a refundable bank guarantee or deposit to ensure that only serious contenders who have the ability to implement the resolution plan submit one and participate in the negotiation process.

(v) *Performance security:* The request for resolution plans shall require the resolution applicant, in case its resolution plan is approved under sub-section (4) of section 30, to provide a performance security within the time specified therein and such performance security shall stand forfeited if the resolution applicant of such plan, after its approval by the Adjudicating Authority, fails to implement or contributes to the failure of implementation of that plan in accordance with the terms of the plan and its implementation schedule. [Regulation 36B(4A)]

Explanation I.– For the purposes of this sub-regulation, "performance security" shall mean security of such nature, value, duration and source, as may be specified in the request for resolution plans with the approval of the committee, having regard to the nature of resolution plan and business of the corporate debtor.

In the case of ***Tata Steel Ltd Vs. Liberty House Group Pte Ltd. & Others***

The CoC gave equal opportunity to all three RAs to submit improved financial offer. Instead of filing an improved financial offer, the appellant filed an application before the NCLAT for restraining the RP and the CoC from considering improved financial offer. The NCLAT noted that the process document does not curtail the powers of the CoC to maximise value and as per the process document, the CoC has absolute discretion, but without being under any obligation, to update, amend or supplement the information, assessment or assumptions and right to change, update, amend, supplement, modify, add to, delay or otherwise annul or cease the resolution process at any point in time. It observed that granting more opportunity to all the eligible resolution applicants to revise their financial offers, even by giving more opportunity, is permissible in law. However, all such process should be complete within the time frame.

Source: IBBI Handbook 2019

(vi) *Modification in RFRP:* Any modification in the request for resolution plan or the evaluation matrix issued under sub-regulation (1), shall be deemed to be a fresh issue and shall be subject to timeline under sub-regulation (3). It is provided that such modifications shall not be made more than once. [Regulation 36B(5)]

(vii) *Extension of time for submission of resolution plan:* The resolution professional may, with the approval of the committee, extend the timeline for submission of resolution plans. [Regulation 36B(6)]

(viii) *Issue of request for resolution plan for asset wise sale of CD:* If the resolution professional, does not receive a resolution plan in response to the request under this regulation, he may, with the approval of the committee, issue request for resolution plan for sale of one or more of assets of the corporate debtor. [Regulation 36B(6A)]

(ix) *Reissue of RFRP:* The resolution professional may, with the approval of the committee, re-issue request for resolution plans, if the resolution plans received in response to an earlier request are not satisfactory, subject to the condition that the request is made to all prospective resolution applicants in the final list: Provided that provisions of sub-regulation (3) (the 30-day minimum timeline to submit the resolution plan) shall not apply for submission of resolution plans under this sub-regulation. [Regulation 36B(7)]

Can insolvency proceedings be withdrawn even after invitation of Resolution Plan?

In the matter of ***'Brilliant Alloys Pvt. Ltd. v. Mr. S. Rajagopal & Ors.',*** the Supreme Court held that Regulation 30A of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 has to be read subject to Section 12A of the Insolvency and Bankruptcy code, 2016 which does not impose the condition that withdrawal application has to be filed before the invitation of expression of interest. Thus, the Apex Court upheld withdrawal of CIRP even after the Resolution Professional issued invitation for expression of interest from resolution applicants to submit resolution plans under Regulation 36A of IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016.

3. Strategy for Marketing of Assets of the Corporate Debtor (Regulation 36C)

Regulation 36 C was inserted in the CIRP Regulations by IBBI vide notification dated 16th September, 2022 (w.e.f. 16-09-2022) for maximising the value of CD under CIRP. It has following provisions:

(1) The resolution professional shall prepare a **strategy for marketing of the assets** of the corporate debtor in consultation with the committee, **where the total assets as per the last available financial statements exceed one hundred crore rupees** and may prepare such strategy in other cases.

(2) Decision of implementing such strategy along with its cost shall be subject to the approval of the committee.

(3) The member(s) of committee may also take measures for marketing of the assets of the corporate debtor.

Resolution Plan (Regulation 37)

A resolution plan shall provide for the measures, as may be necessary, for insolvency resolution of the corporate debtor for maximization of value of its assets, including but not limited to the following: -

(a) transfer of all or part of the assets of the corporate debtor to one or more persons;

(b) sale of all or part of the assets whether subject to any security interest or not;

(ba) restructuring of the corporate debtor, by way of merger, amalgamation and demerger;

(c) the substantial acquisition of shares of the corporate debtor, or the merger or consolidation of the corporate debtor with one or more persons;

(ca) cancellation or delisting of any shares of the corporate debtor, if applicable;

(d) satisfaction or modification of any security interest;

(e) curing or waiving of any breach of the terms of any debt due from the corporate debtor;

(f) reduction in the amount payable to the creditors;

(g) extension of a maturity date or a change in interest rate or other terms of a debt due from the corporate debtor;

(h) amendment of the constitutional documents of the corporate debtor;

(i) issuance of securities of the corporate debtor, for cash, property, securities, or in exchange for claims or interests, or other appropriate purpose;

(j) change in portfolio of goods or services produced or rendered by the corporate debtor;

(k) change in technology used by the corporate debtor; and

(l) obtaining necessary approvals from the Central and State Governments and other authorities.

(m) sale of one or more assets of corporate debtor to one or more successful resolution applicants submitting resolution plans for such assets; and manner of dealing with remaining assets.

In the case of ***Edelweiss Asset Reconstruction Company Ltd. Vs. Synergies Dooray Automotive Ltd. & Others [Company Appeal (AT) (Insolvency) No. 169 to 173 of 2017],*** the AA's order dated August 2, 2017, approving a resolution plan was challenged on the basis that the resolution plan provided for merger and amalgamation, which is not permissible as it violates section 30(2)(e) of the IBC. It was noted that a resolution plan may provide for merger or consolidation of the corporate debtor with one or more persons in terms of regulation 37(1)(c) of the CIRP Regulations. The NCLAT held: "The I&B Code is a code by itself and section 238 provides overriding effect of it over the provisions of the other Acts, if any of the provisions of an Act is in conflict with the provisions of the I&B Code."

The Evaluation Matrix

The evaluation matrix is defined in the CIRP Regulations (regulation 2(1) (ha)) as such parameters to be applied and the manner of applying such parameters, as approved by the CoC, for consideration of resolution plans for its approval.

The evaluation matrix is required to be shared with the PRAs along with the RFRP.

This matrix lists the criteria on which the resolution plans will be evaluated by the CoC. The matrix sets out the parameters to be applied (and the manner of applying them), as laid down by the CoC, for resoluplans being considered for approval. This enables the CoC to use the criteria stated in the matrix to compare one resolution plan with another. This ensures more transparency in the evaluation process, reducing the possibilities of challenges to the process. The CoC should think carefully about the contents of the evaluation matrix, avoiding generic statements that may be subjective and difficult to follow.

Submission of Resolution Plan

Once the RFRP, IM, and evaluation matrix are provided to the prospective resolution applicants (PRAs), they undertake diligence of the CD and submit the resolution plan to the RP as per the provisions of the IBC, CIRP Regulations, and RFRP. Section 30 of the Code prescribes the manner in which are resolution plan may be submitted by a resolution applicant.

1. Documents accompanying Resolution Plan

   Affidavit for eligibility u/s 29A to be filed with RP: A resolution applicant may submit a resolution plan along with an affidavit stating that he is eligible under section 29A to the resolution professional prepared on the basis of the information memorandum. {Section 30(1)}

2. Modification in the resolution plan*:*

   The resolution professional may, if envisaged in the request for resolution plan-

   (a) allow modification of the resolution plan received under sub-regulation (1), but not more than once; or

   (b) use a challenge mechanism to enable resolution applicants to improve their plans.

   {Regulation 39 (1A)}

3. Examination of resolution plan by Resolution Professional

   Section 30(2) of the Code provides that the resolution professional shall examine each resolution plan received by him to confirm that each resolution plan –

   (a) provides for the payment of insolvency resolution process costs in a manner specified by the Board in priority to the payment] of other debts of the corporate debtor;

   (b) provides for the payment of debts of operational creditors in such manner as may be specified by the Board which shall not be less than-

      (i) the amount to be paid to such creditors in the event of a liquidation of the corporate debtor under section 53; or

      (ii) the amount that would have been paid to such creditors, if the amount to be distributed under the resolution plan had been distributed in accordance with the order of priority in sub-section (1) of section 53 whichever is higher, and Each resolution plan shall provide for the payment of debts of financial creditors, who do not vote in favour of the resolution plan, in such manner as may be specified by the Board, which shall not be less than the amount to be paid to such creditors in accordance with sub-section (1) of section 53 in the event of a liquidation of the corporate debtor.

   (c) provides for the management of the affairs of the corporate debtor after approval of the resolution plan;

   (d) the implementation and supervision of the resolution plan;

   (e) does not contravene any of the provisions of the law for the time being in force

   (f) conforms to such other requirements as may be specified by the Board.

Further explanations for clause (b) is provided as:

Explanation 1. — For removal of doubts, it is hereby clarified that a distribution in accordance with the provisions of this clause shall be fair and equitable to such creditors.

Explanation 2. — For the purpose of this clause, it is hereby declared that on and from the date of commencement of the Insolvency and Bankruptcy Code (Amendment) Act, 2019, the provisions of this clause shall also apply to the corporate insolvency resolution process of a corporate debtor- (i) where a resolution plan has not been approved or rejected by the Adjudicating Authority; (ii) where an appeal has been preferred under section 61 or section 62 or such an appeal is not time barred under any provision of law for the time being in force; or (iii) where a legal proceeding has been initiated in any court against the decision of the Adjudicating Authority in respect of a resolution plan;

Deemed approval of shareholders

Explanation. — For the purposes of clause (e), if any approval of shareholders is required under the Companies Act, 2013 or any other law for the time being in force for the implementation of actions under the resolution plan, such approval shall be deemed to have been given and it shall not be a contravention of that Act or law.

Regulation 38 of CIRP Regulations provides for mandatory contents of the resolution plan as follows:		
(1) The amount payable under a resolution plan – (a) to the operational creditors shall be å paid in priority over financial creditors; and (b) to the financial creditors, who have a right to vote under sub-section (2) of section 21 and did not vote in favour of the resolution plan, shall be paid in priority over financial creditors who voted in favour of the plan. (1A) A resolution plan shall include a statement as to how it has dealt with the interests of all stakeholders, including financial creditors and operational creditors, of the corporate debtor. (1B) A resolution plan shall include a statement giving details if the resolution applicant or any of its related parties has failed to implement or contributed to the failure of implementation of any other resolution plan approved by the Adjudicating Authority at any time in the past.	(2) A resolution plan shall provide: (a) the term of the plan and its implementation schedule; (b) the management and control of the business of the corporate debtor during its term; and (c) adequate means for supervising its implementation,; (d) provides for the manner in which proceedings in respect of avoidance transactions, if any, under Chapter III or fraudulent or wrongful trading under Chapter VI of Part II of the Code, will be pursued after the approval of the resolution plan and the manner in which the proceeds, if any, from such proceedings shall be distributed: Provided that this clause shall not apply to any resolution plan that has been submitted to the Adjudicating Authority under sub-section (6) of section 30 on or before the date of commencement of the IBBI (Insolvency Resolution Process for Corporate Persons) (Second Amendment) Regulations, 2022.	(3) A resolution plan shall demonstrate that – (a) it addresses the cause of default; (b) it is feasible and viable; (c) it has provisions for its effective implementation; (d) it has provisions for approvals required and the timeline for the same; and (e) the resolution applicant has the capability to implement the resolution plan.

The committee may consider the requirement of a monitoring committee for the implementation of the resolution plan.

Where the committee considers that a monitoring committee for the implementation of the resolution plan is required, it may, while approving the resolution plan, decide to constitute the same with the resolution professional or propose another insolvency professional, or any other person as its members:

Provided that where the resolution professional is proposed to be part of the monitoring committee, the monthly fee payable to him shall not exceed the monthly fee received by him during the corporate insolvency resolution process.

Approval of resolution plan by Committee of Creditors (CoC)

According to section 30 (3) of the Code, the resolution professional shall present to the committee of creditors for its approval such resolution plans which confirm the conditions referred to in sub-section (2).

Regulation 39(2) of CIRP Regulations provides that the resolution professional shall submit to the committee all resolution plans which comply with the requirements of the Code and regulations made thereunder along with the details of following transactions, if any, observed, found or determined by him: -

(a) preferential transactions under section 43;

(b) undervalued transactions under section 45;

(c) extortionate credit transactions under section 50; and

(d) fraudulent transactions under section 66, and the orders, if any, of the adjudicating authority in respect of such transactions.

Regulation 39(1B) of CIRP Regulations provide for that the committee shall not consider any resolution plan- (a) received after the time as specified by the committee under regulation 36B; or (b) received from a person who does not appear in the final list of prospective resolution applicants; or (c) does not comply with the provisions of sub-section (2) of section 30 and sub-regulation (1).

Regulation 39(3) provides that the committee shall-

(a) evaluate the resolution plans received under sub-regulation (2) as per evaluation matrix;

(b) record its deliberations on the feasibility and viability of each resolution plan; and

(c) vote on all such resolution plans simultaneously.

Approval of Resolution Plan

- Section 30(4) of the Code provides that the committee of creditors may approve a resolution plan by a vote **of not less than sixty-six per cent** of voting share of the financial creditors, after considering its feasibility and viability, the manner of distribution proposed, which may take into account the order of priority amongst creditors as laid down in sub-section (1) of section 53, including the priority and value of the security interest of a secured creditor and such other requirements as may be specified by the Board:

  Provided that the committee of creditors shall not approve a resolution plan, submitted before the commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2017, where the resolution applicant is ineligible under section 29A and may require the resolution professional to invite a fresh resolution plan where no other resolution plan is available with it:

Provided further that where the resolution applicant referred to in the first proviso is ineligible under clause (c) of section 29A, the resolution applicant shall be allowed by the committee of creditors such period, not exceeding thirty days, to make payment of overdue amounts in accordance with the proviso to clause (c) of section 29A:

Provided also that nothing in the second proviso shall be construed as extension of period for the purposes of the proviso to sub-section (3) of section 12, and the corporate insolvency resolution process shall be completed within the period specified in that sub-section:

Provided also that the eligibility criteria in section 29A as amended by the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018 shall apply to the resolution applicant who has not submitted resolution plan as on the date of commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018.

Regulation 39(3A) and Regulation 39(3B) of CIRP Regulations provide for criterion for approval of resolution plan by CoC as follows:

Where only one resolution plan is put to vote, it shall be considered approved if it receives requisite votes.

Where two or more resolution plans are put to vote simultaneously, the resolution plan, which receives the highest votes, but not less than requisite votes, shall be considered as approved.

Where two or more resolution plans receive equal votes, but not less than requisite votes, the committee shall approve any one of them, as per the tie-breaker formula announced before voting.

Where none of the resolution plans receives requisite votes, the committee shall again vote on the resolution plan that received the highest votes, subject to the timelines under the Code.

<table>
<tr><td colspan="4">Illustration. - The committee is voting on two resolution plans, namely, A and B, simultaneously. The voting outcome is as under:</td></tr>
<tr><td rowspan="2">Voting outcome</td><td colspan="2">% of votes in favour of</td><td rowspan="2">Status of approval</td></tr>
<tr><td>Plan A</td><td>Plan B</td></tr>
<tr><td>1.</td><td>55</td><td>60</td><td>No Plan is approved, as neither of the Plans received requisite votes. The committee shall vote again on Plan B, which received the higher votes, subject to the timelines under the Code.</td></tr>
<tr><td>2.</td><td>70</td><td>75</td><td>Plan B is approved, as it received higher votes, which is not less than requisite votes.</td></tr>
<tr><td>3.</td><td>75</td><td>75</td><td>The committee shall approve either Plan A or Plan B, as per the tie-breaker formula announced before voting.</td></tr>
</table>

Can resolution applicant attend meeting of CoC considering resolution plan?

The resolution applicant may attend the meeting of the committee of creditors in which the resolution plan of the applicant is considered. {Section 30(5)}

Provided that the resolution applicant shall not have a right to vote at the meeting of the committee of creditors unless such resolution applicant is also a financial creditor.

Submission of resolution plan to CoC:

- *Section* 30(6) of the Code provides that the resolution professional shall submit the resolution plan as approved by the committee of creditors to the Adjudicating Authority.
- *Timeline for submission of Resolution plan approved by CoC:* Regulation 39(4) of the Code provides that the resolution professional shall endeavour to submit the resolution plan approved by the committee to the Adjudicating Authority at least fifteen days before the maximum period for completion of corporate insolvency resolution process under section 12, along with a compliance certificate in Form H of the Schedule-I and the evidence of receipt of performance security required under sub-regulation (4A) of regulation 36B.

According to Section 30 –

- A resolution applicant to file an affidavit stating that it is eligible under section 29A.
- Added an Explanation to sub-section (2) of section 30 to clarify that if any approval of shareholders is required under the Companies Act, 2013 or any other law for the time being in force for the implementation of actions under the resolution plan, such approval shall be deemed to have been given and it shall not be a contravention of that Act or law.
- Substituted sub-section (4) of section 30, inter alia, reducing the threshold for voting from 75% to 66% for approving a resolution plan by committee of creditors.

The request for resolution plans shall require the resolution applicant, in case its resolution plan is approved under sub-section (4) of section 30, to provide a performance security within the time specified therein and such performance security shall stand forfeited if the resolution applicant of such plan, after its approval by the Adjudicating Authority, fails to implement or contributes to the failure of implementation of that plan in accordance with the terms of the plan and its implementation schedule. {Regulation 36B(4A)}

Approval of resolution plan by AA (Section 31)

Approval of resolution plan by the Adjudicating Authority (AA) {Section 31(1)}:

- If the Adjudicating Authority is satisfied that the resolution plan as approved by the committee of creditors under sub-section (4) of section 30 meets the requirements as referred to in sub-section (2) of section 30, it shall by order approve the resolution plan.
- Resolution plan, so approved, shall be binding on the corporate debtor and its employees, members, creditors, including the Central Government, any State Government or any local authority to whom a debt in respect of the payment of dues arising under any law for the time being in force, such as authorities to whom statutory dues are owed, guarantors and other stakeholders involved in the resolution plan.
- It is provided that the Adjudicating Authority shall, before passing an order for approval of resolution plan under this sub-section, satisfy that the resolution plan has provisions for its effective implementation.

Rejection of resolution plan by the Adjudicating Authority {Section 31(2)}:

- Where the Adjudicating Authority is satisfied that the resolution plan does not confirm to the requirements referred to in sub-section (1), it may, by an order, reject the resolution plan.

Consequences of Approval of Resolution Plan {Section 31(3)}: After the order of approval under sub-section (1), -

(a) the moratorium order passed by the Adjudicating Authority under section 14 shall cease to have effect; and

(b) the resolution professional shall forward all records relating to the conduct of the corporate insolvency resolution process and the resolution plan to the Board to be recorded on its.

Duty of Resolution Applicant to obtain necessary approval {Section 31(4)}: The resolution applicant shall, pursuant to the resolution plan approved under sub-section (1), obtain the necessary approval required under any law for the time being in force within a period of one year from the date of approval of the resolution plan by the Adjudicating Authority under sub-section (1) or within such period as provided for in such law, whichever is later:

Provided that where the resolution plan contains a provision for combination, as referred to in section 5 of the Competition Act, 2002, the resolution applicant shall obtain the approval of the Competition Commission of India under that Act prior to the approval of such resolution plan by the committee of creditors.

Provisions of Regulation 39 of CIRP Regulations:

- The resolution professional shall forthwith send a copy of the order of the Adjudicating Authority approving or rejecting a resolution plan to the participants and the resolution applicant. *{Regulation 39(5)}*

- The resolution professional shall, within fifteen days of the order of the Adjudicating Authority approving a resolution plan, intimate each claimant, the principle or formulae, as the case may be, for payment of debts under such resolution plan.

- It is provided that this sub-regulation shall apply to every corporate insolvency resolution process ongoing and commencing on or after the date of commencement of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) (Fifth Amendment) Regulations, 2020; *{Regulation 39(5A)}*

- A provision in a resolution plan which would otherwise require the consent of the members or partners of the corporate debtor, as the case may be, under the terms of the constitutional documents of the corporate debtor, shareholders' agreement, joint venture agreement or other document of a similar nature, shall take effect notwithstanding that such consent has not been obtained. *{Regulation 39(6)}*

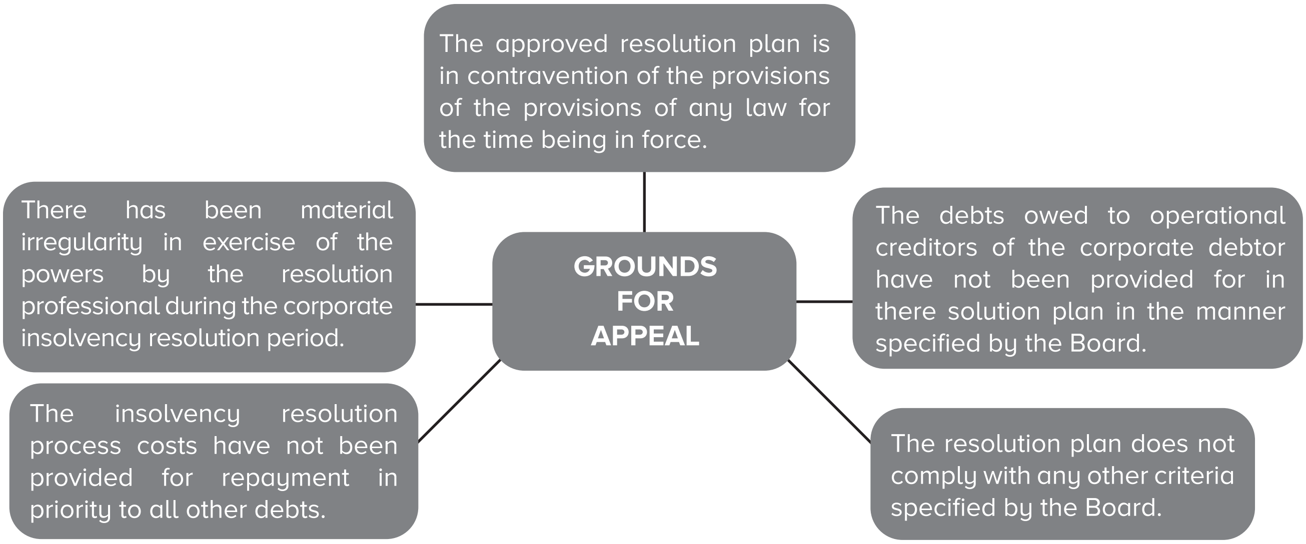
- No proceedings shall be initiated against the interim resolution professional or the resolution professional, as the case may be, for any actions of the corporate debtor, prior to the insolvency commencement date. *{Regulation 39(7)}*

- A person in charge of the management or control of the business and operations of the corporate debtor after a resolution plan is approved by the Adjudicating Authority, may make an application to the Adjudicating Authority for an order seeking the assistance of the local district administration in implementing the terms of a resolution plan. *{Regulation 39(8)}*

- A creditor, who is aggrieved by non-implementation of a resolution plan approved under sub-section (1) of section 31, may apply to the Adjudicating Authority for directions. *{Regulation 39(9)}*

Appeal (Section 32)

Any appeal from an order approving the resolution plan shall be in the manner and on the grounds laid down in sub-section (3) of section 61.



Section 61(3) of the Code provides that an appeal against an order approving a resolution plan under section 31 may be filed on the following grounds, namely: –

(i) the approved resolution plan is in contravention of the provisions of any law for the time being in force;

(i) there has been material irregularity in exercise of the powers by the resolution professional during the corporate insolvency resolution period;

(iii) the debts owed to operational creditors of the corporate debtor have not been provided for in the resolution plan in the manner specified by the Board;

(iv) the insolvency resolution process costs have not been provided for repayment in priority to all other debts; or

(v) the resolution plan does not comply with any other criteria specified by the Board.

Liability for Prior Offences (Section 32A)

Section 32A provides relief to the resolution applicant or the persons who shall be in charge of the management of the company in the future by way of immunity from the liability of offences that the promoters or the persons in charge of the corporate debtor had committed prior to the initiation of CIRP, subject to certain conditions. The Section also bars any action being taken against the property of the corporate debtor pursuant to an offence committed prior to the CIRP, subject to the condition that the property is covered under the resolution plan approved by the AA or sale under liquidation and the resolution plan should have resulted in change in management/control of the corporate debtor such that debarred persons are not in management/control of the corporate debtor post resolution. However, the immunity is not provided for the property of any other person, other than the corporate debtor. The Section further provides that notwithstanding the immunity given in sub-sections (1) & (2), the corporate debtor or any person who may be required to extend assistance/co-operation to any authority investigating an offence committed prior to the commencement of CIRP, has been mandated to assist and co-operate accordingly.

(1) *Immunity to Corporate Debtor from pre CIRP offences:* Notwithstanding anything to the contrary contained in this Code or any other law for the time being in force, the liability of a corporate debtor for an offence committed prior to the commencement of the corporate insolvency resolution process shall cease, and the corporate debtor shall not be prosecuted for such an offence from the date the resolution plan has been approved by the Adjudicating Authority under section 31, if the resolution plan results in the change in the management or control of the corporate debtor to a person who was not-

(a) a promoter or in the management or control of the corporate debtor or a related party of such a person; or

(b) a person with regard to whom the relevant investigating authority has, on the basis of material in its possession, reason to believe that he had abetted or conspired for the commission of the offence, and has submitted or filed a report or a complaint to the relevant statutory authority or Court:

Provided that if a prosecution had been instituted during the corporate insolvency resolution process against such corporate debtor, it shall stand discharged from the date of approval of the resolution plan subject to requirements of this sub-section having fulfilled:

Provided further that every person who was a “designated partner” as defined in clause (j) of section 2 of the Limited Liability Partnership Act, 2008 or an “officer who is in default”, as defined in clause (60) of section 2 of the Companies Act, 2013, or was in any manner in-charge of, or responsible to the corporate debtor for the conduct of its business or associated with the corporate debtor in any manner and who was directly or indirectly involved in the commission of such offence as per the report submitted or complaint filed by the investigating authority, shall continue to be liable to be prosecuted and punished for such an offence committed by the corporate debtor notwithstanding that the corporate debtor’s liability has ceased under this sub-section.

(2) Property covered under resolution plan approved by AA also immune from pre-CIRP offences: No action shall be taken against the property of the corporate debtor in relation to an offence committed prior to the commencement of the corporate insolvency resolution process of the corporate debtor, where such property is covered under a resolution plan approved by the Adjudicating Authority under section 31, which results in the change in control of the corporate debtor to a person, or sale of liquidation assets under the provisions of Chapter III of Part II of this Code to a person, who was not -

(i) a promoter or in the management or control of the corporate debtor or a related party of such a person; or

(ii) a person with regard to whom the relevant investigating authority has, on the basis of material in its possession, reason to believe that he had abetted or conspired for the commission of the offence, and has submitted or filed a report or a complaint to the relevant statutory authority or Court.

Explanation- For the purposes of this sub-section, it is hereby clarified that, -

(i) an action against the property of the corporate debtor in relation to an offence shall include the attachment, seizure, retention or confiscation of such property under such law as may be applicable to the corporate debtor;

(ii) nothing in this sub-section shall be construed to bar an action against the property of any person, other than the corporate debtor or a person who has acquired such property through corporate insolvency resolution process or liquidation process under this Code and fulfils the requirements specified in this section, against whom such an action may be taken under such law as may be applicable.

(3) Assistance by CD to investigating authority: Subject to the provisions contained in sub-sections (1) and (2), and notwithstanding the immunity given in this section, the corporate debtor and any person, who may be required to provide assistance under such law as may be applicable to such corporate debtor or person, shall extend all assistance and co-operation to any authority investigating an offence committed prior to the commencement of the corporate insolvency resolution process.

CASE LAWS

1. Principles for a Resolution Plan

   The National Company Law Appellate Tribunal (NCLAT), in the matter of ***Binani Industries Limited v. Bank of Baroda & Anr.,*** while approving the revised resolution plan submitted by Ultratech Cement Limited in the insolvency resolution process initiated against the corporate debtor-Binani Cement Limited, laid down certain principles that a resolution plan should comply with. These include, inter alia that:

   (a) Functionally, the resolution plan shall resolve insolvency, maximise the value of assets of the corporate debtor, and promote entrepreneurship, availability of credit, and balance the interests of all the stakeholders. The resolution plan is not a sale, or auction, or recovery or liquidation but a resolution of the Corporate Debtor as a going concern.

   (b) A resolution process under IBC is not an auction. Feasibility and viability of a 'Resolution Plan' are not amenable to bidding or auction. It requires application of mind by the 'Financial Creditors' who understand the business well.

   (c) A resolution process under IBC is not recovery. Recovery is an individual effort by a creditor to recover its dues through a process that has debtor and creditor on opposite sides. The 'I&B Code' prohibits and discourages recovery.A resolution process is not a liquidation. The IBC does not allow liquidation of a Corporate Debtor directly and permits liquidation only on failure of the resolution process.

   (d) The IBC aims to balance the interests of all stakeholders and does not maximise value for financial creditors. Therefore, the dues of operational creditors must get at least similar treatment as compared to the due of financial creditors.

   (e) Any resolution plan if shown to be discriminatory against one or other financial creditor or the operational creditor, can be held to be against the provisions of IBC.

   The Supreme Court, dismissed an appeal against the NCLAT order. The NCLAT order is significant since it clarifies the underlying principles that a resolution plan should comply with.

2. Former directors of Corporate Debtor are entitled to receive Resolution Plan

   In the matter of ***Vijay Kumar Jain v. Standard Chartered Bank and others,*** an appeal was filed with Supreme Court against orders rejecting the prayer of an erstwhile director for getting copy of the resolution plans from the RP. Both the NCLT and NCLAT ruled that appellant had no right to receive the resolution plans.

   The Resolution Professional (RP) has contended that only the members of CoC are entitled to have resolution plans, as per Section 30(3) IBC read with Regulation 39(2) CIRP Regulations. Relying on the Notes on Clauses to Section 24 of the Code, they argued that the members of suspended Board of Directors are permitted to participate in CoC meetings only for the purpose of giving information regarding the financial status of the debtor.

   The Supreme Court expressly rejected the argument based on Notes on Clauses to Section 24 of the Code and noted that every participant is entitled to a notice of every meeting of the committee of creditors. Such notice of meeting must contain an agenda of the meeting, together with the copies of all documents relevant for matters to be discussed and the issues to be voted upon at the meeting vide Regulation 21(3)(iii). Court said the expression "documents" is a wide expression which would certainly include resolution plans.

   The judgment also clarified that the RP can take an undertaking from the erstwhile director to maintain confidentiality of the information.

3. Whether NCLAT can direct successful resolution applicant to modify its resolution plan?

   In ***Maharashtra Seamless Limited Vs. Padmanabhan Venkatesh and Others [Civil Appeal No. 4242 of 2019, 2020 SCC Online SC 67],*** an appeal was preferred against an order passed by the NCLAT wherein it had directed the successful resolution applicant to modify its resolution plan because the value of the resolution plan was lower than the liquidation value of the CD. The Supreme Court observed that the IBC and its underlying provisions do not provide that the resolution applicant has to match the liquidation value and that the object behind the valuation process is to assist the CoC to take a decision on the resolution plan. Relying on the Essar judgment, the Supreme Court held that the court ought to cede ground to the commercial wisdom of the creditors rather than assess the resolution plan on the basis of quantitative analysis.

4. In *Committee of Creditors of* ***Essar Steel India Limited Through Authorised Signatory Vs. Satish Kumar Gupta & Others [Civil Appeal No. 8766-67/2019 Diary No. 24417/2019 with other Civil Appeals and WP(C)s],*** the Supreme Court provided clarity on the roles of various stakeholders, namely the RP, the resolution applicant, the CoC, and the AA and the NCLAT, regarding the resolution plan in a CIRP and settled the following among other issues:

   Subrogation: Section 31(1) makes it clear that once a resolution plan is approved by the CoC, it shall be binding on all stakeholders, including guarantors. This provision ensures that the successful resolution applicant starts running the business of the CD on a fresh slate as it were. It is difficult to accept the argument that, the part of the resolution plan which states that the claims of the guarantor on account of subrogation shall be extinguished, cannot be applied to the guarantees furnished by the erstwhile directors of the CD.

   Claims: All claims must be submitted to and decided by the RP so that a prospective resolution applicant knows exactly what must be paid in order that it may then take over and run the business of the CD. A successful resolution applicant cannot suddenly be faced with “undecided” claims after the resolution plan submitted by him has been accepted as this would amount to a hydra head popping up which would throw into uncertainty amounts payable by it.

   (Source: IBBI 2019 Handbook)

5. In ***Hem Singh Bharana Vs. Pawan Doot Estate Pvt. Ltd. & Ors. [CA (AT) (Ins.) No. 1481 of 2022]***, During pendency of approval of the resolution plan before the AA, ex-promoter submitted revised settlement proposal under section 12A of the Code and filed an application seeking to keep the resolution in abeyance. As the AA rejected the said application, an appeal was filed before the NCLAT on the ground that there is no bar on CoC in accepting the settlement proposal under section 12A even if they have already approved a resolution plan. The NCLAT dismissed the appeal while relying on the judgment of SC in ***Ebix Singapore Pvt. Ltd. V. Committee of Creditors of Eudcomp Solutions Limited and Anr.***, wherein it was held that after approval of a resolution plan by the CoC, it itself is bound by its decision and cannot be allowed to go back from its decision.

6. In ***Hindalco Industries Ltd. Vs. Hirakud Industrial Works Ltd. & Ors. [CA AT (Ins.) No. 42,43,52 and 53 of 2022]*** the resolution plan approved by the AA was challenged on the grounds of fraudulent initiation of CIRP and illegal constitution of CoC. The NCLAT quashed the resolution plan and observed that the CoC was formed without admission and verification of claims of the FCs; thereby, violating CIRP Regulations. It observed that collusion existed between FC and CD, as they belonged to the same group. The inter-connections existed between the CD, FC, members of CoC and the holding companies of the successful resolution applicant (SRA) through common directors sitting on the board of more than one company with common registered addresses and email ids. The NCLAT imposed penalty on FC and CD and ordered for a complete investigation by IBBI.

7. In ***Jindal Stainless Ltd. Vs. Shailendra Ajmera [CA (AT) (Ins.) No. 1058 of 2022],*** after closure of challenge process, Shyam Sel and Power Ltd., one of the resolution applicants filed the revised plan

after the last date of submission of amended resolution plan. The AA directed CoC to consider their revised resolution plan. Jindal Stainless Ltd., one of the resolution applicants preferred on appeal before the NCLAT against this order of the AA. The NCLAT while relying on SC judgment in Ngaitlang Dhar v. Panna Pragati Infrastructure Private Limtied & Ors. see set aside the order passed by AA and directed the RP to initiate fresh voting process on the resolution plans received in the due time. It further held that after adoption of Swiss challenge method to find out the best plan, one resolution applicant cannot be allowed to submit a revised plan.

Source: IBBI Quarterly Newsletter Jan-March 2023

8. In the case of ***Ramkrishna Forgings Limited Vs. Ravindra Loonkar, Resolution Professional of ACIL Limited & Anr , Civil Appeal No.1527 of 2022,*** judgement dated November 21, 2023, Hon'ble Supreme Court inter alia observed that having considered the matter in depth, the Court is unable to uphold the decisions rendered by the Adjudicating Authority-NCLT as also the NCLAT. The moot question involved is the extent of the jurisdiction and powers of the Adjudicating Authority to go on the issue of revaluation in the background of the admitted and undisputed factual position that no objection was raised by any quarter with regard to any deficiency/irregularity, either by the RP or the appellant or the CoC, in finally approving the Resolution Plan which was sent to the Adjudicating Authority-NCLT for approval. Further, the statutory requirement of the RP involving two approved valuers for giving reports apropos fair market value and liquidation value was duly complied with and the figures in both reports were not at great variance. Significantly, the same were then put up before the CoC, which is the decision-maker and in the driver's seat, so to say, of the Corporate Debtor. *K Sashidhar (supra) and Committee of Creditors of Essar Steel India Ltd. (supra)* are clear authorities that the CoC's decision is not to be subjected to unnecessary judicial scrutiny and intervention. This came to be reiterated in *Maharashtra Seamless Limited (supra),* which also emphasised that the CoC's commercial analysis ought not to be qualitatively examined and the direction therein of the NCLAT to direct the successful Resolution Applicant to enhance its fund flow was disapproved of by this Court. Thus, if the CoC, including the FC(s) to whom money is due from the Corporate Debtor, had undertaken repeated negotiations with the appellant with regard to the Resolution Plan and thereafter, with a majority of 88.56% votes, approved the final negotiated Resolution Plan of the appellant, which the RP, in turn, presented to the Adjudicating Authority-NCLT for approval, unless the same was failing the tests of the provisions of the Code, especially Sections 30 & 31, no interference was warranted. In *Kalpraj Dharamshi v Kotak Investment Advisors Limited, (2021) 10 SCC 401,* the Court concluded that *'... in view of the paramount importance given to the decision of CoC,* which is to be taken on the basis of *"commercial wisdom",* NCLAT was not correct in law in interfering with the commercial decision taken by CoC by a thumping majority of 84.36%.' (Para 27)

LESSON ROUND-UP

- 'Resolution applicant' means a person, who individually or jointly with any other person, submits a resolution plan to the resolution professional pursuant to the invitation made under clause (h) of subsection (2) of section 25. [Section 5(25)]
- 'Resolution plan' means a plan proposed by resolution applicant for insolvency resolution
- Section 29A declares certain persons ineligible to be a resolution applicant and prohibits such persons from submitting a resolution plan. MSMEs are exempted from the application of certain clauses under Section 29A.
- The resolution professional, under clause (h) of sub-section (2) of section 25, invites prospective resolution applicants, who fulfil such criteria as may be laid down by him with the approval of committee of creditors.
- As per section 30(1) a resolution applicant may submit a resolution plan along with an affidavit stating that he is eligible under section 29A to the resolution professional prepared on the basis of the information memorandum.

- The resolution professional is required to submit each resolution plan, which conforms to the criteria mentioned in section 30(2), to the committee of creditors who shall approve a resolution plan by a by a vote of not less than sixty-six percent of voting share of the financial creditors. Once the resolution plan is approved by the committee of creditors, it is then presented to the adjudicating authority for its approval.
- Section 31(4) provides that the resolution applicant shall, pursuant to the resolution plan approved under sub-section (1), obtain the necessary approval required under any law for the time being in force within a period of one year from the date of approval of the resolution plan by the Adjudicating Authority under sub- section (1) or within such period as provided for in such law, whichever is later.
- The proviso to Section 31(4) lays down that where the resolution plan contains a provision for combination, as referred to in section 5 of the Competition Act, 2002, the resolution applicant shall obtain the approval of the Competition Commission of India under that Act prior to the approval of such resolution plan by the committee of creditors.
- Resolution plan approved by the Adjudicating Authority under section 31(1) shall be binding on the corporate debtor and its employees, members, creditors, guarantors, including the Central Government, any State Government or any local authority to whom a debt in respect of the payment of dues arising under any law for the time being in force, such as authorities to whom statutory dues are owed and other stakeholders involved in the resolution plan.
- After approval of resolution plan the moratorium order passed by the Adjudicating Authority under section 14 shall cease to have effect; and the resolution professional shall forward all records relating to the conduct of the corporate insolvency resolution process and the resolution plan to the Board to be recorded on its database.
- Section 32 of the Code deals with appeals from an order approving the resolution plan. Section 32 lays down that any appeal from an order approving the resolution plan shall be in the manner and on the grounds laid down in sub-section (3) of section 61.
- Section 32A provides relief to the resolution applicant or the persons who shall be in charge of the management of the company in the future by way of immunity from the liability of offences that the promoters or the persons in charge of the corporate debtor had committed prior to the initiation of CIRP, subject to certain conditions. The Section also bars any action being taken against the property of the corporate debtor pursuant to an offence committed prior to the CIRP, subject to the condition that the property is covered under the resolution plan approved by the AA or sale under liquidation and the resolution plan should have resulted in change in management/control of the corporate debtor such that debarred persons are not in management/control of the corporate debtor post resolution. However, the immunity is not provided for the property of any other person, other than the corporate debtor.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. What is meant by 'resolution plan'? Mention the aspects examined by resolution professional for confirming a resolution plan and presenting the same to Committee of Creditors.
2. Section 29A of the Insolvency and Bankruptcy Code, 2016 provides for the persons who are not eligible to be resolution applicant. Discuss the provisions in brief.
3. Mention the provisions relating to the approval of resolution plan under section 31 of the Insolvency and Bankruptcy Code, 2016.
4. State the changes brought about in section 30 of the Insolvency and Bankruptcy Code, 2016 by the Insolvency and Bankruptcy Code (Second Amendment) Act, 2018.

5. What are the grounds on which an appeal against an order approving a resolution plan under section 31 of the Insolvency and Bankruptcy Code, 2016 may be filed?

REFERENCES

- IBBI 2019 Handbook
- IBBI Quarterly Newsletter Jan-Mar 2023

Pre-Packaged Insolvency Resolution Process

Lesson 20

KEY CONCEPTS

■ Pre-packaged insolvency commencement date ■ Pre-packaged insolvency resolution process costs ■ Pre-packaged insolvency resolution process period ■ Applicant ■ Resolution Professional ■ Preliminary Information Memorandum ■ Committee ■ Participant ■ Resolution applicant

Learning Objectives

To understand:

- Concept of Pre-packaged Insolvency Resolution Process (PPIRP)
- Time period for completion of PPIRP
- Initiation of the process
- Duties and powers of Resolution Professionalt
- Conduct and conclusion of the process

Lesson Outline

- Introduction
- Initiation of Pre – Packaged Insolvency Resolution Process
- Time-period for completion of process
- Duties and powers of Resolution Professional
- List of claims and preliminary information memorandum
- Consideration and approval of Resolution Plan
- Termination of Pre-packaged Insolvency Resolution process
- Lesson Round-Up
- Test Yourself

REGULATORY FRAMEWORK

- Section 54A to 54P of the Insolvency and Bankruptcy Code, 2016
- Insolvency and Bankruptcy Board of India (Pre - packaged Insolvency Resolution Process) Regulations, 2021

INTRODUCTION

It appears that 'pre-pack' has no statutory definition. It is probably because it has evolved over the time, differently in different jurisdictions and every jurisdiction has a unique variant(s) of pre-pack, which allows the stakeholders to modify it further to an extent to suit their needs. It has different nomenclature such as pre-packaged insolvency resolution, pre-arranged insolvency resolution and pre-plan sale in the USA, pre-pack sale in the UK, scheme of arrangement in Singapore, etc. As nomenclature suggests, pre-pack is a restructuring plan which is agreed to by the debtor and its creditors prior to the insolvency filing, and then sanctioned by the court on an expedited basis. In the UK context, it generally refers to a pre-agreed business sale by an insolvency practitioner which does not require prior court and/or creditor sanction.

With the background of the formal process in India being afflicted with high costs, pre-pack allows for a cost-effective and speedy resolution process. Pre-pack also identifies and alienates the role of the Insolvency/Resolution professional as an expert in the process.

Benefits of pre - pack insolvency resolution process

- It consolidates the benefit of both formal and informal proceedings of resolution, thus broadening the options for stakeholders
- It enables faster resolution as the corporate debtor can prepare a settlement plan or resolution plan with the creditors before going to NCLT
- Reduced burden on NCLT due to out of court settlements
- With the suspension of CIRP until March 2021, pre-pack has come as a relief to promoters and corporate debtors
- It allows the corporate debtor retain control till a settlement is reached with the creditors

PRE-PACKAGED INSOLVENCY RESOLUTION PROCESS

Section 54A to 54P of the Insolvency and Bankruptcy Code, 2016 ('Code') read with the Insolvency and Bankruptcy Board of India (Pre-packaged Insolvency Resolution Process) Regulations,2021 lays down the provisions of a pre-packaged insolvency resolution process with respect to its initiation, manner of carrying out the process, appointment of resolution professional, termination etc.

Corporate debtors eligible for pre-packaged insolvency resolution process (Section 54A)

(1) An application for initiating pre-packaged insolvency resolution process may be made in respect of a corporate debtor classified as a micro, small or medium enterprise under sub-section (1) of section 7 of the Micro, Small and Medium Enterprises Development Act, 2006.

(2) Without prejudice to sub-section (1), an application for initiating pre-packaged insolvency resolution process may be made in respect of a corporate debtor, who commits a default referred to in section 4, subject to the following conditions, that--

MSME Threshold			
Class	Capital Investment in Plant and Machinery or Equipment (Crore)	Cap in Turnover (crore)	Applicability of Pre-pack
Micro Enterprise	1 crore	5 crores	✓
Small Enterprise	10 crores	50 crores	✓
Medium Enterprise	50 crores	250 crores	✓

(a) it has not undergone pre-packaged insolvency resolution process or completed corporate insolvency resolution process, as the case may be, during the period of three years preceding the initiation date;

(b) it is not undergoing a corporate insolvency resolution process;

(c) no order requiring it to be liquidated is passed under section 33;

(d) it is eligible to submit a resolution plan under section 29A;

(e) the financial creditors of the corporate debtor, not being its related parties, representing such number and such manner as may be specified, have proposed the name of the insolvency professional to be appointed as resolution professional for conducting the pre-packaged insolvency resolution process of the corporate debtor, and the financial creditors of the corporate debtor, not being its related parties, representing not less than sixty-six per cent in value of the financial debt due to such creditors, have approved such proposal in such form as may be specified:

What is the minimum default amount for pre-pack cases?

The Ministry of Corporate Affairs vide its notification dated April 09, 2021 specified ten lakh rupees as the minimum amount of default for the matters relating to the pre-packaged insolvency resolution process of corporate debtor.

Provided that where a corporate debtor does not have any financial creditors, not being its related parties, the proposal and approval under this clause shall be provided by such persons as may be specified;

(f) the majority of the directors or partners of the corporate debtor, as the case may be, have made a declaration, in such form as may be specified, stating, inter alia -

(i) that the corporate debtor shall file an application for initiating pre-packaged insolvency resolution process within a definite time period not exceeding ninety days;

(ii) that the pre-packaged insolvency resolution process is not being initiated to defraud any person; and

(iii) the name of the insolvency professional proposed and approved to be appointed as resolution professional under clause (e);

(g) the members of the corporate debtor have passed a special resolution, or at least three-fourth of the total number of partners, as the case may be, of the corporate debtor have passed a resolution, approving the filing of an application for initiating prepackaged insolvency resolution process;

(3) The corporate debtor shall obtain an approval from its financial creditors, not being its related parties, representing not less than sixty-six per cent in value of the financial debt due to such creditors, for the filing of an application for initiating pre-packaged insolvency resolution process, in such form as may be specified:

Provided that where a corporate debtor does not have any financial creditors, not being its related parties, the approval under this sub-section shall be provided by such persons as may be specified.

(4) Prior to seeking approval from financial creditors under sub section (3), the corporate debtor shall provide such financial creditors with -

(a) the declaration referred to in clause (f) of sub-section (2);

(b) the special resolution or resolution referred to in clause (g) of sub-section (2);

(c) a base resolution plan which conforms to the requirements referred to in section 54K, and such other conditions as may be specified; and

(d) such other information and documents as may be specified.

Duties of resolution professional before initiation of pre-packaged insolvency resolution process (Section 54B)

As per Section 54B(1), the insolvency professional, proposed to be appointed as the resolution professional, shall have the following duties commencing from the date of the approval under clause (e) of sub-section (2) of section 54A, namely:-

(a) prepare a report in such form as may be specified, confirming whether the corporate debtor meets the requirements of section 54A, and the base resolution plan conforms to the requirements referred to in clause (c) of sub-section (4) of section 54A;

(b) file such reports and other documents, with the Board, as may be specified; and

(c) perform such other duties as may be specified.

Section 54B (3) provides that the fees payable to the insolvency professional in relation to the duties performed under sub-section (1) shall be determined and borne in such manner as may be specified and such fees shall form part of the pre-packaged insolvency resolution process costs, if the application for initiation of pre-packaged insolvency resolution process is admitted.

When will the duties of insolvency professional under Section 54B (1) of the Code cease?

Section 54B(2) provides the following circumstances:

(a) If the corporate debtor fails to file an application for initiating pre-packaged insolvency resolution process within the time period as stated under the declaration referred to in clause (f) of sub-section (2) of section 54A; or

(b) the application for initiating pre-packaged insolvency resolution process is admitted or rejected by the Adjudicating Authority, as the case may be.

Application to initiate pre-packaged insolvency resolution process (Section 54C)

(1) Where a corporate debtor meets the requirements of section 54A, a corporate applicant thereof may file an application with the Adjudicating Authority for initiating prepackaged insolvency resolution process.

(2) The application under sub-section (1) shall be filed in such form, containing such particulars, in such manner and accompanied with such fee as may be prescribed.

Applicant: As per Regulation 2(1) (a) of IBBI (PIRP) Regulations, 2021, 'applicant' means the corporate applicant, filing an application for initiation of pre-packaged insolvency resolution process under section 54C;

(3) The corporate applicant shall, along with the application, furnish-

(a) the declaration, special resolution or resolution, as the case may be, and the approval of financial creditors for initiating pre-packaged insolvency resolution process in terms of section 54A;

(b) the name and written consent, in such form as may be specified, of the insolvency professional proposed to be appointed as resolution professional, as approved under clause (e) of sub-section (2) of section 54A, and his report as referred to in clause (a) of sub-section (1) of section 54B;

(c) a declaration regarding the existence of any transactions of the corporate debtor that may be within the scope of provisions in respect of avoidance of transactions under Chapter III or fraudulent or wrongful trading under Chapter VI, in such form as may be specified;

(d) information relating to books of account of the corporate debtor and such other documents relating to such period as may be specified.

(4) The Adjudicating Authority shall, within a period of fourteen days of the receipt of the application, by an order,--

(a) admit the application, if it is complete; or

(b) reject the application, if it is incomplete.

Provided that the Adjudicating Authority shall, before rejecting an application, give notice to the applicant to rectify the defect in the application within seven days from the date of receipt of such notice from the Adjudicating Authority.

Time limit for completion of pre-packaged insolvency resolution process (Section 54D)

(1) The pre-packaged insolvency resolution process shall be completed within a period of one hundred and twenty days from the pre-packaged insolvency commencement date.

(2) Without prejudice to sub-section (1), the resolution professional shall submit the resolution plan, as approved by the committee of creditors, to the Adjudicating Authority under sub-section (4) or sub-section (12), as the case may be, of section 54K, within a period of ninety days from the pre-packaged insolvency commencement date.

(3) Where no resolution plan is approved by the committee of creditors within the time period referred to in sub-section (2), the resolution professional shall, on the day after the expiry of such time period, file an application with the Adjudicating Authority for termination of the pre-packaged insolvency resolution process in such form and manner as may be specified.

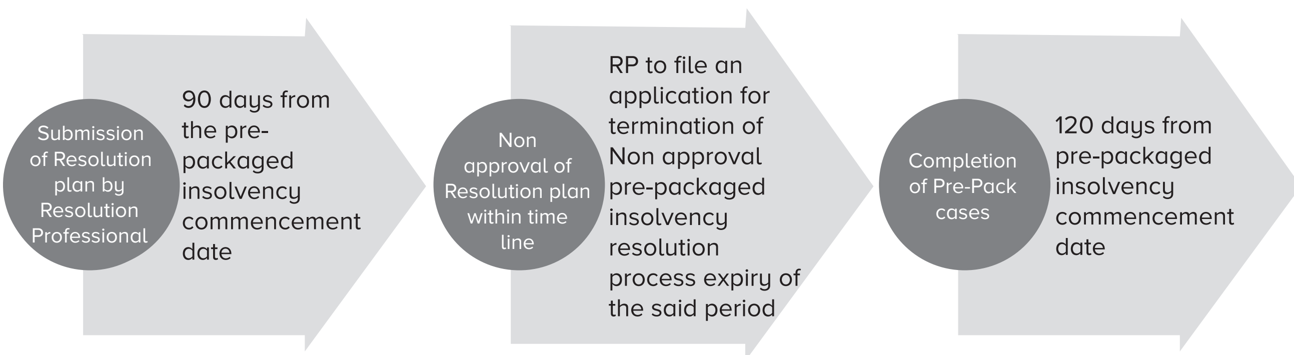


Fig. Timeline of pre-packaged insolvency resolution process

Declaration of moratorium and public announcement during pre-packaged insolvency resolution process (Section 54E)

(1) The Adjudicating Authority shall, on the pre-packaged insolvency commencement date, along with the order of admission under section 54C -

(a) declare a moratorium for the purposes referred to in sub-section (1) read with sub-section (3) of section 14, which shall, mutatis mutandis apply, to the proceedings under this Chapter;

(b) appoint a resolution professional -

(i) as named in the application, if no disciplinary proceeding is pending against him; or

(ii) based on the recommendation made by the Board, if any disciplinary proceeding is pending against the insolvency professional named in the application.

(c) cause a public announcement of the initiation of the pre-packaged insolvency resolution process to be made by the resolution professional, in such form and manner as may be specified, immediately after his appointment.

Timeline for public announcement:

The RP shall make a public announcement within two days of the commencement of the process.

(2) The order of moratorium shall have effect from the date of such order till the date on which the pre-packaged insolvency resolution process period comes to an end.

Duties and powers of resolution professional during pre-packaged insolvency resolution process (Section 54F)

(1) The resolution professional shall conduct the pre-packaged insolvency resolution process of a corporate debtor during the pre-packaged insolvency resolution process.

Duties of resolution professional [Section 54F(2)]

(a) confirm the list of claims submitted by the corporate debtor under section 54G, in such manner as may be specified;

(b) inform creditors regarding their claims as confirmed under clause (a), in such manner as may be specified;

(c) maintain an updated list of claims, in such manner as may be specified;

(d) monitor management of the affairs of the corporate debtor;

(e) inform the committee of creditors in the event of breach of any of the obligations of the Board of Directors or partners, as the case may be, of the corporate debtor, under the provisions of this chapter and the rules and regulations made thereunder;

(f) constitute the committee of creditors and convene and attend all its meetings;

Powers of resolution professional [Section 54F(3)]

(a) access all books of accounts, records and information available with the corporate debtor;

(b) access the electronic records of the corporate debtor from an information utility having financial information of the corporate debtor;

(c) access the books of accounts, records and other relevant documents of the corporate debtor available with government authorities, statutory auditors, accountants and such other persons as may be specified;

(d) attend meetings of members, Board of Directors and committee of directors, or partners, as the case may be, of the corporate debtor;

(e) appoint accountants, legal or other professionals in such manner as may be specified;

(g) prepare the information memorandum on the basis of the preliminary information memorandum submitted under section 54G and any other relevant information, in such form and manner as may be specified;

(h) file applications for avoidance of transactions under Chapter III or fraudulent or wrongful trading under Chapter VI, if any; and

(i) such other duties as may be specified.

(f) collect all information relating to the assets, finances and operations of the corporate debtor for determining the financial position of the corporate debtor and the existence of any transactions that may be within the scope of provisions relating to avoidance of transactions under Chapter III or fraudulent or wrongful trading under Chapter VI, including information relating to:

(i) business operations for the previous two years from the date of pre-packaged insolvency commencement date;

(ii) financial and operational payments for the previous two years from the date of pre-packaged insolvency commencement date;

(iii) list of assets and liabilities as on the initiation date; and

(iv) such other matters as may be specified;

(g) take such other actions in such manner as may be specified.

(4) From the date of appointment of the resolution professional, the financial institutions maintaining accounts of the corporate debtor shall furnish all information relating to the corporate debtor available with them to the resolution professional, as and when required by him.

(5) The personnel of the corporate debtor, its promoters and any other person associated with the management of the corporate debtor shall extend all assistance and cooperation to the resolution professional as may be required by him to perform his duties and exercise his powers, and for such purposes, the provisions of subsections (2) and (3) of section 19 shall, *mutatis mutandis* apply, in relation

(6) The fees of the resolution professional and any expenses incurred by him for conducting the pre-packaged insolvency resolution process shall be determined in such manner as may be specified:

Provided that the committee of creditors may impose limits and conditions on such fees and expenses: Provided further that the fees and expenses for the period prior to the constitution of the committee of creditors shall be subject to ratification by it.

(7) The fees and expenses referred to in sub-section (6) shall be borne in such manner as may be specified.

Who shall bear the fee of RP where the corporate debtor fails to file an application or the application for initiation of the process is rejected?

In such a case, the fee payable to the resolution professional for performing duties under sub-section (3) of section 54B shall be borne by the corporate debtor.

List of claims and preliminary information memorandum (Section 54G)

(1) The corporate debtor shall, within two days of the pre-packaged insolvency commencement date, submit to the resolution professional the following information, updated as on that date, in such form and manner as may be specified, namely:-

(a) a list of claims, along with details of the respective creditors, their security interests and guarantees, if any; and

(b) a preliminary information memorandum containing information relevant for formulating a resolution plan.

(2) Where any person has sustained any loss or damage as a consequence of the omission of any material information or inclusion of any misleading information in the list of claims or the preliminary information memorandum submitted by the corporate debtor, every person who -

(a) is a promoter or director or partner of the corporate debtor, as the case may be, at the time of submission of the list of claims or the preliminary information memorandum by the corporate debtor; or

(b) has authorised the submission of the list of claims or the preliminary information memorandum by the corporate debtor, shall, without prejudice to section 77A, be liable to pay compensation to every person who has sustained such loss or damage.

(3) No personshall be liable under sub-section (2), if the list of claims or the preliminary information memorandum was submitted by the corporate debtor without his knowledge or consent.

(4) Subject to section 54E, any person, who sustained any loss or damage as a consequence of omission of material information or inclusion of any misleading information in the list of claims or the preliminary information memorandum shall be entitled to move a court having jurisdiction for seeking compensation for such loss or damage.

Preliminary information memorandum

Section 5(23A) of the Code states that "preliminary information memorandum" means a memorandum submitted by the corporate debtor under clause (b) of sub-section (1) of section 54G.

Management of affairs of corporate debtor (Section 54H)

During the pre-packaged insolvency resolution process period,-

(a) The management of the affairs of the corporate debtor shall continue to vest in the Board of Directors or the partners, as the case may be, of the corporate debtor, subject to such conditions as may be specified;

b) The Board of Directors or the partners, as the case may be, of the corporate debtor, shall make every eneavour to protect and preserve the value of the property of the corporate debtor, and manage its operations as a going concern; and

(c) The promoters, members, peronnel and partners, as the case may be, of the corporate debtor, shall exercise and discharge their contractual or statutory rights and obligations in relation to the corporate debtor, subject to the provisions of this chapter and such other conditions and restrictions as may be prescribed.

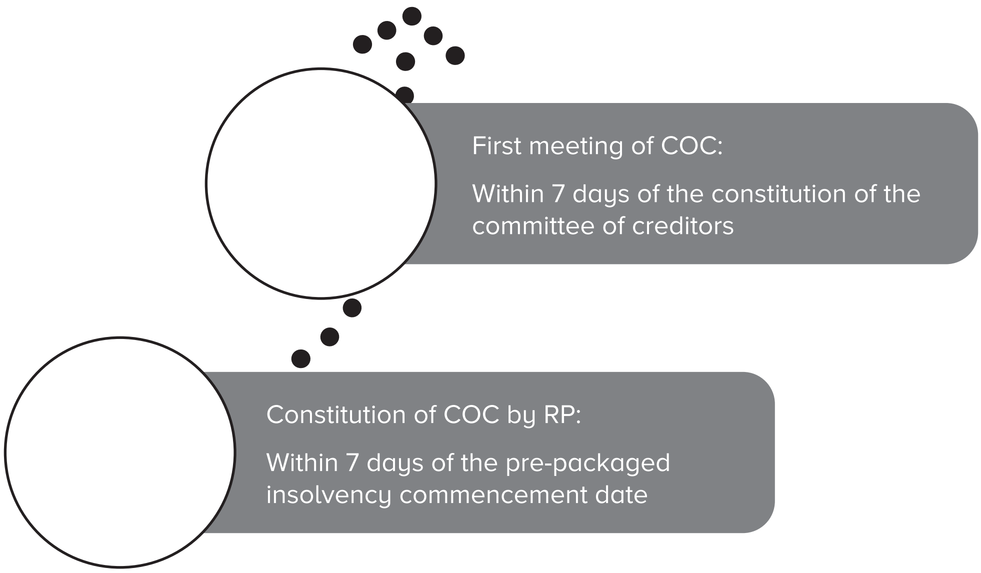
Committee of Creditors (Section 54I)

(1) The resolution professional shall, within seven days of the pre-packaged insolvency commencement date, constitute a committee of creditors, based on the list of claims confirmed under clause (a) of sub-section (2) of section 54F:

Provided that the composition of the committee of creditors shall be altered on the basis of the updated list of claims, in such manner as may be specified, and any such alteration shall not affect the validity of any past decision of the committee of creditors.

(2) The first meeting of the committee of creditors shall be held within seven days of the constitution of the committee of creditors.

(3) Provisions of section 21, except sub-section (1) thereof, shall, *mutatis mutandis* apply, in relation to the committee of creditors under this Chapter: Provided that for the purposes of this sub-section, references to the “resolution professional” under sub-sections (9) and (10) of section 21, shall be construed as references to “corporate debtor or the resolution professional”.



Vesting management of corporate debtor with resolution professional (Section 54J)

Section 54J(1) provides that where the committee of creditors, at any time during the pre-packaged insolvency resolution process period, by a vote of not less than sixty-six per cent of the voting shares, resolves to vest the management of the corporate debtor with the resolution professional, the resolution professional shall make an application for this purpose to the Adjudicating Authority, in such form and manner as may be specified.

Section 54J(3) provides that notwithstanding anything to the contrary contained in this chapter, the provisions of:

(a) sub-sections (2) and (2A) of section 14 (moratorium)

(b) section 17 (Management of affairs of corporate debtor by IRP)

(c) clauses (e) to (g) of section 18 (Duties of IRP)

(d) sections 19 and 20 (Personnel to extend co-operation to IRP and management of operations of corporate debtor as going concern)

(e) sub-section (1) of section 25 (Duty of RP to preserve and protect the assets of corporate debtor)

(f) clauses (a) to (c) and clause (k) of sub-section (2) of section 25 (duties of RP) and

Section 54J(2) of the Code provides that on an application made under sub-section (1), if the Adjudicating Authority is of the opinion that during the pre-packaged insolvency resolution process —

(a) the affairs of the corporate debtor have been conducted in a fraudulent manner; or

(b) there has been gross mismanagement of the affairs of the corporate debtor, it shall pass an order vesting the management of the corporate debtor with the resolution professional.

(g) section 28 (Approval of COC for certain actions) shall, *mutatis mutandis* apply, to the proceedings under this chapter, from the date of the order under sub-section (2), until the pre-packaged insolvency resolution process period comes to an end.

Consideration and approval of resolution plan (Section 54K)

(1) The corporate debtor shall submit the base resolution plan, referred to in clause (c) of sub-section (4) of section 54A, to the resolution professional within two days of the prepackaged insolvency commencement date, and the resolution professional shall present it to the committee of creditors.

(2) The committee of creditors may provide the corporate debtor an opportunity to revise the base resolution plan prior to its approval under sub-section (4) or invitation of prospective resolution applicants under sub-section (5 as the case may be.

Explanation I – For the removal of doubts, it is hereby clarified that, the corporate debtor being a resolution applicant under clause (25) of section 5, may submit the base resolution plan either individually or jointly with any other person.

Explanation II – For the purposes of subsections (4) and (14), claims shall be considered to be impaired where the resolution plan does not provide for the full payment of the confirmed claims as per the updated list of claims maintained by the resolution professional.

(3) The resolution plans and the base resolution plan, submitted under this section shall conform to the requirements referred to in sub-sections (1) and (2) of section 30, and the provisions of sub-sections (1), (2) and (5) of section 30 shall, *mutatis mutandis* apply, to the proceedings under this Chapter.

Requirements of resolution plan

A resolution applicant may submit a resolution plan along with an affidavit stating that he is eligible under section 29A to the resolution professional prepared on the basis of the information memorandum.

The resolution professional shall examine each resolution plan received by him to confirm that each resolution plan –

(a) provides for the payment of insolvency resolution process costs in a manner specified by the Board in priority to the payment of other debts of the corporate debtor;

(b) provides for the payment of debts of operational creditors in such manner as may be specified by the Board which shall not be less than-

(i) the amount to be paid to such creditors in the event of a liquidation of the corporate debtor under section 53; or

(ii) the amount that would have been paid to such creditors, if the amount to be distributed under the resolution plan had been distributed in accordance with the order of priority in sub-section (1) of section 53, whichever is higher, and provides for the payment of debts of financial creditors, who do not vote in favour of the resolution plan, in such manner as may be specified by the Board, which shall not be less than the amount to be paid to such creditors in accordance with sub-section (1) of section 53 in the event of a liquidation of the corporate debtor.

(c) provides for the management of the affairs of the corporate debtor after approval of the resolution plan;

(d) The implementation and supervision of the resolution plan;

(e) does not contravene any of the provisions of the law for the time being in force;

(f) confirms to such other requirements as may be specified by the Board.

(4) The committee of creditors may approve the base resolution plan for submission to the Adjudicating Authority if it does not impair any claims owed by the corporate debtor to the operational creditors.

(5) Where -

(a) the committee of creditors does not approve the base resolution plan under sub-section (4); or

(b) the base resolution plan impairs any claims owed by the corporate debtor to the operational creditors, the resolution professional shall invite prospective resolution applicants to submit a resolution plan or plans, to compete with the base resolution plan, in such manner as may be specified.

(6) The resolution applicants submitting resolution plans pursuant to invitation under sub-section (5), shall fulfil such criteria as may be laid down by the resolution professional with the approval of the committee of creditors, having regard to the complexity and scale of operations of the business of the corporate debtor and such other conditions as may be specified.

(7) The resolution professional shall provide to the resolution applicants -

(a) the basis for evaluation of resolution plans for the purposes of sub-section (9), as approved by the committee of creditors subject to such conditions as may be specified; and

(b) the relevant information referred to in section 29, which shall, *mutatis mutandis* apply, to the proceedings under this chapter, in such manner as may be specified.

(8) The resolution professional shall present to the committee of creditors, for its evaluation, resolution plans which conform to the requirements referred to in sub-section (2) of section 30.

(9) The committee of creditors shall evaluate the resolution plans presented by the resolution professional and select a resolution plan from amongst them.

(10) Where, on the basis of such criteria as may be laid down by it, the committee of creditors decides that the resolution plan selected under sub-section (9) is significantly better than the base resolution plan, such resolution plan may be selected for approval under sub-section (12):

Provided that the criteria laid down by the committee of creditors under this sub-section shall be subject to such conditions as may be specified.

(11) Where the resolution plan selected under sub-section (9) is not considered for approval or does not fulfil the requirements of sub-section (10), it shall compete with the base resolution plan, in such manner and subject to such conditions as may be specified, and one of them shall be selected for approval under sub-section (12).

(12) The resolution plan selected for approval under sub-section (10) or sub-section (11), as the case may be, may be approved by the committee of creditors for submission to the Adjudicating Authority:

Provided that where the resolution plan selected for approval under sub-section (11) is not approved by the committee of creditors, the resolution professional shall file an application for termination of the pre-packaged insolvency resolution process in such form and manner as may be specified.

(13) The approval of the resolution plan under sub-section (4) or sub-section (12), as the case may be, by the committee of creditors, shall be by a vote of not less than sixty-six per cent. of the voting shares, after considering its feasibility and viability, the manner of distribution proposed, taking into account the order of priority amongst creditors as laid down in sub-section (1) of section 53, including the priority and value of the security interest of a secured creditor and such other requirements as may be specified.

(14) While considering the feasibility and viability of a resolution plan, where the resolution plan submitted by the corporate debtor provides for impairment of any claims owed by the corporate debtor, the

committee of creditors may require the promoters of the corporate debtor to dilute their shareholding or voting or control rights in the corporate debtor:

Provided that where the resolution plan does not provide for such dilution, the committee of creditors shall, prior to the approval of such resolution plan under sub-section (4) or sub-section (12), as the case may be, record reasons for its approval.

(15) The resolution professional shall submit the resolution plan as approved by the committee of creditors under sub-section (4) or sub-section (12), as the case may be, to the Adjudicating Authority.

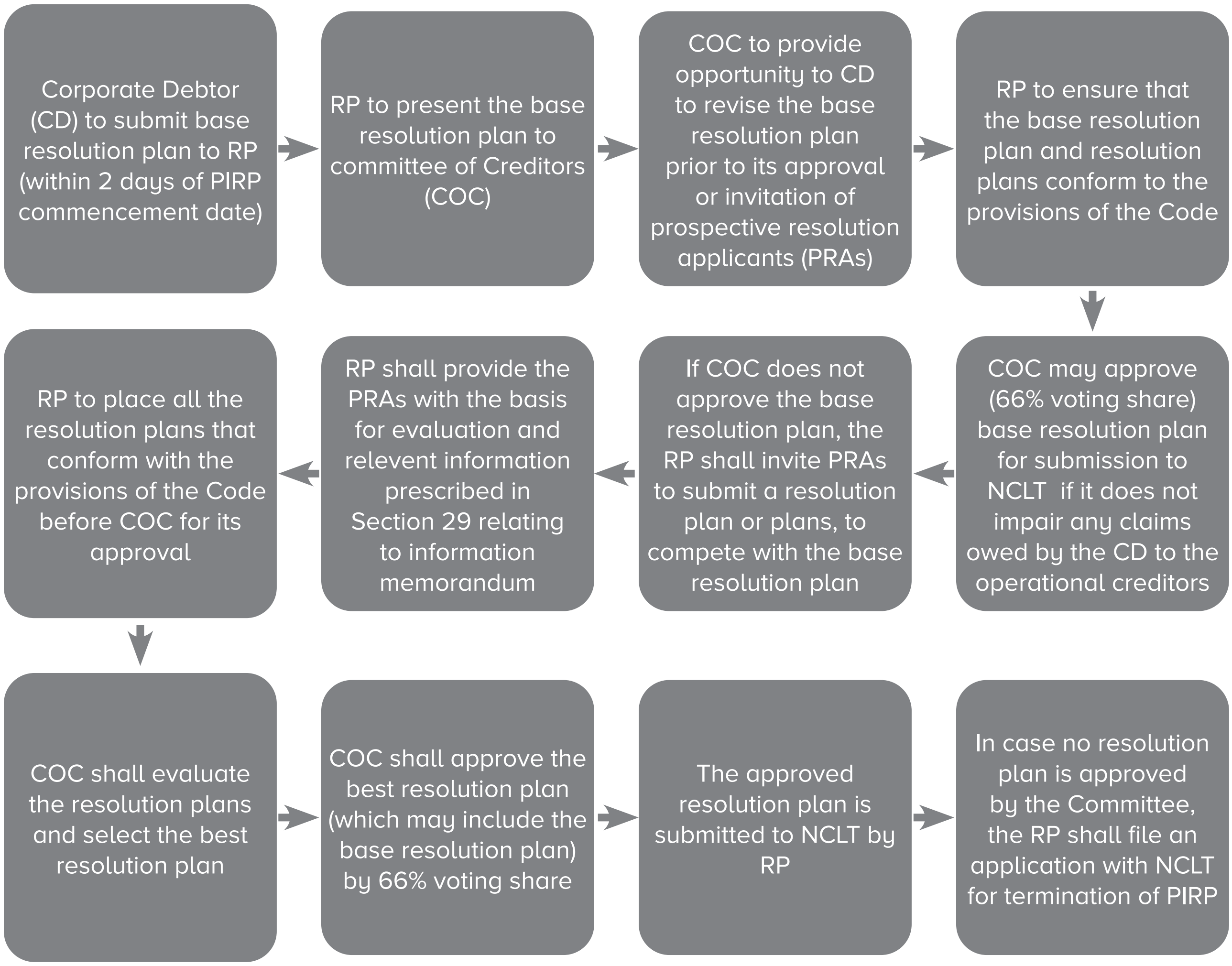


Fig: Consideration and approval of Resolution Plan

Approval of resolution plan (Section 54L)

(1) If the Adjudicating Authority is satisfied that the resolution plan as approved by the committee of creditors under sub-section (4) or sub-section (12) of section 54K, as the case may be, subject to the conditions provided therein, meets the requirements as referred to in sub-section (2) of section 30, it shall, within thirty days of the receipt of such resolution plan, by order approve the resolution plan:

Provided that the Adjudicating Authority shall, before passing an order for approval of a resolution plan under this sub-section, satisfy itself that the resolution plan has provisions for its effective implementation.

(2) The order of approval under sub-section (1) shall have such effect as provided under sub-sections (1), (3) and (4) of section 31, which shall, *mutatis mutandis* apply, to the proceedings under this Chapter.

(3) Where the Adjudicating Authority is satisfied that the resolution plan does not conform to the requirements referred to in sub-section (1), it may, within thirty days of the receipt of such resolution plan, by an order, reject the resolution plan and pass an order under section 54N.

(4) Notwithstanding anything to the contrary contained in this section, where the Adjudicating Authority has passed an order under sub-section (2) of section 54J and the resolution plan approved by the committee of creditors under sub-section (4) or sub-section (12), as the case may be, of section 54K, does not result in the change in the management or control of the corporate debtor to a person who was not a promoter or in the management or control of the corporate debtor, the Adjudicating Authority shall pass an order -

(a) rejecting such resolution plan;

(b) terminating the pre-packaged insolvency resolution process and passing a liquidation order in respect of the corporate debtor as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section (1) of section 33; and

(c) declaring that the pre-packaged insolvency resolution process costs, if any, shall be included as part of the liquidation costs for the purposes of liquidation of the corporate debtor.

Termination of pre-packaged insolvency resolution process (Section 54N)

(1) Where the resolution professional files an application with the Adjudicating Authority, -

(a) under the proviso to sub-section (12) of section 54K; or

(b) under sub-section (3) of section 54D,the Adjudicating Authority shall, within thirty days of the date of such application, by an order, -

(i) terminate the pre-packaged insolvency resolution process; and

(ii) provide for the manner of continuation of proceedings initiated for avoidance of transactions under Chapter III or proceedings initiated under section 66 and section 67A, if any.

(2) Where the resolution professional, at any time after the pre-packaged insolvency commencement date, but before the approval of resolution plan under sub-section (4) or sub-section (12), as the case may be, of section 54K, intimates the Adjudicating Authority of the decision of the committee of creditors, approved by a vote of sixty-six per cent of the voting shares, to terminate the pre-packaged insolvency resolution process, the Adjudicating Authority shall pass an order under sub-section (1).

What happens when the Adjudicating Authority has passed an order for termination of pre-packaged insolvency resolution process pursuant to the decision of COC?

As per Section 54N(4) of the Code, the Adjudicating Authority shall further pass an order —

(a) of liquidation of corporate debtor;

(b) declare that the pre-packaged insolvency resolution process costs, if any, shall be included as part of the liquidation costs for the purposes of liquidation of the corporate debtor.

Any appeal from an order approving the resolution plan under sub-section (1) of section 54L, shall be on the grounds laid down in sub-section (3) of section 61 (Section 54M)

(3) Where the Adjudicating Authority passes an order under sub-section (1), the corporate debtor shall bear the pre-packaged insolvency resolution process costs, if any.

Initiation of corporate insolvency resolution process (Section 54-O)

(1) The committee of creditors, at any time after the pre-packaged insolvency commencement date but before the approval of resolution plan under sub-section (4) or sub-section (12), as the case may be, of section 54K, by a vote of sixty-six per cent. of the voting shares, may resolve to initiate a corporate insolvency resolution process in respect of the corporate debtor, if such corporate debtor is eligible for corporate insolvency resolution process under Chapter II.

(2) Notwithstanding anything to the contrary contained in Chapter II, where the resolution professional intimates the Adjudicating Authority of the decision of the committee of creditors under sub-section (1), the Adjudicating Authority shall, within thirty days of the date of such intimation, pass an order to -

(a) terminate the pre-packaged insolvency resolution process and initiate corporate insolvency resolution process under Chapter II in respect of the corporate debtor;

(b) appoint the resolution professional referred to in clause (b) of sub-section (1) of section 54E as the interim resolution professional, subject to submission of written consent by such resolution professional to the Adjudicatory Authority in such form as may be specified; and

(c) declare that the pre-packaged insolvency resolution process costs, if any, shall be included as part of insolvency resolution process costs for the purposes of the corporate insolvency resolution process of the corporate debtor.

(3) Where the resolution professional fails to submit written consent under clause (b) of sub-section (2), the Adjudicating Authority shall appoint an interim resolution professional by making a reference to the Board for recommendation, in the manner as provided under section 16.

Section 54-O(4) of the Code provides that where the Adjudicating Authority passes an order under sub-section (2):				
(a) such order shall be deemed to be an order of admission of an application under section 7 and shall have the same effect;	(b) the corporate insolvency resolution process shall commence from the date of such order;	(c) the proceedings initiated for avoidance of transaction under Chapter III or proceedings initiated under section 66 and section 67 A, if any, shall continue during the corporate insolvency resolution process;	(d) for the purposes of sections 43, 46 and 50, references to "insolvency commencement date" shall mean "pre-packaged insolvency commencement date"; and	(e) in computing the relevant time or the period for avoidable transactions, the time period for the duration of the prepackaged insolvency resolution process shall also be included, notwithstanding anything to the contrary contained in sections 43, 46 and 50.

Application of provisions of Chapters II, III, VI and VII to this Chapter (Section 54P)

(1) Save as provided under this Chapter, the provisions of sections 24, 25A, 26, 27, 28, 29A, 32A, 43 to 51, and the provisions of Chapters VI and VII of this Part shall, *mutatis mutandis* apply, to the pre-packaged insolvency resolution process, subject to the following, namely:

(a) reference to "members of the suspended Board of Directors or the partners" under clause (b) of sub-section (3) of section 24 shall be construed as reference to "members of the Board of Directors or the partners, unless an order has been passed by the Adjudicating Authority under section 54J";

(b) reference to “clause (j) of sub-section (2) of section 25” under section 26 shall be construed as reference to “clause (h) of sub-section (2) of section 54F”;

(c) reference to “section 16” under section 27 shall be construed as reference to “section 54E”;

(d) reference to “resolution professional” in sub-sections (1) and (4) of section 28 shall be construed as “corporate debtor”;

(e) reference to “section 31” under sub-section (3) of section 61 shall be construed as reference to “sub-section (1) of section 54L”;

(f) reference to “section 14” in sub-sections (1) and (2) of section 74 shall be construed as reference to “clause (a) of sub-section (1) of section 54E”;

(g) reference to “section 31” in sub-section (3) of section 74 shall be construed as” reference to “sub-section (1) of section 54L”.

(2) Without prejudice to the provisions of this Chapter and unless the context otherwise requires, where the provisions of Chapters II, III, VI and VII are applied to the proceedings under this Chapter, references to -

(a) “insolvency commencement date” shall be construed as references to “prepackaged insolvency commencement date”;

(b) “resolution professional” or “interim resolution professional”, as the case may be, shall be construed as references to the resolution professional appointed under this Chapter;

(c) “corporate insolvency resolution process” shall be construed as references to “pre-packaged insolvency resolution process”; and

(d) “insolvency resolution process period” shall be construed as references to “prepackaged insolvency resolution process period.”

LESSON ROUND-UP

- Sections 54A to 54P of the Code contain provisions relating to Pre-packaged Insolvency Resolution Process.
- An application for initiating pre-packaged insolvency resolution process may be made in respect of a corporate debtor classified as a micro, small or medium enterprise under sub-section (1) of section 7 of the Micro, Small and Medium Enterprises Development Act, 2006. The minimum amount of default for initiating pre-packaged insolvency resolution process is Rs. 10 lakhs.
- Pre-packaged insolvency resolution process shall be completed within a period of one hundred and twenty days from the pre-packaged insolvency commencement date.
- The resolution professional shall submit the resolution plan, as approved by the committee of creditors to the Adjudicating Authority within a period of ninety days from the pre-packaged insolvency commencement date.
- A application for pre-packaged insolvency resolution process may be filed by a corporate applicant.
- Insolvency and Bankruptcy Board of India (Pre-packaged Insolvency Resolution Process) Regulations, 2021 contains the procedure for pre-packaged insolvency resolution process.
- The corporate debtor shall, within two days of the pre-packaged insolvency commencement date, submit to the resolution professional a list of claims and a preliminary information memorandum.
- During the pre-packaged insolvency resolution process period, the management of the affairs of the corporate debtor shall continue to vest in the Board of Directors or the partners, as the case may be, of the corporate debtor.

- The resolution professional shall, within seven days of the pre-packaged insolvency commencement date, constitute a committee of creditors, based on the list of claims confirmed. As per Section 54I(2),the first meeting of the committee of creditors shall be held within seven days of the constitution of the committee of creditors.
- The committee of creditors, at any time during the pre-packaged insolvency resolution process period, by a vote of not less than sixty-six per cent. of the voting shares, resolve to vest the management of the corporate debtor with the resolution professional.
- The corporate debtor shall submit the base resolution plan to the resolution professional within two days of the pre-packaged insolvency commencement date, and the resolution professional shall present it to the committee of creditors.
- The committee of creditors shall evaluate the resolution plans presented by the resolution professional and select a resolution plan from amongst them. The resolution plan approved by the committee of creditors is submitted to the Adjudicating Authority by the Resolution Professional.
- The Adjudicating Authority shall, before passing an order for approval of a resolution plan under this sub-section, satisfy itself that the resolution plan has provisions for its effective implementation.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).

1. What is the rationale behind the introduction of pre-packaged insolvency resolution process?
2. How is pre-packaged insolvency resolution process different from the corporate insolvency resolution process under Chapter II of Part II of the Code?
3. State the powers and duties of Resolution Professional in relation to pre-packaged insolvency resolution process.
4. What is the role of the Committee of Creditors in pre-packaged insolvency resolution process?
5. Discuss the provisions relating to the approval of resolution plan in relation to pre-packaged insolvency resolution process.
6. Explain the provisions pertaining to termination of pre-packaged insolvency resolution process.

Cross Border Insolvency

Lesson 21

KEY CONCEPTS

■ UNCITRAL ■ Foreign proceeding ■ Foreign representative ■ Establishment ■ State ■ Reorganization

Learning Objectives

To understand:

- Objectives of effective insolvency law
- UNCITRAL guide on insolvency law
- Model law on cross border insolvency
- World Bank principles
- Insolvency Law Committee Recommendations.

Lesson Outline

- Introduction
- Key objectives of effective and efficient insolvency law
- UNCITRAL
- UNCITRAL Legislative guide on insolvency law
- UNCITRAL Model law on Cross Border insolvency
- Purpose of Model law
- World Bank Principles – effective insolvency and creditor rights
- US Bankruptcy Code
- Enabling provisions for cross border transactions under IBC
- Insolvency Law Committee (ILC)
- Case Laws
- Lesson Round-Up
- Test Yourself

REGULATORY FRAMEWORK

- Section 234 & 235 of the Insolvency and Bankruptcy Code, 2016
- UNCITRAL Model Law

INTRODUCTION

Cross-border insolvency (sometimes called international insolvency) regulates the treatment of financially distressed debtors where such debtors have assets or creditors in more than one country. In recent times, the number of cross-border insolvency cases has increased significantly. The increasing frequency of cross-border insolvencies reflects the continuing expansion of global trade and investment. However, national insolvency laws are often ill-equipped to deal with cases of a cross-border nature and they have by and large not kept pace with the trend. Fraud by insolvent debtors, in particular by concealing assets or transferring them to foreign jurisdictions, is another increasing problem, in terms of both its frequency and its magnitude.

There is also a lack of communication and coordination among courts and administrators from concerned jurisdictions. These deficiencies frequently results in inadequate and inharmonious legal approaches, which hamper the rescue of financially troubled businesses. Such inadequate and uncoordinated legal approaches, unconducive to a fair and efficient administration of cross-border insolvencies, impede the protection of the assets of the insolvent debtor and affect the maximization of the value of those assets. Such approaches are not only unpredictable and time-consuming in their application, but also lack transparency and the necessary tools to address the issues. All these factors adversely affect the value of the assets of financially troubled businesses and hamper their rescue. Moreover, the absence of predictability in the cross-border insolvency processes impedes capital flow and is a disincentive to cross-on border investment.

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> The organisation of insolvency proceedings with an international element is not an easy or straightforward matter. Solutions to the phenomenon of cross-border insolvency are reliant a number of complex and interrelated questions to which the courts and legislatures in different jurisdictions have provided varying answers.
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Cross-border insolvency problems are not limited to the failure of major international businesses. A domestic business may have foreign branches or subsidiaries, or a foreign business may have domestic branches or subsidiaries. Property located in a foreign country may provide security for a debt so that domestic assets can be used to pay unsecured creditors. Foreign creditors may have valid claims in domestic bankruptcy cases, and domestic creditors may have valid claims in foreign bankruptcy cases. Any one of these situations raises a transnational insolvency problem.

CURRENT CROSS BORDER INSOLVENCY SCENARIO

Insolvency laws aim to assist both the debtor and the creditor in the management and disposition of the debtor's assets. Recently insolvency petitions against numerous companies are being admitted. A few of these companies also have assets in other jurisdictions, and one of the crucial questions that arise is the treatment of such assets. This is the sphere of cross-border insolvency laws.

The Insolvency Law Committee constituted by the Ministry of Corporate Affairs submitted its first Report in March 2018 which recommended amendments to the Insolvency and Bankruptcy Code, 2016 based on the experience gained from implementation of the Code. With respect to cross-border insolvency, the Committee noted that the existing provisions in the Code (sections 234 and 235) do not provide a comprehensive framework for cross-border insolvency matters. The Committee decided to attempt to provide a comprehensive framework for this purpose based on the UNCITRAL Model Law on Cross-Border Insolvency, 1997 which could be made a part of the Code by inserting a separate part for this purpose.

Further, the Standing Committee on Finance (2020-2021) in its Thirty- Second Report on "Implementation of Insolvency & Bankruptcy Code-Pitfalls and Solutions" noted that the Insolvency Law Committee on cross border Insolvency (2018) had suggested the Incorporation of UNCITRAL Model Law on cross Border Insolvency into the Insolvency and Bankruptcy Code. The Committee also noted that an expert Committee on Cross-Border Insolvency Rule/Regulations Committee (CBIRC) had been constituted for recommending rules and regulations for smooth implementation of proposed cross border insolvency provisions, which are under consideration. Once the recommendations are adopted, the committee hope that the cross-border insolvency framework would go a long way in ensuring coordination and communication between jurisdictions to successfully address the resolution of cross border insolvency cases. The committee, therefore, recommended In a situation where an insolvency that the adoption of the provision of the cross- border Insolvency petition is admitted against a Framework should be expedited.

Globally, cross-border insolvency laws are based on one country providing assistance to the other in taking control of the assets and eventual disposition of such assets of the debtor company. Such aims are achieved by the mutual recognition of each country's insolvency regime. For example, the UK recognizes the insolvency provisions of certain Commonwealth jurisdictions and courts in the UK are bound to assist courts in such Commonwealth jurisdictions. India is not one of the jurisdictions that qualify for the benefit under this route. The European Union has one of the most effective cross-border regimes where, under Insolvency Regulations, the country where proceedings are initiated against the debtor and the Centre of Main interest is located in such country, the laws of that country automatically take priority and have the same effect in all other member states and govern all issues except those specifically excluded.

In a situation where an insolvency petition is admitted against a company and the committee of creditors (CoC) fails to arrive at a resolution plan, the company is ordered to be liquidated under the Insolvency and Bankruptcy Code, 2016. In this situation, the regime governing the disposition of the foreign assets of a company is inadequate, and there is an urgent need for a framework on cross-border insolvency.

Some countries have adopted the UN Commission on International Trade Law (UNCITRAL) Model law on cross-border insolvency, adopted in 1997.

The model law is designed to provide a harmonized approach to the treatment of cross-border insolvency proceedings, facilitate cooperation between the courts and office holders involved in the insolvency in diff jurisdictions, and provide for the mutual recognition of judgements and direct access of foreign representatives to the courts of the enacting state. India has not adopted the model law.

As regards cross-border insolvency laws in India, under the Companies Act, 1956, a court could order the winding-up of an unregistered company, which included a foreign company. However, if an Indian company with assets abroad was sought to be wound up, there was no specific statutory process for the proceedings. It was based on the mutual recognition of foreign decrees as in the Code of Civil Procedure, 1908, in India. Foreign creditors could also independently proceed against the assets of the company located in the foreign jurisdiction. In the absence of such recognition, it is difficult for a liquidator to gather information on the assets and enforce the disposition of foreign assets in a liquidation.

This problem was recognized by the Justice Eradi Committee in 2000 which called for the urgent adoption of the UNCITRAL Model Law, in whole or in part, for India to have an effective cross-border insolvency regime. Thereafter, the N.l. Mitra committee report set out in detail the then prevailing cross-border insolvency regime and once again reiterated the recommendation for the adoption of the UNCITRAL Model law. The Banking Law Reforms Committee (BLRC) report, on the basis of which the Insolvency and Bankruptcy Code, 2016 is formulated, decided to take-up question of cross-border insolvency in the next stage of deliberations.

In its current form, the Code contains only two provisions that may possibly enable and assist the liquidator with respect to a company having assets in a foreign jurisdiction. Section 234 of the Code allows the union government to enter into reciprocal agreements with other countries to enforce the provisions of the Code. Section 235 envisages a 'letter of request' by the liquidator for action on the assets of the company situated in another country. However, there must exist a reciprocal arrangement with such country. It is important to appreciate that the Code does not envisage the adoption of the UNCITRAL Model law or any cross-border insolvency regime.

The Insolvency Law Committee Report (ILC) on cross-border insolvency, observed that Sections 234 and 235 of the Code did not provide a comprehensive framework on cross-border insolvency matters and stated that it has attempted to formulate a framework based on the UNCITRAL Model Law. If the code is to be effective in the management and disposition of foreign assets of debtor companies, it is the need of the hour that India put in place a framework for cross-border insolvency. Till such time, liquidation of foreign assets will be a long-drawn process.

KEY OBJECTIVES OF EFFECTIVE AND EFFICIENT INSOLVENCY LAW

Although approaches in different countries may vary but there is a broad agreement that an effective and efficient insolvency regime should aim to achieve the following key objectives in a balanced manner:

1. Maximization of value of assets
2. ensuring equitable treatment of similarly situated creditors
3. Provision for timely, efficient and impartial resolution of insolvency
4. Preservation of the insolvency estate to allow equitable distribution to creditors
5. Ensuring a transparent and predictable insolvency law that contains incentives for gathering and dispensing information
6. Recognition of existing creditor rights and establishment of clear rules for ranking of priority claims
7. Establishment of a framework for cross-border insolvency

The United Nations Commission on International Trade (UNCITRAL)

The United Nations Commission on International Trade Law (UNCITRAL) is a subsidiary body of the General assembly. The United Nations Commission on International Trade Law (UNCITRAL) was established by the General assembly in 1966 [resolution 2205 (XXi) of 17 December 1966].

The Commission carries out its work at annual sessions, which are held in alternate years at united Nations Headquarters in New York and at the Vienna international Centre at Vienna.

The united Nations Commission on international trade law prepares international legislative texts for use by States in modernizing commercial law and non-legislative texts for use by commercial parties in negotiating transactions.

Examples of Legislative texts:

- UNCITRAL Model Law on International Commercial Arbitration
- UNCITRAL Model Law on Cross Border Insolvency
- UNCITRAL Model Law on Procurement of Goods, Construction and Services
- UNCITRAL Model Law on International Credit Transfers
- UNCITRAL Model Law on Electronic Commerce

Examples of Non-Legislative texts:

- UNCITRAL Arbitration Rules
- UNCITRAL Conciliation Rules
- UNCITRAL Notes on Organizing Arbitral Proceedings
- UNCITRAL Legal Guide on International Countertrade Transactions

UNCITRAL LEGISLATIVE GUIDE ON INSOLVENCY LAWS

The Legislative Guide on insolvency law was prepared by the United Nations Commission on International Trade Law (UNCITRAL). the project arose from a proposal made to the Commission in 1999 that UNCITRAL should undertake further work on insolvency law, specifically corporate insolvency, to foster and encourage the adoption of effective national corporate insolvency regimes.

Organization and Scope of the Legislative Guide

The legislative Guide on insolvency law is intended be used as a reference by national authorities and legislative bodies when preparing new laws benefits and regulations or reviewing the adequacy of existing laws and regulations.

The Guide discusses issues central to the design of an effective and efficient insolvency law, which, despite numerous differences in policy and legislative treatment, are recognized in many legal systems.

The legislative Guide also discusses the increasing use and importance of other tools for addressing preparatory insolvency, specifically restructuring negotiations entered into voluntarily between a debtor and its key creditors, which are not regulated by the insolvency law.

An exploratory meeting to consider the feasibility of such a project was held in December 1999. On the basis of the recommendation of that meeting, the Commission gave Working Group V (insolvency law) a mandate to prepare a comprehensive statement of key objectives and core features for a strong insolvenc y, debtor- creditor regime, including out-of-court restructuring, and a legislative guide containing flexible approaches to the implementation of to such objectives and features, including a discussion of the alternative approaches possible and the perceived and detriments of such approaches.

The first draft of the legislative guide on insolvency law was considered by Working Group V in July 2001 and work developed through seven one-week sessions, the final meeting taking place in late March 2004. In addition to representatives of the 36 member States of the Commission representatives of many other States and a number of international organizations, both intergovernmental and non-governmental, participated actively in the work. The work was also undertaken in close with Working Group VI (Security interests), to ensure collaboration entered into voluntarily between a debtor and coordination of the treatment of security in insolvency with the legislative guide on secured transactions being developed by UNCITRAL.

The final negotiations on the draft legislative guide on insolvency law were held during the thirty-seventh session of UNCITRAL in New York from 14 to 21 June 2004 and the text was adopted by consensus on 25 June 2004. Subsequently, the General assembly adopted resolution 59/40 of 2 December 2004 in which it expressed its appreciation to UNCITRAL for completing and adopting the Legislative Guide.

Purpose

The purpose of the Legislative Guide on Insolvency Law is to assist the establishment of an efficient and effective legal framework to address the financial difficulties of debtors. The Legislative Guide provides a comprehensive statement of the key objectives and principles that should be reflect in a State's insolvency laws. It is intended to inform and assist insolvency law reform around the world, providing a reference tool for national authorities and legislative bodies when preparing new laws and regulations or reviewing the adequacy of existing laws and regulations. The advice provided aims at achieving a balance between the need to address a debtor's financial difficulties as quickly and efficiently as possible; the interests of the various parties directly concerned with that financial difficulties , principally creditors and other stakeholders in the debtor's business; and public policy concerns, such as employment and taxation. The Legislative Guide assists the reader to evaluate the different approaches and solutions available and to choose the one most suitable to the local context.

Relevance to international trade

It is increasingly recognized that strong and effective insolvency regimes are important for all States as a means of preventing or limiting financial crises and facilitating rapid and orderly workouts from excessive indebtedness. Such regimes can facilitate the orderly reallocation of economic resources from businesses that are not viable to more efficient and profitable activities; provide incentives that not only encourage entrepreneurs to undertake investment, but also encourage managers of failing businesses to take early steps to address that failure and preserve employment; reduce the costs of business; and increase the availability of credit. Comparative analysis of the effectiveness of insolvency systems has become both common and essential for lending purposes, affecting States at all levels of economic development.

Much of the legislation relating to corporations and particularly to their treatment in insolvency deals with the single corporate entity, notwithstanding that the business of corporations is increasingly being conducted, both nationally and internationally, through enterprise groups - groups of corporations, sometimes very large, that are interconnected by various forms of ownership and control. These groups, found extensively in both emerging and developed markets, are a common vehicle for conducting international trade and finance. When some or all of the constituent parts of such groups become insolvent, there are currently very few domestic law regimes and no international or regional legal regimes that can effectively coordinate the conduct of the resulting insolvency proceedings, often involving multiple jurisdictions.

Key provisions

The legislative guide is divided into four parts. They are as follows:

Part one discusses the key objectives of an insolvency law, structural issues such as the relationship between insolvency law and other law, the types of mechanisms available for resolving a debtor's financial difficulties and the institutional framework required to support an effective insolvency regime.

Part two deals with core features of an effective insolvency law, following as closely as possible the various stages of an insolvency proceeding from their commencement to discharge of the debtor and closure of the proceedings. Key elements are identified as including: standardized commencement criteria; a stay to protect the assets of the insolvency estate that includes actions by secured creditors; post-commencement finance; participation of creditors; provision for expedited reorganization proceedings; simplified requirements for submission and verification of claims; conversion of reorganization to liquidation when reorganization fails; and clear rules for discharge of the debtor and closure of insolvency proceedings.

Part three addresses the treatment of enterprise groups in insolvency, both nationally and internationally. While many of the issues addressed in parts one and two are equally applicable to enterprise groups, there are that only apply in the enterprise group context. Part three thus builds upon and supplements parts one and two. at the domestic level, the commentary and recommendations of part three cover various mechanisms that can be used to streamline insolvency proceedings involving two or more members of the same enterprise group. These include: procedural coordination of multiple proceedings concerning different debtors; issues concerning post-commencement and post-application finance in a group context; avoidance provisions; substantive consolidation of insolvency proceedings affecting two or more group members; appointment of a single or the same insolvency representative to all group members subject to insolvency; and coordinated reorganization plans. in terms of the international treatment of groups, part three focuses on cooperation and coordination, extending provisions based upon the Model law on Cross-Border insolvency to the group context and, as appropriate, considering the applicability to the international context of the mechanisms proposed to address enterprise group insolvencies in the national context.

Part four focuses on the obligations that might be imposed upon those responsible for making decisions with respect to the management of an enterprise when that enterprise faces imminent insolvency or insolvency becomes unavoidable. The aim of imposing such obligations, which are enforceable once insolvency proceedings commence, is to protect the legitimate interests of creditors and other stakeholders and to provide incentives for timely action to minimize the effects of financial distress experienced by the enterprise.

UNCITRAL Legislative Guide on Insolvency Law *vis-a-vis* UNCITRAL Model Law on Cross- Border Insolvency

A model law generally is used differently than a legislative guide. Specifically, a model law is a legislative text recommended to States for enactment as part of national law, with or without modification. As such, model laws generally propose a comprehensive set of legislative solutions to address a particular topic and the language employed supports direct incorporation of the provisions of the model law into a national law.

The focus of a legislative guide, on the other hand, is upon providing guidance to legislators and other users and for that reason guides generally include a substantial commentary discussing and analysing relevant issues. It is not intended that the recommendations of a legislative guide be enacted as part of national law as such. rather, they outline the core issues that it would be desirable to address in that law, with some recommendations providing specific guidance on how certain legislative provisions might be drafted.

UNCITRAL MODEL LAW ON CROSS BORDER INSOLVENCY

The UNCITRAL Model law on Cross-Border insolvency, adopted in 1997, is designed to assist States to equip their insolvency laws with a modern, harmonized and fair framework to address more effectively instances of cross-border insolvency. Those instances include cases where the insolvent debtor has assets in more than one State or where some of the creditors of the debtor are not from the State where the insolvency proceeding is taking place.

The Model law is designed to assist States to equip their insolvency laws with a modern legal framework to more effectively address cross-border insolvency proceedings concerning debtors experiencing severe financial distress or insolvency. It focuses on authorizing and encouraging cooperation and coordination between jurisdictions, rather than attempting the unification of substantive insolvency law, and respects the differences among national procedural laws. For the purposes of the Model Law, a cross-border insolvency is one where the insolvent debtor has assets in more than one State or where some of the creditors of the debtor are not from the State where the insolvency proceeding is taking place.

Relevance to international trade

Although the number of cross-border insolvency cases has increased significantly since the 1990s, the adoption of national or international legal regimes equipped to address the issues raised by those cases has not kept pace. the lack of such regimes has often resulted in inadequate and uncoordinated approaches to cross-border insolvency that are not only unpredictable and time-consuming in their application, but lack both transparency and the tools necessary to address the disparities and, in some cases, conflicts that may occur between national laws and insolvency regimes. These factors have impeded the protection of the value of the assets of financially troubled businesses and hampered their rescue.

The UNCITRAL Model law has been adopted in as many as 44 countries and, therefore, forms part of international best practices in dealing with cross border insolvency issues. The model law deals with four major principles of cross-border insolvency, namely:			
(a) direct access to foreign insolvency professionals and foreign creditors to participate in or commence domestic insolvency proceedings against a defaulting debtor;	(b) recognition of foreign proceedings & provision of remedies;	(c) cooperation between domestic and foreign courts & domestic and foreign insolvency practioners; and	(d) coordination between two or more concurrent insolvency proceedingsin different countries. The main proceeding is determined by the concept of centre of main interest (COMI).

Key provisions

The Model Law focuses on four elements identified as key to the conduct of cross-border insolvency cases: access, recognition, relief (assistance) and cooperation.

(a) Access

These provisions give representatives of foreign insolvency proceedings and creditors a right of access to the courts of an enacting State to seek assistance and authorize representatives of local proceedings being conducted in the enacting State to seek assistance elsewhere.

(b) Recognition

One of the key objectives of the Model Law is to establish simplified procedures for recognition of qualifying foreign proceedings in order to avoid time-consuming legalization or other processes that often apply and to provide certainty with respect to the decision to recognize. These core provisions accord recognition to orders issued by foreign courts commencing qualifying foreign proceedings and appointing the foreign representative of those proceedings. Provided it satisfies specified requirements, a qualifying foreign proceeding should be recognized as either a main proceeding, taking place where the debtor had its centre of main interests at the date of commencement of the foreign proceeding or a non-main proceeding, taking place where the debtor has an establishment. Recognition of foreign proceedings under the Model Law has several effects - principal amongst them is the relief accorded to assist the foreign proceeding.

(c) Relief

A basic principle of the Model law is that the relief considered necessary for the orderly and fair conduct of cross-border insolvencies should be available to assist foreign proceedings. By specifying the relief that is available, the Model law neither imports the consequences of foreign law into the insolvency system of the enacting State nor applies to the foreign proceedings the relief that would be available under the law of the enacting State. Key elements of the relief available include interim relief at the discretion of the court between the making of an application for recognition and the decision on that application, an automatic stay upon recognition of main proceedings and relief at the discretion of the court for both main and non-main proceedings following recognition.

(d) Cooperation and coordination

These provisions address cooperation among the courts of States where the debtor's assets are located and coordination of concurrent proceedings concerning that debtor. The Model law expressly empowers courts to cooperate in the areas governed by the Model law and to communicate directly with foreign counterparts. Cooperation between courts and foreign representatives and between representatives, both foreign and local, is also authorized. The provisions addressing coordination of concurrent proceedings aim to foster decisions that would best achieve the objectives of both proceedings, whether local and foreign proceedings or multiple foreign proceedings.

PURPOSE OF MODEL LAW

The Preamble to UNCITRAL Model law on Cross-Border insolvency provides that:

The purpose of this Law is to provide effective mechanisms for dealing with cases of cross-border insolvency so as to promote the objectives of:

(a) Cooperation between the courts and other competent authorities of this State and foreign States involved in cases of cross-border insolvency;

(b) Greater legal certainty for trade and investment;

(c) Fair and efficient administration of cross-border insolvencies that protects the interests of all creditors and other interested persons, including the debtor;

(d) Protection and maximization of the value of the debtor's assets; and

(e) Facilitation of the rescue of financially troubled businesses, thereby protecting investment and preserving employment.

SCOPE OF APPLICATION

UNCITRAL Model law on Cross-Border insolvency applies where:

(a) assistance is sought in this State by a foreign court or a foreign representative in connection with a foreign proceeding; or

(b) assistance is sought in a foreign State in connection with a proceeding under identify laws of the enacting State relating to insolvency; or

(c) foreign proceeding and a proceeding under identify laws of the enacting State relating to insolvency in respect of the same debtor are taking place concurrently; or

(d) Creditors or other interested persons in a foreign State have an interest in requesting the commencement of, or participating in, a proceeding under identify laws of the enacting State relating to insolvency.

UNCITRAL Model law on Cross-Border insolvency does not apply to a proceeding concerning [designate any types of entities, such as banks or insurance companies, that are subject to a special insolvency regime in this State and that this State wishes to exclude from this law]. [Article 1]

Principle of supremacy of international obligations

Article 3 provides that to the extent the Model Law conflicts with an obligation of the State enacting the Model law arising out of any treaty or other form of agreement to which it is a party with one or more other States, the requirements of the treaty or agreement prevail.

Interpretation

In the interpretation of Model law, regard is to be had to its international origin and to the need to promote uniformity in its application and the observance of good faith. [Article 8]

DEFINITIONS

a) "Foreign proceeding" means a collective judicial or administrative proceeding in a foreign State, including an interim proceeding, pursuant to a law relating to insolvency in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation;

b) "Foreign main proceeding" means a foreign proceeding taking place in the State where the debtor has the centre of its main interests;

c) "Foreign non-main proceeding" means a foreign proceeding, other than a foreign main proceeding, taking place in a State where the debtor has an establishment within the meaning of subparagraph (f) of this article;

d) "Foreign representative" means a person or body, including one appointed on an interim basis, authorized in a foreign proceeding to administer the reorganization or the liquidation of the debtor's assets or affairs or to act as a representative of the foreign proceeding;

e) "Foreign court" means a judicial or other authority competent to control or supervise a foreign proceeding;

f) "establishment" means any place of operations where the debtor carries out a non-transitory economic activity with human means and goods or services;

g) the word "State", as used in the preamble and throughout the Model law, refers to the country that enacts the law (the "enacting State"). the term should not be understood as referring, for example, to a state in a country with a federal system.

Competent court or authority

The functions under the Model law relating to recognition of foreign proceedings and cooperation with foreign courts shall be performed by the court, courts, authority or authorities as specified in the Model Law who are competent to perform those functions in the enacting State. [Article 4]

GENERAL PROVISIONS

Scope of Application (Article 1)

The model Law applies where:-

According to article 1 of the Model law, it applies where:

(a) Assistance is sought in the enacting State by a foreign court or a foreign representative in connection with a foreign proceeding; or

(b) Assistance is sought in a foreign State in connection with a proceeding under the laws of the enacting State relating to insolvency; or

(c) A foreign proceeding and a proceeding under the laws of the enacting State relating to insolvency in respect of the same debtor are taking place concurrently; or

(d) Creditors or other interested persons in a foreign State have an interest in requesting the commencement of, or participating in, a proceeding under the laws of the enacting State relating to insolvency.

It further says that the Model law does not apply to a proceeding concerning any types of entities, such as banks or insurance companies, that are subject to a special insolvency regime in a State and that State wishes to exclude from the law (the type of entity to be excluded may be designated).

Banks or insurance companies are mentioned as examples of entities that the enacting State might decide to exclude from the scope of the Model law. the reason for the exclusion would be that the insolvency of such entities gives rise to the particular need to protect vital interests of a large number of individuals, or that the insolvency of those entities usually requires particularly prompt and circumspect action (for instance to avoid massive withdrawals of deposits). For those reasons, the insolvency of such types of entities is in many States administered under a special regulatory regime. the enacting State might decide to exclude the insolvency of entities other than banks and insurance companies.

Types of Foreign Proceedings Covered

To fall within the scope of the Model law, a foreign insolvency proceeding needs to possess certain attributes. these include the basis in insolvency-related law of the originating State; involvement of creditors collectively; control or supervision of the assets and affairs of the debtor by a court or another official body; and reorganization or liquidation of the debtor as the purpose of the proceeding. Within those parameters, a variety of collective proceedings would be eligible for recognition, be they compulsory or voluntary, corporate or individual, winding- up or reorganization. it also includes those proceedings in which the debtor retains some measure of control over its assets, albeit under court supervision (e.g. suspension of payments, “debtor in possession”). An inclusive approach is also used as regards the possible types of debtors covered by the Model law.

Principle of supremacy of international obligations (Article 3)

Article 3 provides that to the extent the Model Law conflicts with an obligation of the State enacting the Model law arising out of any treaty or other form of agreement to which it is a party with one or more other States, the requirements of the treaty or agreement prevail.

Competent court or authority (Article 4)

The functions under the Model law relating to recognition of foreign proceedings and cooperation with foreign courts shall be performed by the court, courts, authority or authorities as specified in the Model Law who are competent to perform those functions in the enacting State.

ACCESS OF FOREIGN REPRESENTATIVES AND CREDITORS TO COURTS IN STATE ENACTING MODEL LAW

Right of Direct Access (Article 9)

A foreign representative is entitled to apply directly to a court in the State enacting law. Article 9 is limited to expressing the principle of direct access by the foreign representative to courts of the enacting State, thus freeing the representative from having to meet formal requirements such as licences or consular action.

Application by a Foreign Representative to Commence a Proceeding (Article 11)

According to Article 11, a foreign representative is entitled to apply to commence a proceeding under the laws of the enacting State relating to insolvency, if the conditions for commencing such proceeding otherwise met.

A foreign representative has this right without prior recognition of the foreign proceeding because the commencement of an insolvency proceeding might be crucial in cases of urgent need for preserving the assets of the debtor.

The Model law avoids the need to rely on cumbersome and time-consuming letters rogatory or other forms of diplomatic or consular communications that might otherwise have to be used. This facilitates a coordinated, cooperative approach to cross-border insolvency and makes fast action possible.

In addition to establishing the principle of direct court access for the foreign representative, the Model law:

(a) Establishes simplified proof requirements for seeking recognition and relief for foreign proceedings, which avoid time-consuming "legalization" requirements involving notarial or consular procedures (Article 15);

(b) Provides that the foreign representative has procedural standing for commencing an insolvency proceeding in the enacting State (under the conditions applicable in the enacting State) and that the foreign representative may participate in an insolvency proceeding in the enacting State (Articles 11 and 12);

(c) Confirms, subject to other requirements of the enacting State, access of foreign creditors to the courts of the enacting State for the purpose of commencing in the enacting State an insolvency proceeding or participating in such a proceeding (Article 13);

(d) Gives the foreign representative the right to intervene in proceedings concerning individual actions in the enacting State affecting the debtor or its assets (Article 24);

(e) Provides that the mere fact of a petition for recognition in the enacting State does not mean that the courts in that State have jurisdiction over all the assets and affairs of the debtor (Article 10).

Upon recognition of a foreign proceeding, the foreign representative is entitled to participate in a proceeding regarding the debtor under the laws of the enacting State relating to insolvency (Article 12).

Article 12 is limited to giving the foreign representative procedural standing (or "procedural legitimation") to make petitions, requests or submissions concerning issues such as protection, realization or distribution of assets of the debtor or cooperation with the foreign proceeding and does not vest the foreign representative with any specific powers or rights.

Protection of creditors and other interested persons

Foreign creditors have the same rights regarding the commencement of and participation in a proceeding under the laws of the enacting State relating to insolvency as creditors in the State.

The Model law contains following provisions to protect the interests of the creditors (in particular local creditors), the debtor and other affected persons:

Availability of temporary relief upon application for recognition of a foreign proceeding or upon recognition is subject to the discretion of the court; it is expressly stated that in granting such relief the court must be satisfied that the interests of the creditors and other interested persons, including the debtor, are adequately protected (Article 22, paragraph 1);

The court may subject the relief it grants to conditions it considers appropriate; and

The court may modify or terminate the relief granted, if so requested by a person affected thereby (Article 22, paragraphs 2 and 3).

In addition to those specific provisions, the Model Law in a general way provides that the court may refuse to take an action governed by the Model law if the action would be manifestly contrary to the public policy of the enacting State (Article 6).

Notification to Foreign Creditors of a Proceeding (Article 14)

Article 14 of the Model law provides that whenever under laws of the enacting State relating to insolvency, a notification is to be given to creditors, such notification shall also be given to the known creditors that do not have addresses in the State. The court may order that appropriate steps be taken with a view to notifying any creditor whose address is not yet known. The main purpose of notifying foreign creditors is to inform them of the commencement of the insolvency proceeding and of the time-limit to file their claims.

Such notification shall be made to the foreign creditors individually, unless the court considers that, under the circumstances, some other form of notification would be more appropriate. No letters rogatory or other, similar formality is required. When a notification of commencement of a proceeding is to be given to foreign creditors, the notification shall:

(a) Indicate a reasonable time period for filing claims and specify the place for their filing;

(b) Indicate whether secured creditors need to file their secured claims; and

(c) Contain any other information required to be included in such a notification to creditors pursuant to the law of this State and the orders of the court.

RECOGNITION OF A FOREIGN PROCEEDING AND RELIEF

Application for Recognition of a Foreign Proceeding (Article 15)

Article 15 defines the core procedural requirements for an application by a foreign representative for recognition. In incorporating the provision into national law, it is desirable not to encumber the process with additional requirements beyond these requirements. a foreign representative may apply to the court for recognition of the foreign proceeding in which the foreign representative has been appointed. An application for recognition shall be accompanied by:

(a) A certified copy of the decision commencing the foreign proceeding and appointing the foreign representative; or

(b) A certificate from the foreign court affirming the existence of the foreign proceeding and of the appointment of the foreign representative; or

(c) In the absence of evidence referred to in subparagraphs (a) and (b) above, any other evidence acceptable to the court of the existence of the foreign proceeding and of the appointment of the foreign representative.

An application for recognition shall also be accompanied by a statement identifying all foreign proceedings in respect of the debtor that are known to the foreign representative. The court may require a translation of documents supplied in support of the application for recognition into an official language of State.

The Model law presumes that documents submitted in support of the application for recognition need not be authenticated in any special way, in particular by legalization. According to Article 16, the court is entitled to presume that those documents are authentic whether or not they have been legalized. "legalization" is a term often used for the formality by which a diplomatic or consular agent of the State in which the document is to be produced certifies the authenticity of the signature, the capacity in which the person signing the document has acted and, where appropriate, the identity of the seal or stamp on the document.

In respect of the provision relaxing any requirement of legalization, the question may arise whether that is in conflict with the international obligations of the enacting State. Several States are parties to bilateral or multilateral treaties on mutual recognition and legalization of documents. According to Article 3 of the Model Law, if there is still a conflict between the Model Law and a treaty, the treaty will prevail. In order not to prevent recognition because of non-compliance with a mere technicality, the law allows evidence other than that specified; that provision, however, does not compromise the court's power to insist on the presentation of evidence acceptable to it.

It further requires that an application for recognition must be accompanied by a statement identifying all foreign proceedings in respect of the debtor that are known to the foreign representative. That information is needed by the court not so much for the decision on recognition itself but for any decision granting relief in favour of the foreign proceeding. In order to tailor such relief appropriately and make sure that the relief is consistent with any other insolvency proceeding concerning the same debtor, the court needs to be aware of all foreign proceedings concerning the debtor that may be under way in third States.

Decision to Recognize a Foreign Proceeding (Article 17)

Subject to Article 6, a foreign proceeding shall be recognized if:

(a) The foreign proceeding is a proceeding within the meaning as defined under Article 2;

(b) The foreign representative applying for recognition is a person or body within the meaning as defined under Article 2;

(c) The application meets the requirements of Article 15; and

(d) The application has been submitted to the court referred to in Article 4.

The foreign proceeding shall be recognized as a foreign main proceeding if it is taking place in the State where the debtor has the centre of its main interests; or as a foreign non-main proceeding if the debtor has an establishment within the meaning of subparagraph (f) of Article 2 in the foreign State.

The purpose of Article 17 is to indicate that, if recognition is not contrary to the public policy of the enacting State and if the application meets the above said requirements, recognition will be granted as a matter of course. a decision to recognize a foreign proceeding would normally be subject to review or rescission, as any other court decision.

Subsequent Information (Article 18)

The foreign representative shall inform the court immediately, if from the time of filing the application forrecognition of the foreign proceeding, there is:

(a) any substantial change in the status of the recognized foreign proceeding or the status of the foreign representative's appointment; and

(b) any other foreign proceeding regarding the same debtor that becomes known to the foreign representative.

It is possible that, after the application for recognition or after recognition, changes may occur in the foreign proceeding that would have affected the decision on recognition or the relief granted on the basis of recognition.

For example, the foreign proceeding may be terminated or transformed from a liquidation proceeding into a reorganization proceeding, or the terms of the appointment of the foreign representative may be modified or the appointment itself terminated. The technical modifications in the status of the proceedings or the terms of the appointment are frequent, but that only some of those modifications are such that they would affect the decision granting relief or the decision recognizing the proceeding; therefore, the provision only calls for information of "substantial" changes.

Relief That may be Granted upon Application for Recognition of a Foreign Proceeding (Article 19)

According to Article 19, from the time of filing an application for recognition until the application is decided upon, the court may, at the request of the foreign representative, where relief is urgently needed to protect the assets of the debtor or the interests of the creditors, grant relief of a provisional nature, including:

(a) Staying execution against the debtor's assets;

(b) entrusting the administration or realization of all or part of the debtor's assets located in a State to the foreign representative or another person designated by the court, in order to protect and preserve the value of assets that, by their nature or because of other circumstances, are perishable, susceptible to devaluation or otherwise in jeopardy; and

(c) any relief mentioned in Article 21.

Relief available under Article 19 is provisional in the sense that, the relief terminates when the application for recognition is decided upon; however, the court is given the opportunity to extend the measure, as provided in Article 21. The court may refuse to grant relief under this Article if such relief would interfere with the administration of a foreign main proceeding.

Effects of Recognition of a Foreign main Proceeding (Article 20)

Once foreign proceeding is recognized which is a foreign main proceeding, the following are the effects:

(a) Commencement or continuation of individual actions or individual proceedings concerning the debtor's assets, rights, obligations or liabilities is stayed;

(b) execution against the debtor's assets is stayed; and

(c) the right to transfer, encumber or otherwise dispose of any assets of the debtor is suspended.

The effects provided by Article 20 are not discretionary in nature. These flow automatically from recognition of the foreign main proceeding. The automatic effects under Article 21 apply only to main proceedings.

Relief that may be Granted upon Recognition of a Foreign Proceeding (Article 21)

Upon recognition of a foreign proceeding, whether main or non-main, where it is necessary to protect the assets of the debtor or the interests of the creditors, the court may, at the request of the foreign representative, grant any appropriate relief, including:

(a) Staying the commencement or continuation of individual actions or individual proceedings concerning the debtor's assets, rights, obligations or liabilities, to the extent they have not been stayed under article 20;	(b) Staying execution against the debtor's assets to the extent it has not been stayed under article 20;	(c) Suspending the right to transfer, encumber or otherwise dispose of any assets of the debtor to the extent this right has not been suspended under article 20;	(d) Providing for the examination of witnesses, the taking of evidence or the delivery of information concerning the debtor's assets, affairs, rights, obligations orliabilities;	e) Entrusting the administration or realization of all or part of the debtor's assets located in this State to the foreign representative or another person designated by the court;	(f) Extending relief granted under article 19; and	(g) Granting any additional relief that may be available to a person or body administering a reorganization or liquidation under the law of the enacting State under the laws of that State.

Upon recognition of a foreign proceeding, whether main or non-main, the court may, at the request of the foreign representative, entrust the distribution of all or part of the debtor's assets located in the State enacting the Model law to the foreign representative or another person designated by the court, provided that the court is satisfied that the interests of creditors are adequately protected.

In granting relief under this article to a representative of a foreign non-main proceeding, the court must be satisfied that the relief relates to assets that, under the law of the enacting State, should be administered in the foreign non-main proceeding or concerns information required in that proceeding.

Protection of creditors and other interested persons (Article 22)

The court may under Article 22, at the request of the foreign representative or a person affected by relief granted, or at its own motion, modify or terminate such relief. In granting or denying relief under article 19 or 21, or in modifying or terminating relief, the court must be satisfied that the interests of the creditors and other interested persons, including the debtor, are adequately protected.

The idea underlying article 22 is that there should be a balance between relief that may be granted to the foreign representative and the interests of the persons that may be affected by such relief.

Actions to Avoid acts Detrimental to Creditors (Article 23)

Under many national laws both individual creditors and insolvency administrators have a right to bring actions to avoid or otherwise render ineffective acts detrimental to creditors. Such a right, insofar as it pertains to individual creditors, is often not governed by insolvency law but by general provisions of law (such as the civil code); the right is not necessarily tied to the existence of an insolvency proceeding against the debtor so that the action may be instituted prior to the commencement of such a proceeding. the person having such a right is typically only an affected creditor and not another person such as the insolvency administrator. Furthermore, the conditions for these individual-creditor actions are different from the conditions applicable to similar actions that might be initiated by an insolvency administrator.

The procedural standing conferred by Article 23 extends only to actions that are available to the local insolvency administrator in the context of an insolvency proceeding, and the article does not equate the foreign representative with individual creditors who may have similar rights under a different set of conditions. Such actions of individual creditors fall outside the scope of Article 23.

The Model law expressly provides that a foreign representative has "standing" to initiate actions to avoid or otherwise render ineffective legal acts detrimental to creditors. The provision is drafted narrowly in that it does not create any substantive right regarding such actions and also does not provide any solution involving conflict of laws. The effect of the provision is that a foreign representative is not prevented from initiating such actions by the sole fact that the foreign representative is not the insolvency administrator appointed in the enacting State.

Cooperation with Foreign Courts and Foreign Representatives

Chapter IV (Articles 25-27), on cross-border cooperation, is a core element of the Model law. Its objective is to enable courts and insolvency administrators from two or more countries to be efficient and achieve optimal results. Cooperation as described the chapter is often the only realistic way, for example, to prevent dissipation of assets, to maximize the value of assets.

Articles 25 and 26 not only authorize cross-border cooperation, also mandate it by providing that the court and the insolvency administrator "shall cooperate to the maximum extent possible". The articles are designed to overcome the widespread problem of national laws lacking rules providing a legal basis for cooperation by local courts with foreign courts in dealing with cross-border foreign representative insolvenices.

Enactment of such a legal basis would be particularly helpful in legal systems in which the discretion given to judges to operate outside areas of express statutory authorization is limited.

However, even in jurisdictions in which there is a tradition of wider judicial latitude, enactment of a legislative framework for cooperation has proved to be useful. To the extent that cross-border judicial cooperation in the enacting State is based on the principle of comity among nations, the enactment of Articles 25-27 offers an opportunity for making that principle more concrete and adaptable to the particular circumstances of cross-border insolvencies.

Intervention by a foreign representative in proceedings (Article 24)

Upon recognition of a foreign proceeding, in the foreign representative may, provided the requirements of the law of the State are met, intervene in any proceedings in they which the debtor is a party. The purpose of Article 24 is to avoid the denial of standing to the foreign representative to intervene in proceedings merely because the procedural legislation may not have conteplated the foreign representative among those having such standing. The article applies to foreign representatives of both main and non-main proceedings.

The articles in chapter IV leave certain decisions, in particular when and how to cooperate, to the courts and, subject to the supervision of the courts, to the insolvency administrators. For a court to cooperate with a foreign court or a foreign representative regarding a foreign proceeding, the Model law does not require a previous formal decision to recognize that foreign proceeding.

Cooperation and direct communication between courts or foreign representatives (Article 25)

The court is entitled to communicate directly with, or to request information or assistance directly from, foreign courts orforeign representatives. the ability of courts, with appropriate involvement of the parties, to communicate "directly" and to request information and assistance "directly" from foreign courts or foreign representatives is intended to avoid the use of time-consuming procedures traditionally in use, such as letters rogatory.

Cooperation and direct communication between a person or body administering a reorganization or liquidation under the law of the enacting state and foreign courts or foreign representatives (Article 26)

Article 26 on international cooperation between persons who are appointed to administer assets of insolvent debtors reflects the important role that such persons can play in devising and implementing cooperative arrangements, within the parameters of their authority. The provision makes it clear that an insolvency administrator acts under the overall supervision of the competent court. The Model law does not modify the rules already existing in the insolvency law of the enacting State on the supervisory functions of the court over the activities of the insolvency administrator.

According to Article 27, Cooperation may be implemented by any appropriate means, including:

- (a) appointment of a person or body to act at the direction of the court;
- (b) Communication of information by any means considered appropriate by the court;
- (c) Coordination of the administration and supervision of the debtor's assets and affairs;
- (d) approval or implementation by courts of agreements concerning the coordination of proceedings;
- (e) Coordination of concurrent proceedings regarding the same debtor;
- (f) the enacting State may wish to list additional forms or examples of cooperation.

Concurrent Proceedings

Commencement of a Proceeding after Recognition of a Foreign main Proceeding (Article 28)

After recognition of a foreign main proceeding, a proceeding under the laws of the enacting State relating to insolvency may be commenced only if the debtor has assets in the State enacting the Model Law. The effects of that proceeding shall be restricted to the assets of the debtor that are located in such State and to the extent necessary to implement cooperation and coordination under Articles 25, 26 and 27 to other assets of the debtor that, under the law of such State, should be administered in that proceeding.

Article 28, in conjunction with Article 29, provides that recognition of a foreign main proceeding will not prevent the commencement of a local insolvency proceeding concerning the same debtor as long as the debtorhas assets in the State.

Coordination of a Proceeding (Article 29)

Article 29 gives guidance to the court that deals with cases where the debtor is subject to a foreign proceeding and a local proceeding at the same time. Where a foreign proceeding and a proceeding under the laws of the enacting State relating to insolvency are taking place concurrently regarding the same debtor, the court shall seek cooperation and coordination under Articles 25, 26 and 27, and the following shall apply:

(a) When the proceeding in the State (which has enacted Model law) is taking place at the time the application for recognition of the foreign proceeding is filed,

(i) any relief granted under Article 19 or 21 must be consistent with the proceeding in such State; and

(b) When the proceeding in such State commences after recognition, or after the filing of the application for recognition, of the foreign proceeding,

(i) Any relief in effect under Article 19 or 21 shall be reviewed by the court and shall be modified or terminated if inconsistent with the proceeding in this State; and

(c) in granting, extending or modifying relief granted to a representative of a foreign non-main proceeding, the court must be satisfied that the relief relates to assets which, according to the law of the enacting State, should be administered in the foreign non-main proceeding or concerns information required in that proceeding.

(ii) if the foreign proceeding is recognized in such State as a foreign main proceeding, article 20 does not apply;	(ii) if the foreign proceeding is a foreign main proceeding, the stay and suspension referred to in Article 20 shall be modified or terminated, if inconsistent withthe proceeding in such State;	

The salient principle embodied in Article 29 is that the commencement of a local proceeding does not prevent or terminate the recognition of a foreign proceeding. This principle is essential for achieving the objectives of the Model law in that it allows the court in the enacting State in all circumstances to provide relief in favour of the foreign proceeding.

Coordination of more than one Foreign Proceeding (Article 30)

Article 30 deals with cases where the debtor is subject to insolvency proceedings in more than one foreign State and foreign representatives of more than one foreign proceeding seek recognition or relief in the enacting State. The provision applies whether or not an insolvency proceeding is pending in the enacting State. If, in addition to two or more foreign proceedings, there is a proceeding in the enacting State, the court will have to act pursuant to both Article 29 and Article 30.

In respect of more than one foreign proceeding regarding the same debtor, the court shall seek cooperation and coordination under Articles 25, 26 and 27, and the following shall apply:

(a) any relief granted under Article 19 or 21 to a representative of a foreign non-main proceeding after recognition of a foreign main proceeding must be consistent with the foreign main proceeding;

(b) if a foreign main proceeding is recognized after recognition, or after the filing of an application for recognition, of a foreign non-main proceeding, any relief in effect under Article 19 or 21 shall be reviewed by the court and shall be modified or terminated if inconsistent with the foreign main proceeding; and

(c) if, after recognition of a foreign non-main proceeding, another foreign non-main proceeding is recognized, the court shall grant, modify or terminate relief for the purpose of facilitating coordination of the proceedings.

The objective of Article 30 is similar to that of Article 29 in that the key issue in the case of concurrent proceedings is to promote cooperation, coordination and consistency of relief granted to different proceedings. Such consistency will be achieved by appropriate tailoring of relief to be granted or by modifying or terminating relief already granted. Unlike Article 29, which, as a matter of principle, gives primacy to the local proceeding, Article 30 gives preference to the foreign main proceeding, if there is one.

Rule of Payment in Concurrent Proceedings (Article 32)

Without prejudice to secured claims or rights in rem, a creditor who has received part payment in respect of its claim in a proceeding, pursuant to a law relating to insolvency, in a foreign State, may not receive a payment for the same claim in a proceeding under the laws of the enacting State relating to insolvency regarding the same debtor, so long as the payment to the other creditors of the same class is proportionately less than the payment the creditor has already received.

The rule set forth in Article 32, also referred to as the hotchpotch rule, is a useful safeguard in a legal regime for coordination and cooperation in the administration of cross-border insolvency proceedings. It is intended to avoid situations in which a creditor might obtain more favourable treatment than the other creditors of the same class by obtaining payment of the same claim in insolvency proceedings in different jurisdictions.

WORLD BANK PRINCIPLES — EFFECTIVE INSOLVENCY AND CREDITOR RIGHTS SYSTEMS

The World Bank Principles were originally developed in 2001 in response to a request from the international community in the wake of the financial crises in emerging markets in the late 90s. At the time, there were no internationally recognized benchmarks or standards to evaluate the effectiveness of domestic creditor rights and insolvency systems. The World Bank's initiative began in 1999, with the constitution of an ad hoc committee of partner organizations, and with the assistance of leading international experts who participated in the World Bank's Task Force and Working Groups. The Principles were vetted in a series of five regional conferences, involving officials and experts from some 75 countries, and drafts were placed on the World Bank's website for public comment. The Bank's Board of directors approved the Principles in 2001 for use in connection with the joint IMF-World Bank program to develop Reports on the Observance of Standards and Codes (ROSC), subject to reviewing the experience and updating the Principles as needed.

From 2001 to 2004, the Principles were used to assess country systems under the ROSC and Financial Sector Assessment Program (FSAP) in some 24 countries in all regions of the world. Assessments using the Principles have been instrumental to the Bank's developmental and operational work, and in providing assistance to member countries. This has yielded a wealth of experience and enabled the Bank to test the suffix of the Principles as a benchmark in a wide range of diverse country systems. In taking stock of that experience, the Bank has consulted a wide range of interested parties at the national and international level, including civil society, business and financial sectors, investors, professional groups, and others.

In 2003, the World Bank convened the Global Forum on Insolvency Risk Management (FIRM) to discuss the experience and lessons from the application of the Principles in the assessment program. The forum consisted of over 200 experts from 31 countries to discuss the lessons from the principles and to discuss further refinements with them. During 2003 and 2004, the Bank also convened three working group sessions of the Global Judges Forum, involving judges from approximately 70 countries, who have assisted the Bank in its review of the institutional framework principles and in developing more detailed recommendations for strengthening court practices for commercial enforcement and insolvency proceedings. Other regional fora have also provided a means for sharing experience and obtaining feedback in areas of the Principles, including the Forum on Asian insolvency reform (Fair) from 2002-2004 (organized by OECD and co- sponsored with the Bank and the Asian development Bank), and Forum on insolvency in Latin America (Fila) in 2004 organised by the Bank.

In the area of the insolvency law framework and creditor rights systems, staffs of the Bank maintained participation in the UNCITRAL working groups on insolvency law and security interests and liaised with UNCITRAL staff and experts to ensure consistency between the Bank's Principles and the UNCITRAL Legislative Guide on Insolvency Law. The Bank has also benefited from an ongoing collaboration with the International Association of Insolvency Regulators (IAIR) to survey regulatory practices of IAIR member countries and develop recommendations for strengthening regulatory capacity and frameworks for insolvency systems. A similar collaboration with INSOL International has provided feedback and input in the area of directors' and officers' liability and informal workout systems.

Based on the experience gained from the use of the Principles, and following extensive consultations, the Principles have been thoroughly reviewed and updated. The revised Principles have benefited from wide consultation and, more importantly, from the practical experience of using them in the context of the Bank's assessment and operational work.

The World Bank Principles have been designed as a broad-spectrum assessment tool to assist countries in their efforts to evaluate and improve core aspects of their commercial law systems that are fundamental to a sound investment climate, and to promote commerce and economic growth. Efficient, reliable and transparent creditor rights and insolvency systems are of key importance for reallocation of productive resources in the corporate sector, for investor confidence and forward looking corporate restructuring. These systems also play a pivotal role in times of crisis to enable a country and stakeholders to promptly respond to and resolve matters of corporate financial distress on systemic scales.

The Principles emphasize contextual, integrated solutions and the policy choices involved in developing those solutions. The Principles highlight the relationship between the cost and flow of credit (including secured credit) and the laws and institutions that recognize and enforce credit agreements (Part A). The Principles also outline key features and policy choices relating to the legal framework for risk management and informal corporate workout systems (Part B), formal commercial insolvency law frameworks (Part C) and the implementation of these systems through sound institutional and regulatory frameworks (Part D).

The principles have broader application beyond corporate insolvency regimes and creditor rights. the Principles are designed to be flexible in their application, and do not offer detailed prescriptions for national systems. The Principles embrace practices that have been widely recognized and accepted as good practices internationally. as legal systems and business and commerce are evolutionary in nature, so too are the Principles, and it is anticipated that these will continue to be reviewed going forward to take account of significant changes and developments.

THE WORLD BANK PRINCIPLES – A SUMMARY

A brief summary of the key elements of the World Bank Principles for effective insolvency and creditor rights systems is given below:

1. Credit Environment

Compatible credit and enforcement systems : A regularized system of credit should be supported by mechanisms that provide efficient, transparent and reliable methods for recovering debt, including seizure and sale of immovable and movable assets and sale or collection of intangible assets, such as debt owed to the debtor by third parties. An efficient system for enforcing debt claims is crucial to a functioning credit system, especially for unsecured credit. a creditor's ability to take possession of a debtor's property and to sell it to satisfy the debt is the simplest, most effective means of ensuring prompt payment. It is far more effective than the threat of an insolvency proceeding, which often requires a level of proof and a prospect of procedural delay that in all but extreme cases make it not credible to debtors as leverage for payment.

Collateral systems : One of the pillars of a modern credit economy is the ability to own and freely transfer ownership interests in property, and to grant a security interest to credit providers with respect to such interests and rights as a means of gaining access to credit at more affordable prices. Secured transactions play an enormously important role in a well-functioning market economy. Laws on secured credit mitigate lenders' risks of default and thereby increase the flow of capital and facilitate low cost financing. Discrepancies and uncertainties in the legal framework governing security interests are the main reasons for high costs and unavailability of credit, especially in developing countries.

The legal framework for secured lending addresses the fundamental features and elements for the creation, recognition and enforcement of security interests in all types of assets, movable and immovable, tangible and intangible, including inventories, receivables, proceeds and future property, and on a global basis, including both possessory and non-possessory interests. the law should encompass any or all of a debtor's obligations to a creditor, present or future and between all types of persons. In addition, it should provide for effective notice and registration rules to be adapted to all types of property, and clear rules of priority on competing claims or interests in the same assets. For security rights and notice to third parties to be effective, they must be capable of being publicized at reasonable costs and easily accessible to stakeholders. A reliable, affordable, public registry system is therefore essential to promote optimal conditions for asset based lending. Where several registries exist, the registration system should be integrated to the maximum extent possible so that all notices recorded under the secured transactions legislation can be easily retrieved.

Enforcement systems: A modern, credit-based economy requires predictable, transparent and affordable enforcement of both unsecured and secured credit claims by efficient mechanisms outside of insolvency, as well as a sound insolvency system. These systems must be designed to work in harmony. Commerce is a system of commercial relationships predicated on express or implied contractual agreements between an enterprise and a wide range of creditors and constituencies. Although commercial transactions have become increasingly complex as more sophisticated techniques are developed for pricing and managing risks, the basic rights governing these relationships and the procedures for enforcing these rights have not changed much. These rights enable parties to rely on contractual agreements, fostering confidence that fuels investment, lending and commerce. Conversely, uncertainty about the enforceability of contractual rights increases the cost of credit to compensate for the increased risk of non-performance or, in severe cases, leads to credit tightening.

Credit information systems: A modern credit-based economy requires access to complete, accurate and reliable information concerning borrowers' payment histories. This process should take place in a legal environment that provides the framework for the creation and operation of effective credit information systems. Permissible uses of information from credit information systems should be clearly circumscribed, especially regarding information about individuals. Legal controls on the type of information collected and distributed by credit information systems may often be used to advance public policies, including anti-discrimination laws.

Privacy concerns should be addressed through notice of the existence of such systems, notice of when any information from such systems is used to make adverse decisions, and access by data subjects to stored credit information with the ability to dispute and have corrected inaccurate or incomplete information. An effective enforcement and supervision mechanism should be in place that provides efficient, inexpensive, transparent and predictable methods for resolving disputes concerning the operation of credit information systems along with proportionate sanctions which encourage compliance but that are not so stringent as to discourage operations of such systems.

Informal corporate workouts : Corporate workouts should be supported by an environment that encourages participants to restore an enterprise to financial viability. Informal workouts are negotiated in the "shadow of the law." accordingly, the enabling environment must include clear laws and procedures that require disclosure of or access to timely and accurate financial information on the distressed enterprise; encourage lending to, investment in or recapitalization of viable distressed enterprises; support a broad range of restructuring activities, such as debt write-offs, reschedulings, restructurings and debt-equity conversions; and provide favourable or neutral tax treatment for restructurings. A country's financial sector should promote an informal out-of-court process for dealing with cases of corporate financial difficulty in which banks and other financial institutions have a significant exposure— especially in markets where enterprise insolvency is systemic.

2. Insolvency Law Systems

Commercial insolvency: Though approaches vary, effective insolvency systems have a number of aims and objectives. Systems should aspire to:

(i) integrate with a country's broader legal and commercial systems;	(ii) maximize the value of a firm's assets and recoveries by creditors;	(iii) provide for both efficient liquidation of nonviable businesses and those where liquidation is likely to produce a greater return to creditors and reorganization of viable businesses;	(iv) strike a careful balance between liquidation and reorganization, allowing for easy conversion of proceedings from one proceeding to another;
(v) provide for equitable treatment of similarly situated creditors, including similarly situated foreign and domestic creditors;	(vi) provide for timely, efficient and impartial resolution of insolvencies;	(vi) provide for timely, efficient and impartial resolution of insolvencies;	(viii) prevent the premature dismemberment of a debtor's assets by individual creditors seeking quick judgments;

(ix) provide a transparent procedure that contains, and consistently applies, clear risk allocation rules and incentives for gathering and dispensing information;	(x) recognize existing creditor rights and respect the priority of claims with a predictable and established process; and	(xi) establish a framework for cross-border insolvencies, with recognition of foreign proceedings.

Where an enterprise is not viable, the main thrust of the law should be swift and efficient liquidation to maximize recoveries for the benefit of creditors. Liquidations can include the preservation and sale of the business, as distinct from the legal entity. On the other hand, where an enterprise is viable, meaning it can be rehabilitated, its assets are often more valuable if retained in a rehabilitated business than if sold in a liquidation. The rescue of a business preserves jobs, provides creditors with a greater return based on higher going concern values of the enterprise, potentially produces a return for owners and obtains for the country the fruits of the rehabilitated enterprise.

The rescue of a business should be promoted through formal and informal procedures. rehabilitation should permit quick and easy access to the process, protect all those involved, permit the negotiation of a commercial plan, enable a majority of creditors in favor of a plan or other course of action to bind all other creditors (subject to appropriate protections) and provide for supervision to ensure that the process is not subject to abuse.

3. Implementation: Institutional and Regulatory Frameworks

Strong institutions and regulations are crucial to an effective insolvency system. The institutional framework has three main elements: the institutions responsible for insolvency proceedings, the operational system through which cases and decisions are processed and the requirements needed to preserve the integrity of those institutions— recognizing that the integrity of the insolvency system is the linchpin for its success.

4. Overarching Considerations of sound Investment Climates

Transparency, accountability and corporate governance: Minimum standards of transparency and corporate governance should be established to foster communication and cooperation. Disclosure of basic information – including financial statements, operating statistics and detailed cash flows – is recommended for sound risk assessment. Accounting and auditing standards should be compatible with international best practices so that creditors can assess credit risk and monitor a debtor's financial viability. A predictable, reliable legal framework and judicial process are needed to implement reforms, ensure fair treatment of all parties and deter unacceptable practices.

> Transparency increases confidence in decision making and so encourages the use of out of court restructuring options. Such options are preferable because they often provide higher returns to lenders than straight liquidation through the legal process–and because they avoid the costs, complexities and uncertainties of the legal process.

Corporate law and regulation should guide the conduct of the borrower's options are preferable because shareholders. a corporation's board of directors should be responsible, accountable and independent of management, subject to best practices on corporate governance. The law should be imposed impartially and consistently. Creditor rights and insolvency systems interact with and are affected by these additional systems, and are most effective when good practices are adopted in other relevant parts of the legal system, especially the commercial law.

Transparency and Corporate Governance: Transparency and good corporate governance are the cornerstones of a strong lending system and corporate sector. Transparency exists when information is assembled and made readily available to other parties and, when combined with the good behavior of "corporate citizens," creates an informed and communicative environment conducive to greater cooperation among all parties. Transparency and corporate governance are especially important in emerging markets, which are more sensitive to volatility from external factors. Without transparency, there is a greater likelihood that loan pricing will not reflect underlying risks, leading to higher interest rates and other charges. transparency and strong corporate governance are needed in both domestic and cross-border transactions and at all phases of investment–at the inception when making a loan, when managing exposure while the loan is outstanding, and especially once a borrower's financial difficulties become apparent and the lender is seeking to exit the loan.

Predictability: Investment in emerging markets is discouraged by the lack of well-defined and predictable risk allocation rules and by the inconsistent application of written laws. Moreover, during systemic crises investors often demand uncertainty risk premiums too onerous to permit markets to clear. Some investors may avoid emerging markets entirely despite expected returns that far outweigh known risks. Rational lenders will demand risk premiums to compensate for systemic uncertainty in making, managing and collecting investments in emerging markets. The likelihood that creditors will have to rely on risk allocation rules increases as fundamental factors supporting investment deteriorate. That is because risk allocation rules set minimum standards that have considerable application in limiting downside uncertainty, but that usually do not enhance returns in non- distressed markets. During actual or perceived systemic crises, lenders tend to concentrate on reducing risk, and risk premiums soar. At these times the inability to predict downside risk can cripple markets. The effect can impinge on other risks in the country, causing lender reluctance even towards untroubled borrowers.

UNITED STATES BANKRUPTCY CODE

In the United States of America, all bankruptcy cases are handled in federal courts under rules outlined in the "Bankruptcy Code", a federal law. it is a uniform federal law that governs all bankruptcy cases in America. The Bankruptcy Code was enacted in 1978 by § 101 of the Bankruptcy Reform Act, 1978 and is codified as title 11 of the United States Code. The procedural aspects of the bankruptcy process are governed by the Federal rules of Bankruptcy Procedure (Bankruptcy rules).

Six basic types of bankruptcy cases are provided for under the US Bankruptcy Code.

Chapter 7 titled "liquidation" in Chapter 7 Bankruptcy, a court-appointed trustee or administrator takes possession of non-exempt assets, liquidates these assets and then uses the proceeds to pay creditors.

Chapter 9 titled "adjustment of debts of a Municipality". Chapter 9 Bankruptcy proceedings provides for reorganization which is available to municipalities. In Chapter 9 Bankruptcy proceedings a municipality (which includes cities, towns, villages, counties, taxing districts, municipal utilities, and school districts) get protection from creditors and a municipality can pay back debt through a confirmed payment plan.

Chapter 11 titled "reorganization". Unlike Chapter 7 where the business ceases operations and a trustee sells all of its assets, under Chapter 11 the debtor remains in control of its business operations and repay creditors concurrently through a court-approved reorganization plan.

Chapter 12 was added to the Bankruptcy Code in 1986. It allows a family farmer or fisherman to continue to operate the business while the plan is being carried out.	Chapter 13 enables individuals with regular income to develop a plan to repay all or part of their debts.	Chapter 15 was added to the Bankruptcy Code in 2005. It provides mechanism for dealing with insolvency cases involving debtors, claimants and other interested parties involving more than one country. Under Chapter 15 a representative of a corporate bankruptcy proceeding outside the country can get access to the united States courts.

Chapter 11 Reorganization

American bankruptcy procedures enable sick Companies to restructure its debt obligations even while remaining operational. In this context, one must recognise that in the US the well-known Chapter 11 bankruptcy proceedings are considered as re-organization/ resurrection process for corporates.

Chapter 11 consists of sections 1101 to 1174 and is divided into following four sub chapters:

Sub-chapter I – Office and administration (Sections 1101 to 1116)

Sub-chapter II – The plan (Sections 1121 to 1129)

Sub-chapter III – Post confirmation matters (Sections 1141 to 1146)

Sub-chapter IV – Reorganization (Sections 1161 to 1174)

Many companies are known to have revived under Chapter 11. Further, Chapter 11 ensures the emergence of companies with sustainable debt levels and profitable working. Chapter 11 bankruptcy proceedings are available to every business, whether organized as a corporation, partnership or sole proprietorship, and to individuals, although it is most prominently used by corporate entities. One of the most remarkable events in recent business history has been the decision of General Motors Corporation USA to file bankruptcy proceedings — a decision forced on the company after it lost market share in the ongoing recession. Its assets were significantly lower than its liabilities. It has emerged from 40 days bankruptcy protection after creating a "new GM" made up of the best assets with fewer brand, fewer employees, etc. For that matter, Chapter 11 could even recover WorldCom which emerged from bankruptcy as MCI during 2004. Railroad Section 363 under Chapter 11 of US Bankruptcy law is an established procedure which enables companies to sell assets free of debts and encumbrances to preserve the value of the enterprise. A company under Chapter 11 can choose to sell off particular assets. A bankrupt company, the "debtor," might use this Code to "reorganize" its business and become profitable again.

The key to a successful Chapter 11 case is the continued operation of the debtor's business. In addition to running the business, the debtor or the trustee must fulfill additional duties required by the Bankruptcy Code and work with creditors, the court, and other parties to obtain financing for ongoing business operations.

Salient Features of Chapter 11

- Chapter 11 is not a declaration of insolvency

- Companies don't file under Chapter 11 to liquidate; they do so in order to continue operating and to take the necessary steps to emerge as a financially stronger business, reorganizing their operations or balance sheet or in some cases by selling substantially all its assets.

- Management remains in control of the business during the chapter 11 rehabilitative process. Trustees, administrators and monitors typically are not appointed.

- Chapter 11 normally does not cause interruption to business operations.

- The company is given breathing room during the process - an "automatic stay" generally prevents parties from taking legal action against the company or taking the company's assets.

- Most publicly-held companies prefer to file under Chapter 11 rather than Chapter 7 because they can still run their business and control the bankruptcy process. Chapter 11 provides a process for rehabilitating the business of the company.

Sometimes the company successfully works out a plan to return to profitability; sometimes, in the end, it liquidates. Under Chapter 11 reorganization, a company usually keeps doing business and its stock and bonds may continue to trade in securities markets.

The U.S. trustee, the bankruptcy arm of the department of Justice, appoints one or more committees to represent the interests of creditors and stockholders in working with the company to develop a plan of reorganization to enable it to get out of debt. The plan must be accepted by the creditors, bondholders, and stockholders, and confirmed by the court. However, even if creditors or stockholders vote against the plan, the court can disregard the vote and still confirm the plan if it finds that the plan treats creditors and stockholders fairly.

Committees of creditors and stockholders negotiate a plan with the company to relieve the company from repaying part of its debt so that the company is able to get back to its normal condition.

After the committees work with the company to develop a plan, the bankruptcy court must find that it legally complies with the Bankruptcy Code before the plan can be implemented.

Thus, Chapter 11 bankruptcy involves a reorganization plan that accommodates debt reorganization through a payment plan and the major advantage is that the debtors generally remain in possession of their property and operate their business under the supervision of Court. Chapter 11 debtors also often keep a substantial portion of their assets. The provisions of Chapter 11 allow the debtor, relief from pending obligations and the opportunity to reorganize its business and restructure debts while continuing to operate the business. Under this chapter a company can choose to sell off particular assets. Accordingly, subsidiaries outside US need not be included in the Chapter 11 filings.

There is therefore no change in the legal status of its subsidiaries that are kept out of Chapter 11 filings. Further, debtors audit, debtors counselling, Mandatory debtor education, etc. are provided under US Bankruptcy laws which help in minimizing the fraudulent bankruptcies. In the light of the above, a need is felt to have similar legal framework in India which allows continuity of business during bankruptcy proceedings, control over the management of company filing bankruptcy application, keeping subsidiaries / certain assets outside the purview of bankruptcy application, etc. in line with Chapter 11 of US Bankruptcy Code.

Enabling provisions for cross border transactions under Insolvency and Bankruptcy Code, 2016

Sections 234 and 235 of the Insolvency and Bankruptcy Code, 2016 make provisions to deal with cases involving cross border insolvency.

Agreements with foreign countries – Section 234 empower the central government to enter into an agreement with other countries to resolve situations pertaining to cross border insolvency. Section 234 of the Code provides that:

- The Central Government may enter into an agreement with the Government of any country outside India for enforcing the provisions of this Code. [Section 234(1)]

- The Central Government may, by notification in the Official Gazette, direct that the application of provisions of this Code in relation to assets or property of corporate debtor or debtor, including a personal guarantor of a corporate debtor, as the case may be, situated at any place in a country outside India with which reciprocal arrangements have been made, shall be subject to such conditions as may be specified. [Section 234(2)]

Letter of request to a country outside India in certain cases – Section 235 of the Code lays down that notwithstanding anything contained in this Code or any law for the time being in force if, in the course of insolvency resolution process, or liquidation or bankruptcy proceedings, as the case may be, under this Code, the resolution professional, liquidator or bankruptcy trustee, as the case may be, is of the opinion that assets of the corporate debtor or debtor, including a personal guarantor of a corporate debtor, are situated in a country outside India with which reciprocal arrangements have been made under section 234, he may make an application to the adjudicating authority that evidence or action relating to such assets is required in connection with such process or proceeding. [Section 235(1)]

The Adjudicating Authority on receipt of an application under sub-section (1) and, on being satisfied that evidence or action relating to assets under sub-section (1) is required in connection with insolvency resolution process or liquidation or bankruptcy proceeding, may issue a letter of request to a court or an authority of such country competent to deal with such request. [Section 235(2)]

The current cross border insolvency framework in India is dependent on India entering bilateral agreements with other countries. Finalisation of bilateral agreements is a long drawn process as it involves long term negotiations and thus takes a lot of time. Moreover, every trade is distinct and thus it would be difficult for the adjudicating authorities to enforce the agreements/treaties entered into with other countries.

INSOLVENCY LAW COMMITTEE (ILC) ON CROSS BORDER INSOLVENCY

The Ministry of Corporate Affairs has constituted the Insolvency Law Committee (ILC) to recommend amendments to the Insolvency and Bankruptcy Code of India, 2016. The Committee has submitted its 2nd report to the Government on 16 October 2018 recommending amendments in the insolvency and Bankruptcy Code, 2016 with respect to cross-border insolvency.

The necessity of having Cross Border insolvency Framework under the insolvency and Bankruptcy Code arises from the fact that many Indian companies have a global presence and many foreign companies have presence in India. Inclusion of comprehensive legal framework dealing with cross border insolvency will be a major step forward and will bring Indian insolvency law on a par with that of matured jurisdictions.

The ILC has recommended the adoption of the UNCITRAL Model law of Cross Border insolvency, 1997, as it provides for a comprehensive framework to deal with cross-border insolvency issues. The Committee proposed a draft 'Part Z' in the insolvency and Bankruptcy Code, 2016, based on an analysis of the UNCITRAL Model law. The Committee has also recommended a few carve outs to ensure that there is no inconsistency between the domestic insolvency framework and the proposed Cross Border insolvency Framework.

The UNCITRAL Model law has been adopted in as many as 44 countries and, therefore, forms part of international best practices in dealing with cross border insolvency issues. The advantages of the Model law are the precedence given to domestic proceedings and protection of public interest. The other advantages include greater confidence generation among foreign investors, adequate flexibility for seamless integration with the domestic insolvency law and a robust mechanism for international cooperation.

The Model law deals with four major principles of cross-border insolvency, namely direct access to foreign insolvency professionals and foreign creditors to participate in or commence domestic insolvency proceedings against a defaulting debtor; recognition of foreign proceedings & provision of remedies; cooperation between domestic and foreign courts & domestic and foreign insolvency practitioners; and coordination between two or more concurrent insolvency proceedings in different countries.

The main proceeding is determined by the Concept of Centre of Main Interest (COMI).

The necessity of having Cross Border insolvency Framework under the insolvency and Bankruptcy Code arises from the fact that many Indian companies have a global footprint and many foreign companies have presence in multiple countries including India. although the proposed Framework for Cross Border insolvency will enable us to deal with Indian companies having foreign assets and vice versa, it still does not provide for a framework for dealing with enterprise groups, which is still work in progress with UNCITRAL and other international bodies. The inclusion of the Cross Border insolvency Chapter in the Insolvency and Bankruptcy Code of India, 2016, will be a major step forward and will bring Indian insolvency law at par with that of matured jurisdictions.

Key recommendations of the committee

Applicability: the Committee recommended that at present, draft Part Z should be extended to corporate debtors only.

Duplicity of regimes: the Committee noted that currently the Companies act, 2013 contains provisions to deal with insolvency of foreign companies. It observed that once Part Z is enacted, it will result in a dual regime to handle insolvency of foreign companies. It recommended that the Ministry of Corporate Affairs undertake a study of such provisions in the Companies act, 2013 to assess whether to retain them.

Reciprocity: the Committee recommended that the Model law may be adopted initially on a reciprocity basis. This may be diluted subsequently upon re-examination. Reciprocity indicates that a domestic court will recognise and enforce a foreign court's judgment only if the foreign country has adopted similar legislation to the domestic country.

Access to Foreign representatives: the Model law allows foreign insolvency professionals and foreign creditors access to domestic courts to seek remedies directly. Direct access with regards to foreign creditors is envisaged under the Code even presently. With respect to access by foreign insolvency professionals to Indian courts, the Committee recommended that the Central Government be empowered to devise a mechanism that is practicable in the current Indian legal framework.

Centre of Main interests (COMI): the Model law allows recognition of foreign proceedings and provides relief based on this recognition. Relief may be provided if the foreign proceeding is a main proceeding or non-main proceeding. If the domestic courts determine that the debtor has its COMI in a foreign country, such foreign proceedings will be recognised as the main proceedings. This recognition will result in certain automatic relief, such as allowing foreign representatives greater powers in handling the debtor's estate.

For non-main proceedings, such relief is at the discretion of the domestic court. the Committee recommended that a list of indicative factors comprising COMI may be inserted through rule-making powers. Such factors may include location of the debtor's books and records, and location of financing.

Cooperation: the Model law lays down the basic framework for cooperation between domestic and foreign courts, and domestic and foreign insolvency professionals. Given that the infrastructure of adjudicating authorities under the Code is still evolving, the cooperation between adjudicating authorities and foreign courts is proposed to be subject to guidelines to be notified by the Central Government.

Concurrent Proceedings: the Model law provides a framework for commencement of domestic insolvency proceedings, when a foreign insolvency proceeding has already commenced or vice versa. It also provides for coordination of two or more concurrent insolvency proceedings in diff countries by encouraging cooperation between courts. The Committee recommended adopting provisions in relation to these in draft Part Z.

Public policy considerations: Part Z provides that the adjudicating authority may refuse to take action under the Code if it is contrary to public policy. The Committee recommended that in proceedings where the authority is of the opinion that a violation of public policy may be involved, a notice must be issued to the Central Government. If the authority does not issue notice, the Central Government may be empowered to apply to it directly.

CASE LAW

Jet Airways (India) Ltd. v. State Bank of India & Anr. Company Appeal (AT) (Insolvency) No. 707 of 2019

This is the first case touching the realm of cross border insolvency in India. In the instant case Jet Airways (India) limited, ('Company') was subjected to parallel insolvency proceedings in India as well as in the Netherlands. in India, the Company has been admitted into a corporate insolvency resolution process under the insolvency and Bankruptcy Code, 2016 (the "Indian Proceedings"). Pursuant to the order of the NCLT and resolutions duly passed at the meeting of the committee of creditors of the Company ("CoC") dated 16 July 2019, the Resolution Professional (RP) had been appointed, resulting in the powers of the board of directors of the Company being vested with the RP.

In the Netherlands, the Company has been declared bankrupt and the Dutch trustee had been appointed to manage the estate of the Company (the "Dutch Proceedings").

On an application made by the Dutch trustee, appealing the 20 June 2019 order of the NCLT before the Hon'ble National Company Law Appellate Tribunal, New Delhi ("NCLAT"), the NCLAT, by its orders dated 12 July 2019 and 21 august 2019 ("NCLAT Order"), inter alia, directed the RP, in consultation with the CoC, to consider the prospect of cooperating with the Dutch trustee so as to have joint "corporate insolvency resolution process of the Company" and further vide its order dated 04 September 2019 directed the RP under the Indian proceedings to reach an arrangement/agreement with the Dutch trustee to extend such cooperation to each other, further allowing the CoC to guide the RP to enable him to prepare an agreement in reaching the terms of arrangement of cooperation with the Dutch trustee in the best interest of the Company and all its stakeholders ("Proposed Cooperation").

The NCLAT set aside the order dated 20th June, 2019 passed by the National Company law tribunal, Mumbai Bench in so far it related to the observations that the 'Dutch Court' has no jurisdiction in the matter of 'corporate insolvency resolution process' of 'Jet Airways (India) Limited, (Offshore Regional Hub) and the consequential directions as given to the 'Resolution Professional' in respect of 'Offshore proceedings'. However, NCLAT did not interfered with the order of admission of application under Section 7 of the Code filed by the 'State Bank of India' against 'Jet Airways (India) limited', therefore, joint 'Corporate Insolvency Resolution Process' will continue in accordance with Insolvency and Bankruptcy Code, 2016.

The Parties facilitated the Proposed Cooperation with formulation of a 'Cross Border insolvency Protocol'. The key agreements under the said Protocol was as follows:

(i) this Protocol represents a statement of intentions and guidelines designed to minimize the costs and maximize value of assets/recoveries for all creditors of the Proceedings, by promoting the sharing of relevant information among the Parties and the international coordination of related activities in the Proceedings, while respecting the separate interests of creditors and other interested parties to the Proceeding, and the independence, sovereignty, and authority of the NCLT/NCLAT and Dutch Bankruptcy Court.

(ii) in recognition of the substantive differences among the Proceedings in both jurisdictions, this Protocol shall not impose on the RP or the Dutch trustee any duties or obligations (i) that may be inconsistent with or that may conflict with the duties or obligations to which the Parties are subject under applicable law, or (ii) that are not in the interests of the Company's estate represented by the Parties and/or its creditors. Furthermore, nothing in this Protocol should be interpreted in any way so as to interfere with

    (i) the proper discharge of any duty, obligation or function of the Parties, or

    (ii) the exercise of statutory or other powers otherwise available to a Party under applicable law.

(iii) the Parties should coordinate with each other and cooperate in all aspects of the Proceedings in terms of this Protocol. in doing so, the Parties acknowledge and agree that the Parties shall deal in good faith with each other in the interests of maximizing value of assets/recovery for all of the Company's creditors.

The Parties recognised that the Company being an Indian company with its centre of main interest in India, the Indian Proceedings are the main insolvency proceedings and the Dutch Proceedings are the non-main insolvency proceedings:

(a) *Coordination* – to promote international cooperation and the coordination of activities in the Proceedings; and to provide for the orderly, effective, efficient, and timely administration of the Proceedings in order to reduce their cost and maximize recovery for creditors.

(b) *Communication* – to promote communication among the Parties and the CoC; and to provide, wherever possible, for direct communication among NCLT, NCLAT and Dutch Bankruptcy Court.

(c) *Information and data sharing* – to provide for the sharing of relevant information and data among the Parties in order to promote effective, efficient, and fair proceedings, and to avoid duplication of effort and activities by the parties.

(d) *Preservation* – to identify, preserve, and maximize the value of the Company's worldwide assets for the collective benefit of all creditors and other interested parties.

(e) *Claims Reconciliation* – To coordinate an efficient and transparent claims process.

(f) *Maximize value of assets/recoveries* – to cooperate in marshalling the assets of the Company in order to maximize value of assets/recovery for all of the Company's creditors.

(g) *Comity* – to maintain the independent jurisdiction, sovereignty, and authority of NCLT, NCLAT and Dutch Bankruptcy Court.

(iv) the Dutch trustee in the Indian Proceedings:

(a) in the spirit of cooperation, the Dutch trustee aims to not take any decision under the Dutch Proceedings that would adversely impact the interests of the Company or the creditors. in the event it becomes necessary for the Dutch trustee in compliance of the Dutch Bankruptcy Court or any other court, or under any applicable law, to take any decision that might adversely impact the interests of the Company or the creditors, the Ddutch trustee shall give advance intimation of such decision to the RP.

(b) in the event a resolution plan for the Company is submitted to the NCLT, the Dutch trustee shall facilitate the submission (by the Company) of a consistent reorganization plan in the Dutch Proceedings ("schuldeisersakkoord") in order to implement the resolution plan in the Dutch jurisdiction incorporating the payout mechanism that is included in such resolution plan so submitted to the NCLT for distribution of various amounts to various stakeholders including the creditors of the Company, in accordance with applicable Dutch laws.

(v) the Dutch trustee shall seek inputs, notify the RP and consult the RP, and will be mindful of the Indian Proceedings prior to any material decision being taken in the Dutch Proceedings, which may, inter alia, include:

(a) matters relating to any proposal or approval of a plan of reorganization or a resolution plan or plan of compromise or any other similar arrangement in the Dutch Proceedings

(b) matters relating to assuming, ratifying, rejecting, repudiating, modifying or assigning executory contracts having a material impact on the assets, operations, obligations, rights, property or business of the Company; and

(c) matters which are otherwise prohibited under Section 14 of the Insolvency and Bankruptcy Code, 2016.

(vi) The ‘Committee of Creditors’ have no role to play as the agreement reached between the ‘Dutch administrator’ and the ‘Resolution Professional’ of India is on the basis of the direction of this appellate tribunal. In spite of the same, unfortunately the ‘Committee of Creditors’ interfered with the matter and put its view to the ‘Resolution Professional’ resulting into difference of the suggestions.

(vii) The NCLAT clarified that the ‘Dutch Trustee (Administrator) will work in co-operation with the ‘Resolution Professional of India’ and, if any, suggestion is required to be given, he may give it to the ‘Resolution Professional’. The draft of ‘Cross Border Insolvency Protocol’ clause is made final and should be treated as a direction of this appellate tribunal and it would be mandatory to comply with the order of this appellate tribunal subject to the other procedures which are to be followed in terms of the ‘Insolvency and Bankruptcy Code, 2016’.

LESSON ROUND-UP

- Globally, cross-border insolvency laws are based on one country providing assistance to the other in taking control of the assets and eventual disposition of such assets of the debtor company.
- Cross-border insolvency regulates the treatment of financially distressed debtors where such debtors have assets or creditors in more than one country.
- A company is said to be insolvent when its liabilities exceed its assets which results in its inability to pay off the debts. Cross border insolvency issues arise when a non-resident is either a debtor or contributory or creditor.
- Since national insolvency laws have by and large not kept pace with the trend, they are often ill equipped to deal with cases of cross border nature. It hampers the rescue of financially troubled business.
- The United Nations Commission on International Trade Law (UNCITRAL) prepares international legislative texts for use by States in modernizing commercial law and non-legislative texts for use by commercial parties in negotiating transactions.
- The Legislative Guide on Insolvency Law was prepared by UNCITRAL on insolvency law, specifically corporate insolvency, to foster and encourage the adoption of effective national corporate insolvency regimes in 2004.
- The legislative Guide on insolvency law is intended to be used as a reference by national authorities and legislative bodies when preparing new laws and regulations or reviewing the adequacy of existing laws and regulations.
- The UNCITRAL Model law on Cross-Border insolvency, adopted in 1997, is designed to assist States to equip their insolvency laws with a modern, harmonized and fair framework to address more effectively instances of cross-border insolvency.
- The Model Law focuses on four elements identified as key to the conduct of cross-border insolvency cases, i.e., access, recognition, relief (assistance) and cooperation.
- In the United States of America, all bankruptcy cases are handled in federal courts under rules outlined in the Bankruptcy Code, a federal law. The Bankruptcy Code was enacted in 1978 and is codified as title 11 of the United States Code.
- Sections 234 and 235 of the Insolvency and Bankruptcy Code, 2016 make provisions to deal with ases involving cross border insolvency.
- Section 234 of the Code empowers the central government to enter into an agreement with other countries to resolve situations pertaining to cross border insolvency.
- The Insolvency Law Committee (ILC) on cross border insolvency set-up by Government for a robust cross-border insolvency law in India has submitted its recommendations.

- The ILC has recommended the adoption of the UNCITRAL Model law of Cross Border Insolvency, 1997, as it provides for a comprehensive framework to deal with cross-border insolvency issues.
- The Committee has proposed a draft 'Part Z' in the Insolvency and Bankruptcy Code, 2016 relating to cross-border insolvency.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).

1. Companies through their multi-layered structures, move cash and other assets to other jurisdictions, which creates hurdle in regulating cross-border insolvency and financial distress. Discuss.
2. Why is UNCITRAL Model law on Cross Border insolvency a preferred legislation worldwide in dealing with cross-border insolvency?
3. Mention the salient provisions of the UNCITRAL Legislative Guide on insolvency laws.
4. Discuss whether the Insolvency and Bankruptcy Code, 2016 provides a robust mechanism to deal with cross border insolvency?
5. The recent recommendations of the Insolvency Law Committee (ILC) on cross-border insolvency are in line with the provisions set-out in the UNCITRAL Model law on cross-border insolvency. Discuss.
6. What do you understand by Centre of Main Interest (COMI) under UNCITRAL Model law? Ascertaining the COMI will be critical to the working of the cross border insolvency law in India. Discuss.

Liquidation on or after failing of Resolution Plan

Lesson 22

KEY CONCEPTS

■ Liquidator ■ Liquidation Cost ■ Liquidation Commencement Date ■ Financial Sector Regulator ■ Claims ■ New Value ■ Security Interest

Learning Objectives

To understand the:

- Initiation of Liquidation
- Appointment and Role of Liquidator
- Liquidation Estate
- Distribution of assets in Liquidation
- Dissolution of Corporate Debtor

Lesson Outline

- Introduction
- Initiation of Liquidation
- Appointment of Liquidator and Fee to be paid
- Powers and Duties of Liquidator
- Liquidation Estate
- Powers of Liquidator to Access Information
- Consolidation of claims
- Distribution of assets
- Dissolution of Corporate Debtor
- Lesson Round-Up
- Test Yourself
- List of Further Readings
- Other References (Including Websites / Video Links)

REGULATORY FRAMEWORK

- Section 33 to 54 of the Insolvency and Bankruptcy Code, 2016
- The Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016

INTRODCTION

Sections 33 to 54 in Chapter III of Part II of the Insolvency and Bankruptcy Code,2016 lay down the law relating to liquidation process for corporate persons.

An attempt is first made to resolve the insolvency of corporate debtor through corporate insolvency resolution process laid down in Chapter II of Part II of the Code. The provisions relating to liquidation in Chapter III of Part II of the Code comes into effect only if the attempt to resolve corporate insolvency under Chapter II of the Code fail.

It can thus be seen that the primary focus of the legislation is to ensure revival and continuation of the corporate debtor by protecting the corporate debtor from its own management and from a corporate death by liquidation."

The Hon'ble Supreme Court in the matter of ***'Swiss Ribbons Pvt. Ltd. & Anr. Vs. Union of India & Ors.'***, observed:

"What is interesting to note is that the Preamble does not, in any manner, refer to liquidation, which is only availed of as a last resort if there is either no resolution plan or the resolution plans submitted are not up to the mark. Even in liquidation, the liquidator can sell the business of the corporate debtor as a going concern....

The Insolvency and Bankruptcy Board of India has made the **Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016** to regulate the liquidation process under Chapter III of Part II of the Insolvency and Bankruptcy Code, 2016. These regulations are amended from time to time by the Insolvency and Bankruptcy Board of India.

INITIATION OF LIQUIDATION

Section 33 of the Code lists out the triggers for initiating the liquidation process for corporate persons. Section 33 of the Code reads as follows:

"(1) Where the Adjudicating Authority,

(a) before the expiry of the insolvency resolution process period or the maximum period permitted for completion of the corporate insolvency resolution process under section 12 or the fast track corporate insolvency resolution process under section 56, as the case may be, does not receive are solution plan under sub-section (6) of section 30; or

(b) rejects the resolution plan under section 31 for the non-compliance of the requirements specified there in, it shall-

(i) pass an order requiring the corporate debtor to be liquidated in the manner as laid down in this Chapter;

(ii) issue a public announcement stating that the corporate debtor is in liquidation; and

(iii) require such order to be sent to the authority with which the corporate debtor is registered.

(2) Where the resolution professional, at any time during the corporate insolvency resolution process but before confirmation of resolution plan, intimates the Adjudicating Authority of the decision of the committee of creditors approved by not less than sixty-six percent of the voting share to liquidate the corporate debtor, the Adjudicating Authority shall pass a liquidation order as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section (1).

Explanation.–For the purpose of this sub-section, it is hereby declared that the committee of creditors may take the decision to liquidate the corporate debtor, any time after its constitution under sub-section(1) of section 21 and before the confirmation of the resolution plan, including at any time before the preparation of the information memorandum.

(3) Where the resolution plan approved by the Adjudicating Authority under Section 31 or under sub-section (1) of Section 54L is contravened by the concerned corporate debtor, any person other than the corporate debtor, whose interests are prejudicially affected by such contravention, may make an application to the Adjudicating Authority for a liquidation order as referred to in sub-clauses (i), (ii),(iii) of clause (b) sub-section (1).

(4) On receipt of an application under sub-section (3), if the Adjudicating Authority determines that the corporate debtor has contravened the provisions of the resolution plan, it shall pass a liquidation order as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section(1).

(5) Subject to section 52, when a liquidation order has been passed, no suit or other legal proceeding shall be instituted by or against the corporate debtor:

Provided that a suit or other legal proceeding may be instituted by the liquidator, on behalf of the corporate debtor, with the prior approval of the Adjudicating Authority.

In the matter of ***'Vedikat Nut Crafts Pvt. Ltd.'***, after perusing records, the Adjudicating Authority could not see any reason for not inviting resolution plan despite the fact that even a period of one month as balance period of 180 days was still available. NCLT observed that there was no reason for the Committee of Creditors to jump to the conclusion of seeking liquidation of the company without seeking extension of time of 90 days, without inviting expression of interest by the prospective resolution plan applicant as it falls foul of legal provisions and fair play. It presents a tell tale story of the irregularity committed by the Committee of Creditors. To say the least such a decision is arbitrary and should not be sustained.

(6) the provisions of sub-section (5) shall not apply to legal proceedings in relation to such transactions as may be notified by the Central Government in consultation with any financial sector regulator.

(7) The order for liquidation under this section shall be deemed to be a notice of discharge to the officers, employees and workmen of the corporate debtor, except when the business of the corporate debtor is continued during the liquidation process by the liquidator."

WHEN CAN LIQUIDATION BE ORDERED

1. Where the Adjudicating Authority does not receive a resolution plan before the expiry of Corporate Insolvency Resolution Process or Fast Track Insolvency Process under the Code.
2. Where the Adjudicating Authority rejects the resolution plan for non-compliance of requirements under Section 31 of the Code.
3. Where, at any time before confirmation of resolution plan, including at any time before the preparation of the information memorandum, the committee of creditors resolve to liquidate the corporate debtor.
4. Where the corporate debtor contravenes the terms of the resolution plan.

1. ***Where the Adjudicating Authority does not receive are solution plan***

   If the Adjudicating Authority, before the expiry of the insolvency resolution process period or the maximum period permitted for completion of the corporate insolvency resolution process under section 12 or the fast track corporate insolvency resolution process under section 56, as the case may be, does not receive are solution plan under sub-section (6) of section 30, it shall pass an order requiring the corporate debtor to be liquidated in the manner as laid down in Chapter III of Part II of the Code. [Section 33(1)]

2. ***Where the Adjudicating Authority rejects the resolution plan***

   If the Adjudicating Authority rejects there solution plan under section 31 for the non-compliance of the requirements specified therein, it shall pass an order requiring the corporate debtor to be liquidated in the manner as laid down in Chapter III of Part II of the Code.

   In both the scenarios above i.e., where the Adjudicating Authority does not receive are solution plan or where the Adjudicating Authority rejects the resolution plan, it shall:

   - pass an order requiring the corporate debtor to be liquidated in the manner as laid down in this Chapter;
   - issue a public announcement stating that the corporate debtor is in liquidation; and
   - require such order to be sent to the authority with which the corporate debtor is registered. [Section 33 (1)]

3. ***Where, at any time before confirmation of resolution plan, the committee of creditors resolve to liquidate corporate debtor***

   Where the resolution professional, at any time during the corporate insolvency resolution process but before confirmation of resolution plan, intimates the Adjudicating Authority of the decision of the committee of creditors approved by not less than sixty-six percent of the voting share to liquidate the corporate debtor, the Adjudicating Authority shall pass a liquidation order as referred to in sub-clauses (i), (ii)and (iii) of clause (b) of sub-section (1). [Section 33 (2)]

   The Insolvency and Bankruptcy Code (Second Amendment) Act, 2018 has amended sub-section (2) of section 33 to provide for a reduced threshold from seventy-five percent to **sixty-six percent** of voting share for obtaining the approval of the committee of creditors for making an application to the Adjudicating Authority to pass a liquidation order.

   It may be noted that the committee of creditors may take the decision to liquidate the corporate debtor, any time after its constitution under sub-section (1) of section 21 and before the confirmation of the resolution plan, including at any time before the preparation of the information memorandum. [Explanation to Section 33(1)]

4. ***Where the corporate debtor violates the terms of the resolution plan***

   Where the resolution plan approved by the Adjudicating Authority under section 31 (Corporate Insolvency Resolution Process) or under sub-section (1) of section 54L (Pre-packaged Insolvency Resolution Process), is contravened by the concerned corporate debtor, any person other than the corporate debtor, whose interests are prejudicially affected by such contravention, may make an application to the Adjudicating Authority for a liquidation order as referred to in sub-clauses (i), (ii), (iii) of clause (b) sub-section (1). [Section 33(3)]

   On receipt of an application under sub-section (3), if the Adjudicating Authority determines that the corporate debtor has contravened the provisions of the resolution plan, it shall pass a liquidation order as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section (1). [Section 33(4)]

   Bar to filing of suits and legal proceedings - Section 33 (5) provides that subject to section 52, when a liquidation order has been passed, no suit or other legal proceeding shall be instituted by or against the corporate debtor: Provided that a suit or other legal proceeding may be instituted by the liquidator, on behalf of the corporate debtor, with the prior approval of the Adjudicating Authority.

In the matter of ***Small Industries Development Bank of India v. Tirupati Jute Industries Limited [CP (IB) 508/KB/18*** and connected matters], the Adjudicating Authority noted that the resolution plan, which has been submitted for its approval, was subject to extinguishment of all claims (except criminal proceedings) against the Corporate Debtor, exemption of all taxes/dues by the Government/ local authorities, and closure of all proceedings pending against the Corporate Debtor relating to such dues. The Adjudicating Authority rejected the plan and ordered for liquidation. It observed that such a plan should not have been approved by the CoC, as it was not consistent with the provisions of section 30(2)(e) of the Code. It also observed that the Resolution Professional did not give correct advice when he submitted the plan for approval of CoC and therefore, it would not be proper to appoint him as the Liquidator.

Section 33 (6) further provides that the provisions of sub-section (5) shall not apply to legal proceedings in relation to such transactions as may be notified by the Central Government in consultation with any financial sector regulator.

"Financial Sector Regulator" means an authority or body constituted under any law for the time being in force to regulate services or transactions of financial sector and includes the Reserve Bank of India, the Securities and Exchange Board of India, the Insurance Regulatory and Development Authority of India, the Pension Fund Regulatory Authority and such other regulatory authorities as may be notified by the Central Government. [Section 3(18)]

Liquidation order to be deemed to be a notice of discharge- The order for liquidation under section 33 shall be deemed to be a notice of discharge to the officers, employees and work men of the corporate debtor, except when the business of the corporate debtor is continued during the liquidation process by the liquidator. [Section 33(7)]

Time for completion of Compromise or Arrangement: Regulation 2B of the IBBI (Liquidation Process) Regulations 2016 provides that where a compromise or arrangement is proposed under section 230 of the Companies Act, 2013, it shall be completed within ninety days of the order of liquidation under section 33.

It is provided that a person, who is not eligible under the Code to submit a resolution plan for insolvency resolution of the corporate debtor, shall not be a party in any manner to such compromise or arrangement. It is provided further that the liquidator shall file the proposal of compromise or arrangement only in cases where such recommendation has been made by the committee under regulation 39BA of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016: Provided further that the liquidator shall not file such proposal after expiry of thirty days from the liquidation commencement date.

The time taken on compromise or arrangement, not exceeding ninety days, shall not be included in the liquidation period.

In the case of ***Chennai Metro Rail Ltd. Vs. Lanco Infratech Ltd. (Represented by the Liquidator) & Ors. [Application No. 2826 of 2019]*** *judgement dated 15.10.2020,* Madras High Court held that Section 279 of the Companies Act, 2013 applies only in cases of winding up under the Companies Act, 2013 and not the Code. Section 279 of the Act deals with both pending suits and institution of new suits, while section 33(5) of the Code deals with new proceedings and Section 33(5) of the Code overrides section 279 of Act, by virtue of section 238 and by the principle 'special law overrides general law'.

APPOINTMENT OF LIQUIDATOR AND FEE TO BE PAID

Section 34 of the Code provides for the appointment of liquidator and the fees to be paid to him.

According to Section 5 (18) of the Code, a **"liquidator"** means an insolvency professional appointed as a liquidator in accordance with the provisions of Chapter III or Chapter V of this Part, as the case may be.

The Insolvency and Bankruptcy Code (Second Amendment) Act, 2018 has amended section 34 so as to require a written consent of resolution professional in specified form for appointment as a liquidator.

Resolution Professional to act as liquidator- Section 34 (1) provides that where the Adjudicating Authority passes an order for liquidation of the corporate debtor under section 33, the resolution professional appointed for the corporate insolvency resolution process under Chapter II or for the pre-packaged insolvency resolution process under Chapter III-A shall, subject to submission of a written consent by the resolution professional to the Adjudicatory Authority in specified form, shall act as the liquidator for the purposes of liquidation unless replaced by the Adjudicating Authority under sub-section (4).

Powers to vest in liquidator-Section 34 (2) further provides that on the appointment of a liquidator under section 34, all powers of the board of directors, key managerial personnel and the partners of the corporate debtor, as the case may be, shall cease to have effect and shall be vested in the liquidator.

Personnel of corporate debtor to extend all assistance and cooperation to the liquidator-Section 34 (3) mandates that the personnel of the corporate debtor shall extend all assistance and cooperation to the liquidator as may be required by him in managing the affairs of the corporate debtor and provisions of section 19 shall apply in relation to voluntary liquidation process as they apply in relation to liquidation process with the substitution of references to the liquidator for references to the interim resolution professional.

Replacement of resolution professional- Sub-section (4) of section 34 makes provision for the replacement of resolution professional. According to sub-section (4), the Adjudicating Authority shall by order replace the resolution professional, if:

a) the resolution plan submitted by the resolution professional under section 30 was rejected for failure to meet the requirements mentioned in sub-section (2) of section 30; or

(b) the Board recommends the replacement of a resolution professional to the Adjudicating Authority for reasons to be recorded in writing; or

(c) the resolution professional fails to submit written consent under sub-section (1).

For the purposes of clause (a) and clause (c) of sub-section (4), the Adjudicating Authority may direct the Board to propose the name of another insolvency professional to be appointed as a liquidator. [Section 34 (5)]

Taking charge as liquidator

In the case of ***'S. Muthuraju Vs. Commissioner of Police and Another'***, a group / mob of unknown persons hurled threats with weapons and did not allow the liquidator to enter the premise of the corporate debtor (CD) and carry out his functions. The Hon'ble NCLT directed the Superintendent of Police to give adequate police protection to the liquidator to enable him to perform his duties.

Can CoC challenge the appointment of liquidator after the liquidation order is passed by the Adjudicating Authority?

In the case of ***'Punjab National Bank Vs. Mr. Kiran Shah, Liquidator of ORG Informatics Ltd.'***, NCLAT held that after the liquidation order, the CoC has no role to play and that they are simply claimants, whose matters are to be determined by the liquidator and hence cannot move an application for his removal.

The Board shall propose the name of another insolvency professional along with written consent from the insolvency professional in the specified form within ten days of the direction issued by the Adjudicating Authority under sub-section (5). [Section 34(6)]

The Adjudicating Authority shall, on receipt of the proposal of the Board for the appointment of an insolvency professional as liquidator, by an order appoint such insolvency professional as the liquidator. [Section 34 (7)]

The matter of replacing the Resolution Professional (RP) was considered by the National Company Law Appellate Tribunal (NCLAT) in the matter of ***'Devendra Padamchand Jain v. State Bank of India'***. This case dealt with an appeal by the then RP of VNR Infrastructures, against the order of the National Company Law Tribunal (NCLT), Hyderabad bench, removing him and appointing another liquidator.

The NCLAT held that apart from the committee of creditors, the NCLT is also empowered to remove the RP, but it should be for the reasons and in the manner provided under the relevant section. In this case, RP had failed to properly examine the resolution plan and had not stated that the plan he submitted met all the requirements of section 30(2) of the Code. The NCLAT held that the NCLT has jurisdiction to remove the RP if it is not satisfied with its functioning, which amounts to non-compliance with section 30(2) of the Code.

Fee for the conduct of liquidation proceedings-Section 34(8) provides that an insolvency professional proposed to be appointed as a liquidator shall charge such fee for the conduct of the liquidation proceedings and in such proportion to the value of the liquidation estate assets, as may be specified by the Board.

The fees for the conduct of the liquidation proceedings under sub-section (8) shall be paid to the liquidator from the proceeds of the liquidation estate under section 53. [Section 34(9)]

POWERS AND DUTIES OF LIQUIDATOR

Section 35 provides an on-exhaustive list of powers and duties of the liquidator to ensure orderly completion of the liquidation proceedings.

Section 35(1) provides that subject to the directions of the Adjudicating Authority, the liquidator shall have the following powers and duties:

(a) to verify claims of all the creditors;

(b) to take into his custody or control all the assets, property, effects and actionable claims of the corporate debtor;

(c) to evaluate the assets and property of the corporate debtor in the manner as may be specified by the Board and prepare a report;

(d) to take such measures to protect and preserve the assets and properties of the corporate debtor as he considers necessary;

(e) to carry on the business of the corporate debtor for its beneficial liquidation as he considers necessary;

(f) subject to section 52, to sell the immovable and movable property and actionable claims of the corporate debtor in liquidation by public auction or private contract, with power to transfler such property to any person or body corporate, or to sell the same in parcels in such manner as may be specified: Provided that the liquidator shall not sell the immovable and movable property or actionable claims of the corporate debtor in liquidation to any person who is not eligible to be a resolution applicant;

(g) subject to section 52, to sell the immovable and movable property and actionable claims of the corporate debtor in liquidation by public auction or private contract, with power to transfer such property to any person or body corporate, or to sell the same in parcels in such manner as may be specified:

(h) to take out, in his official name, letter of administration to any deceased contributory and to do in his official name any other act necessary for obtaining payment of any money due and payable from a contributory or his estate which cannot be ordinarily done in the name of the corporate debtor, and in all such cases, the money due and payable shall, for the purpose of enabling the liquidator to take out the letter of administration or recover the money, be deemed to be due to the liquidator himself;

(i) to obtain any professional assi5tance from any person or appoint any professional, in discharge of his duties, obligations and responsibilities;

(j) to invite and settle claims of creditors and claimants and distribute proceeds in accordance with the provisions of this Code;

(k) to institute or defend any suit, prosecution or other legal proceedings, civil or criminal, in the name of on behalf of the corporate debtor;

(l) to investigate the financial affairs of the corporate debtor to determine undervalued or preferential transactions;

(m) to take all such actions, steps, or to sign, execute and verify any paper, deed, receipt document, application, petition, affidavit, bond or instrument and tor such purpose to use the common seal, if any, as may be necessary for liquidation, distribution of assets and in discharge of his duties and obligations and functions as liquidator;

(n) to apply to the Adjudicating Authority for such orders or directions as may be necessary for the liquidation of the corporate debtor and to report the progress of the liquidation process in a manner as may be specified by the Board; and

(o) to perform such other functions as may be specified by the Board.

Section 35(2) further provides that the liquidator shall have the power to consultany of the stakeholders entitled to a distribution of proceeds under section 53.

First proviso to section 35(2) provides that any such consultation shall not be binding on the liquidator. The second provison further provides that the records of any such consultation shall be made available to all other stakeholders not so consulted, in a manner specified by the Board.

Stakeholders' Consultation Committee

Regulation 31 A of the IBBI (Liquidation Process) Regulations,2016 mandates constitution of Stakeholders' Consultation Committee by the Liquidator, comprising of all creditors of the corporate debtor, within sixty days from the liquidation commencement date, based on the list of stakeholders prepared under regulation 31, to advise him on matters

(a) remuneration of professionals appointed under regulation 7;

(b) sale under regulation 32, including manner of sale, pre-bid qualifications, reserve price, marketing strategy and auction process.;

(c) fees of the liquidator;

(d) valuation under sub- regulation (2) of regulation 35;

(e) the manner in which proceedings in respect of preferential transactions, undervalued transaction, extortionate credit transaction or fraudulent or wrongful trading, if any, shall be pursued after closure of liquidation proceedings and the manner in which the proceeds, if any, from these proceedings shall be distributed;

(f) review of marketing strategy in case of failure of sale of corporate debtor as a going concern;

(g) continuation or institution of any suits or legal proceedings by or against the corporate debtor;

(h) extension of payment of balance sale consideration as provided in clause (12) of Para 1 of Schedule I, beyond ninety days, to be disclosed in the auction notice.

In the case of ***B.R. Traders Vs. Venkataramanarao Nagarajan & Ors. [CA (AT) (Ins.) No. 189 of 2019 and other appeals] Order dated 13.11.2019,*** *NCLAT* observed that the liquidator is duty bound to make every endeavour to protect and preserve the value of the property of the CD and manage the operations as a going concern.

In the case of ***IFCI Ltd. & Ors. Vs. BS Ltd. (in liquidation) IA No. 1148/2020 in CP(IB) No. 278/7/HDB/2018] order dated 07.01.2021,*** NCLT inter alia observed that the liquidator has been endowed with very wide powers as a quasi-judicial functionary under the Code. Section 35(2) empowers the liquidator to consult any of the stakeholders entitled to a distribution of proceeds under section 53, but the proviso makes it amply clear that such consultation is not binding on the liquidator.

LIQUIDATION ESTATE

Section 36 provides for the creation of a liquidation estate comprising the assets of the corporate debtor as set out in section 36(3). Section 36 also lists out the assets which are to be excluded from the liquidation estate. The Central Government has been given the power to notify assets, in consultation with the appropriate financial sector regulators, which will be excluded from the estate in the interest of efficient functioning of the financial markets.

Section 36(1) provides that for the purposes of liquidation, the liquidator shall for man estate of the assets mentioned in sub-section(3), which will be called the liquidation estate in relation to the corporate debtor.

Section 36(2) further provides that the liquidator shall hold the liquidation estate as a fiduciary for the benefit of all the creditors.

Liquidation estate shall comprise all liquidation estate assets-Section 36(3) provides the assets that comprise the liquidation estate while Section 36(4) provides the list of ass ets that must be excluded from the liquidation estate.

Assets to be included in the liquidation estate:

(a) any assets over which the corporate debtor has ownership rights, including all rights and interests therein as evidenced in the balance sheet of the corporate debtor or an information utility or records in the registry or any depository recording securities of the corporate debtor or by any other means as may be specified by the Board, including shares held in any subsidiary of the corporate debtor;

(b) assets that may or may not be in possession of the corporate debtor including but not limited to encumbered assets;

(c) tangible assets, whether movable or immovable;

(d) intangible assets including but not limited to intellectual property, securities (including shares held in a subsidiary of the corporate debtor) and financial instruments, insurance policies, contractual rights;

(e) assets subject to the determination of ownership by the court or authority;

(f) any assets or their value recovered through proceedings for avoidance of transactions in accordance with this Chapter;

(g) any asset of the corporate debtor in respect of which a secured creditor has relinquished security interest;

(h) any other property belonging to or vested in the corporate debtor at the insolvency commencement date; and

(i) all proceeds of liquidation as and when they are realised.

What shall not be included in the liquidation estate assets?

(a) assets owned by a third party which are in possession of the corporate debtor, including -

  (i) assets held in trust for any third party;

  (ii) bailment contracts;

  (iii) all sums due to any workmen or employee from the provident fund, the pension fund and the gratuity fund;

  (iv) other contractual arrangements which donot stipulate transfer of title but only use of the assets; and

  (v) such other assets as may be notified by the Central Government in consultation with any financial sector regulator.

(b) assets in security collateral held by financial services providers and are subject to netting and set-off in multi-lateral trading or clearing transactions;

(c) personal assets of any shareholder or partner of a corporate debtor as the case may be provided such assets are not held on account of avoidance transactions that may be avoided under this Chapter;

(d) assets of any Indian or foreign subsidiary of the corporate debtor; or

(e) any other assets as may be specified by the Board, including assets which could be subject to set-off on account of mutual dealings between the corporate debtor and any creditor.

Regulation 46A of the IBBI (Liquidation Process) Regulations, 2016, provides for exclusion of certain assets from the liquidation estate. It specifies that wherever the corporate debtor has given possession to an allottee in a real estate project, such asset shall not form a part of the liquidation estate of the corporate debtor for the purposes of clause (e) of sub-section (4) of section 36,

Are the dues in respect to Provident Fund/Pension Fund/Gratuity Fund part of the liquidation estate?

In the case of ***'Precision Fasteners Ltd. vs. Employees Provident Fund Organisation'***, the liquidators ought a declaration regarding attachment of movable and immovable properties of the CD (under liquidation) under Employees' Provident Funds and Miscellaneous Provisions Act, 1952 as null and void to enable him to dispose of these properties along side other assets of the CD. The AAnoted that in terms of the Code, the dues in respect to Provident Fund/Pension Fund/Gratuity Fund are not part of the liquidation estate. The AAvacated the attachment with a direction to the liquidate or to sell the assets and pay off the provident fund dues in priority to all claims payable by the CD in liquidation.

POWERS OF LIQUIDATOR TO ACCESS INFORMATION

Section 37 provides that the liquidator shall have the power to access any information systems for the purpose of admission and proof of claims and identification of assets to be held in the liquidation estate. This power to access information ensures easier verification of claims and identification of assets and liabilities of the corporate debtor.

Power to access any information systems- Section 37(1) provides that notwithstanding any thing contained in any other law for the time being in force, the liquidator shall have the power to access any information systems for the purpose of admission and proof of claims and identification of the liquidation estate assets relating to the corporate debtor from the following sources:

(a) an information utility;

(b) credit information systems regulated under any law for the time being in force;

(c) any agency of the Central, State or Local Government including any registration authorities;

(d) information systems for financial and non-financial liabilities regulated under any law for the time being in force;

(e) information systems for securities and assets posted as security interest regulated under any law for the time being in force;

(f) any database maintained by the Board; and

(g) any other source as may be specified by the Board.

Financial information required by creditors- The creditors may require the liquidator to provide the many financial information relating to the corporate debtor in such manner as may be specified. [Section 37(2)]

The liquidator shall provide information referred to in sub-section (2) to such creditors who have requested for such information within a period of seven days from the date of such request or provide reasons for not providing such information. [Section 37(3)]

CONSOLIDATION OF CLAIMS

Section 38 prescribes a time period for the collection of claims by the liquidator. It also specifies the methods by which different categories of creditors can submit and prove their claims.

Receipt or collection of claims- Section 38(1) provides that the liquidator shall receive or collect the claims of creditors within a period of thirty days from the date of the commencement of the liquidation process.

Submission of claim by financial creditor- According to section 38(2), a financial creditor may submit a claim to the liquidator by providing are cord of such claim with an information utility.

In cases where the information relating to the claim is not recorded in the information utility, the financial creditor may submit the claim in the same manner provided for the submission of claims for the operational creditor under sub-section(3).

Submission of claim by operational creditor- An operational creditor may submit a claim to the liquidator in such form and in such manner and along with such supporting documents required to prove the claim as may be specified by the Board. [Section 38(3)]

Claims by creditor who is partly a financial and partly an operational creditor-A creditor who is partly a financial creditor and partly an operational creditor shall submit claims to the liquidator to the extent of his financial debt in the manner as provided in sub-section (2) and to the extent of his operational debt under sub-section(3). [Section 38(4)]

Withdrawal or variation of claims- A creditor may withdraw or vary his claim under section 38 with in fourteen days of its submission. [Section 38(5)

Verification of Claims

Section 39 prescribes the procedure to be followed for the verification of claims by the liquidator.

According to section 39(1), the liquidator shall verify the claims submitted under section 38 within such time as specified by the Board. As per Regulation 30 of Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016, the verification must be done within thirty days from the last date of receipt of claims.

The liquidator may require any creditor or the corporate debtor or any other person to produce any other document or evidence which he thinks necessary for the purpose of verifying the whole or any part of the claim. [Section 39(2)]

Whether a liquidator can decide a claim of an appellant where a resolution plan is not approved and order of liquidation is passed?

In the case of ***'Prasad Gempex v. Star Agro Marine Exports Pvt. Ltd. & Ors.'***, it was held that " .....In case the resolution plan is not approved and the order of liquidation is passed, in such case, it will be open to the appellant to file claim before the liquidator in accordance with the provisions as referred to above and the liquidator will decide the claim under section 40 of the Code."

Admission or Rejection of Claims

Section 40 lays down the procedure for the admission and rejection of claims.

Admission or rejection of claims- The liquidator may, after verification of claims under section 39, either admit or reject the claim, in whole or in part, as the case may be. But if the liquidator rejects a claim, he shall record in writing the reasons for such rejection. [Section 40(1)]

Communication of decision- The liquidator shall communicate his decision of admission or rejection of claims to the creditor and corporate debtor within seven days of such admission or rejection of claims. [Section 40(2)]

Determination of Valuation of Claims

Section 41 provides that the liquidator shall determine the value of claims admitted under section 40 in such manner as may be specified by the Insolvency and Bankruptcy Board of India.

Appeal against the Decision of Liquidator

According to section 42, a credit or may appeal to the Adjudicating Authority against the decision of the liquidator accepting or rejecting the claims within fourteen days of the receipt of such decision.

T**he Insolvency and Bankruptcy Code (Second Amendment) Act, 2018** amended section 42 to provide clarity that a creditor may appeal to the Adjudicating Authority against the decision of the liquidator in both the scenarios i.e, acceptance or rejection of claims.

Preferential Transactions and Relevant Time

Related parties of ten possess information of the corporate debtor's financial affairs and may collude with him to siphon off assets with the knowledge that the corporate debtor might be come insolvent in the near future. Section 43 in validates transfers of property or an interest thereof given during the relevant time to a person for the benefit of a creditor, surety orguarant or on account of antecedent debt or other liabilities which have the effect of putting such creditor, surety orguarant or in a better position than the position which he would have been in if such transfer had not been made.

***Exceptions*– What constitutes preferential transaction?**

As per Section 43(2) of the Code, a corporate debtor shall be deemed to have given a preference, if-

(a) there is a transfer of property or an interest thereof of the corporate debtor for the benefit of a creditor or a surety or aguarant or for or on account of an antecedent financial debtor operational debtor other liabilities owed by the corporate debtor; and

(b) the transfer under clause (a) has the effect of putting such creditor or a surety or a guarantor in a beneficial position than it would have been in the event of a distribution of assets being made in accordance with section 53.

Section 43 also prescribes the relevant time for avoidance of transactions which may amount to preferences.

Application to Adjudicating Authority for avoidance of preferential transactions- Section 43(1) lays down that where the liquidator or there solution professional, as the case may be, is of the opinion that the corporate debtor has at a relevant time given a preference in such transactions and in such manner as laid down in sub- section (2) of section 43 to any persons as referred to in sub-section (4), he shall apply to the Adjudicating Authority for avoidance of preferential transactions and for, one or more of the orders referred to in section 44. Section 43(3) provides that for the purposes of sub-section (2), a preference shall not include the following transfers:

(a) transfer made in the ordinary course of the business or financial affairs of the corporate debtor or the transferee;

(b) any transfer creating a security interest in property acquired by the corporate debtor to the extent that-

(i) such security interest secures new value and was given at the time of or after the signing of a security agreement that contains a description of such property as security interest, and was used by corporate debtor to acquire such property; and

(ii) such transfer was registered with an information utility on or before thirty days after the corporate debtor receives possession of such property:

Provided that any transfer made in pursuance of the order of a court shall not, preclude such transfer to be deemed as giving of preference by the corporate debtor.

Relevant time for preferential transactions

As per Section 43(4), the preferential transaction is at a relevant time if:

- It is given to a related party (other than by reason only of being an employee), during the period of two years preceding the insolvency commencement date; or
- a preference is given to a person other than a related party during the period of one year preceding the insolvency commencement date.

Explanation- For the purpose of sub-section (3) of section 43, "new value" means money or its worth in goods, services, or new credit, or release by the transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable by the liquidator or the resolution professional under this Code, including proceeds of such property, but does not include a financial debtor operational debt substituted for existing financial debt or operational debt.

Orders in Case of Preferential Transactions

Section 44 specifies the orders that may be passed by the Adjudicating Authority in relation to the avoidance of a preferential transaction. These orders are passed to reverse the effects of the preferential transaction and require the person to whom the preference is granted to pay back any gains he may have made as a result of such preference.

Section 44 lays down that the Adjudicating Authority, may, on an application made by the resolution professional or liquidator under sub-section(1) of section 43, by an order:

(a) require any property transferred in connection with the giving of the preference to be vested in the corporate debtor;

(b) require any property to be so vested if it represents the application either of the proceeds of sale of property so transferred or of money so transferred;

(c) release or discharge (in whole or in part) of any security interest created by the corporate debtor;

(d) require any person to pay such sums in respect of benefits received by him from the corporate debtor, such sums to the liquidator or the resolution professional, as the Adjudicating Authority may direct;

(e) direct any guarantor, whose financial debts or operational debts owed to any person were released or discharged (in whole or in part) by the giving of the preference, to be under such new or revived financial debts or operational debts to that person as the Adjudicating Authority deems appropriate;

(f) direct for providing security or charge on any property for the discharge of any financial debtor operational debt under the order, and such security or charge to have the same priority as a security or chargere leased or discharged wholly or in part by the giving of the preference; and

(g) direct for providing the extent to which any person whose property is so vested in the corporate debtor, or on whom financial debts or operational debts a reimposed by the order, are to be proved in the liquidation or the corporate insolvency resolution process for financial debts or operational debts which arose from, or were released or discharged wholly or in part by the giving of the preference:

Transactions in good faith and for value- An order by the Adjudicating Authority under section 44 shall not-

- affect any interest in property which was acquired from a person other than the corporate debtor or any interest derived from such interest and was acquired in good faith and for value;
- require a person, who received a benefit from the preferential transaction in good faith and for value to pay a sum to the liquidator or the resolution professional.

Presumption- For the purpose of this section, it is clarified that where a person, who has acquired an interest in property from another person other than the corporate debtor, or who has received a benefit from the preference or such another person to whom the corporate debtor gave the preference, -

- had sufficient information of the initiation or commencement of insolvency resolution process of the corporate debtor;
- is a related party, it shall be presumed that the interest was acquired, or the benefit was received otherwise than in good faith unless the contrary is shown. [Explanation I to section 44]

Effect of public announcement- A person shall be deemed to have sufficient information or opportunity to avail such information if a public announcement regarding the corporate insolvency resolution process has been made under section 13. [Explanation II to section 44].

Avoidance of Undervalued Transactions

Section 45 provides for the avoidance of undervalued transactions.

Application to Adjudicating Authority-According to section 45(1), if the liquidator or the resolution professional, as the case may be, on an examination of the transactions of the corporate debtor referred to in sub-section (2) determines that certain transactions were made during the relevant period under section 46, which were under valued, he shall make an application to the Adjudicating Authority to declare such transactions as void and reverse the effect of such transaction in accordance with this Chapter.

Relevant period for avoidable transaction [Section 46(1)]

- transaction was made with any person within the period of one year preceding the insolvency commencement date; or
- transaction was made with a related party within the period of two years preceding the insolvency commencement date.

What constitutes undervalued transaction?

Section 45(2) provides that a transaction shall be considered undervalued where the corporate debtor–

(a) makes a gift to a person; or

(b) enters into a transaction with a person which involves the transfer of one or more assets by the corporate debtor for a consideration the value of which is significantly less than the value of the consideration provided by the corporate debtor, and such transaction has not taken place in the ordinary course of business of the corporate debtor.

Sub-section (2) of section 46 empowers the Adjudicating Authority to require an independent expert to assess evidence relating to the value of the transactions mentioned in section 46.

In the case of ***Anuj Jain Vs. Axis Bank Ltd. & Ors. [Civil Appeal Nos. 8512-8527 of 2019 with other appeals]*** *judgement dated 26.02.2020,* Hon'ble Supreme Court inter alia observed that:

(a) ***Preferential Transactions:*** A CD shall be deemed to have given a preference at a relevant time if: (i) there is a transfer of property or the interest thereof of the CD for the benefit of a creditor or surety or guarantor for or on account of an antecedent financial debt or operational debt or other liability; (ii) such transfer has the effect of putting such creditor or surety or guarantor in a beneficial position than it would have been in the event of distribution of assets in accordance with section 53 of the Code; and (iii) preference is given, either during the period of two years/one year preceding the ICD when the beneficiary is a related/an unrelated party. However, such deemed preference may not be an offending preference, if it falls into any or both exclusions provided by section 43(3). Section 43(3)(a) exempts transfers made in ordinary course of business of the CD or the transferee. This calls for purposive interpretation. The expression 'or', appearing as disjunctive between the expressions 'corporate debtor' and 'transferee', ought to be read as 'and'. Therefore, a preference shall not include the transfer made in the ordinary course of the business of the CD and the transferee.

(b) ***Duties and responsibilities of RP:*** The RP shall – (i) sift through all transactions relating to the property/ interest of the CD backwards from the ICD and up to the preceding two years; (ii) identify persons involved in the transactions and put them in two categories: (1) related party under section 5(24) and (2) remaining persons; (iii) identify which of the said transactions of preceding two years, the beneficiary is a related party of the CD and in which the beneficiary is not a related party. The sub -set relating to unrelated parties shall be trimmed to include only the transactions preceding one year from the ICD; (iv) examine every transaction in each of these sub -sets to find out whether (1) the transaction is of transfer of property of the CD or its interest in it; and (2) beneficiary involved in the transaction stands in the capacity of creditor/surety/guarantor; (v) scrutinise the shortlisted transactions to find, if the transfer is for or on account of antecedent financial debt/operational debt/other liability of the CD; (vi) examine the scanned and scrutinised transactions to find, if the transfer has the effect of putting such creditor/surety/guarantor in beneficial position, then it would have been in the event of distribution of assets under section 53. If answer is in the affirmative, the transaction shall be deemed to be of preferential, provided it does not fall within the exclusion under section 43(3); and then (vii) apply to the AA for necessary orders, after carrying out the aforesaid volumetric and gravimetric analysis of the transactions.

c) ***Undervalued and fraudulent transactions:*** As the transactions are held as preferential, it is not necessary to examine whether these are undervalued and/or fraudulent. In preferential transaction, the question of intent is not involved and by virtue of legal fiction, upon existence of the given ingredients, a transaction is deemed to be of giving preference at a relevant time, while undervalued transaction requires different enquiry under sections 45 and 46 where the AA is required to examine the intent, if such transactions were to defraud the creditors. The AA needs to examine the aspect of preferential, undervalued and fraudulent separately and distinctively.

Application by Creditor in Cases of Undervalued Transactions

Section 47 provides for an application to the Adjudicating Authority by creditors, shareholders or partners of the corporate debtor to set aside a transaction at under value where the liquidator or resolution professional has not reported such transaction to the adjudicating authority.

Application by creditor, member or a partner of a corporate debtor- According to section 47 (1), where an under valued transaction has taken place and the liquidator or the resolution professional as the case may be, has not reported it to the Adjudicating Authority, a creditor, member or a partner of a corporate debtor, as the case may be, may make an application to the Adjudicating Authority to declare such transactions void and reverse their effect in accordance with this Chapter.

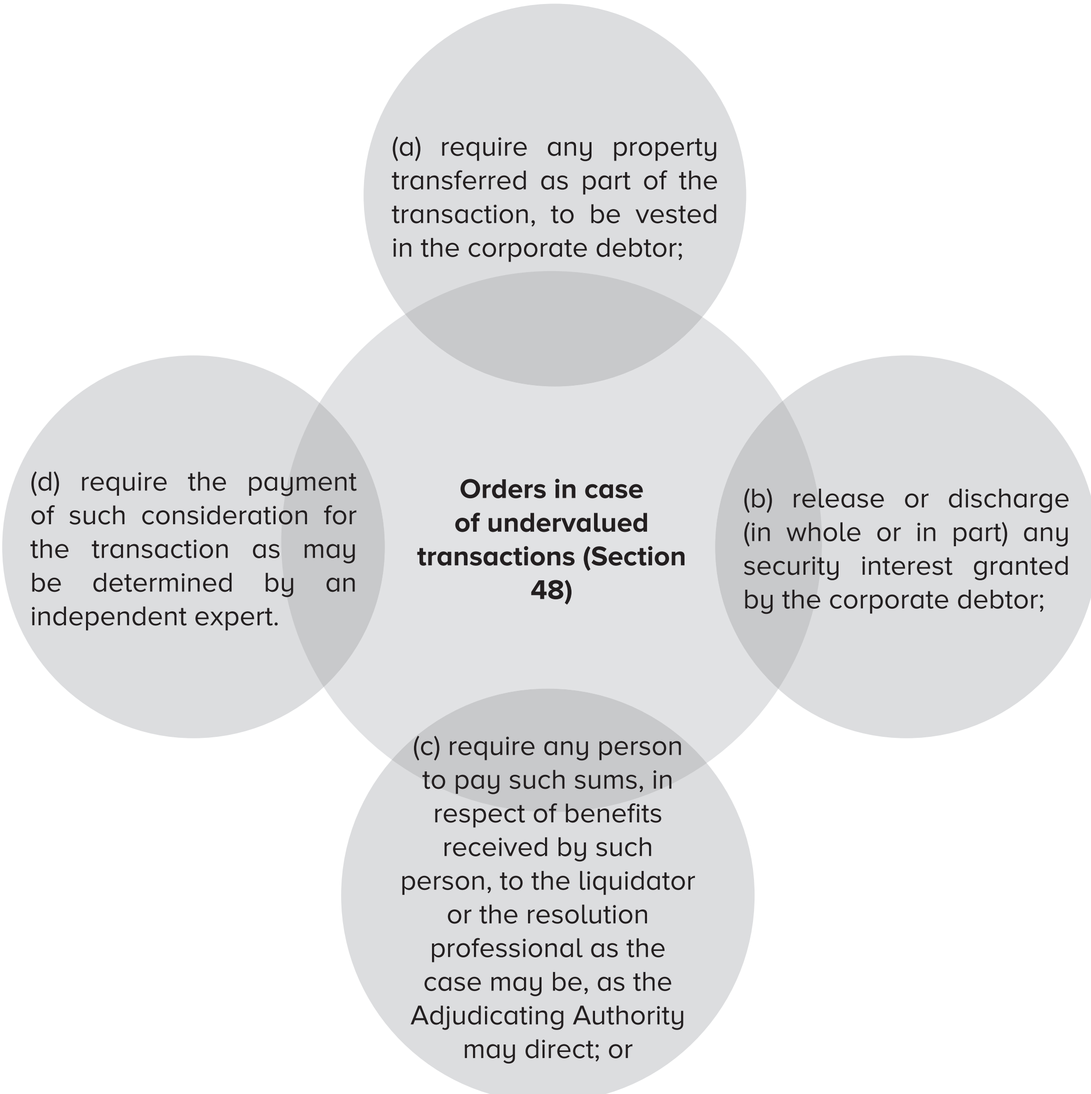
Order by Adjudicating Authority- Sub-section (2) further lays down that where, the Adjudicating Authority, after examination of the application made under sub-section (1), is satisfied that -

- undervalued transactions had occurred; and
- liquidator or the resolution professional, as the case may be, after having sufficient information or opportunity to avail information of such transactions did not report such transaction to the Adjudicating Authority,

it shall pass an order-

(a) restoring the position as it existed before such transactions and reversing the effects thereof in the manner as laid down in section 45 and section 48;

(b) requiring the Board to initiate disciplinary proceedings against the liquidator or the resolution professional as the case may be.



Transactions Defrauding Creditors

Section 49 strikes at transactions entered into with the intention of prejudicing the interests of a person who has made or may make a claim against the corporate debtor. According to section 49, where the corporate debtor has entered into an undervalued transaction as referred to in sub-section (2) of section 45, the Adjudicating Authority shall make an order-

What constitutes transactions defrauding creditors?

As per Section 49 of the Code, a transaction shall be considered as defrauding creditors where transaction was deliberately entered into by such corporate debtor -

(a) for keeping assets of the corporate debtor beyond the reach of any person who is entitled to make a claim against the corporate debtor; or

(b) in order to adversely affect the interests of such a person in relation to the claim.

(i) restoring the position as it existed before such transaction as if the transaction had not been entered into; and

(ii) protecting the interests of persons who are victims of such transactions.

The proviso appended to section 49 makes it clear that an order under section 49 -

(a) shall not affect any interest in property which was acquired from a person other than the corporate debtor and was acquired in good faith, for value and without notice of the relevant circumstances, or affect any interest deriving from such an interest, and

(b) shall not require a person who received a benefit from the transaction in good faith, for value and without notice of the relevant circumstances to pay any sum unless he was a party to the transaction.

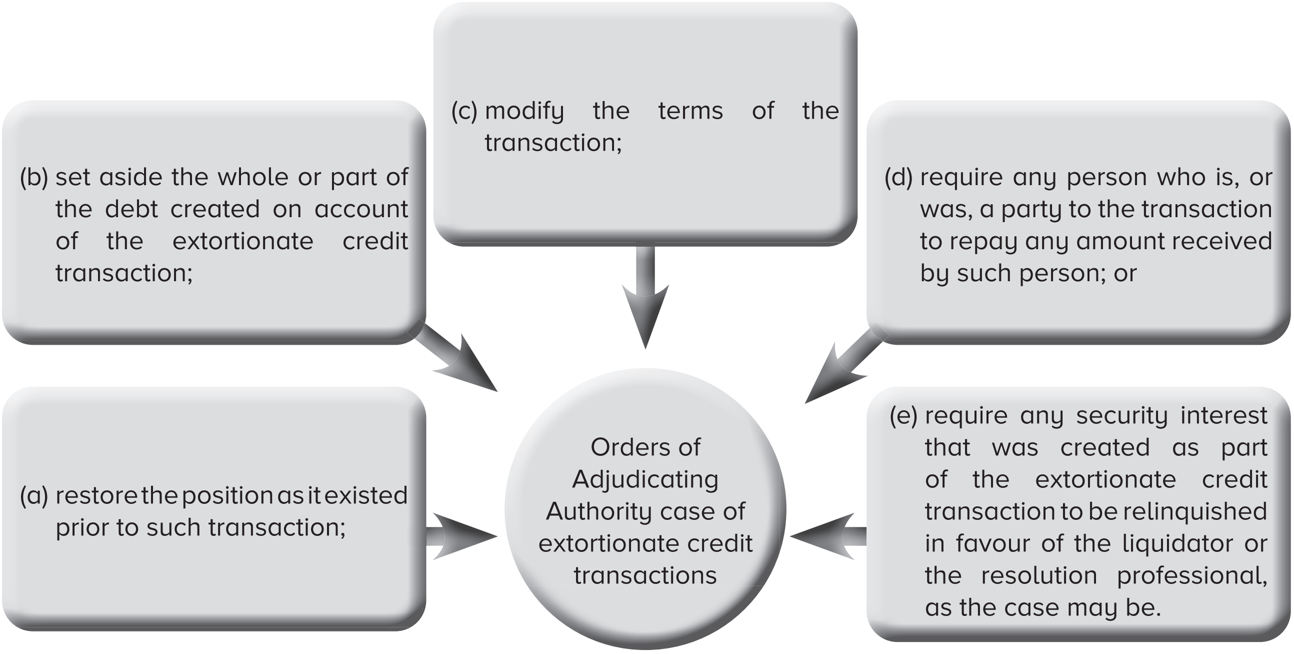
Extortionate Credit Transactions

Section 50 strikes at extortionate credit transactions entered in to by the corporate debtor in the period of two years preceding the insolvency commencement date.

Application for avoidance of extortionate credit transactions- Section 50(1) lays down that where the corporate debtor has been a party to an extortionate credit transaction involving the receipt of financial or operational debt during the period within two years preceding the insolvency commencement date, the liquidator or the resolution professional as the case may be, may make an application for avoidance of such transaction to the Adjudicating Authority if the terms of such transaction required exorbitant payments to be made by the corporate debtor.

Board to specify the circumstances- According to sub-section (2), the Board may specify the circumstances in which a transactions which shall be covered under sub-section (1).

Exception- The Explanation appended to section 50 clarifies that for the purpose of this section, any debt extended by any person providing financial services which is in compliance with any law for the time being in force in relation to such debt shall in no event be considered as an extortionate credit transaction.



Secured Creditor in Liquidation Proceedings

Section 52 provides for options exercisable by a secured creditor. In a liquidation proceeding, the secured creditor may realise its security interest out side the liquidation proceedings or choose to relinquish its security interest and participate in the distribution of assets or he may release the security interest. If a secured creditor decides to realise its security, the amount of insolvency resolution process costs payable by the secured creditor shall be deducted from the realised proceeds. If there is a surplus realised from the enforcement of a security interest, the secured creditor has to account for the same to the liquidator. Similarly, if the proceeds of the realisation of the secured assets are not sufficient to pay the debts owed to the secured creditor, he may claim under section 53 for such unpaid amount.

What are the options available for a secured creditor?

As per Section 52(1) of the Code, a secured creditor in the liquidation proceedings may-

a) relinquish its security interest to the liquidation estate and receive proceeds from the sale of assets by the liquidator in the manner specified in section 53; or

b) realise its security interest in the manner specified in this section.

"Security interest" means right, title or interest or a claim to property, created in favour of, or provided for a secured creditor by a transaction which secures payment or performance of an obligation and includes mortgage, charge, hypothecation, assignment and encumbrance or any other agreement or arrangement securing payment or performance of any obligation of any person:

Provided that security interest shall not include a performance guarantee. [Section 3(31)]

Liquidator to be informed- Where the secured creditor realises security interest under clause (b) of sub-section(1), he shall inform the liquidator of such security interest and identify the asset subject to such security interest to be realised. [Section 52(2)]

Verification by liquidator- Sub-section (3) lays down that before any security interest is realised by the secured creditor under this section, the liquidator shall verify such security interest and permit the secured creditor to realise only such security interest, the existence of which may be proved either -

(a) by the records of such security interest maintained by an information utility; or

(b) by such other means as may be specified by the Board.

Secured assets- A secured creditor may enforce, realise, settle, compromise or deal with the secured assets in accordance with such law as applicable to the security interest being realised and to the secured creditor and apply the proceeds to recover the debts due to it. [Section 52(4)]

Realisation of secured asset- Section 52(5) provides that if in the course of realising a secured asset, any secured creditor faces resistance from the corporate debtor or any person connected there within taking possession of, selling or otherwise disposing of the security, the secured creditor may make an application to the Adjudicating Authority to facilitate the secured creditor to realise such security interest in accordance with law for the time being in force.

The Adjudicating Authority, on the receipt of an application from a secured credit or under sub-section (5) may pass such order as may be necessary to permit a secured creditor to realise security interest in accordance with law for the time being in force. [Section 52(6)]

What shall a secured creditor do when the enforcement of security interest yields an amount in excess of the debts due to him?

As per Section 52(7) of the Code, the secured creditor shall-

(a) account to the liquidator for such surplus; and

(b) tender to the liquidator any surplus funds received from the enforcement of such secured assets.

Deduction of insolvency resolution process costs- Sub-section (8) lays down that the amount of insolvency resolution process costs, due from secured creditors who realise their security interests in the manner provided in section 52, shall be deducted from the proceeds of any realisation by such secured creditors, and they shall transfer such amounts to the liquidator to be included in the liquidation estate.

Unpaid debts of secured creditor- Where the proceeds of the realisation of the secured assets are not adequate to repay debts owed to the secured creditor, the unpaid debts of such secured creditor shall be paid by the liquidator in the manner specified in clause (e) of sub-section (1) of section 53. [Section 52(9)]

DISTRIBUTION OF ASSETS

Section 53 deals with distribution of assets in liquidation. The Insolvency and Bankruptcy Code, 2016 makes significant changes in the priority of claims for distribution of liquidation proceeds. Incase of liquidation, the assets will be distributed in the following order, incase of liquidation: (i) fees of insolvency professional and costs related to the resolution process, (ii) workmen's dues for the preceding 24 months and secured creditors, (iii) employee wages, (iv) unsecured creditors, (v) government dues and remaining secured creditors (any remaining debt if they enforce their collateral), (vi) any remaining debt, and (vii) shareholders.

"Liquidation cost" means any cost incurred by the liquidator during the period of liquidation subject to such regulations, as may be specified by the Board. [Section 5(16)]

"Liquidation commencement date" means the date on which proceedings for liquidation commence in accordance with section 33 or section 59, as the case may be. [Section 5(17)]

According to priority of claims, unsecured financial creditors shall be paid before the Government. This is intended to promote alternative sources of finance and the consequent development of bond markets in India.

Contractual arrangements between recipients with equal ranking- Sub-section (2) lays down that any contractual arrangements between recipients under sub-section (1) with equal ranking, if disrupting the order of priority under that sub-section shall be disregarded by the liquidator.

Deduction of fees payable to liquidator- Sub-section (3) makes provision for deduction of fees payable to liquidator. It provides that the fees payable to the liquidator shall be deducted proportionately from the proceeds payable to each class of recipients under sub-section (1), and the proceeds to the relevant recipient shall be distributed after such deduction.

> The *Explanation* appended to section 53 clarifies that for the purpose of this section-
>
> (i) at each stage of the distribution of proceeds in respect of a class of recipients that rank equally, each of the debts will either be paid in full, or will be paid in equal proportion within the same class of recipients, if the proceeds are insufficient to meet the debts in full; and
>
> (ii) the term “workmen’s dues” shall have the same meaning as assigned to it in section 326 of the Companies Act, 2013.

Order of Priority

↓

Insolvency resolution process cost and liquidation cost

↓

- Workmen dues (24 months preceding the liquidation commencement date)
- Secured creditor who has relinquished security

↓

Employees’ wages and unpaid dues (12 months preceding the liquidation commencement date)

↓

Unsecured creditors

↓

- Central or State Government dues
- Secured creditor who has enforced security interest

↓

Remaining debts and dues

↓

Preference shareholders

↓

Equity shareholders or partners

Fig. Order of distribution of asset

DISSOLUTION OF CORPORATE DEBTOR

Section 54 provides that after the affairs of the corporate debtor have been wound up and its assets are completely liquidated, the liquidator shall make an application to the adjudicating authority for the dissolution of the corporate debtor.

> As per Regulation 45(3) of the Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016, the liquidator shall submit an application along with the final report prior to dissolution and the compliance certificate in Form H to the Adjudicating Authority for -
>
> - closure of the liquidation process of the corporate debtor where the corporate debtor is sold as a going concern; or
> - for the dissolution of the corporate debtor, in cases not covered above.

Application to the Adjudicating Authority – Sub-section (1) of section 54 lays down that where the assets of the corporate debtor have been completely liquidated, the liquidator shall make an application to the Adjudicating Authority for the dissolution of such corporate debtor.

Date of dissolution – According to sub-section (2), the Adjudicating Authority shall on application filed by the liquidator under sub-section (1) order that the corporate debtor shall be dissolved from the date of that order and the corporate debtor shall be dissolved accordingly.

Copy of Order – A copy of an order under sub-section (2) shall within seven days from the date of such order, be forwarded to the authority with which the corporate debtor is registered. [Section 54(3)]

Early dissolution- Regulation 14 of the IBBI (Liquidation) Process Regulations, 2016, provides that any time after the preparation of the Preliminary Report, if it appears to the liquidator that- (a) the realizable properties of the corporate debtor are insufficient to cover the cost of the liquidation process; and (b) the affairs of the corporate debtor do not require any further investigation;

he shall consult the consultation committee and if it advises for early dissolution, he may apply, along with a detailed report incorporating the views of the consultation committee, to the Adjudicating Authority for early dissolution of the corporate debtor and for necessary directions in respect of such dissolution.

LESSON ROUND-UP

- Liquidation provisions in Chapter III of Part II of the Code came into effect if the attempts to resolve corporate insolvency under Chapter II of the Code fail. Section 33 of the Code lists out the triggers for initiating the liquidation process for corporate persons.
- Section 34 of the Code provides for the appointment of liquidator and the fees to be paid to him. 'Liquidator' means an insolvency professional appointed as a liquidator in accordance with the provisions of Chapter III or Chapter V of this Part, as the case may be.
- The Insolvency and Bankruptcy Code (Second Amendment) Act, 2018 has amended section 34 so as to require a written consent of resolution professional in specified form for appointment as a liquidator.
- Section 35 provides a non-exhaustive list of powers and duties of the liquidator to ensure orderly completion of the liquidation proceedings.
- Section 37 provides that the liquidator shall have the power to access any information systems for the purpose of admission and proof of claims and identification of assets to be held in the liquidation estate.

- Section 36 provides for the creation of a liquidation estate comprising the assets of the corporate debtor as set out in section 36(3). Section 36 also lists out the assets which are to be excluded from the liquidation estate.
- Section 38 prescribes a time period for the collection of claims by the liquidator. It also specifies the methods by which different categories of creditors can submit and prove their claims.
- According to section 42, a creditor may appeal to the Adjudicating Authority against the decision of the liquidator accepting or rejecting the claims within fourteen days of the receipt of such decision.
- Section 53 deals with distribution of assets in liquidation. The Insolvency and Bankruptcy Code, 2016 makes significant changes in the priority of claims for distribution of liquidation proceeds.
- 'Liquidation cost' means any cost incurred by the liquidator during the period of liquidation subject to such regulations, as may be specified by the Board.
- 'Liquidation commencement date' means the date on which proceedings for liquidation commence in accordance with section 33 or section 59, as the case may be.
- Section 54 provides that after the affairs of the corporate debtor have been wound up and its assets are completely liquidated, the liquidator shall make an application to the adjudicating authority for the dissolution of the corporate debtor.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).

1. Discuss the grounds for the initiation of Liquidation process for corporate persons by the Adjudicating Authority.
2. Mention the powers and duties of Liquidator under section 35 of the Insolvency and Bankruptcy Code, 2016.
3. Write a note on Liquidation Estate.
4. What orders can be passed by the Adjudicating Authority for the avoidance of a preferential transaction?
5. What is the order of priority in distribution of proceeds from the sale of the assets during liquidation?

LIST OF FURTHER READINGS

- Insolvency and Bankruptcy Code, 2016 (Bare Act)

OTHER REFERENCES (Including Websites / Video Links)

- https://ibbi.gov.in

Voluntary Liquidation

Lesson 23

KEY CONCEPTS

■ Liquidation ■ Liquidator ■ Liquidation Commencement Date ■ Voluntary Liquidation ■ Process of voluntary liquidation ■ Declaration of solvency

Learning Objectives

To understand:

- Concept of Voluntary Liquidation
- Initiation of Voluntary Liquidation
- Powers & Duties of Liquidator in Voluntary Liquidation
- Effect of Voluntary Liquidation
- Dissolution of company under voluntary liquidation
- Reports to be filed by Liquidator
- Preservation of Records by Liquidator
- Distribution of proceeds by Liquidator

Lesson Outline

- Introduction
- Regulatory Mechanism
- Steps involved in Voluntary Liquidation
- Initiation of Voluntary Liquidation
- Who may initiate voluntary liquidation
- Declaration of Solvency
- Appointment of Liquidator
- Eligibility for appointment as liquidator
- Intimation to Regulatory Authorities
- Voluntary Liquidation Commencement Date
- Effect of liquidation
- Order by Adjudicating Authority
- Powers and Functions of the Liquidator
- Claims
- Realisation of Assets
- Proceeds of Liquidation and Distribution of Proceeds
- Timeline for Voluntary Liquidation Process
- Case Laws
- Lesson Round-Up
- Test Yourself
- References

REGULATORY FRAMEWORK

- Section 59 of the Insolvency and Bankruptcy Code, 2016
- The Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations, 2017

INTRODUCTION

The Banking Law Reform Committee (BLRC) Report- Volume 1, Rationale for the Code provides voluntary liquidation as a mechanism of liquidation of a non- defaulting company- "As an application for voluntary liquidation Where a firm has not defaulted on any debt (or where a firm has no debt), it may make any application to be liquidated voluntarily in such manner as may be specified by the Board". Voluntary Liquidation is a gateway for easy exit for company which has not defaulted on any debt and has no intention to defraud creditors.

The winding-up process by creditors and the voluntary winding up by members of a company have been shifted from the Companies Act, 1956, and the Companies Act, 2013, to the IBC, and these are regarded as "Liquidation Process" and "Voluntary Liquidation Process" under it. Section 255 of the IBC, notified with effect from November 15, 2016, amended the Companies Act, 2013, in accordance with Schedule XI of the IBC, which now defines the term "winding up." A new section was added to the Companies Act, 2013, namely section 2(94A), which defines the expression "winding up" as "winding up under this Act or liquidation under the IBC."

It is also relevant that the enactment of the IBC triggered the removal of provisions of "voluntary winding up" and winding up on the grounds of "inability to pay debts" from the Companies Act, 2013. The proceedings relating to these are now under the ambit of the IBC.

Liquidation in cases of default in payment or repayment of any debt is not directly possible. For such entities, the emphasis is on resolution, and if the resolution process does not result in an approved resolution plan, a liquidation order is passed by the AA under section 33 of the IBC. As opposed to this, in a case of "no default," or in other words, in case there is no "insolvency," a corporate person can initiate voluntary liquidation directly under section 59 of the IBC.

Regulatory Mechanism

The IBC sets out a clear procedure for the voluntary liquidation of a corporate person. Section 59(1) of the IBC states that a corporate person who intends to liquidate voluntarily and has not committed any default, may initiate voluntary liquidation proceedings under the provisions of Chapter V of the IBC. Section 59(2) states that voluntary liquidation in the case of a corporate person under subsection (1) shall follow the procedural requirements and meet the conditions as may be prescribed by IBBI.

The Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations, 2017 (Voluntary Liquidation Regulations) details the process to be followed in the voluntary liquidation of corporate persons. There are seven chapters in these regulations, detailing the process from the commencement of liquidation to the distribution of liquidation proceeds.

Steps Involved in Voluntary Liquidation

1. Submission of Declaration(s) to ROC, stating that the company will be able to pay its dues and is not being liquidated to defraud any person;
2. Passing of special resolution for approving the proposal of voluntary liquidation and appointment of liquidator, within four weeks of the aforesaid declaration(s). If a corporate person owes debts, approval of two-third majority creditors would also be required;
3. **Public Announcement** inviting claims of all stakeholders, within five days of such approval, in newspaper as well as on website of the corporate person;
4. Intimation to the ROC and the Board about the approval, within seven days of such approval;
5. Preparation of **Preliminary Report** about the capital structure, estimates of assets and liabilities, proposed plan of action etc., and submission of the same to a corporate person within forty-five days of such Approval;
6. Verification of claims, within thirty days form the last date for receipt of claims and preparation of list of stakeholders, within forty-five days from the last date for receipt of claims;
7. Opening of a bank account in the name of the corporate person followed by the words **'in voluntary liquidation'**, in a scheduled bank, for the receipt of all moneys due to the corporate person;
8. Sale of assets, recovery of monies due to corporate person, realization of uncalled capital or unpaid capital contribution;
9. Distribution of the proceeds to the stakeholders within 30 days from receipt of the amount;
10. Submission of **Final Report** by the liquidator to the corporate person, ROC and the Board and application to the National Company Law Tribunal (NCLT) for the dissolution;
11. Submission of NCLT order regarding the dissolution, to the concerned ROC within fourteen days of the receipt of order.

Regulatory Framework for Voluntary Liquidation of Corporate Persons:

Chapter V of Part II of the Insolvency and Bankruptcy Code, 2016 and The Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations, 2017.

Initiation of Voluntary Liquidation

Section 59 of the Code sets out the process of initiation of voluntary liquidation of a company. Sub-section 2 of section 59 provides that the voluntary liquidation of a corporate person under sub-section (1) shall meet such conditions and procedural requirements as may be specified by the Board.

This process has been adapted in regulation 3 of the Voluntary Liquidation Regulations for corporate persons other than a company. The process is elaborated as follows:

Who may initiate Voluntary Liquidation?

A corporate person who intends to liquidate itself voluntarily and has not committed any default may initiate voluntary liquidation proceedings under the provisions of this Chapter. [Section 59(1)]

Declaration of Solvency

There should be a declaration from a majority of the directors verified by an affidavit stating that:

(a) they have made a full inquiry into the affairs of the company and formed an opinion that it has no debt, or in case it has, it will be able to pay its debts completely from the value obtained from the assets to be sold in the voluntary liquidation proceedings; and

(b) the company is not being liquidated to defraud any person.

Documents accompanying Solvency:

The said declaration should be accompanied by:

(a) audited financial statements and record(s) of business operations of the company for the previous two years, or for the period since its incorporation, whichever is most recent;

(b) a report of valuation of the assets of the company, in case it is prepared by a registered valuer.

The IBBI(Voluntary Liquidation Process) Regulations,2017 provides in Regulation 3(4) that the declaration under sub-regulation (1)(a) or under section 59(3)(a) shall list each debt of the corporate person as on that date and state that the corporate person will be able to pay all its debts in full from the proceeds of assets to be sold in the liquidation.

The IBBI (Voluntary Liquidation Process) Regulations, 2017 provides in Regulation 3(5) that the declaration under sub-regulation (1)(a) or under section 59(3)(a) shall provide that the corporate person has made provision for preservation of its records after its dissolution.

Shareholders/Contributories Approval

Section 59(3) (c) of the Code provides mandatory timeline for holding of general meeting of members of the corporate debtor to approve voluntary winding up. Within four weeks of a declaration by the Board of Directors, there shall be

(i) a **special resolution** of the members of the company in a general meeting requiring the company to be liquidated voluntarily and **appointing an insolvency professional** to act as the liquidator; or

(ii) a resolution of the members of the company in a general meeting requiring the company to be liquidated voluntarily as a result of expiry of the period of its duration, if any, fixed by its articles or on the occurrence of any event in respect of which the articles provide that the company shall be dissolved, as the case may be and appointing an insolvency professional to act as the liquidator:

In either case, an insolvency professional to act as the liquidator shall be appointed by a resolution.

Creditors' Resolution: It is also provided that if the company owes any debt to any person, creditors representing two-thirds in value of the debt of the company shall approve the resolution passed by shareholders within seven days of such resolution.

Regulation 3 (1) to 3(3) of Voluntary Liquidation Regulations provide similar provisions for voluntary liquidation of corporate persons other than company as follows:

1) Declaration of solvency to be made by majority of

   (i) the designated partners, if a corporate person is a limited liability partnership,

   (ii) individuals constituting the governing body in case of other corporate persons, as the case may be.

2) Such declaration shall be verified by an affidavit stating that-
   (i) they have made a full inquiry into the affairs of the corporate person and they have formed an opinion that either the corporate person has no debt or that it will be able to pay its debts in full from the proceeds of assets to be sold in the liquidation
   (ii) the corporate person is not being liquidated to defraud any person;
   (iii) the corporate person has made sufficient provision to meet the obligations arising on account of pending matters.
3) Such declaration shall be accompanied with the documents, namely: —
   (i) audited financial statements and record of business operations of the corporate person for the previous two years or for the period since its incorporation, whichever is later;
   (ii) a report of the valuation of the assets of the corporate person, if any prepared by a registered valuer.
   (iii) disclosure about pending proceedings or assessments before statutory authorities, and pending litigations, in respect of the corporate person
4) within Four weeks of such declaration , there shall be-
   (i) a resolution passed by a special majority of the partners or contributories, as the case may be, of the corporate person requiring the corporate person to be liquidated and appointing an insolvency professional to act as the liquidator; or
   (ii) a resolution of the partners or contributories, as the case may be, requiring the corporate person to be liquidated as a result of expiry of the period of its duration, if any, fixed by its constitutional documents or on the occurrence of any event in respect of which the constitutional documents provide that the corporate person shall be dissolved, as the case may be, and appointing an insolvency professional to act as the liquidator.

If the corporate person owes any debt to any person, creditors representing two-thirds in value of the debt of the corporate person shall approve the resolution passed by partners or contributories, as stated above, within seven days of such resolution.

Appointment of Liquidator

Regulation 5 of Voluntary Liquidation Regulations provides that-

- the corporate person shall appoint an insolvency professional as liquidator, and, wherever required, may replace him by appointing another insolvency professional as liquidator.
- Appointment or replacement of liquidator shall be made by a resolution passed under clause (c) of sub-section (3) of section 59 or clause (c) of sub-regulation (1) of regulation 3, as the case may be.
- Only an insolvency professional who meets the eligibility criterion laid down in Regulation 6 can be appointed as Liquidator.
- It is provided that such resolution, passed by the members, partners, or contributories, shall contain the terms and conditions of appointment of the liquidator, including the remuneration payable to him.
- A duty has been casted on the insolvency professional that he shall, within seven days of his appointment as liquidator, intimate the Board about such appointment.

Eligibility for appointment as liquidator

Regulation 6 sets out the eligibility requirement, which is similar to the eligibility requirement for appointment of a liquidator under the Liquidation Process Regulations. Primarily, it deals with the requirement of a liquidator to be **"independent."** Regulation 6 lays down following criterion for appointment of liquidator:

(1) An insolvency professional shall be eligible to be appointed as a liquidator if he, and every partner or director of the insolvency professional entity of which he is a partner or director is independent of the corporate person:

Explanation:

1) A person shall be considered independent of the corporate person, if he-
   (a) is eligible to be appointed as an independent director on the board of the corporate person under section 149 of the Companies Act, 2013 , where the corporate person is a company;
   (b) is not a related party of the corporate person; or
   (c) has not been an employee or proprietor or a partner-
      (i) of a firm of auditors or secretarial auditors or cost auditors of the corporate person at any time in the last three years; or
      (ii) of a legal or a consulting firm, that has or had any transaction with the corporate person contributing ten per cent or more of the gross turnover of such firm at any time in the last three years.

(2) An insolvency professional shall not be eligible to be appointed as a liquidator if he, or the insolvency professional entity of which he is a partner or director is under a restraint order of the Board.

(3) A liquidator shall disclose the existence of any pecuniary or personal relationship with the concerned corporate person or any of its stakeholders as soon as he becomes aware of it, to the Board and the Registrar.

(4) An insolvency professional shall not continue as a liquidator if the insolvency professional entity of which he is a director or partner, or any other partner or director of such insolvency professional entity represents any other stakeholder in the same liquidation.

Liquidator's remuneration: Regulation 7 of Voluntary Liquidation Regulations provides for that the remuneration payable to the liquidator shall form part of the liquidation cost.

Intimation to Regulatory Authorities

Section 59(4) of the Code provides that –

- the company shall notify the Registrar of Companies and the Board about the resolution passed to liquidate the company.
- the intimation shall be sent within seven days of such a resolution or the subsequent approval by the creditors, as the case may be.

Similar provisions are specified for corporate person other than a company in the Regulation 3(2) of Voluntary Liquidation Regulations that the corporate person shall notify the Registrar and the Board about the resolution passed by partners or contributories to liquidate the corporate person within seven days of such resolution or the subsequent approval by the creditors, as the case may be.

Voluntary Liquidation Commencement Date

According to section 59(5) of the Code, subject to approval of the creditors, the voluntary liquidation proceedings in respect of a company shall be deemed to have commenced from the date of passing of the resolution by the members, partners or contributories.

Regulation 3(3) provides that the liquidation proceedings in respect of a corporate person other than a company shall be deemed to have commenced from the date of passing of the resolution by partners or contributories under sub-clause (c) of sub-regulation (1) subject to approval of the creditors as stated in proviso to regulation 3 (1) (c).

Effect of liquidation

As per regulation 4 of the Voluntary Liquidation Regulations,

- The corporate person shall cease to carry on its business from the liquidation commencement date, except as far as required for the beneficial winding up of its business.
- However, the corporate person shall continue to exist until it is dissolved under section 59(8) of the IBC.

Application of Sections 35 to 53 of the IBC

Section 59(6) of the Code provides for that the provisions of sections 35 to 53 of Chapter III and Chapter VII shall apply to voluntary liquidation proceedings for corporate persons with such modifications as may be necessary.

Chapter III deals with the liquidation process of a corporate person in case of failure of the insolvency resolution process to receive a resolution plan and the subsequent order by the AA for liquidation of corporate persons. Chapter VII deals with offences and penalties. Hence, provisions in the IBC relating to the powers and duties of the liquidator, claim verifications, the conduct of the liquidation process, and offences and penalties that apply to a post-CIRP liquidation also apply to voluntary liquidation.

Application to Adjudicating Authority (AA) for dissolution of corporate person

Section 59(7) of the Code mandates the liquidator to make an application to the Adjudicating Authority for dissolution of such corporate person, where the affairs of the corporate person have been completely wound up, and its assets completely liquidated.

Regulation 38(3) of Voluntary Liquidation Regulations provides that the liquidator shall submit the Final Report and the compliance certificate in Form-H along with the application under sub-section (7) of section 59 to the Adjudicating Authority.

Order by Adjudicating Authority-

The Adjudicating Authority shall on an application filed by the liquidator under sub-section (7), pass an order that the corporate debtor shall be dissolved from the date of that order and the corporate debtor shall be dissolved accordingly. [Section 59(8)]

Thus, once the affairs of the corporate debtor have been wound up and its assets completely liquidated, the liquidator shall make an application to the adjudicating authority for the dissolution of the corporate debtor and the corporate debtor shall be dissolved by the order of the adjudicating authority.

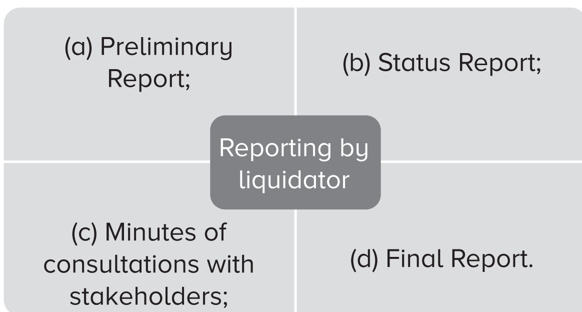
Copy of Order- A copy of an order under sub-section (8) shall within fourteen days from the date of such order, be forwarded to the authority with which the corporate person is registered. [Section 59(9)]

Powers and Functions of the Liquidator

Chapter IV of Voluntary Liquidation Regulations provides for powers and functions of the Liquidator for voluntary liquidation of the corporate persons in Regulation 8 to 14**.**

Reporting

Regulation 8(1) provides that the liquidator shall prepare and submit following reports and minutes in the manner specified under these Regulations:



According to regulation 8(2), subject to other provisions of these Regulations, the liquidator shall make

- the above stated reports and minutes available to a stakeholder in either electronic or physical form, on receipt of-
  - (a) an application in writing;
  - (b) cost of making such reports available to it; and
  - (c) an undertaking from the stakeholder that it shall maintain confidentiality of such reports and shall not use these to cause an undue gain or undue loss to itself or any other person.

Preliminary Report (Regulation 9)

Timeline for submission of Preliminary Report:

The liquidator shall submit a Preliminary Report to the corporate person within forty five days from the liquidation commencement date.

Preliminary Report shall provide for the following contents in detail-

The liquidator shall submit a Preliminary Report detailing-[Regulation 9(1)]

(a) the capital structure of the corporate person;

(b) the estimates of its assets and liabilities as on the liquidation commencement date based on the books of the corporate person: Provided that if the liquidator has reasons to believe, to be recorded in writing, that the books of the corporate person are not reliable, he shall also provide such estimates based on reliable records and data otherwise available to him;

(c) Whether he intends to make any further inquiry in to any matter relating to the promotion, formation or failure of the corporate person or the conduct of the business thereof; and

(d) the proposed plan of action for carrying out the liquidation, including the timeline within which he proposes to carry it out and the estimated liquidation costs.

Registers and books of account (Regulation 10)

Completion of registers and books of account: Where the books of account of the corporate person are incomplete on the liquidation commencement date, the liquidator shall have them completed and brought up-to-date, with all convenient speed. [Regulation 10(1)]

Registers and books of accounts to be maintained: The liquidator shall maintain the following registers and books, as may be applicable, in relation to the liquidation of the corporate person:- (a) Cash Book; (b) Ledger; (c) Bank Ledger; (d) Register of Fixed Assets and Inventories; (e) Securities and Investment Register; (f) Register of Book Debts and Outstanding Debts; (g) Tenants Ledger; (h) Suits Register; (i) Decree Register; (j) Register of Claims and Dividends; (k) Contributories Ledger; (l) Distributions Register; (m) Fee Register; (n) Suspense Register; (o) Documents Register; (p) Books Register; (q) Register of unclaimed dividends and undistributed proceeds; and] (r) such other books or registers as may be necessary to account for transactions entered into by him in relation to the corporate person. [Regulation 10(2)]

Forms for maintaining the registers and books: The registers and books under sub-regulation (2) may be maintained in the forms indicated in Schedule II, with such modifications as the liquidator may deem fit in the facts and circumstances of the liquidation. [Regulation 10(3)]

Duty of Liquidator to keep account of expenses: Regulation 10(4) also makes it mandatory for the liquidator to keep receipts for all payments made or expenses incurred by him.

Engagement of professionals (Regulation 11)

Who may be appointed by a Liquidator: A liquidator may engage professionals to assist him in the discharge of his duties, obligations and functions for a reasonable remuneration and such remuneration shall form part of the liquidation cost. [Regulation 11(1)]

Who cannot be engaged by the liquidator: Following professionals cannot be engaged by a liquidator

- his relative,
- a related party of the corporate person, or
- one who has served as an auditor to the corporate person at any time during the five years preceding the liquidation commencement date. [Regulation 11(2)]

Disclosure by a professional: A professional engaged or proposed to be engaged under sub-regulation(1) shall disclose the existence of any pecuniary or personal relationship with any of the stakeholders, or the corporate person as soon as he becomes aware of it, to the liquidator. [Regulation 11(3)]

Consultation with stakeholders (Regulation 12)

Duty of stakeholders to extend assistance: The stakeholders consulted under section 35(2) shall extend all assistance and cooperation to the liquidator to complete the liquidation of the corporate person. [Regulation 12(1)]

Particulars of consultation: The liquidator shall maintain the particulars of any consultation with the stakeholders made under this Regulation. [Regulation 12(2)]

Extortionate credit transactions (Regulation 13)

A transaction shall be considered an extortionate credit transaction under section 50(2) where the terms-

(a) require the corporate person to make exorbitant payments in respect of the credit provided; or

(b) are unconscionable under the principles of law relating to contracts.

Public announcement by the Liquidator (Regulation 14)

Form of Public Announcement: The liquidator shall make a public announcement in Form A of Schedule I within five days from his appointment. [Regulation 14(1)]

Invitation of claim: The public announcement shall-

(a) call upon stakeholders to submit their claims as on the liquidation commencement date; and

(b) provide the last date for submission of claim, which shall be thirty days from the liquidation commencement date. [Regulation 14(2)]

Publication of Public Announcement: The announcement shall be published-

(a) in one English and one regional language newspaper with wide circulation at the location of the registered office and principal office, if any, of the corporate person and any other location where in the opinion of the liquidator, the corporate person conducts material business operations;

(b) on the website, if any, of the corporate person; and

(c) on the website, if any, designated by the Board for this purpose [Regulation 14(3)].

CLAIMS

Provisions for claims are provided in Chapter V from Regulations 15 to 30 of Voluntary Liquidation Regulations.

Proof of claim (Regulation 15)

A person, who claims to be a stakeholder, shall prove his claim for debt or dues to him, including interest, if any, as on the liquidation commencement date.

Claims by operational creditors (Regulation 16)

Form to be filed: A person claiming to be an operational creditor of the corporate person, other than a workman or employee, shall submit proof of claim to the liquidator in person, by post or by electronic means in Form B of Schedule I. [Regulation 16(1)]

Proof of claim: The existence of debt due to an operational creditor under this Regulation may be proved on the basis of-

(a) the records available with an information utility; or

(b) other relevant documents which adequately establish the debt, including any of the following –

- (i) a contract for the supply of goods or services with corporate person, supported by an invoice demanding payment for the goods and services supplied to the corporate person;
- (ii) an order of a court or tribunal that has adjudicated upon the non-payment of a debt, if any; and
- (iii) financial accounts of the corporate person. [Regulation 16(2)]

Claims by financial creditors (Regulation 17)

Form to be filed: A person claiming to be a financial creditor of the corporate person shall submit proof of claim to the liquidator in electronic means in Form C of Schedule I. [Regulation 17(1)]

Proof of claim: The existence of debt due to the financial creditor may be proved on the basis of-

(a) the records available in an information utility; or

(b) other relevant documents which adequately establish the dwebt, including any or all of the following –

- (i) a financial contract supported by financial statements as evidence of the debt;
- (ii) a record evidencing that the amounts committed by the financial creditor to the corporate person under a facility has been drawn by the corporate person;
- (iii) financial statements showing that the debt has not been repaid; and
- (iv) an order of a court or tribunal that has adjudicated upon the non-payment of a debt, if any. [Regulation 17(2)]

Claims by workmen and employees (Regulation 18)

Form to be filed: A person claiming to be a workman or an employee of the corporate person shall submit proof of claim to the liquidator in person, by post or by electronic means in Form D of Schedule I. [Regulation 18(1)]

One proof of claim: Where there are dues to numerous workmen or employees of the corporate person, an authorized representative may submit one proof of claim for all such dues on their behalf in Form E of Schedule I. [Regulation 18(2)]

Proof of claim: The existence of dues to workmen or employees may be proved by them, individually or collectively, on the basis of-

(a) records available in an information utility; or

(b) other relevant documents which adequately establish the dues, including any or all of the following -

- (i) a proof of employment such as contract of employment for the period for which such workman or employee is claiming dues;
- (ii) evidence of notice demanding payment of unpaid amount and any documentary or other proof that payment has not been made; and
- (iii) an order of a court or tribunal that has adjudicated upon the non-payment of dues, if any. [Regulation 18(3)]

Duty of the liquidator to admit claim in absence of claim by workman or employee: The liquidator shall admit the claims of a workman or an employee on the basis of the books of account of the corporate person if such workman or employee has not made a claim. [Regulation 18(4)]

Claims by other stakeholders (Regulation 19)

Form to be filed: A person, claiming to be a stakeholder other than those under Regulations 16, 17 or 18 shall submit proof of claim to the liquidator in person, by post or by electronic means in Form F of Schedule I. [Regulation 19(1)]

Proof of claim: The existence of the claim of the stakeholder may be proved on the basis of –

(a) the records available in an information utility;

Or

(b) other relevant documents which adequately establish the claim, including any or all of the following-

(i) documentary evidence of notice demanding payment of unpaid amount or bank statements of the claimant showing that the claim has not been paid and an affidavit that the documentary evidence and bank statements are true, valid and genuine;

(ii) documentary or electronic evidence of his shareholding; and

(iii) an order of a court, tribunal or other authority that has adjudicated upon the non-payment of a claim, if any.[Regulation 19(2)]

Proving security interest (Regulation 20)

The existence of a security interest may be proved by a secured creditor on the basis of-

(a) the records available in an information utility;

(b) certificate of registration of charge issued by the Registrar of Companies;

(c) proof of registration of charge with the Central Registry of Securitisation Asset Reconstruction and Security Interest of India; or

(d) other relevant documents which adequately establish the security interest.

Production of bills of exchange and promissory notes (Regulation 21)

Where a person seeks to prove a debt in respect of a bill of exchange, promissory note or other negotiable instrument or security of a like nature for which the corporate person is liable, such bill of exchange, note, instrument or security, as the case may be, shall be produced before the liquidator before the claim is admitted.

Substantiation of claims (Regulation 22)

The liquidator may call for such other evidence or clarification as he deems fit from a claimant for substantiating the whole or part of its claim.

Cost of proof (Regulation 23)

A claimant shall bear the cost of proving its claim. Costs incurred by the liquidator for verification and determination of a claim shall form part of liquidation cost. It is provided that if a claim or part of the claim is found to be false, the liquidator shall endeavor to recover the costs incurred for verification and determination of claim from such claimant, and shall provide the details of the claimant to the Board.

Determination of amount of claim (Regulation 24)

Where the amount claimed by a claimant is not precise due to any contingency or any other reason, the liquidator shall make the best estimate of the amount of the claim, based on consultation with the claimant and the corporate person and the information available with him.

Debt in foreign currency (Regulation 25)

The claims denominated in foreign currency shall be valued in Indian currency at the official exchange rate as on the liquidation commencement date.

Explanation- "The official exchange rate" is the reference rate published by the Reserve Bank of India or derived from such reference rates.

Periodical payments (Regulation 26)

In the case of rent, interest and such other payments of a periodical nature, a person may claim only for any amounts due and unpaid up to the liquidation commencement date.

Debt payable at future time (Regulation 27)

A person may prove for a claim whose payment was not yet due on the liquidation commencement date and is entitled to distribution in the same manner as any other stakeholder. Subject to any contract to the contrary, where a stakeholder has proved for a claim under sub-regulation (1), and the debt has not fallen due before distribution, he is entitled to distribution of the admitted claim reduced as follows:

$$\frac{x}{(1+r)^n}$$

where–

(a) "x" is the value of the admitted claim;

(b) "r" is the closing yield rate (%) of government securities of the maturity of "n" on the date of distribution as published by the Reserve Bank of India; and

(c) "n" is the period beginning with the date of distribution and ending with the date on which the payment of the debt would otherwise be due, expressed in years and months in a decimalized form.

Mutual credits and set-off (Regulation 28)

Where there are mutual dealings between the corporate person and another party, the sums due from one party shall be set off against the sums due from the other to arrive at the net amount payable to the corporate person or to the other party.

Illustration: X owes Rs.100 to the corporate person. The corporate person owes Rs.70 to X. After set off, Rs.30 is payable by X to the corporate person.

Verification of claims (Regulation 29)

Time for verification of claim: The liquidator shall verify the claims submitted within thirty days from the last date for receipt of claims and may either admit or reject the claim, in whole or in part, as the case may be, as per section 40 of the Code. [Regulation 29(1)]

Appeal to the Adjudicating Authority: A creditor may appeal to the Adjudicating Authority against the decision of the liquidator as per section 42 of the Code. [Regulation 29(2)}

List of stakeholders (Regulation 30)

Contents of list of stakeholders:

The liquidator shall prepare a list of stakeholders on the basis of proofs of claims submitted and accepted under these Regulations, with-

(a) the amounts of claim admitted, if applicable,

(b) the extent to which the debts or dues are secured or unsecured, if applicable,

(c) the details of the stakeholders, and

(d) the proofs admitted or rejected in part, and the proofs wholly rejected. [Regulation 30 (1)]

Timeline for preparing list of stakeholders[Regulation 30 (2)]*:*

- *When claim is filed by stakeholder:* The liquidator shall prepare the list of stakeholders within forty-five days from the last date for receipt of claims.
- *When no claim is filed by stakeholder:* It is provided that where no claim from creditors has been received till the last date for receipt of claims, the liquidator shall prepare the list of stakeholders within fifteen days from the last date for receipt of claims.

List of stakeholders available for inspection or display: The list of stakeholders, as modified from time to time, shall be-

(a) available for inspection by the persons who submitted proofs of claim;

(b) available for inspection by members, partners, directors and guarantors of the corporate person;

(c) displayed on the website, if any, of the corporate person;

(d) displayed on the website, if any, designated by the Board for this purpose. [Regulation 30 (3)]

REALISATION OF ASSETS

Provisions for realization of assets are provided in Chapter VI from Regulations 31 to 33 of Voluntary Liquidation Regulations.

Manner of Sale (Regulation 31)

As approved by corporate person: The liquidator may value and sell the assets of the corporate person in the manner and mode approved by the corporate person in compliance with provisions, if any, in the applicable statute.

> *Explanation:* "assets" include an asset, all assets, a set of assets or parcel of assets, as the case may be, in relation to sale of assets.

Recovery of monies due (Regulation 32)

Maximisation of value of assets and dues: The liquidator shall endeavor to recover and realize all assets of and dues to the corporate person in a time-bound manner for maximization of value for the stakeholders.

Liquidator to realize uncalled capital or unpaid capital contribution (Regulation 33)

Realisation of amount due from contributory: The liquidator shall realize any amount due from any contributory to the corporate person. [Regulation 33 (1)]

Realisation of uncalled capital and calls in arrear:

- The liquidator shall be entitled to call and realize the uncalled capital of the corporate person and to collect the arrears if any due on calls made prior to the liquidation commencement date.
- The liquidator shall exercise this power notwithstanding any charge or encumbrance on the uncalled capital of the corporate person.
- A 15 days demand notice shall be served to the contributory to make the payments within fifteen days from the receipt of the notice.
- Along with right to serve demand notice to collect dues or calls-in-arrear, the liquidator is vested with the right to hold all moneys so realized subject to the rights, if any, of the holder of any such charge or encumbrance. [Regulation 33 (2)]

Distribution to be made to contributory: No distribution shall be made to a contributory, unless he makes his contribution to the uncalled or unpaid capital as required in the constitutional documents of the corporate person. [Regulation 33 (3)]

PROCEEDS OF LIQUIDATION AND DISTRIBUTION OF PROCEEDS

Provisions for claims are provided in Chapter VII from Regulations 34 to 41 of Voluntary Liquidation Regulations.

All money to be paid in to bank account (Regulation 34)

Opening Bank Account in a scheduled bank: The liquidator shall open a bank account

- in the name of the corporate person followed by the words ‘in voluntary liquidation’,
- in a scheduled bank,
- for the receipt of all moneys due to the corporate person. [Regulation 34 (1)]

Deposit of the realized amount by next working day: The liquidator shall pay to the credit of the bank account opened under sub-regulation (1) all moneys, including cheques and demand drafts received by him as the liquidator of the corporate person, and the realizations of each day shall be deposited into the bank account without any deduction not later than the next working day. [Regulation 34 (2)]

Use of deposits in bank: The money in the credit of the bank account shall not be used except in accordance with section 53(1) i.e. waterfall mechanism for distribution of realized amount in accordance with the priority and manner laid down in Section 53(1). [Regulation 34 (3)]

Cheque or online payment above specified limit: All payments out of the account by the liquidator above five thousand rupees shall be made by cheques drawn or online banking transactions against the bank account. [Regulation 34 (4)].

Distribution (Regulation 35)

Timeline for distribution of proceeds: The liquidator shall distribute the proceeds from realization within thirty days from the receipt of the amount to the stakeholders. [Regulation 35 (1)]

Deduction of liquidation costs before such distribution: The liquidation costs shall be deducted before such distribution is made. [Regulation 35 (2)]

Distribution of asset to stakeholder: The liquidator may, with the approval of the corporate person, distribute amongst the stakeholders, an asset that cannot be readily or advantageously sold due to its peculiar nature or other special circumstances. [Regulation 35 (3)]

Return of money (Regulation 36)

Refund of money to which stakeholder is not entitled to: A stakeholder shall forthwith return any monies received by him in distribution, which he was not entitled to at the time of distribution, or subsequently became not entitled to.

Completion of liquidation (Regulation 37)

Timeline for completion of Liquidation process: Regulation 37(1) provides for that the liquidator shall endeavour to complete the liquidation process of the corporate person and submit the Final Report under regulation 38 within: -

(a) two hundred and seventy days from the liquidation commencement date where the creditors have approved the resolution under clause (c) of sub-section (3) of section 59 or clause (c) of sub-regulation (1) of regulation 3, and

(b) ninety days from the liquidation commencement date in all other cases.

In the event of the liquidation process continuing for more than the period stipulated in Regulation 37(1) the liquidator shall

(a) hold a meeting of the contributories of the corporate person within fifteen days –

  (i) from the end of two hundred and seventy days or ninety days, as the case may be, and

  (ii) thereafter at the end of every succeeding two hundred and seventy days or ninety days, as the case may be, as stipulated in Regulation 37(1), till submission of application for dissolution of the corporate person; and

(b) shall present Status Report(s)indicating progress in liquidation, including-

  (i) settlement of list of stakeholders;

  (ii) details of any assets that remains to be sold and realized;

  (iii) distribution made to the stakeholders;

  (iv) distribution of unsold assets made to the stakeholders;

  (v) developments in any material litigation, by or against the corporate person;

  (vi) filing of, and developments in applications for avoidance of transactions in accordance with Chapter III of Part II of the Code. [Regulation 37 (2)]

Enclosures with the Status Report: The Status Report shall enclose the audited accounts of the liquidation showing the receipts and payments pertaining to liquidation since the liquidation commencement date. [Regulation 37 (3)]

Final Report (Regulation 38)

Contents of Final Report: Regulation 38 (1) provides for that the liquidator shall prepare the Final Report on completion of the liquidation process.

Final Report shall consist of-[Regulation 38 (1)]

- (a) audited accounts of the liquidation, → showing receipts and payments pertaining to liquidation since the liquidation commencement date; and
- (b) a statement demonstrating that-
  - (i) the assets of the corporate person has been disposed of;
  - (ii) the debt of the corporate person has been discharged to the satisfaction of the creditors;
  - (iii) no litigation is pending against the corporate person or sufficient provision has been made to meet the obligations arising from any pending litigation.
- (c) a sale statement in respect of all assets containing -
  - he realized value;
  - (i) cost of realization, if any;
  - (ii) the manner and mode of sale;
  - (iii) an explanation for the shortfall, if the value realized is less than the value assigned by the registered valuer in the report of the valuation of assets under section 59(3)(b)(ii) or Regulation 3(1)(b)(ii), as the case may be;
  - (iv) the person to whom the sale is made; and (vi) any other relevant details of the sale.

Final Report to be submitted to Regulatory Authorities: The liquidator shall send the Final Report forthwith, to the Registrar and the Board. [Regulation 38 (2)]

Submission of Final Report and Compliance Certificate to AA: The liquidator shall submit the Final Report and the compliance certificate in Form-H along with the application under sub-section (7) of section 59 to the Adjudicating Authority. [Regulation 38 (3)]

Corporate Voluntary Liquidation Account (Regulation 39)

Open Corporate Voluntary Liquidation Account: The Board shall operate and maintain an Account to be called the Corporate Voluntary Liquidation Account in the Public Accounts of India.

It is provided that until the Corporate Voluntary Liquidation Account is operated as part of the Public Accounts of India, the Board shall open a separate bank account with a Scheduled bank for the purposes of this regulation. [Regulation 39(1)]

Unclaimed dividend and undistributed proceeds to be deposited in the account: A liquidator shall deposit the amount of unclaimed dividends, if any, and undistributed proceeds, if any, in a liquidation process along with any income earned thereon till the date of deposit, into the Corporate Voluntary Liquidation Account before he submits an application under sub-section (7) of section 59 for dissolution of the corporate person. [Regulation 39(2)]

15 days' time for deposit of unclaimed dividends or undistributed proceeds in hand: A liquidator, who holds any amount of unclaimed dividends or undistributed proceeds in a liquidation process on the date of commencement of the Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) (Amendment) Regulations, 2020, shall deposit the same within fifteen days of the date of such commencement, along with any income earned thereon till the date of deposit. [Regulation 39(3)]

Interest for delay in deposit in the Account: A liquidator, who fails to deposit any amount into the Corporate Voluntary Liquidation Account under this regulation, shall deposit the same along with interest thereon at the rate of twelve percent per annum from the due date of deposit till the date of deposit. [Regulation 39(4)]

Submission of evidence of deposit of the amount in the Account to Regulatory Authorities: A liquidator shall submit to the authority with which the corporate person is registered and the Board, the evidence of deposit of the amount into the Corporate Voluntary Liquidation Account under this regulation, and a statement in Form-G setting forth the nature of the amount deposited into the Corporate Voluntary Liquidation Account, and the names and last known addresses of the stakeholders entitled to receive the unclaimed dividends or undistributed proceeds. [Regulation 39(5)]

Receipt of Deposit: The liquidator shall be entitled to a receipt from the Board for any amount deposited into the Corporate Voluntary Liquidation Account under this regulation. [Regulation 39(6)]

Form for filing claim for amount deposited in the account: A stakeholder, who claims to be entitled to any amount deposited into the Corporate Voluntary Liquidation Account, may apply to the Board in Form-I for an order for withdrawal of the amount.

Regulation (7) provides that prior to dissolution of the corporate person, a stakeholder, who claims to be entitled to any amount deposited into the Corporate Voluntary Liquidation Account, may apply to the liquidator in Form-I for withdrawal of the amount.

As per Regulation (7A), on receipt of request under sub-regulation (7), the liquidator after verification of the claim, shall request the Board for release of amount to him for onward distribution.

Regulation (7B) states that the Board on receipt of request under sub-regulation (7A) may release the amount to the liquidator.

Regulation (7C) provides that the liquidator shall, after making the distribution to the stakeholder shall intimate the Adjudicating Authority of such distribution.

According to Regulation (7D), after dissolution of the corporate person, a stakeholder, who claims to be entitled to any amount deposited into the Corporate Voluntary Liquidation Account, may apply to the Board in Form-I for an order for withdrawal of the amount.

Regulation (7E) states that if any other person other than the stakeholder claims to be entitled to any amount deposited to the Corporate Voluntary Liquidation Account, he shall submit evidence to satisfy the liquidator or the Board, as the case may be, that he is so entitled.

Detection of Fraud or Insolvency (Regulation 40)

Application to AA to suspend the process of liquidation: Regulation 40 lays down following situations in which the liquidator shall make an application to the Adjudicatory Authority to suspend the process of liquidation and pass any such orders as it deems fit:

(i) Where the liquidator is of the opinion that the liquidation is being done to defraud a person [Regulation 40(1)]

(ii) Where the liquidator is of the opinion that the corporate person will not be able to pay its debts in full from the proceeds of assets to be sold in the liquidation [Regulation 40(2)]

Preservation of records (Regulation 41)

Preservation of copies of records: The liquidator shall preserve copies of all such records which are required to give a complete account of the voluntary liquidation process. [Regulation 41(1)]

Records to be preserved: Without prejudice to the generality of the obligations under sub-regulation (1), the liquidator shall preserve copies of records relating to or forming the basis of:-

[Regulation 41(2)]

(a) his appointment as liquidator, including the terms of appointment;

(b) handing over / taking over of the assignment;

(c) initiation of voluntary liquidation process;

(d) public announcement;

(e) claims, verification of claims, and list of stakeholders;

(f) engagement of professionals, registered valuers, etc. including work done, reports etc., submitted by them;

(g) all filings with the Adjudicating Authority, Appellate Authority, High Courts, Supreme Court, whichever applicable and their orders;

(h) statutory filings with Board and insolvency professional agencies;

(i) correspondence during the voluntary liquidation process;

(j) cost of voluntary liquidation process;

(k) all reports, registers, documents such as preliminary report, annual status report, final report prior to dissolution, various registers and books, etc. mentioned in Regulation 8 and 10 of principal regulations; and

(l) any other records, which is required to give a complete account of the process.

Minimum period of preservation of records

The liquidator shall preserve:

(a) electronic copy of all records(physical and electronic) for a minimum period of eight years; and

(b) a physical copy of records for a minimum period of three years; from the date of dissolution of the corporate person, before the Board, the Adjudicating Authority, Appellate Authority or any Court, whichever is later. [Regulation 41(3)]

Duty to handover records to new liquidator: In case of replacement of liquidator during the process, the outgoing liquidator shall handover the records under sub-regulation (1) and (2) to the new liquidator. [Regulation 41(4)]

Duty of liquidator to preserve record at safe place and produce them: The liquidator shall preserve the records at a secure place and shall be obliged to produce records as may be required under the Code and the principal regulations. [Regulation 41(5)]

Details of preservation of records to be filed with the application for dissolution of corporate person: The liquidator shall, along with the application filed under sub-section (7) of section 59 to the Adjudicating Authority, provide the details and manner of preservation of records under sub-regulation (1) and (2). Explanation - The records referred to in this regulation includes records pertaining to the period of a liquidation process during which the liquidator acted as such, irrespective of the fact that he did not take up the assignment from its commencement or continue the assignment till its conclusion. [Regulation 41(6)]

Time line for Voluntary Liquidation Process T=Liquidation Commencement Date			
Sl. No	**Section / Regulation**	**Description of Task**	**Norm (Number of Days)**
1	Section 59(3)(a), Regulation 3(1) (a)	Declaration from majority of directors / partners regarding solvency of corporate person and it not being liquidated to defraud any person	T – 28
2.	Section 59[(3)(c) and (5)], Regulation 3(1) (c) and 3(3)	Passing of resolution / special resolution by members / partners about commencement of voluntary liquidation process and appointment of insolvency professional as liquidator	T = 0
3.	Proviso to Section 59(3)(c), Regulation 3(1)(c)	Approval of creditors representing two-third in value of debt, if the corporate person owes any debt, of the resolution passed under section 59(3)(c) or regulation 3(1)(c)	T + 7
4.	Regulation 5(2)	Intimation by Insolvency Professional regarding his appointment as Liquidator, to the Board	T + 7
5.	Regulation 14 (1)	Public Announcement in Form A by the Liquidator	T + 5
6.	Section 59(4), Reg. 3(2)	Notification to Registrar of Companies and Board about the resolution passed under section 59(3)(c) and regulation 3(1)(c) or subsequent approval of creditors thereto, as the case may be, by corporate person	T + 7 or T + 14
7.	Section 38(1), Regulation 14 (2)	Submission of claims by stakeholders	T + 30
8.	Section 38(5)	Withdrawal/ modification of claim by stakeholders	T + 44
9.	Regulation 9(1)	Submission of preliminary report to the corporate person by the Liquidator	T + 45
10.	Regulation 29(1)	Verification of claims by the Liquidator	T + 60
11.	Section 40 (2)	Intimation about decision of acceptance/ rejection of claim to the stakeholders by the Liquidator	T + 67
12.	Regulation 30(2)	Preparation of list of stakeholders by the Liquidator	T + 45*/75
13.	Section 42	Appeal by creditor against the decision of the Liquidator	T + 81
14.	Regulation 35(1)	Distribution of the proceeds to stakeholders by the Liquidator	Date of realization + 30 days
15.	Regulation 39(2)	Deposit of amount of unclaimed dividends and undistributed proceeds in Corporate Voluntary Liquidation Account by the Liquidator	Prior to submission of application under sub-section (7) of section 59
16.	Regulation 38(2)	Submission of Final Report to the Board and Registrar of Companies by the Liquidator	T + 90*/270

17.	Section 59(7), Regulation 38(3)	Submission of Final Report, along with the application for dissolution, to AA	T + 90*/270
18.	Regulation 37(1)	Completion of Voluntary Liquidation Process	T + 90*/270
19.	Regulation 37(2)	Meeting of Contributories and presentation of Annual Status Report.	T + 365
*Applicable where approval of creditors was not required under section 59(3)(c) or regulation 3(1)(c)			
Source: The IBBI (Voluntary Liquidation Process) Regulations,2017			

SCHEDULE I		
FORMS	**Events**	**The Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations, 2017**
FORM A	Public Announcement	Regulation 14
FORM B	Proof of claim by operational creditors except Workmen and Employees	Regulation 16
FORM C	Proof of claim by Financial Creditors	Regulation 17
FORM D	Proof of claim by a workman or employee	Regulation 18
FORM E	Proof of claim by Authorised Representative of workmen or employees	Regulation 18(2)
FORM F	Proof of claim by any other stakeholder	Regulation 19
FORM-G	Deposit of Unclaimed Dividends and/or Undistributed Proceeds	Regulation 39(5)
FORM-H	Compliance Certificate	Regulation 38(3)
FORM-I	Withdrawal from Corporate Voluntary Liquidation Account	Regulation 39(7)

CASE LAW-

Nippei Toyoma India Private Limited

The petition was filed by Nippei Toyoma India Private limited to initiate voluntary liquidation proceedings under section 59 of Insolvency and Bankruptcy Code, 2016 (IBC) before NCLT, Mumbai Bench.

Facts of the case

The Company was incorporated under the provisions of Companies Act, 1956 on 27.04.2007. It was engaged in the business of providing engineering services and trading of automotive components for automotive industries. The Company does not have any operations as not carrying on any business activities. Considering the cost and time involved in ensuring compliances regarding the Company, the members of the Company in their Extra Ordinary General Meeting held on 28.09.2017 resolved to voluntary liquidate the Company.

Judgement

The directors of the Company declared on affidavit dated 27.09.2017 that they have made full inquiry into the affairs of the Company, and are of the opinion that the Company has no debts/will be able to pay its debt in full from the proceeds of assets to be sold in the voluntary liquidation and that it is not being wound-up to defraud any person. The directors have appended to the aforesaid affidavit, audited financial statements and record of business operations of the company of previous two financial years viz. year ending on 31.03.2016 and 31.03.2017.

The statement of payment to stakeholders, annexed to the petition, detailed the payment made to various stakeholders and Dividend Distribution Tax. Post the aforementioned payment, the accumulated profit of Rs. 53,06,973/- as dividend and investment in share capital of Rs. 1,00,00,000/- were paid to the members of the Company, thereby, the assets of the company were fully liquidated.

The Independent Auditor certified that during the liquidation period 28.09.2017 to 23.07.2018, the proper books of accounts were kept and the said financial statements comply with the accounting standards under section 133 of Companies Act 2013. Further, it certified that there is no pending litigation involving the Company, there are no long term contracts with the Company for which there may be any foreseeable losses and there is no amount which is to be transferred to the Investor Education and Protection Fund by the Company.

The copy of the final report of the Liquidator dated 12.09.2018 was annexed to the petition, stating how the liquidation process has been conducted from 28.09.2017 to 12.09.2018, that all the assets of the Company have been discharged to the satisfaction of the creditors and that no litigation is pending against the company. The said Final Report of the Liquidator was submitted with the Registrar of Companies vide Form GNL-2 dated 13.09.2018. The Liquidator had filed this petition before the Tribunal under section 59(7) of The Code seeking order of dissolution of the Company.

NCLT noted that on examining the submission made by the counsel appearing for the petitioner and the documents annexed to the petition, it appears that the affairs of the company have been completely wound-up, and its assets completely liquidated.

NCLT in view of the above facts and circumstances and Final Report of the Liquidator directed that the Company shall be dissolved from the date of its order. The Petitioner was further directed to serve a copy of the order upon the Registrar of Companies, with which the Company is registered, within fourteen days of receipt of the order.

Yogeshwar Enterprise Pvt Ltd, Order delivered on: 23/01/2023, National Company Law Tribunal Ahmedabad

Application under Section 59 of the Insolvency and Bankruptcy Code, 2016 read with the Regulation 38 of the Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations, 2017 was filed for voluntary liquidation of Yogeshwar Enterprise Private Limited ("Company")

Facts of the case:

The Company was incorporated as a Private Limited Company under the provisions of the Companies Act, 1956, on 18.10.2010.

The main objects of the Company were doing business and real estate activities and construction. It is submitted that the Board of Directors of the Company were of the opinion to close down the business of the company by way of voluntarily liquidation, because of non-availability of business prospects and lack of long-term financial resources for the company. It was not financially viable to carry on the business activity of the company. Thus, the Directors (BOD) in their board meeting held on 28.10.2021 resolved to voluntarily liquidate the Company.

All the directors have declared on Affidavit dated 27.10.2021 that they have made full enquiry into the affairs of the Company and formed an opinion that the Company will be able to pay its debt in full within 12 months from the commencement of winding up, and further affirmed that by way of voluntary liquidation, the company is not being liquidated to defraud any person.

Audited financial statements and records of business operations of the Company of previous two financial years, viz. year ending 31.03.2020 and 31.03.2021 are also annexed.

The members of the Company in Extra-Ordinary General meeting held on 10.11.2021, as per provision of the Companies Act, 2013, had passed a Special Resolution to liquidate the Company voluntarily and appointed Insolvency Professional, to act as Liquidator.

The Liquidator had notified the Registrar of Companies, Ahmedabad (ROC) about the passing of a Special Resolution under sub-section (4) of Section 59 of the IBC to liquidate the Corporate Person and appointment of Liquidator in Form MGT and Form GNL 2.

The liquidator submitted that they have received no claims as there are no other stakeholders than equity shareholders.

The Liquidator has also submitted the IBBI Circular No. IBBI/LIQ/45/2021 dated 15.11.2021 stating that the point 5 of that circular hereby clarified that "as per the provisions of the Code and the Regulations read with Section 178 of the Income-tax Act, 1961, an Insolvency Professional handling voluntary liquidation process is not required to seek any NOC/NDC from the Income-Tax Department as part of compliance in the said process."

However, the liquidator had served notice of appointment by email and speed post to the Income Tax Department informing them about the voluntary liquidation of the Company and that he has made compliance with the Regulation 14 of the Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations, 2017. However, no response was received nor any request for extension was made by the Income Tax Department.

Judgement:

Necessary compliances as per provisions of the Code have been made by the Corporate Person and the Liquidator. In exercise of the powers conferred under sub-section (8) of Section 59 of the Insolvency and Bankruptcy Code, 2016 Application is allowed with the following directions:

i. Yogeshwar Enterprise Private Limited having CIN U45200GJ2010PTC062656, stands dissolved from the date of this Order.

ii. The Liquidator is directed to file this order with the concerned Registrar of Companies, Income Tax Department and IBBI within 14 days from the date of receipt of an authentic copy this order, for information and necessary action.

iii. The Liquidator is also directed to file this order with all other Statutory Authorities connected with the affairs of the Company.

iv. The Liquidator shall preserve a physical or an electronic copy of the reports, registers and books of account referred to in Regulations 8 and 10 of IBBI Regulations for at least eight years after the dissolution of the Corporate Person, either with himself or with an information utility.

v. Copy of the order be served to the respective parties.

Source: https://nclt.gov.in/

LESSON ROUND-UP

- As per section 59, a corporate person who intends to liquidate itself voluntarily and has not committed any default may initiate voluntary liquidation proceedings under the provisions of Chapter V of Part II of the Code.
- The Insolvency and Bankruptcy Board of India has made the IBBI (Voluntary Liquidation Process) Regulations, 2017 to regulate the voluntary liquidation of corporate persons.
- The corporate person shall from the liquidation commencement date cease to carry on its business except as far as required for the beneficial winding-up of its business.
- Passing of special resolution for approving the proposal of voluntary liquidation and appointment of liquidator, within four weeks of the aforesaid declaration(s). If a corporate person owes debts, approval of two-third majority creditors would also be required.
- Public announcement is issued inviting claims of all stakeholders, within five days of his appointment, in newspaper as well as on website of the corporate person and Board.
- A person, who claims to be a stakeholder, shall prove his claim for debt or dues to him, including interest, if any, as on the liquidation commencement date.
- The liquidator shall verify the claims submitted within thirty days from the last date for receipt of claims and may either admit or reject the claim, in whole or in part, as the case may be, as per section 40 of the Code.
- The liquidator may value and sell the assets of the corporate person in the manner and mode approved by the corporate person in compliance with provisions, if any, in the applicable statute.
- The liquidator shall distribute the proceeds from realization within thirty days from the receipt of the amount to the stakeholders.
- The liquidator shall endeavor to complete the liquidation process within 270 days (in case there are creditors in corporate person) and 90 days in other cases from Liquidation Commencement Date.

TEST YOURSELF

(These are meant for recapitulation only answer to these questions are not to be submittied for evaluation).

1. Who may initiate voluntary liquidation under IBC, 2016?
2. What are the essential contents of Preliminary Report to be filed by liquidator for a corporate person undergoing voluntary liquidation?
3. What are the provisions for preservation of records by liquidator for corporate person undergoing voluntary liquidation?
4. Who has to make public announcement and by what time and in what manner for a corporate person undergoing voluntary liquidation?
5. Write provisions w.r.t. Corporate Voluntary Liquidation Account under the IBBI (Voluntary Liquidation Process) Regulations,2017.

REFERENCES

- IBBI 2019 Handbook
- The IBBI (Voluntary Liquidation Process) Regulations,2017
- The IBC,2016

Debt Recovery & SARFAESI

Lesson 24

KEY CONCEPTS

■ Securitisation ■ Asset reconstruction Company ■ Financial assets ■ Financial Lease ■ Borrower ■ Security Interest ■ Stressed Assets ■ Non-performing asset ■ Financial Institutions ■ Debt Recovery Tribunal

Learning Objectives

To understand:

- The legalframe work provided for law regulating securitisation and reconstruction of financial assets
- SARFAESI Act, 2002
- The important definitions and concepts
- To familiarize the students with the legal frame work pertaining to debt recovery.

Lesson Outline

- Introduction
- SARFAESI Act, 2002
- Asset Reconstruction Companies
- Measures for asset reconstruction
- Enforcement of security interest by creditors
- Central Registry
- Debt Recovery
- Debt Recovery Tribunals (DRT)
- Application to the DRT
- Modes of Recovery
- Lesson Round-Up
- Test Yourself
- List of Further Readings
- Other References (Including Websites/Other Links)

REGULATORY FRAMEWORK

- Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
- Recovery of Debts due to Banks and Financial Institutions Act, 1993

An Act to regulate securitisation and reconstruction of financial assets and enforcement of security interest and to provide for a Central database of security interests created on property rights, and for matters connected therewith or incidental thereto.

INTRODUCTION

In the traditional lending process, a bank makes a loan, maintaining it as an asset on its balance sheet, collecting principal and interest, and monitoring whether there is any deterioration in borrower's creditworthiness.

This requires a bank to hold assets till repayment of loan. The funds of the bank are blocked in these loans and to meet its growing fund requirements, a bank has to raise additional funds from the market. Securitisation is a way of unlocking these blocked funds.

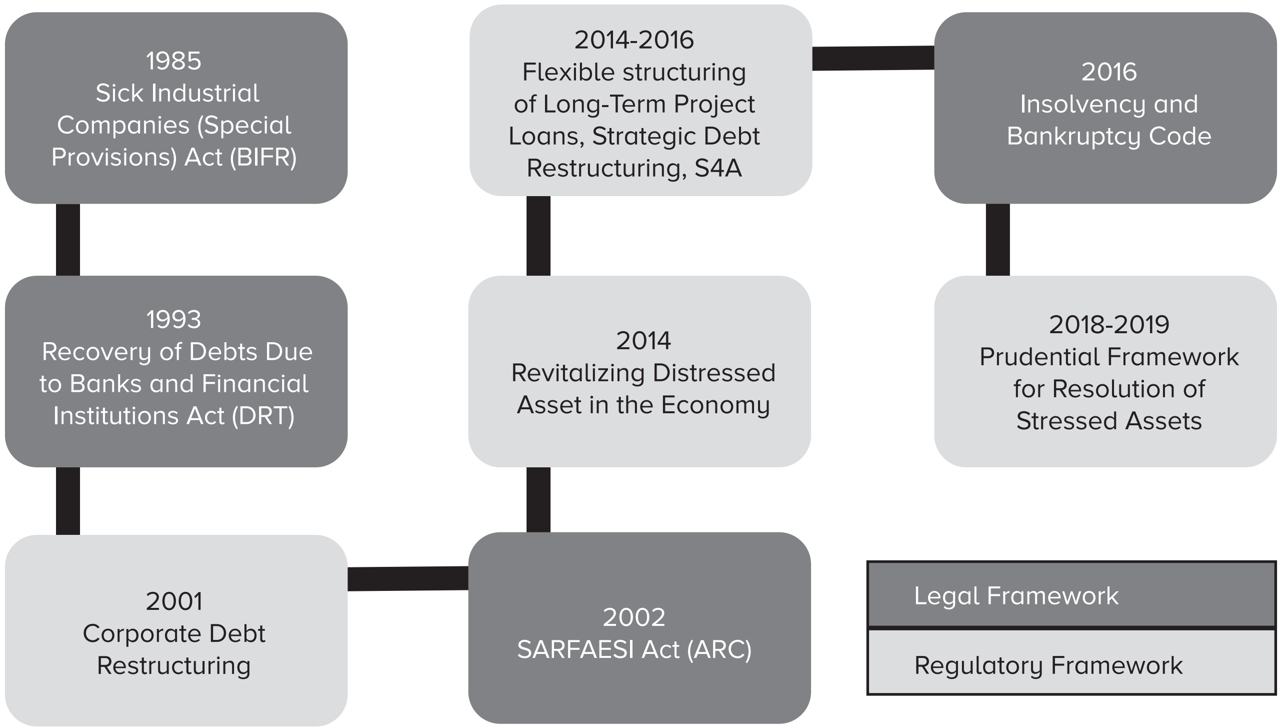
The process leads to the creation of financial instruments that represent ownership interest in, or are secured by a segregated income producing asset or pool of assets. The pool of assets collateralises securities. These assets are generally secured by personal or real property (e.g. automobiles, real estate, or equipment loans), but in some cases are unsecured (e.g. credit card debt, consumer loans).

EVOLUTION OF REGULATORY FRAMEWORKS FOR HANDLING OF STRESSED ASSETS

A sound banking system is an essential requirement for maintaining financial stability in any country. One of the parameters of soundness is the level of non-performing assets (NPAs) in the banking system. In this context, it is common knowledge that the Indian banking system has often been saddled with high levels of NPAs which has been affecting the profitability and eventually the capital position of banks, especially the public sector banks (PSBs). This has been one of the factors which has led to some level of risk aversion among the banks and thereby deceleration of credit growth in the country in the recent years.

In view of its importance for the health of the banking system, management of NPAs has been attracting attention from the RBI and the Government for quite some time now. The first such significant legal framework to manage the stress in the banking system was the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA). It was enacted for timely detection of sickness in industrial units and to undertake speedy action to resolve the insolvency of sick units through a Board of experts, namely the Board for Industrial and Financial Reconstruction (BIFR). SICA failed to meet its objective due to delays caused by legal suits and lack of timely decisions by the stakeholders and, therefore, was finally repealed in the year 2003. Related provisions of this Act were added in the Companies Act, 2013 and the National Company Law Tribunal (NCLT) took over the functions of BIFR. Insolvency resolution frameworks as a tool for handling stressed assets culminated into the Insolvency and Bankruptcy Code, 2016 (IBC). IBC was enacted as a single code to consolidate the existing frameworks for insolvency and bankruptcy and has emerged as a significant tool for recovery.

Other noteworthy legislations which aimed to facilitate recovery of debt for banks and Financial Institutions include the Recovery of Debt due to Banks and Financial Institutions Act, 1993 (RDDBFI Act) and the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002. The former Act attempts to provide speedy recovery through tribunals, namely, Debt Recovery Tribunals (DRTs) whereas the latter allows secured creditors to enforce their security interest without the intervention of the courts. The Act also led to creation of asset reconstruction companies (ARCs) as a permanent institutional arrangement to handle the stressed financial assets of banks and other financial institutions.



Source: *Report of the Committee to Review the Working of Asset Reconstruction Companies, September 2021.*

REGULATION OF SECURITISATION AND RECONSTRUCTION OF FINANCIAL ASSETS OF BANKS AND FINANCIAL INSTITUTIONS

Introduction

The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Ordinance, 2002 was promulgated on the 21st June, 2002 to regulate securitisation and reconstruction of financial assets and enforcement of security interest and for matters connected therewith or incidental thereto. The provisions of the Ordinance enabled banks and financial institutions to manage problems of liquidity, asset liability mismatches and improvement in recovery by exercising powers to take possession of securities, sell them and reduce non-performing assets by adopting measures for recovery or reconstruction.

The SARFAESI Act, 2002 has empowered the Banks and Financial Institutions with vast power to enforce the securities charged to them. The Banks can now issue notices to the defaulters to pay up the dues and if they fail to do so within 60 days of the date of the notice, the banks can take over the possession of assets like factory, land and building, plant and machinery etc. charged to them including the right to transfer by way of lease, assignment or sale and realize the secured assets. In case the borrower refuses peaceful handing over of the secured assets, the bank can also file an application before the District Magistrate or Chief Metropolitan Magistrate for taking possession of assets. The Banks can also take over the management of business of the borrower. The bank in addition can appoint any person to manage the secured assets the possession of which has been taken over by the bank. Banks can package and sell loans via "Securitisation" and the same can be traded in the market like bonds and shares.

SARFAESI ACT

Securitization of financial assets and issue of security receipts:

Acquire financial assets by agreement, issuance of debentures or bonds. Redeem the security receipts given to the QIBs after their realisation.

Reconstruction of financial assets:

Subject to varying RBI standards, take actions for proper management, a sale, a debt restructure, a settlement, or to take control.

Enforcement of security interest:

Enforce the secured creditor's security interest without the need for court action.

Other functions:

Act as a recovery agent for financial institutions (FIs) or banks, as the manager of the secured assets appointed by the lender, or as the receiver assigned by the court.

CONSTITUTIONAL VALIDITY OF THE SARFAESI ACT

The SARFAESI Act, 2002 was challenged in various courts on grounds that it was loaded heavily in favour of lw enders, giving little chance to the borrowers to explain their views once recovery process is initiated under the legislation. Leading the charge against the said Act was Mardia Chemicals in its plea against notice served by ICICI Bank. The Government had, however, argued that the legislation would bring about a financial discipline and reduce the burden of Non-Performing Assets (NPAs) of banks and institutions.

In ***Mardia Chemicals Ltd. v. UOI [2004] 59 CLA 380 (SC)****, it was urged by the petitioner that:*

(a) there was no occasion to enact such a draconian legislation to find a short-cut to realise non-performing assets ('NPAs') without their ascertainment when there already existed the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 ('Recovery of Debt Act') for doing so;

(b) no provision had been made to take into account lenders liability;

(c) that the mechanism for recovery under Section 13 does not provide for an adjudicatory forum of inter se disputes between lender and borrower; and

(d) that the appeal provisions were illusory because the appeal would be maintainable after possession of the property or management of the property was taken over or the property sold and the appeal is not entertainable unless 75 per cent of the amount claimed is deposited with the Debts Recovery Tribunal ('DRT').

The Hon'ble Supreme Court held that though some of the provisions of the Act 2002 were a bit harsh for some of the borrowers but on those grounds the impugned provisions of the Act cannot be said to unconstitutional in the view of the fact that the objective of the Act is to achieve speedier recovery of the dues declared as NPAs and better availability of capital liquidity and resources to help in growth of economy of the country and welfare of the people in general which would sub-serve the public interest.

The Supreme Court observed that the Act provides for a forum and remedies to the borrower to ventilate his grievances against the bank or financial institution, inter alia, with respect to the amount of the demand of the secured debt. After the notice is sent, the borrower may explain the reasons why the measures may or may not be taken under Sub-section (4) of Section 13. The creditor must apply its mind to the objections raised in reply to such notice. There must be meaningful consideration by the Court of the objections raised rather than to ritually reject them and to proceed to take drastic measures under Sub-section (4) of Section 13. The court held that such a procedure/mechanism was conducive to the principles of fairness and that such a procedure was also important from the point of view of the economy of the country and would serve the purpose in the growth of a healthy economy. It would serve as guidance to secured debtors in general in conducting their affairs.

The court opined that the fairness doctrine, cannot be stretched too far, such communication is only for the purposes of the secured debtors knowledge and cannot give an occasion to the secured debtor to resort to any proceeding, which are not permissible under the provisions of the Act. Thus, a secured debtor is not allowed to challenge the reasons communicated or challenge the action likely to be taken by the secured creditor at that point of time unless his right to approach the DRT as provided under section17 matures on any measure having been taken under Sub-section (4) of Section 13.

Moreover, another safeguard is also available to a secured borrower within the framework of the Act i.e. to approach the DRT under Section 17 though such a right accrues only after measures are taken under Sub-section (1) of Section 13.

The Hon'ble Supreme Court, however, found that the requirement of deposit of 75 per cent of the amount claimed before entertaining an appeal (petition) under Section 17 is an oppressive, onerous and arbitrary condition and against all the canons of reasonableness. It held this provision to be invalid and ordered that it was liable to be struck down. The amount of deposit for making an appeal has since been reduced to 5% of the amount claimed, to keep it reasonable and also to check the genuineness of the Appellant.

It maybe noted that-

Non-performing asset means an asset or account of a borrower, which has been classified by a bank or financial institution as sub-standard, doubtful or loss asset,**—**

(a) in case such bank or financial institution is administered or regulated by any authority or body established, constituted or appointed by any law for the time being in force, in accordance with the directions or guidelines relating to assets classifications issued by such authority or body;

(b) in any other case, in accordance with the directions or guidelines relating to assets classifications issued by the Reserve Bank. [Section 2(1)(o)]

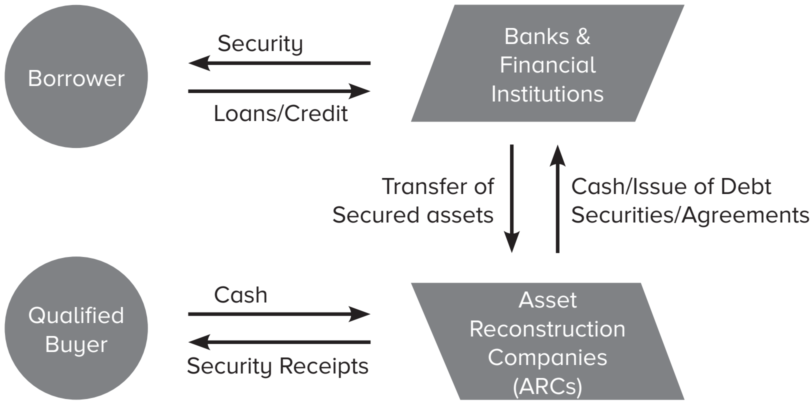
Asset Reconstruction Company

Asset reconstruction company means a company registered with Reserve Bank under section 3 of SARFAESI Act for the purposes of carrying on the business of asset reconstruction or securitisation, or both.

The problem of non-performing loans created due to systematic banking crisis world over has become acute. Focused measures to help the banking systems to realise its NPAs has resulted into creation of specialised bodies called asset management companies which in India have been named asset reconstruction companies ('ARCs'). The buying of impaired assets from banks or financial institutions by ARCs will make their balance sheets cleaner and they will be able to use their time, energy and funds for development of their business. ARCs may be able to mix up their assets, both good and bad, in such a manner to make them saleable.

The main objective of asset reconstruction company ('ARC') is to act as agent for any bank or financial institution for the purpose of recovering their dues from the borrowers on payment of fees or charges, to act as manager of the borrowers' asset taken over by banks, or financial institution, to act as the receiver of properties of any bank or financial institution and to carry on such ancillary or incidental business with the prior approval of Reserve Bank wherever necessary. If an ARC carries on any business other than the business of asset reconstruction or securitisation or the business mentioned above, it shall cease to carry on any such business within one year of doing such other business.

Process under SARFAESI Act



Registration of asset reconstruction companies

As per Section 3(1) of the Act, no asset reconstruction company shall commence or carry on the business of securitisation or asset reconstruction without—

a. obtaining a certificate of registration granted under this section; and

b. having net owned fund of not less than one crore rupees or such other higher amount as the Reserve Bank, may, by notification, specify;

Provided that the Reserve Bank may, by notification, specify different amounts of owned fund for different class or classes of asset reconstruction companies:

The requirement of net owned funds for ARCs has been increased to Rs 300 crore on an ongoing basis from the existing requirement of Rs 100 crore.

However, the RBI has provided a glide path for the existing ARCs to achieve the minimum required NOF of Rs 300 crore — Rs 200 crore by March 31, 2024; and Rs 300 crore by March 31, 2025. *(RBI/2022-23/128 DoR.SIG. FIN.REC.75/26.03.001/2022-23 dt October 11, 2022)*

Provided further that an asset reconstruction company, existing on the commencement of this Act, shall make an application for registration to the Reserve Bank before the expiry of six months from such commencement and notwithstanding anything contained in this sub-section may continue to carry on the business of securitisation or asset reconstruction until a certificate of registration is granted to it or, as the case may be, rejection of application for registration is communicated to it.

Every asset reconstruction company shall make an application for registration to the Reserve Bank in such form and manner as it may specify.

Sub-clause 3 states that the Reserve Bank may, for the purpose of considering the application for registration of an asset reconstruction company to commence or carry on the business of securitisation or asset reconstruction, as the case may be, require to be satisfied, by an inspection of records or books of such asset reconstruction company, or otherwise, that the following conditions are fulfilled, namely:—

i. that the asset reconstruction company has not incurred losses in any of the three preceding financial years;

ii. that such asset reconstruction company has made adequate arrangements for realisation of the financial assets acquired for the purpose of securitisation or asset reconstruction and shall be able to pay periodical returns and redeem on respective due dates on the investments made in the company by the qualified buyers or other persons;

iii. that the directors of asset reconstruction company have adequate professional experience in matters related to finance, securitisation and reconstruction;

iv. that any of its directors has not been convicted of any offence involving moral turpitude;

v. that a sponsor of an asset reconstruction company is a fit and proper person in accordance with the criteria as may be specified in the guidelines issued by the Reserve Bank for such persons;

vi. that asset reconstruction company has complied with or is in a position to comply with prudential norms specified by the Reserve Bank;

vii. that asset reconstruction company has complied with one or more conditions specified in the guidelines issued by the Reserve Bank for the said purpose.

The Reserve Bank may, after being satisfied that the conditions specified in sub-section (3) are fulfilled, grant a certificate of registration to the asset reconstruction company to commence or carry on business of securitisation or asset reconstruction, subject to such conditions, which it may consider, fit to impose.

The Reserve Bank may reject the application made under sub-section (2) if it is satisfied that the conditions specified in sub-section (3) are not fulfilled:

Provided that before rejecting the application, the applicant shall be given a reasonable opportunity of being heard.

Every asset reconstruction company shall obtain prior approval of the Reserve Bank for any substantial change in its management including appointment of any director on the board of directors of the asset reconstruction company or managing director or chief executive officer thereof or change of location of its registered office or change in its name:

Provided that the decision of the Reserve Bank, whether the change in management of an asset reconstruction company is a substantial change in its management or not, shall be final.

Explanation.—For the purposes of this section, the expression "substantial change in management" means the change in the management by way of transfer of shares or change affecting the sponsorship in the company by way of transfer of shares or amalgamation or transfer of the business of the company.

It may be noted that-

Asset reconstruction means acquisition by any asset reconstruction company of any right or interest of any bank or financial institution in any financial assistance for the purpose of realisation of such financial assistance; [Section 2(1)(b)]

Asset reconstruction company means a company registered with Reserve Bank under section 3 for the purposes of carrying on the business of asset reconstruction or securitisation, or both; [Section 2(1)(ba)]

Bank means –

i) a banking company; or

ii) a corresponding new bank; or

iii) the State Bank of India; or

iv) a subsidiary bank; or

iva) a multi-State co-operative bank; or

v) such other bank which the Central Government may, by notification, specify for the purposes of this Act. [Section 2(1)(c)]

Securitisation means acquisition of financial assets by any asset reconstruction company from any originator, whether by raising of funds by such asset reconstruction company from qualified buyers by issue of security receipts representing undivided interest in such financial assets or otherwise; [Section 2(1)(z)]

In 2013, the government amended the Act to include co-operative banks formally under the definition of banks eligible to use it. However, petitions were filed questioning the authority of the notification and the power of Parliament to amend the SARFAESI Act.

The Supreme Court vide order dated 05th May, 2020 in the matter of ***'Pandurang Ganpati Chaugule vs. Vishwasrao Patil Murgud Sahakari Bank Limited'*** held that co-operative are banks under the State legislation and multi-State co-operative banks are 'banks' under section 2(1)(c) of SARFAESI Act,2002. The order also stated that it is permissible for the Parliament to enact the law to provide recovery procedures for bank dues that have been done by providing speedy recovery of secured interest without intervention of the court/ tribunal.

This move helps the co-operative banks to avoid inordinate delays in the recovery of their bad loans due to the involvement of civil courts and co-operative tribunals. The Indian banking system has 1,544 urban co-operative banks (UCBs) and 96,248 rural co-operative banks, with substantial deposits from retail investors. Considering their size, for the smooth functioning of these co-operative banks, speedy recovery of defaulting loans is critical.

Cancellation of certificate of registration

Section 4 provides for cancellation of certificate of registration. It states that Reserve Bank may cancel a certificate of registration granted to an asset reconstruction company, if such company—

a. ceases to carry on the business of securitisation or asset reconstruction; or

b. ceases to receive or hold any investment from a qualified buyer; or

c. has failed to comply with any conditions subject to which the certificate of registration has been granted to it; or

d. at any time fails to fulfil any of the conditions referred to in clauses (a) to (g) of sub-section (3) of section 3; or

e. fails to—

   i. comply with any direction issued by the Reserve Bank under the provisions of this Act; or

   ii. maintain accounts in accordance with the requirements of any law or any direction or order issued by the Reserve Bank under the provisions of this Act; or

   iii. submit or offer for inspection its books of account or other relevant documents when so demanded by the Reserve Bank; or

   iv. obtain prior approval of the Reserve Bank required under sub-section (6) of section 3:

Provided that before cancelling a certificate of registration on the ground that the asset reconstruction company has failed to comply with the provisions of clause (c) or has failed to fulfil any of the conditions referred to in clause (d) or sub-clause (iv) of clause (e), the Reserve Bank, unless it is of the opinion that the delay in cancelling the certificate of registration granted under sub-section (4) of section 3 shall be prejudicial to the public interest or the interests of the investors or the asset reconstruction company, shall give an opportunity to such company on such terms as the Reserve Bank may specify for taking necessary steps to comply with such provisions or fulfilment of such conditions.

Section 4(2) states that an asset reconstruction company aggrieved by the order of cancellation of certificate of registration may prefer an appeal, within a period of thirty days from the date on which such order of cancellation is communicated to it, to the Central Government:

Provided that before rejecting an appeal such company shall be given a reasonable opportunity of being heard.

Section 4(3) states an asset reconstruction company, which is holding investments of qualified buyers] and whose application for grant of certificate of registration has been rejected or certificate of registration has been cancelled shall, notwithstanding such rejection or cancellation be deemed to be an asset reconstruction company until it repays the entire investments held by it (together with interest, if any) within such period as the Reserve Bank may direct.

Acquisition of rights or interest in financial assets

Section 5 states that, notwithstanding anything contained in any agreement or any other law for the time being in force, any asset reconstruction company may acquire financial assets of any bank or financial institution—

(a) by issuing a debenture or bond or any other security in the nature of debenture, for consideration agreed upon between such company and the bank or financial institution, incorporating therein such terms and conditions as may be agreed upon between them; or

(b) by entering into an agreement with such bank or financial institution for the transfer of such financial assets to such company on such terms and conditions as may be agreed upon between them.

Any document executed by any bank or financial institution under sub-section (1) in favour of the asset reconstruction company acquiring financial assets for the purposes of asset reconstruction or securitisation shall be exempted from stamp duty in accordance with the provisions of section 8F of the Indian Stamp Act, 1899:

Provided that the provisions of this sub-section shall not apply where the acquisition of the financial assets by the asset reconstruction company is for the purposes other than asset reconstruction or securitisation.

If the bank or financial institution is a lender in relation to any financial assets acquired under sub-section (1) by the asset reconstruction company, such asset reconstruction company shall, on such acquisition, be deemed to be the lender and all the rights of such bank or financial institution shall vest in such company in relation to such financial assets.

If the bank or financial institution is holding any right, title or interest upon any tangible asset or intangible asset to secure payment of any unpaid portion of the purchase price of such asset or an obligation incurred or credit otherwise provided to enable the borrower to acquire the tangible asset or assignment or licence of intangible asset, such right, title or interest shall vest in the asset reconstruction company on acquisition of such assets under sub-section (1).

Unless otherwise expressly provided by this Act, all contracts, deeds, bonds, agreements, powers- of-attorney, grants of legal representation, permissions, approvals, consents or no-objections under any law or otherwise and other instruments of whatever nature which relate to the said financial asset and which are subsisting or having effect immediately before the acquisition of financial asset under sub-section (1) and to which the concerned bank or financial institution is a party or which are in favour of such bank or financial institution shall, after the acquisition of the financial assets, be of as full force and effect against or in favour of the asset reconstruction company, as the case may be, and may be enforced or acted upon as fully and effectually as if, in the place of the said bank or financial institution, asset reconstruction company, as the case may be, had been a party thereto or as if they had been issued in favour of asset reconstruction company, as the case may be.

If, on the date of acquisition of financial asset under sub-section (1), any suit, appeal or other proceeding of whatever nature relating to the said financial asset is pending by or against the bank or financial institution, save as provided in the third proviso to sub-section (1) of section 15 of the Sick Industrial Companies (Special Provisions) Act, 1985, the same shall not abate, or be discontinued or be, in any way, prejudicially affected by reason of the acquisition of financial asset by the asset reconstruction company, as the case may be, but the suit, appeal or other proceeding may be continued, prosecuted and enforced by or against the asset reconstruction company, as the case may be.

On acquisition of financial assets under sub-section (1), the asset reconstruction company, may with the consent of the originator, file an application before the Debts Recovery Tribunal or the Appellate Tribunal or any court or other Authority for the purpose of substitution of its name in any pending suit, appeal or other proceedings and on receipt of such application, such Debts Recovery Tribunal or the Appellate Tribunal or court or Authority shall pass orders for the substitution of the asset reconstruction company in such pending suit, appeal or other proceedings.

It may be noted that-

Financial asset means debt or receivables and includes—

i) a claim to any debt or receivables or part thereof, whether secured or unsecured; or

ii) any debt or receivables secured by, mortgage of, or charge on, immovable property; or

iii) a mortgage, charge, hypothecation or pledge of movable property; or

iv) any right or interest in the security, whether full or part underlying such debt or receivables; or

v) any beneficial interest in property, whether movable or immovable, or in such debt, receivables, whether such interest is existing, future, accruing, conditional or contingent; or

(va) any beneficial right, title or interest in any tangible asset given on hire or financial lease or conditional sale or under any other contract which secures the obligation to pay any unpaid portion of the purchase price of such asset or an obligation incurred or credit otherwise provided to enable the borrower to acquire such tangible asset; or

(vb) any right, title or interest on any intangible asset or licence or assignment of such intangible asset, which secures the obligation to pay any unpaid portion of the purchase price of such intangible asset or an obligation incurred or credit otherwise extended to enable the borrower to acquire such intangible asset or obtain licence of the intangible asset; or

vi) any financial assistance. [Section 2(1)(l)]

Financial institution means—

i) a public financial institution within the meaning of section 4A of the Companies Act, 1956;

ii) any institution specified by the Central Government under sub-clause (ii) of clause (h) of section 2 of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993;

iii) the International Finance Corporation established under the International Finance Corporation (Status, Immunities and Privileges) Act, 1958;

iiia) a debenture trustee registered with the Board and appointed for secured debt securities;

iiib) asset reconstruction company, whether acting as such or managing a trust created for the purpose of securitisation or asset reconstruction, as the case may be;

iv) any other institution or non-banking financial company as defined in clause (f) of section 45-I of the Reserve Bank of India Act, 1934 (2 of 1934), which the Central Government may, by notification, specify as financial institution for the purposes of this Act. [Section 2(1)(n)]

Transfer of pending applications to any one of Debts Recovery Tribunals in certain cases

Section 5A stipulates that if any financial asset, of a borrower acquired by an asset reconstruction company, comprise of secured debts of more than one bank or financial institution for recovery of which such banks or financial institutions has filed applications before two or more Debts Recovery Tribunals the asset reconstruction company may file an application to the Appellate Tribunal having jurisdiction over any of such Tribunals in which such applications are pending for transfer of all pending applications to any one of the Debts Recovery Tribunals as it deems fit.

On receipt of such application for transfer of all pending applications under sub-section (1), the Appellate Tribunal may, after giving the parties to the application an opportunity of being heard, pass an order for transfer of the pending applications to any one of the Debts Recovery Tribunals.

Notwithstanding anything contained in the Recovery of Debts Due to Banks and Financial Institutions Act, 1993, any order passed by the Appellate Tribunal under sub-section (2) shall be binding on all the Debts Recovery

Tribunals referred to in sub-section (1) as if such order had been passed by the Appellate Tribunal having jurisdiction on each such Debts Recovery Tribunal.

Any recovery certificate, issued by the Debts Recovery Tribunal to which all the pending applications are transferred under sub-section (2), shall be executed in accordance with the provisions contained in sub-section (23) of section 19 and other provisions of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 shall, accordingly, apply to such execution.

It may be noted that-

Debt shall have the meaning assigned to it in clause (g) of section 2 of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (51 of 1993) and includes –

(a) unpaid portion of the purchase price of any tangible asset given on hire or financial lease or conditional sale or under any other contract;

(b) any right, title or interest on any intangible asset or licence or assignment of such intangible asset, which secures the obligation to pay any unpaid portion of the purchase price of such intangible asset or an obligation incurred or credit otherwise extended to enable any borrower to acquire the intangible asset or obtain licence of such asset; [Section 2(1)(ha)]

Debts Recovery Tribunal means the Tribunal established under sub-section (1) of section 3 of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993; name changed Recovery of Debts and Bankruptcy Act, 1993 [Section 2(1)(i)]

Notice to obligor and discharge of obligation of such obligor

Section 6 of this Act states that the bank or financial institution may, if it considers appropriate, give a notice of acquisition of financial assets by any asset reconstruction company, to the concerned obligor and any other concerned person and to the concerned registering authority including Registrar of Companies in whose jurisdiction the mortgage, charge, hypothecation, assignment or other interest created on the financial assets had been registered.

Where a notice of acquisition of financial asset under sub-section (1) is given by a bank or financial institution, the obligor, on receipt of such notice, shall make payment to the concerned asset reconstruction company, as the case may be, and payment made to such company in discharge of any of the obligations in relation to the financial asset specified in the notice shall be a full discharge to the obligor making the payment from all liability in respect of such payment.

Where no notice of acquisition of financial asset under sub-section (1) is given by any bank or financial institution, any money or other properties subsequently received by the bank or financial institution, shall constitute monies or properties held in trust for the benefit of and on behalf of the asset reconstruction company, as the case may be, and such bank or financial institution shall hold such payment or property which shall forthwith be made over or delivered to asset reconstruction company, as the case may be, or its agent duly authorised in this behalf.

Issue of security by raising of receipts or funds by asset reconstruction company

Without prejudice to the provisions contained in the Companies Act, the Securities Contracts (Regulation) Act, 1956 and the Securities and Exchange Board of India Act, 1992, any asset reconstruction company, may, after acquisition of any financial asset under sub- section (1) of section 5, offer security receipts to qualified institute buyers or such other category of investors including non-institutional investors as may be specified by the Reserve Bank in consultation with the Board, from time to time, for subscription in accordance with the provisions of those Acts.

A asset reconstruction company may raise funds from the qualified buyers by formulating schemes for acquiring financial assets and shall keep and maintain separate and distinct accounts in respect of each such scheme for every financial asset acquired out of investments made by a qualified buyer and ensure that realisations of such financial asset is held and applied towards redemption of investments and payment of returns assured on such investments under the relevant scheme.

The scheme for the purpose of offering security receipts under sub-section (1) or raising funds under sub-section (2), may be in the nature of a trust to be managed by the asset reconstruction company, and the asset reconstruction company shall hold the assets so acquired or the funds so raised for acquiring the assets, in trust for the benefit of the qualified buyers holding the security receipts or from whom the funds are raised.

The provisions of the Indian Trusts Act, 1882 shall, except in so far as they are inconsistent with the provisions of this Act, apply with respect to the trust referred to in clause (a) above.

In the event of non-realisation under sub-section (2) of financial assets, the qualified buyers of an asset reconstruction company, holding security receipts of not less than seventy-five percent of the total value of the security receipts issued under a scheme by such company, shall be entitled to call a meeting of all the qualified buyers and every resolution passed in such meeting shall be binding on the company.

The qualified buyers shall, at a meeting called under sub-section (3), follow the same procedure, as nearly as possible as is followed at meetings of the board of directors of the asset reconstruction company, as the case may be.

It may be noted that-

Qualified buyer means a financial institution, insurance company, bank, state financial corporation, state industrial development corporation, trustee or asset reconstruction company which has been granted a certificate of registration under sub-section (4) of section 3 or any asset management company making investment on behalf of mutual fund or a foreign institutional investor registered under the Securities and Exchange Board of India Act, 1992 or regulations made thereunder, any category of non-institutional investors as may be specified by the Reserve Bank under sub-section (1) of section 7 or any other body corporate as may be specified by the Board. [Section 2(1)(u)]

How will an asset reconstruction company raise fund from qualified buyers?

As per Section 7(2) of SARFAESI Act, an asset reconstruction company may raise funds from the qualified buyers by formulating schemes for acquiring financial assets and shall keep and maintain separate and distinct accounts in respect of each such scheme for every financial asset acquired out of investments made by a qualified buyer and ensure that realisations of such financial asset is held and applied towards redemption of investments and payment of returns assured on such investments under the relevant scheme.

Exemption from registration of security receipt

Section 8 of the Act contains exemption from registration of security receipt. Notwithstanding anything contained in sub-section (1) of section 17 of the Registration Act, 1908,**—**

(a) any security receipt issued by the asset reconstruction company, as the case may be, under sub-section (1) of section 7, and not creating, declaring, assigning, limiting or extinguishing any right, title or interest, to or in immovable property except in so far as it entitles the holder of the security receipt to an undivided interest afforded by a registered instrument; or

(b) any transfer of security receipts, shall not require compulsory registration.

It may be noted that –

Security receipt means a receipt or other security, issued by a asset reconstruction company to any qualified buyer pursuant to a scheme, evidencing the purchase or acquisition by the holder thereof, of an undivided right, title or interest in the financial asset involved in securitisation; [Section 2(1)(zg)]

Measures for assets reconstruction

Without prejudice to the provisions contained in any other law for the time being in force, an asset reconstruction company may, for the purposes of asset reconstruction, provide for any one or more of the following measures, namely:—

(a) the proper management of the business of the borrower, by change in, or take over of, the management of the business of the borrower;

(b) the sale or lease of a part or whole of the business of the borrower;

(c) rescheduling of payment of debts payable by the borrower;

(d) enforcement of security interest in accordance with the provisions of this Act;

(e) settlement of dues payable by the borrower;

(f) taking possession of secured assets in accordance with the provisions of this Act;

(g) conversion of any portion of debt into shares of a borrower company:

Provided that conversion of any part of debt into shares of a borrower company shall be deemed always to have been valid, as if the provisions of this clause were in force at all material times.

The Reserve Bank shall, for the purposes of sub-section (1), determine the policy and issue necessary directions including the direction for regulation of management of the business of the borrower and fees to be charged.

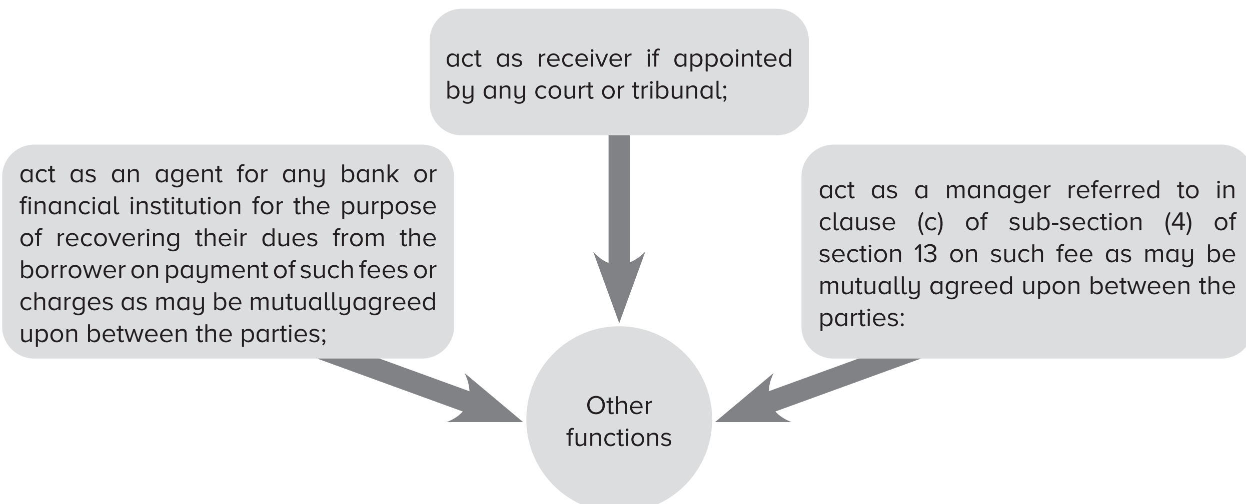
The asset reconstruction company shall take measures under sub-section (1) in accordance with policies and directions of the Reserve Bank determined under sub-section (2).

It may be noted that –

Borrower means any person who has been granted financial assistance by any bank or financial institution or who has given any guarantee or created any mortgage or pledge as security for the financial assistance granted by any bank or financial institution and includes a person who becomes borrower of an asset reconstruction company consequent upon acquisition by it of any rights or interest of any bank or financial institution in relation to such financial assistance or who has raised funds through issue of debt securities. [Section 2(1)(f)]

Other functions of asset reconstruction company

Section 10 of the acts states that, any asset reconstruction company registered under section 3 may—



Provided that no asset reconstruction company shall act as a manager if acting as such gives rise to any pecuniary liability.

Save as otherwise provided in sub-section (1), no asset reconstruction company which has been granted a certificate of registration under sub-section (4) of section 3, shall commence or carry on, without prior approval of the Reserve Bank, any business other than that of securitisation or asset reconstruction:

Provided that an asset reconstruction company which is carrying on, on or before the commencement of this Act, any business other than the business of securitisation or asset reconstruction or business referred to in sub-section (1), shall cease to carry on any such business within one year from the date of commencement of this Act.

Explanation.—For the purposes of this section, "asset reconstruction company'' or "asset reconstruction company'' does not include its subsidiary.

How are disputes relating to securitisation or reconstruction resolved?

According to Section 11 of SARFAESI Act, where any dispute relating to securitisation or reconstruction or non- payment of any amount due including interest arises amongst any of the parties, namely, the bank, or financial institution, or asset reconstruction company or qualified buyer, such dispute shall be settled by conciliation or arbitration as provided in the Arbitration and Conciliation Act, 1996, as if the parties to the dispute have consented in writing for determination of such dispute by conciliation or arbitration and the provisions of that Act shall apply accordingly.

Power of Reserve Bank to determine policy and issue directions

Under Section 12 of the Act, if the Reserve Bank is satisfied that in the public interest or to regulate financial system of the country to its advantage or to prevent the affairs of any asset reconstruction company from being conducted in a manner detrimental to the interest of investors or in any manner prejudicial to the interest of such asset reconstruction company, it is necessary or expedient so to do, it may determine the policy and give directions to all or any asset reconstruction company in matters relating to income recognition, accounting standards, making provisions for bad and doubtful debts, capital adequacy based on risk weights for assets and also relating to deployment of funds by the asset reconstruction company, as the case may be, and such company shall be bound to follow the policy so determined and the directions so issued.

Without prejudice to the generality of the power vested under sub-section (1), the Reserve Bank may give directions to any asset reconstruction company generally or to a class of asset reconstruction companies or to any asset reconstruction company in particular as to—

(a) the type of financial asset of a bank or financial institution which can be acquired and procedure for acquisition of such assets and valuation thereof;

(b) the aggregate value of financial assets which may be acquired by any asset reconstruction company;

(c) the fee and other charges which may be charged or incurred for management of financial assets acquired by any asset reconstruction company;

(d) transfer of security receipts issued to qualified buyers.

Power of Reserve Bank to call for statements and information

The Reserve Bank may at any time direct an asset reconstruction company to furnish it within such time as may be specified by the Reserve Bank, with such statements and information relating to the business or affairs of such asset reconstruction company (including any business or affairs with which such company is concerned) as the Reserve Bank may consider necessary or expedient to obtain for the purposes of this Act.

Power of Reserve Bank to carry out audit and inspection

The Reserve Bank may, for the purposes of this Act, carry out or caused to be carried out audit and inspection of an asset reconstruction company from time to time.

It shall be the duty of an asset reconstruction company and its officers to provide assistance and cooperation to the Reserve Bank to carry out audit or inspection under sub-section (1).

Where on audit or inspection or otherwise, the Reserve Bank is satisfied that business of an asset reconstruction company is being conducted in a manner detrimental to public interest or to the interests of investors in security receipts issued by such asset reconstruction company, the Reserve Bank may, for securing proper management of an asset reconstruction company, by an order—

(a) remove the Chairman or any director or appoint additional directors on the board of directors of the asset reconstruction company; or

(b) appoint any of its officers as an observer to observe the working of the board of directors of such asset reconstruction company:

Provided that no order for removal of Chairman or director under clause (a) shall be made except after giving him an opportunity of being heard.

It shall be the duty of every director or other officer or employee of the asset reconstruction company to produce before the person, conducting an audit or inspection under sub-section (1), all such books, accounts and other documents in his custody or control and to provide him such statements and information relating to the affairs of the asset reconstruction company as may be required by such person within the stipulated time specified by him.

ENFORCEMENT OF SECURITY INTEREST

Enforcement of security interest

According to Section 13, notwithstanding anything contained in section 69 or section 69A of the Transfer of Property Act, 1882, any security interest created in favour of any secured creditor may be enforced, without the intervention of the court or tribunal, by such creditor in accordance with the provisions of this Act.

Sub-clause 2 states that, where any borrower, who is under a liability to a secured creditor under a security agreement, makes any default in repayment of secured debt or any instalment thereof, and his account in respect of such debt is classified by the secured creditor as non-performing asset, then, the secured creditor may require the borrower by notice in writing to discharge in full his liabilities to the secured creditor within sixty days from the date of notice failing which the secured creditor shall be entitled to exercise all or any of the rights under sub-section (4).

Provided that—

(i) the requirement of classification of secured debt as non-performing asset under this sub-section shall not apply to a borrower who has raised funds through issue of debt securities; and

(ii) in the event of default, the debenture trustee shall be entitled to enforce security interest in the same manner as provided under this section with such modifications as may be necessary and in accordance with the terms and conditions of security documents executed in favour of the debenture trustee.

Sub-clause 3 states that, the notice referred to in sub-section (*2*) shall give details of the amount payable by the borrower and the secured assets intended to be enforced by the secured creditor in the event of non-payment of secured debts by the borrower.

Sub-clause 3A states that , if, on receipt of the notice under sub-section (*2*), the borrower makes any representation or raises any objection, the secured creditor shall consider such representation or objection and if the secured creditor comes to the conclusion that such representation or objection is not acceptable or tenable, he shall communicate within fifteen days of receipt of such representation or objection the reasons for non- acceptance of the representation or objection to the borrower:

Provided that the reasons so communicated or the likely action of the secured creditor at the stage of communication of reasons shall not confer any right upon the borrower to prefer an application to the Debts Recovery Tribunal under section 17 or the Court of District Judge under section 17A.

Sub-clause 4 states that, in case the borrower fails to discharge his liability in full within the period specified in sub-section (2), the secured creditor may take recourse to one or more of the following measures to recover his secured debt, namely:—

a. take possession of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realising the secured asset;

b. take over the management of the business of the borrower including the right to transfer by way of lease, assignment or sale for realising the secured asset:

   Provided that the right to transfer by way of lease, assignment or sale shall be exercised only where the substantial part of the business of the borrower is held as security for the debt:

   Provided further that where the management of whole of the business or part of the business is severable, the secured creditor shall take over the management of such business of the borrower which is relatable to the security for the debt;

c. appoint any person (hereafter referred to as the manager), to manage the secured assets the possession of which has been taken over by the secured creditor;

d. require at any time by notice in writing, any person who has acquired any of the secured assets from the borrower and from whom any money is due or may become due to the borrower, to pay the secured creditor, so much of the money as is sufficient to pay the secured debt.

Sub-clause 5 states that, any payment made by any person referred to in clause (d) of sub-section (4) to the secured creditor shall give such person a valid discharge as if he has made payment to the borrower.

Sub-clause 5A states that, where the sale of an immovable property, for which a reserve price has been specified, has been postponed for want of a bid of an amount not less than such reserve price, it shall be lawful for any officer of the secured creditor, if so authorised by the secured creditor in this behalf, to bid for the immovable property on behalf of the secured creditor at any subsequent sale.

Sub-clause 5B states that, where the secured creditor, referred to in sub-section (5A), is declared to be the purchaser of the immovable property at any subsequent sale, the amount of the purchase price shall be adjusted towards the amount of the claim of the secured creditor for which the auction of enforcement of security interest is taken by the secured creditor, under sub-section (4) of section 13.

Sub-clause 5C states that, the provisions of section 9 of the Banking Regulation Act, 1949 shall, as far as may be, apply to the immovable property acquired by secured creditor under sub-section (5A).

Sub-clause 6 states that, any transfer of secured asset after taking possession thereof or take over of management under sub-section (*4*), by the secured creditor or by the manager on behalf of the secured creditor shall vest in the transferee all rights in, or in relation to, the secured asset transferred as if the transfer had been made by the owner of such secured asset.

Under section 13(7), where any action has been taken against a borrower under the provisions of sub-section (4), all costs, charges and expenses which, in the opinion of the secured creditor, have been properly incurred by him or any expenses incidental thereto, shall be recoverable from the borrower and the money which is received by the secured creditor shall, in the absence of any contract to the contrary, be held by him in trust, to be applied, firstly, in payment of such costs, charges and expenses and secondly, in discharge of the dues of the secured creditor and the residue of the money so received shall be paid to the person entitled thereto in accordance with his rights and interests.

Under section 13(8), where the amount of dues of the secured creditor together with all costs, charges and expenses incurred by him is tendered to the secured creditor at any time before the date of publication of notice for public auction or inviting quotations or tender from public or private treaty for transfer by way of lease, assignment or sale of the secured assets,—

i. the secured assets shall not be transferred by way of lease assignment or sale by the secured creditor; and

ii. in case, any step has been taken by the secured creditor for transfer by way of lease or assignment or sale of the assets before tendering of such amount under this sub-section, no further step shall be taken by such secured creditor for transfer by way of lease or assignment or sale of such secured assets.

Under section 13(9), subject to the provisions of the Insolvency and Bankruptcy Code, 2016, in the case of financing of a financial asset by more than one secured creditors or joint financing of a financial asset by secured creditors, no secured creditor shall be entitled to exercise any or all of the rights conferred on him under or pursuant to sub-section (*4*) unless exercise of such right is agreed upon by the secured creditors representing not less than sixty per cent in value of the amount outstanding as on a record date and such action shall be binding on all the secured creditors:

Provided that in the case of a company in liquidation, the amount realised from the sale of secured assets shall be distributed in accordance with the provisions of section 529A of the Companies Act, 1956:

Provided further that in the case of a company being wound up on or after the commencement of this Act, the secured creditor of such company, who opts to realise his security instead of relinquishing his security and proving his debt under proviso to sub-section (*1*) of section 529 of the Companies Act, 1956, may retain the sale proceeds of his secured assets after depositing the workmen's dues with the liquidator in accordance with the provisions of section 529A of that Act:

Provided also that liquidator referred to in the second proviso shall intimate the secured creditor the workmen's dues in accordance with the provisions of section 529A of the Companies Act, 1956 and in case such workmen's dues cannot be ascertained, the liquidator shall intimate the estimated amount of workmen's dues under that section to the secured creditor and in such case the secured creditor may retain the sale proceeds of the secured assets after depositing the amount of such estimate dues with the liquidator:

Provided also that in case the secured creditor deposits the estimated amount of workmen's dues, such creditor shall be liable to pay the balance of the workmen's dues or entitled to receive the excess amount, if any, deposited by the secured creditor with the liquidator:

Provided also that the secured creditor shall furnish an undertaking to the liquidator to pay the balance of the workmen's dues, if any.

Explanation.**—**For the purposes of this sub-section,**—**

a. "record date" means the date agreed upon by the secured creditors representing not less than sixty per cent in value of the amount outstanding on such date;

b. "amount outstanding" shall include principal, interest and any other dues payable by the borrower to the secured creditor in respect of secured asset as per the books of account of the secured creditor.

Sub-clause 10 states that, where dues of the secured creditor are not fully satisfied with the sale proceeds of the secured assets, the secured creditor may file an application in the form and manner as may be prescribed to the Debts Recovery Tribunal having jurisdiction or a competent court, as the case may be, for recovery of the balance amount from the borrower.

Sub-clause 11 states that, without prejudice to the rights conferred on the secured creditor under or by this section, secured creditor shall be entitled to proceed against the guarantors or sell the pledged assets without first taking any of the measured specifies in clauses (a) to (d) of sub-section (4) in relation to the secured assets under this Act.

The rights of a secured creditor under this Act may be exercised by one or more of his officers authorised in this behalf in such manner as may be prescribed.

No borrower shall, after receipt of notice referred to in sub-section (2), transfer by way of sale, lease or otherwise (other than in the ordinary course of his business) any of his secured assets referred to in the notice, without prior written consent of the secured creditor.

It may be noted that-

Default means –

(i) non-payment of any debt or any other amount payable by the borrower to any secured creditor consequent upon which the account of such borrower is classified as non-performing asset in the books of account of the secured creditor; or

(ii) non-payment of any debt or any other amount payable by the borrower with respect to debt securities after notice of ninety days demanding payment of dues served upon such borrower by the debenture trustee or any other authority in whose favour security interest is created for the benefit of holders of such debt securities; [Section 2(1)(j)]

Security interest means right, title or interest of any kind, other than those specified in section 31, upon property created in favour of any secured creditor and includes—

(i) any mortgage, charge, hypothecation, assignment or any right, title or interest of any kind, on tangible asset, retained by the secured creditor as an owner of the property, given on hire or financial lease or conditional sale or under any other contract which secures the obligation to pay any unpaid portion of the purchase price of the asset or an obligation incurred or credit provided to enable the borrower to acquire the tangible asset; or

(ii) such right, title or interest in any intangible asset or assignment or licence of such intangible asset which secures the obligation to pay any unpaid portion of the purchase price of the intangible asset or the obligation incurred or any credit provided to enable the borrower to acquire the intangible asset or licence of intangible asset. [Section 2(1)(zf)]

Chief Metropolitan Magistrate or District Magistrate to assist secured creditor in taking possession of secured asset

Where the possession of any secured assets is required to be taken by the secured creditor or if any of the secured assets is required to be sold or transferred by the secured creditor under the provisions of this Act, the secured creditor may, for the purpose of taking possession or control of any such secured assets, request, in writing, the Chief Metropolitan Magistrate or the District Magistrate within whose jurisdiction any such secured asset or other documents relating thereto may be situated or found, to take possession thereof, and the Chief Metropolitan Magistrate or as the case may be, the District Magistrate shall, on such request being made to him**—**

(a) take possession of such asset and documents relating thereto; and

(b) forward such asset and documents to the secured creditor:

Provided that any application by the secured creditor shall be accompanied by an affidavit duly affirmed by the authorised officer of the secured creditor, declaring that—

i. the aggregate amount of financial assistance granted and the total claim of the Bank as on the date of filing the application;

ii. the borrower has created security interest over various properties and that the Bank or Financial Institution is holding a valid and subsisting security interest over such properties and the claim of the Bank or Financial Institution is within the limitation period;

iii. the borrower has created security interest over various properties giving the details of properties referred to in sub-clause (ii) above;

iv. the borrower has committed default in repayment of the financial assistance granted aggregating the specified amount;

v. consequent upon such default in repayment of the financial assistance the account of the borrower has been classified as a non-performing asset;

vi. affirming that the period of sixty days notice as required by the provisions of sub-section (2) of section 13, demanding payment of the defaulted financial assistance has been served on the borrower;

vii. the objection or representation in reply to the notice received from the borrower has been considered by the secured creditor and reasons for non-acceptance of such objection or representation had been communicated to the borrower;

viii. the borrower has not made any repayment of the financial assistance in spite of the above notice and the Authorised Officer is, therefore, entitled to take possession of the secured assets under the provisions of sub-section (4) of section 13 read with section 14 of the principal Act;

ix. that the provisions of this Act and the rules made thereunder had been complied with:

Provided further that on receipt of the affidavit from the Authorised Officer, the District Magistrate or the Chief Metropolitan Magistrate, as the case may be, shall after satisfying the contents of the affidavit pass suitable orders for the purpose of taking possession of the secured assets within a period of thirty days from the date of application:

Provided also that if no order is passed by the Chief Metropolitan Magistrate or District Magistrate within the said period of thirty days for reasons beyond his control, he may, after recording reasons in writing for the same, pass the order within such further period but not exceeding in aggregate sixty days.

Provided also that the requirement of filing affidavit stated in the first proviso shall not apply to proceeding pending before any District Magistrate or the Chief Metropolitan Magistrate, as the case may be, on the date of commencement of this Act.

The District Magistrate or the Chief Metropolitan Magistrate may authorise any officer subordinate to him,—

a) to take possession of such assets and documents relating thereto; and

b) to forward such assets and documents to the secured creditor.

For the purpose of securing compliance with the provisions of sub-section (1), the Chief Metropolitan Magistrate or the District Magistrate may take or cause to be taken such steps and use, or cause to be used, such force, as may, in his opinion, be necessary.

No act of the Chief Metropolitan Magistrate or the District Magistrate any officer authorised by the Chief Metropolitan Magistrate or District Magistrate done in pursuance of this section shall be called in question in any court or before any authority.

It may be noted that-

Financial assistance means any loan or advance granted or any debentures or bonds subscribed or any guarantees given or letters of credit established or any other credit facility extended by any bank or financial institution including funds provided for the purpose of acquisition of any tangible asset on hire or financial lease or conditional sale or under any other contract or obtaining assignment or licence of any intangible asset or purchase of debt securities. [Section 2(1)(k)]

Financial lease means a lease under any lease agreement of tangible asset, other than negotiable instrument or negotiable document, for transfer of lessor's right therein to the lessee for a certain time in consideration of payment of agreed amount periodically and where the lessee becomes the owner of the such assets at the expiry of the term of lease or on payment of the agreed residual amount, as the case may be. [Section 2(1)(ma)]

Secured creditor means—

(i) any bank or financial institution or any consortium or group of banks or financial institutions holding any right, title or interest upon any tangible asset or intangible asset as specified in clause (*l*);

(ii) debenture trustee appointed by any bank or financial institution; or

(iii) an asset reconstruction company whether acting as such or managing a trust set up by such asset reconstruction company for the securitisation or reconstruction, as the case may be; or

(iv) debenture trustee registered with the Board and appointed for secured debt securities; or

(v) any other trustee holding securities on behalf of a bank or financial institution, in whose favour security interest is created by any borrower for due repayment of any financial assistance. [Section 2(1)(zd)]

Manner and effect of takeover of management

When the management of business of a borrower is taken over by an asset reconstruction company under clause (a) of section 9 or, as the case may be, by a secured creditor under clause (b) of sub-section (4) of section 13, the secured creditor may, by publishing a notice in a newspaper published in English language and in a newspaper published in an Indian language in circulation in the place where the principal office of the borrower is situated, appoint as many persons as it thinks fit—

a) in a case in which the borrower is a company as defined in the Companies Act, 1956, to be the directors of that borrower in accordance with the provisions of that Act; or

b) in any other case, to be the administrator of the business of the borrower.

On publication of a notice under sub-section (1),—

a) in any case where the borrower is a company as defined in the Companies Act, 1956, all persons holding office as directors of the company and in any other case, all persons holding any office having power of superintendence, direction and control of the business of the borrower immediately before the publication of the notice under sub-section (*1*), shall be deemed to have vacated their offices as such;

b) any contract of management between the borrower and any director or manager thereof holding office as such immediately before publication of the notice under sub-section (*1*), shall be deemed to be terminated;

c) the directors or the administrators appointed under this section shall take such steps as may be necessary to take into their custody or under their control all the property, effects and actionable claims to which the business of the borrower is, or appears to be, entitled and all the property and effects of the business of the borrower shall be deemed to be in the custody of the directors or administrators, as the case may be, as from the date of the publication of the notice;

d) the directors appointed under this section shall, for all purposes, be the directors of the company of the borrower and such directors or as the case may be, the administrators appointed under this section, shall alone be entitled to exercise all the powers of the directors or as the case may be, of the persons exercising powers of superintendence, direction and control, of the business of the borrower whether such powers are derived from the memorandum or articles of association of the company of the borrower or from any other source whatsoever.

Where the management of the business of a borrower, being a company as defined in the Companies Act, 1956 , is taken over by the secured creditor, then, notwithstanding anything contained in the said Act or in the memorandum or articles of association of such borrower,**—**

a) it shall not be lawful for the shareholders of such company or any other person to nominate or appoint any person to be a director of the company;

b) no resolution passed at any meeting of the shareholders of such company shall be given effect to unless approved by the secured creditor;

c) no proceeding for the winding up of such company or for the appointment of a receiver in respect thereof shall lie in any court, except with the consent of the secured creditor.

Where the management of the business of a borrower had been taken over by the secured creditor, the secured creditor shall, on realisation of his debt in full, restore the management of the business of the borrower to him.

Provided that if any secured creditor jointly with other secured creditors or any asset reconstruction company or financial institution or any other assignee has converted part of its debt into shares of a borrower company and thereby acquired controlling interest in the borrower company, such secured creditors shall not be liable to restore the management of the business to such borrower. (Section 15)

No compensation to directors for loss of office

Notwithstanding anything to the contrary contained in any contract or in any other law for the time being in force, no managing director or any other director or a manager or any person in charge of management of the business of the borrower shall be entitled to any compensation for the loss of office or for the premature termination under this Act of any contract of management entered into by him with the borrower.

Nothing contained in sub-section (1) shall affect the right of any such managing director or any other director or manager or any such person in charge of management to recover from the business of the borrower, moneys recoverable otherwise than by way of such compensation.

Application against measures to recover secured debts

As per section 17(1), any person (including borrower), aggrieved by any of the measures referred to in sub-section (4) of section 13 taken by the secured creditor or his authorised officer under this Chapter, may make an application along with such fee, as may be prescribed, to the Debts Recovery Tribunal having jurisdiction in the matter within forty- five days from the date on which such measure had been taken:

Provided that different fees may be prescribed for making the application by the borrower and the person other than the borrower.

*Explanation.***—**For the removal of doubts, it is hereby declared that the communication of the reasons to the borrower by the secured creditor for not having accepted his representation or objection or the likely action of the secured creditor at the stage of communication of reasons to the borrower shall not entitle the person (including borrower) to make an application to the Debts Recovery Tribunal under this sub-section.

As per section 17(1A), an application under sub-section (1) shall be filed before the Debts Recovery Tribunal within the local limits of whose jurisdiction—

a) the cause of action, wholly or in part, arises;

b) where the secured asset is located; or

c) the branch or any other office of a bank or financial institution is maintaining an account in which debt claimed is outstanding for the time being.

As per section 17(2), the Debts Recovery Tribunal shall consider whether any of the measures referred to in sub-section (4) of section 13 taken by the secured creditor for enforcement of security are in accordance with the provisions of this Act and the rules made thereunder.

If, the Debts Recovery Tribunal, after examining the facts and circumstances of the case and evidence produced by the parties, comes to the conclusion that any of the measures referred to in sub-section (4) of section 13, taken by the secured creditor are not in accordance with the provisions of this Act and the rules made thereunder, and require restoration of the management or restoration of possession, of the secured assets to the borrower or other aggrieved person, it may, by order,—

a) declare the recourse to any one or more measures referred to in sub-section (4) of section 13 taken by the secured creditor as invalid; and

b) restore the possession of secured assets or management of secured assets to the borrower or such other aggrieved person, who has made an application under sub-section (1), as the case may be; and

c) pass such other direction as it may consider appropriate and necessary in relation to any of the recourse taken by the secured creditor under sub-section (4) of section 13.

As per section 17(4), if, the Debts Recovery Tribunal declares the recourse taken by a secured creditor under sub-section (4) of section 13, is in accordance with the provisions of this Act and the rules made thereunder, then, notwithstanding anything contained in any other law for the time being in force, the secured creditor shall be entitled to take recourse to one or more of the measures specified under sub-section (4) of section 13 to recover his secured debt.

Where –

i. any person, in an application under sub-section (1), claims any tenancy or leasehold rights upon the secured asset, the Debt Recovery Tribunal, after examining the facts of the case and evidence produced by the parties in relation to such claims shall, for the purposes of enforcement of security interest, have the jurisdiction to examine whether lease or tenancy,—

   a) has expired or stood determined; or

   b) is contrary to section 65A of the Transfer of Property Act, 1882; or

   c) is contrary to terms of mortgage; or

   d) is created after the issuance of notice of default and demand by the Bank under sub- section (2) of section 13 of the Act; and

ii. the Debt Recovery Tribunal is satisfied that tenancy right or leasehold rights claimed in secured asset falls under the sub-clause (a) or sub-clause (b) or sub-clause (c) or sub-clause (d) of clause (i), then notwithstanding anything to the contrary contained in any other law for the time being in force, the Debt Recovery Tribunal may pass such order as it deems fit in accordance with the provisions of this Act.

As per section 17(5), any application made under sub-section (1) shall be dealt with by the Debts Recovery Tribunal as expeditiously as possible and disposed of within sixty days from the date of such application:

Provided that the Debts Recovery Tribunal may, from time to time, extend the said period for reasons to be recorded in writing, so, however, that the total period of pendency of the application with the Debts Recovery Tribunal, shall not exceed four months from the date of making of such application made under sub-section (1).

If the application is not disposed of by the Debts Recovery Tribunal within the period of four months as specified in sub-section (5), any part to the application may make an application, in such form as may be prescribed, to the Appellate Tribunal for directing the Debts Recovery Tribunal for expeditious disposal of the application pending before the Debts Recovery Tribunal and the Appellate Tribunal may, on such application, make an order for expeditious disposal of the pending application by the Debts Recovery Tribunal.

Save as otherwise provided in this Act, the Debts Recovery Tribunal shall, as far as may be, dispose of the application in accordance with the provisions of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (51 of 1993) and the rules made there under.

Appeal to Appellate Tribunal

Section 18 provides for Appeal to Appellate Tribunal. It states that any person aggrieved, by any order made by the Debts Recovery Tribunal under section 17, may prefer an appeal along with such fee, as may be prescribed to the Appellate Tribunal within thirty days from the date of receipt of the order of Debts Recovery Tribunal.

Provided that different fees may be prescribed for filing an appeal by the borrower or by the person other than the borrower:

Provided further that no appeal shall be entertained unless the borrower has deposited with the Appellate Tribunal fifty percent of the amount of debt due from him, as claimed by the secured creditors or determined by the Debts Recovery Tribunal, whichever is less:

Provided also that the Appellate Tribunal may, for the reasons to be recorded in writing, reduce the amount to not less than twenty-five percent of debt referred to in the second proviso.

Save as otherwise provided in this Act, the Appellate Tribunal shall, as far as may be, dispose of the appeal in accordance with the provisions of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 and rules made thereunder.

Validation of fees levied

Any fee levied and collected for preferring, before the commencement of the Enforcement of Security Interest and Recovery of Debts Laws (Amendment) Act, 2004, an appeal to the Debts Recovery Tribunal or the Appellate Tribunal under this Act, shall be deemed always to have been levied and collected in accordance with law as if the amendments made to sections 17 and 18 of this Act by sections 10 and 12 of the said Act were in force at all material times.

Right to lodge a caveat

Section 18C states that where an application or an appeal is expected to be made or has been made under sub-section (1) of section 17 or section 17A or sub-section (1) of section 18 or section 18B, the secured creditor or any person claiming a right to appear before the Tribunal or the Court of District Judge or the Appellate Tribunal or the High Court, as the case may be, on the hearing of such application or appeal, may lodge a caveat in respect thereof.

Where a caveat has been lodged under sub-section (1),—

(a) the secured creditor by whom the caveat has been lodged (hereafter in this section referred to as the caveator) shall serve notice of the caveat by registered post, acknowledgement due, on the person by whom the application has been or is expected to be made under sub-section (1);

(b) any person by whom the caveat has been lodged (hereafter in this section referred to as the caveator) shall serve notice of the caveat by registered post, acknowledgement due, on the person by whom the application has been or is expected to be made under sub-section (1).

Where after a caveat has been lodged under sub-section (1), any application or appeal is filed before the Tribunal or the court of District Judge or the Appellate Tribunal or the High Court, as the case may be, the Tribunal or the District Judge or the Appellate Tribunal or the High Court, as the case may be, shall serve a notice of application or appeal filed by the applicant or the appellant on the caveator.

Where a notice of any caveat has been served on the applicant or the Appellant, he shall periodically furnish the caveator with a copy of the application or the appeal made by him and also with copies of any paper or document which has been or may be filed by him in support of the application or the appeal.

Where a caveat has been lodged under sub-section (1), such caveat shall not remain in force after the expiry of the period of ninety days from the date on which it was lodged unless the application or appeal referred to in sub-section (1) has been made before the expiry of the said period.

Right of borrower to receive compensation and costs in certain cases

If the Debts Recovery Tribunal or the Court of District Judge, on an application made under section 17 or section 17A or the Appellate Tribunal or the High Court on an appeal preferred under section 18 or section 18A, holds that the possession of secured assets by the secured creditor is not in accordance with the provisions of this Act and rules made thereunder and directs the secured creditors to return such secured assets to the concerned borrowers or any other aggrieved person, who has filed the application under section 17 or section 17A or appeal under section 18 or section 18A, as the case may be, the borrower or such other person shall be entitled to the payment of such compensation and costs as may be determined by such Tribunal or Court of District Judge or Appellate Tribunal or the High Court referred to in section 18B.

CENTRAL REGISTRY

Central Registry

Under section 20, the Central Government may, by notification, set up or cause to be set up from such date as it may specify in such notification, a registry to be known as the Central Registry with its own seal for the purposes of registration of transaction of securitisation and reconstruction of financial assets and creation of security interest under this Act.

The head office of the Central Registry shall be at such place as the Central Government may specify and for the purpose of facilitating registration of transactions referred to in sub-section (*1*), there may be established at such other places as the Central Government may think fit, branch offices of the Central Registry.

The Central Government may, by notification, define the territorial limits within which an office of the Central Registry may exercise its functions.

The provisions of this Act pertaining to the Central Registry shall be in addition to and not in derogation of any of the provisions contained in the Registration Act, 1908, the Companies Act, 1956, the Merchant Shipping Act, 1958, the Patents Act, 1970, the Motor Vehicles Act, 1988, and the Designs Act, 2000 or any other law requiring registration of charges and shall not affect the priority of charges or validity thereof under those Acts or laws.

Central Registrar

The Central Government may, by notification, appoint a person for the purpose of registration of transactions relating to securitisation, reconstruction of financial assets and security interest created over properties, to be known as the Central Registrar.

The Central Government may appoint such other officers with such designations as it thinks fit for the purpose of discharging, under the superintendence and direction of the Central Registrar, such functions of the Central Registrar under this Act as he may, from time to time, authorise them to discharge.

RECOVERY OF DEBTS DUE TO BANKS AND FINANCIAL INSTITUTIONS ACT, 1993

Establishment of Tribunal and Appellate Tribunal

Establishment of Tribunal

Section 3 provides for establishment of Tribunal. It states that, the Central Government shall, by notification, establish one or more Tribunals, to be known as the Debts Recovery Tribunal, to exercise the jurisdiction, powers and authority conferred on such Tribunal by or under this Act.

The Central Government shall by notification establish such number of Debts Recovery Tribunals and its benches as it may consider necessary, to exercise the jurisdiction, powers and authority of the Adjudicating Authority conferred on such Tribunal by or under the Insolvency and Bankruptcy Code, 2016.

The Central Government shall also specify, in the notification referred to in sub-section (1), the areas within which the Tribunal may exercise jurisdiction for entertaining and deciding the applications filed before it.

Composition of Tribunal

A Tribunal shall consist of one person only hereinafter referred to as the Presiding Officer to be appointed, by notification, by the Central Government.

Notwithstanding anything contained in sub-section (*1*), the Central Government may—

(a) authorise the Presiding Officer of any other Tribunal established under any other law for the time being in force to discharge the function of the Presiding Officer of a Debt Recovery Tribunal under this Act in addition to his being the Presiding Officer of that Tribunal; or

(b) authorise the judicial Member holding post as such in any other Tribunal, established under any other law for the time being in force, to discharge the functions of the Presiding Officer of Debts Recovery Tribunal under this Act, in addition to his being the judicial Member of that Tribunal.

JURISDICTION, POWERS AND AUTHORITY OF TRIBUNALS

Jurisdiction, powers and authority of Tribunals

According to Section 17, tribunal shall exercise, on and from the appointed day, the jurisdiction, powers and authority to entertain and decide applications from the banks and financial institutions for recovery of debts due to such banks and financial institutions.

Without prejudice to sub-section (*1*),—

(a) the Tribunal shall exercise, on and from the date to be appointed by the Central Government, the jurisdiction, powers and authority to entertain and decide applications under Part III of Insolvency and Bankruptcy Code, 2016 (31 of 2016).

(b) the Tribunal shall have circuit sittings in all district headquarters.

An Appellate Tribunal shall exercise, on and from the appointed day, the jurisdiction, powers and authority to entertain appeals against any order made, or deemed to have been made, by a Tribunal under this Act.

Without prejudice to sub-section (2), the Appellate Tribunal shall exercise, on and from the date to be appointed by the Central Government, the jurisdiction, powers and authority to entertain appeals against the order made by the Adjudicating Authority under Part III of the Insolvency and Bankruptcy Code, 2016.

PROCEDURE OF TRIBUNALS

Where a bank or a financial institution has to recover any debt from any person, it may make an application to the Tribunal within the local limits of whose jurisdiction—

(a) the branch or any other office of the bank or financial institution is maintaining an account in which debt claimed is outstanding, for the time being; or

(aa) the defendant, or each of the defendants where there are more than one, at the time of making the application, actually and voluntarily resides, or carries on business, or personally works for gain; or

(b) any of the defendants, where there are more than one, at the time of making the application, actually and voluntarily resides, or carries on business, or personally works for gain; or

(c) the cause of action, wholly or in part, arises:

Provided that the bank or financial institution may, with the permission of the Debts Recovery Tribunal, on an application made by it, withdraw the application, whether made before or after the Enforcement of Security Interest and Recovery of Debts Laws (Amendment) Act, 2004 (30 of 2004) for the purpose of taking action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, if no such action had been taken earlier under that Act:

Provided further that any application made under the first proviso for seeking permission from the Debts Recovery Tribunal to withdraw the application made under sub-section (*1*) shall be dealt with by it as expeditiously as possible and disposed of within thirty days from the date of such application:

Provided also that in case the Debts Recovery Tribunal refuses to grant permission for withdrawal of the application filed under this sub-section, it shall pass such orders after recording the reasons therefor.

Every bank being, multi-State co-operative bank referred to in sub-clause (vi) of clause (d) of section 2, may, at its option, opt to initiate proceedings under the Multi-State Co-operative Societies Act, 2002, to recover debts, whether due before or after the date of commencement of the Enforcement of the Security Interest and Recovery of Debts Laws (Amendment) Act, 2012, from any person instead of making an application under this Chapter.

In case, a bank being, multi-State co-operative bank referred to in sub-clause (vi) of clause (d) of section 2 has filed an application under this Chapter and subsequently opts to withdraw the application for the purpose of initiating proceeding under the Multi-State Co-operative Societies Act, 2002 to recover debts, it may do so with the permission of the Tribunal and every such application seeking permission from the Tribunal to withdraw the application made under sub-section (1A) shall be dealt with by it as expeditiously as possible and disposed of within thirty days from the date of such application:

Provided that in case the Tribunal refuses to grant permission for withdrawal of the application filed under this sub-section, it shall pass such orders after recording the reasons therefor.

Section 19(2) states that where a bank or a financial institution, which has to recover its debt from any person, has filed an application to the Tribunal under sub-section (1) and against the same person another bank or financial institution also has claim to recover its debt, then, the later bank or financial institution may join the applicant bank or financial institution at any stage of the proceedings, before the final order is passed, by making an application to that Tribunal.

Section 19(3) states that every application under sub-section (1) or sub-section (2) shall be in such form, and shall be accompanied with true copies of all documents relied on in support of the claim along with such fee, as may be prescribed:

Provided that the fee may be prescribed having regard to the amount of debt to be recovered:

Provided further that nothing contained in this sub-section relating to fee shall apply to cases transferred to the Tribunal under sub-section (1) of section 31.

Explanation.—For the purposes of this section, documents includes statement of account or any entry in banker's book duly certified under the Bankers' Books Evidence Act, 1891.

Section 19(3A) states that every applicant in the application filed under sub-section (1) or sub-section (*2*) for recovery of debt, shall—

(a) state particulars of the debt secured by security interest over properties or assets belonging to any of the defendants and the estimated value of such securities;

(b) if the estimated value of securities is not sufficient to satisfy the debt claimed, state particulars of any other properties or assets owned by any of the defendants, if any; and

(c) if the estimated value of such other assets is not sufficient to recover the debt, seek an order directing the defendant to disclose to the Tribunal particulars of other properties or assets owned by the defendants.

If any application filed before the Tribunal for recovery of any debt is settled prior to the commencement of the hearing before that Tribunal or at any stage of the proceedings before the final order is passed, the applicant may be granted refund to the fees paid by him at such rates as may be prescribed.

On receipt of application under sub-section (*1*) or sub-section (*2*), the Tribunal shall issue summons with following directions to the defendant—

(a) to show cause within thirty days of the service of summons as to why relief prayed for should not be granted;

(b) direct the defendant to disclose particulars of properties or assets other than properties and assets specified by the applicant under clauses (*a*) and (*b*) of sub-section (*3A*); and

(c) to restrain the defendant from dealing with or disposing of such assets and properties disclosed under clause (*c*) of sub-section (*3A*) pending the hearing and disposal of the application for attachment of properties.

Notwithstanding anything contained in section 65A of the Transfer of Property Act, 1882 (4 of 1882), the defendant, on service of summons, shall not transfer by way of sale, lease or otherwise except in the ordinary course of his business any of the assets over which security interest is created and other properties and assets specified or disclosed under sub-section (3A), without the prior approval of the Tribunal:

Provided that the Tribunal shall not grant such approval without giving notice to the applicant bank or financial institution to show cause as to why approval prayed for should not be granted:

Provided further that defendant shall be liable to account for the sale proceeds realised by sale of secured assets in the ordinary course of business and deposit such sale proceeds in the account maintained with the bank or financial institution holding security interest over such assets.

Section 19(5) states that,

(i) the defendant shall within a period of thirty days from the date of service of summons, present a written statement of his defence including claim for set-off under sub-section (*6*) or a counter-claim under sub-section (*8*), if any, and such written statement shall be accompanied with original documents or true copies thereof with the leave of the Tribunal, relied on by the defendant in his defence:

Provided that where the defendant fails to file the written statement within the said period of thirty days, the Presiding Officer may, in exceptional cases and in special circumstances to be recorded in writing, extend the said period by such further period not exceeding fifteen days to file the written statement of his defence;

(ii) where the defendant makes a disclosure of any property or asset pursuant to orders passed by the Tribunal, the provisions of sub-section (4A) of this section shall apply to such property or asset;

(iii) in case of non-compliance of any order made under clause (ii) of sub-section (4), the Presiding Officer may, by an order, direct that the person or officer who is in default, be detained in civil prison for a term not exceeding three months unless in the meantime the Presiding Officer directs his release:

Provided that the Presiding Officer shall not pass an order under this clause without giving an opportunity of being heard to such person or officer.

Explanation.—For the purpose of this section, the expression 'officer who is in default' shall mean such officer as defined in clause (60) of section 2 of the Companies Act, 2013.

On receipt of the written statement of defendant or on expiry of time granted by the Tribunal to file the written statement, the Tribunal shall fix a date of hearing for admission or denial of documents produced by the parties to the proceedings and also for continuation or vacation of the interim order passed under sub-section (4).

Where a defendant makes an admission of the full or part of the amount of debt due to a bank or financial institution, the Tribunal shall order such defendant to pay the amount, to the extent of the admission within a period of thirty days from the date of such order failing which the Tribunal may issue a certificate in accordance with the provisions of sub-section (22) to the extent of the amount of debt due admitted by the defendant.

Section 19(6) states that, where the defendant claims to set-off against the applicant's demand any ascertained sum of money legally recoverable by him from such applicant, the defendant may, at the first hearing of the application, but not afterwards unless permitted by the Tribunal, present a written statement containing the particulars of the debt the debt sought to be set-off along with original documents and other evidence relied on in support of claim of set-off in relation to any ascertained sum of money, against the applicant.

The written statement shall have the same effect as a plaint in a cross-suit so as to enable the Tribunal to pass a final order in respect both of the original claim and of the set-off.

Section 19(8) states that, a defendant in an application may, in addition to his right of pleading a set-off under sub-section (6), set up, by way of counter-claim against the claim of the applicant, any right or claim in respect of a cause of action accruing to the defendant against the applicant either before or after the filing of the application but before the defendant has delivered his defence or before the time limited for delivering his defence has expired, whether such counter-claim is in the nature of a claim for damages or not.

A counter-claim under sub-section (8) shall have the same effect as a cross-suit so as to enable the Tribunal to pass a final order on the same application, both on the original claim and on the counter-claim.

The applicant shall be at liberty to file a written statement in answer to the counter-claim of the defendant within such period as may be prescribed.

Every application under sub-section (3) or written statement of defendant under sub-section (5) or claim of set-off under sub-section (6) or a counter-claim under sub-section (8) by the defendant, or written statement by the applicant in reply to the counter-claim, under sub-section (10) or any other pleading whatsoever, shall be supported by an affidavit sworn in by the applicant or defendant.

Provided that if there is any evidence of witnesses to be led by any party, the affidavits of such witnesses shall be filed simultaneously by the party with the application or written statement or replies filed under sub-section (10A).

If any of the facts or pleadings in the application or written statement are not verified in the manner provided under sub-section (10A), a party to the proceedings shall not be allowed to rely on such facts or pleadings as evidence or any of the matters set out therein.

Where a defendant sets up a counter-claim in the written statement and in reply to such claim the applicant contends that the claim thereby raised ought not to be disposed of by way of counter-claim but in an independent action, the Tribunal shall decide such issue along with the claim of the applicant for recovery of the debt.

Where, at any stage of the proceedings, the Tribunal on an application made by the applicant along with particulars of property to be attached and estimated value thereof, or otherwise is satisfied, that the defendant, with intent to obstruct or delay or frustrate the execution of any order for the recovery of debt that may be passed against him,—

(i) is about to dispose of the whole or any part of his property; or

(ii) is about to remove the whole or any part of his property from the local limits of the jurisdiction of the Tribunal; or

(iii) is likely to cause any damage or mischief to the property or affect its value by misuse or creating third party interest,

the Tribunal may direct the defendant, within a time to be fixed by it, either to furnish security, in such sum as may be specified in the order, to produce and place at the disposal of the Tribunal, when required, the said property or the value of the same, or such portion thereof as may be sufficient to satisfy the certificate for the recovery of the debt, or to appear and show cause why he should not furnish security.

It also states that, where the defendant fails to show cause why he should not furnish security, or fails to furnish the security required, within the time fixed by the Tribunal, the Tribunal may order the attachment of the whole or such portion of the properties claimed by the applicant as the properties secured in his favour or otherwise owned by the defendant as appears sufficient to satisfy any certificate for the recovery of debt.

The Tribunal may also in the order direct the conditional attachment of the whole or any portion of the property specified under sub-section (13).

If an order of attachment is made without complying with the provisions of sub-section (13), such attachment shall be void.

In the case of disobedience of an order made by the Tribunal under sub-sections (12), (13) and (18) or breach of any of the terms on which the order was made, the Tribunal may order the properties of the person guilty of such disobedience or breach to be attached and may also order such person to be detained in the civil prison for a term not exceeding three months, unless in the meantime the Tribunal directs his release.

Where it appears to the Tribunal to be just and convenient, the Tribunal may, by order—

(a) appoint a receiver of any property, whether before or after grant of certificate for recovery of debt;

(b) remove any person from the possession or custody of the property;

(c) commit the same to the possession, custody or management of the receiver;

(d) confer upon the receiver all such powers, as to bringing and defending suits in the courts or filing and defending applications before the Tribunal and for the realisation, management, protection, preservation and improvement of the property, the collection of the rents and profits thereof, the application and disposal of such rents and profits, and the execution of documents as the owner himself has, or such of those powers as the Tribunal thinks fit; and

(e) appoint a Commissioner for preparation of an inventory of the properties of the defendant or for the sale thereof.

Where a certificate of recovery is issued against a company as defined under the Companies Act, 2013 and such company is under liquidation, the Tribunal may by an order direct that the sale proceeds of secured assets of such company be distributed in the same manner as provided in section 326 of the Companies Act, 2013 or under any other law for the time being in force.

The Tribunal may, after giving the applicant and the defendant, an opportunity of being heard, in respect of all claims, set-off or counter-claim, if any, and interest on such claims, within thirty days from the date of conclusion of the hearings, pass interim or final order as it deems fit which may include order for payment of interest from the date on which payment of the amount is found due up to the date of realisation or actual payment.

Where it is proved to the satisfaction of the Tribunal that the claim of the applicant has been adjusted wholly or in part by any lawful agreement or compromise in writing and signed by the parties or where the defendant has repaid or agreed to repay the claim of the applicant, the Tribunal shall pass orders recording such agreement, compromise or satisfaction of the claim.

While passing the final order under sub-section (20), the Tribunal shall clearly specify the assets of the borrower which security interest is created in favour of any bank or financial institution and direct the Recovery Officers to distribute the sale proceeds of such assets as provided in sub-section (20AB).

Notwithstanding anything to the contrary contained in any law for the time being in force, the proceeds from sale of secured assets shall be distributed in the following orders of priority, namely:—

(i) the costs incurred for preservation and protection of secured assets, the costs of valuation, public notice for possession and auction and other expenses for sale of assets shall be paid in full;

(ii) debts owed to the bank or financial institution.

Explanation.—For the purposes of this sub-section, it is hereby clarified that on or after the commencement of the Insolvency and Bankruptcy Code, 2016, in cases where insolvency and bankruptcy proceedings are pending in respect of secured assets of the borrower, the distribution of proceeds from the sale of secured assets shall be subject to the order of priority as provided in that Code.

As per sub-clause 21, the Tribunal shall send a copy of its final order and the recovery certificate, to the applicant and defendant. The applicant and the defendant may obtain copy of any order passed by the Tribunal on payment on such fee as may be prescribed.

The Presiding Officer shall issue a certificate of recovery along with the final order, under sub-section (20), for payment of debt with interest under his signature to the Recovery Officer for recovery of the amount of debt specified in the certificate.

Any recovery certificate issued by the Presiding Officer under sub-section (22) shall be deemed to be decree or order of the Court for the purposes of initiation of winding up proceedings against a company registered under the Companies Act, 2013 or Limited Liability Partnership registered under the Limited Liability Partnership Act, 2008 or insolvency proceedings against any individual or partnership firm under any law for the time being in force, as the case may be.

Where the Tribunal, which has issued a certificate of recovery, is satisfied that the property is situated within the local limits of the jurisdiction of two or more Tribunals, it may send the copies of the certificate of recovery for execution to such other Tribunals where the property is situated:

Provided that in a case where the Tribunal to which the certificate of recovery is sent for execution finds that it has no jurisdiction to comply with the certificate of recovery, it shall return the same to the Tribunal which has issued it.

The application made to the Tribunal under sub-section (*1*) or sub-section (*2*) shall be dealt with by it as expeditiously as possible and every effort shall be made by it to complete the proceedings in two hearings, and] to dispose of the application finally within one hundred and eighty days from the date of receipt of the application.

The Tribunal may made such orders and give such directions as may be necessary or expedient to give effect to its orders or to prevent abuse of its process or to secure the ends of justice.

Filing of recovery applications, documents and written statements in electronic form

Section 19A provides that notwithstanding anything to the contrary contained in this Act, and without prejudice to the provisions contained in section 6 of the Information Technology Act, 2000, the Central Government may by rules provide that from such date and before such Tribunal and Appellate Tribunal, as may be notified,—

(a) application or written statement or any other pleadings and the documents to be annexed thereto required to be filed shall be submitted in the electronic form and authenticated with digital signature of the applicant, defendant or any other petitioner in such form and manner as may be prescribed;

(b) any summons, notice or communication or intimation as may be required to be served or delivered under this Act, may be served or delivered by transmission of pleadings and documents by electronic form and authenticated in such manner as may be prescribed.

Any interim or final order passed by the Tribunal or Appellate Tribunal displayed on the website of such Tribunal or Appellate Tribunal shall be deemed to be a public notice of such order and transmission of such order by electronic mail to the registered address of the parties to the proceeding shall be deemed to be served on such party.

The Central Government may by rules provide that the electronic form for the purpose specified in this section shall be exclusive, or in the alternative or in addition to the physical form, therefor.

The Tribunal or the Appellate Tribunal notified under sub-section (1), for the purpose of adopting electronic filing, shall maintain its own website or common website with other Tribunals and Appellate Tribunal or such other universally accessible repositories of electronic information and ensure that all orders or directions issued by the Tribunal or Appellate Tribunal are displayed on the website of the Tribunal or Appellate Tribunal, in such manner as may be prescribed.

Explanation.—For the purpose of this section,—

a) 'digital signature' means the digital signature as defined under clause (p) of section 2 of the Information Technology Act, 2000;

b) 'electronic form' with reference to an information or a document means the electronic form as defined under clause (r) of section 2 of the Information Technology Act, 2000.

Under Section 19A, the application made to Tribunal for exercising the powers of the Adjudicating Authority under the Insolvency and Bankruptcy Code, 2016 shall be dealt with in the manner as provided under that Code.

Appeal to the Appellate Tribunal

Section 20 provides for appeal to Appellate Tribunal. It states that save as provided in sub-section (2), any person aggrieved by an order made, or deemed to have been made, by a Tribunal under this Act, may prefer an appeal to an Appellate Tribunal having jurisdiction in the matter.

No appeal shall lie to the Appellate Tribunal from an order made by a Tribunal with the consent of the parties.

Every appeal under sub-section (1) shall be filed within a period of thirty days from the date on which a copy of the order made, or deemed to have been made, by the Tribunal is received by him and it shall be in such form and be accompanied by such fee as may be prescribed:

Provided that the Appellate Tribunal may entertain an appeal after the expiry of the said period of thirty days if it is satisfied that there was sufficient cause for not filing it within that period.

On receipt of an appeal under sub-section (1), or under sub-section (1) of section 181 of the Insolvency and Bankruptcy Code, 2016, the Appellate Tribunal may, after giving the parties to the appeal, an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or setting aside the order appealed against.

The Appellate Tribunal shall send a copy of every order made by it to the parties to the appeal and to the concerned Tribunal.

The appeal filed before the Appellate Tribunal under sub-section (1) shall be dealt with by it as expeditiously as possible and endeavour shall be made by it to dispose of the appeal finally within six months from the date of receipt of the appeal.

Deposit of amount of debt due, on filing appeal

According to Section 21, where an appeal is preferred by any person from whom the amount of debt is due to a bank or a financial institution or a consortium of banks or financial institutions, such appeal shall not be entertained by the Appellate Tribunal unless such person has deposited with the Appellate Tribunal fifty percent of the amount of debt so due from him as determined by the Tribunal under section 19:

Provided that the Appellate Tribunal may, for reasons to be recorded in writing, reduce the amount to be deposited by such amount which shall not be less than twenty-five percent of the amount of such debt so due to be deposited under this section.

Procedure and powers of the Tribunal and the Appellate Tribunal

The Tribunal and the Appellate Tribunal shall not be bound the procedure laid down by the Code of Civil Procedure, 1908, but shall be guided by the principles of natural justice and, subject to the other provisions of this Act and of any rules, the Tribunal and the Appellate Tribunal shall have powers to regulate their own procedure including the places at which they shall have their sittings.

The Tribunal and the Appellate Tribunal shall have, for the purposes of discharging their functions under this Act, the same powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit, in respect of the following matters, namely:—

- summoning and enforcing the attendance of any person and examining him on oath;
- requiring the discovery and production of documents;
- receiving evidence on affidavits;
- issuing commissions for the examination of witnesses or documents;
- reviewing its decisions;
- dismissing an application for default or deciding it ex parte;
- setting aside any order of dismissal of any application for default or any order passed by it ex parte;
- any other matter which may be prescribed.

Any proceeding before the Tribunal or the Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purposes of section 196, of the Indian Penal and the Tribunal or the Appellate Tribunal shall be deemed to be a civil court for all the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973.

For the purpose of proof of any entry in the 'bankers' books', the provisions of the Bankers' Books Evidence Act, 1891 shall apply to all the proceedings before the Tribunal or Appellate Tribunal.

Uniform procedure for conduct of proceedings

According to Section 22A, The Central Government may, for the purpose of this Act, by rules, lay down uniform procedure consistent with the provisions of this Act for conducting the proceedings before the Tribunals and Appellate Tribunals.

Right to legal representation and Presenting Officers

Section 23 states that, a bank or a financial institution making an application to a Tribunal or an appeal to an Appellate Tribunal may authorise one or more legal practitioners or any of its officers to act as Presenting Officers and every person so authorised by it may present its case before the Tribunal or the Appellate Tribunal.

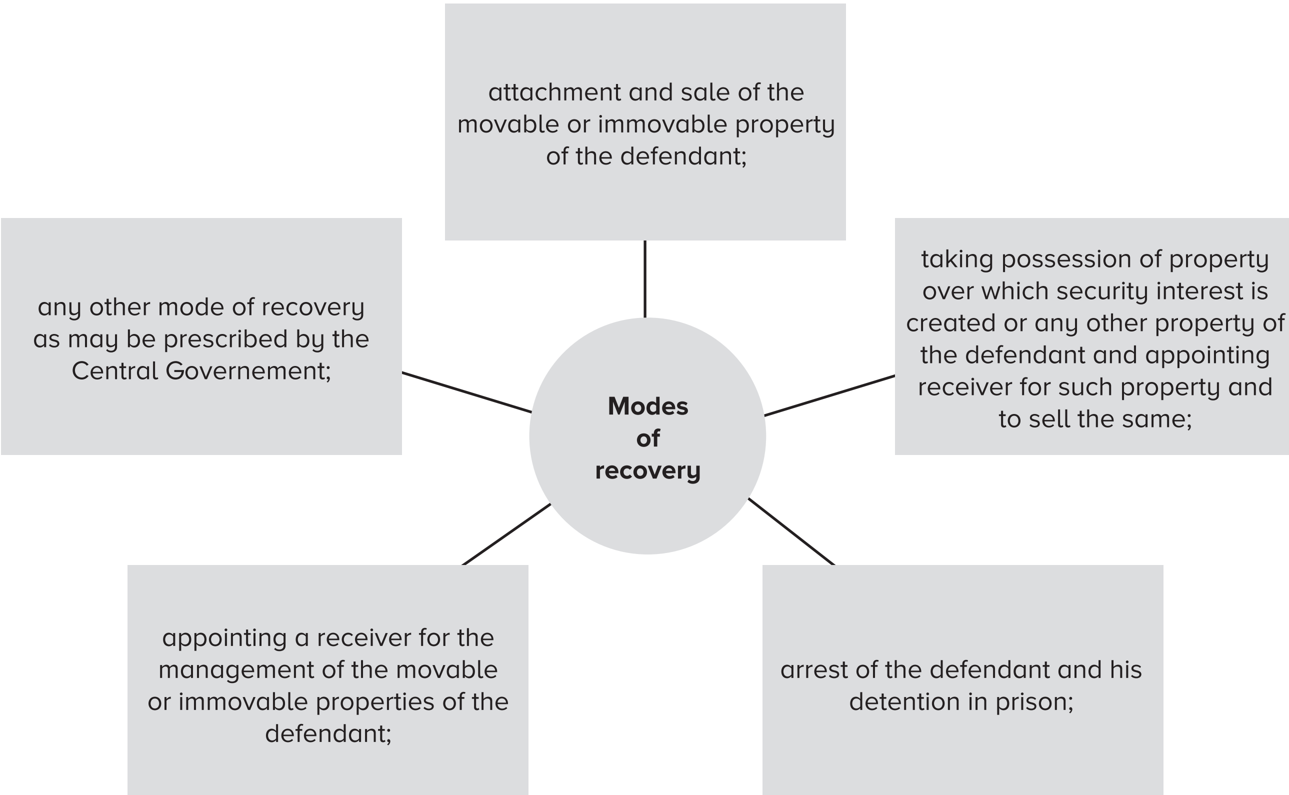
The defendant may either appear in person or authorise one or more legal practitioners or any of his or its officers to present his or its case before the Tribunal or the Appellate Tribunal.

RECOVERY OF DEBT DETERMINED BY TRIBUNAL

Chapter V deals with Recovery of Debt Determined by Tribunal

Modes of recovery of debts

Section 25 provides for modes of recovery of debts. It states that the Recovery Officer shall, on receipt of the copy of the certificate under sub-section (7) of section 19, proceed to recover the amount of debt specified in the certificate by one or more of the following modes, namely:—



Validity of certificate and amendment thereof

According to section 26, it shall not be open to the defendant to dispute before the Recovery Officer the correctness of the amount specified in the certificate, and no objection to the certificate on any other ground shall also be entertained by the Recovery Officer.

Notwithstanding the issue of a certificate to a Recovery Officer, the Presiding Officer shall have power to withdraw the certificate or correct any clerical or arithmetical mistake in the certificate by sending intimation to the Recovery Officer.

The Presiding Officer shall intimate to the Recovery Officer any order withdrawing or cancelling a certificate or any correction made by him under sub-section (2).

Stay of proceedings under certificate and amendment or withdrawal thereof

Section 27, states that notwithstanding that a certificate has been issued to the Recovery Officer for the recovery of any amount, the Presiding Officer, may by an order, grant time for payment of the amount, provided the defendant makes a down payment of not less than twenty-five per cent of the amount specified in the recovery certificate and gives an unconditional undertaking to pay the balance within a reasonable time, which is acceptable to the applicant bank or financial institution holding recovery certificate.

The Recovery Officer shall, after receipt of the order passed under sub-section (*1*), stay the proceedings until the expiry of the time so granted.

Where defendant agrees to pay the amount specified in the Recovery Certificate and proceeding are stayed by the Recovery Officer, the defendant shall forfeit right to file appeal against the orders of the Tribunal.

Where the defendant commits any default in payment of the amount under sub-section (*1*), the stay of recovery proceedings shall stand withdrawn and the Recovery Officer shall take steps for recovery of remaining amount of debt due and payable.

Where a certificate for the recovery of amount has been issued, the Presiding Officer shall keep the Recovery Officer informed of any amount paid or time granted for payment, subsequent to the issue of such certificate to the Recovery Officer.

Where the order giving rise to a demand of amount for recovery of debt has been modified in appeal, and, as a consequence thereof the demand is reduced, the Presiding Officer shall stay the recovery of such part of the amount of the certificate as pertains to the said reduction for the period for which the appeal remains pending.

Where a certificate for the recovery of debt has been received by the Recovery Officer and subsequently the amount of the outstanding demands is reduced or enhanced as a result of an appeal, the Presiding Officer shall, when the order which was the subject matter of such appeal has become final and conclusive, amend the certificate or withdraw it, as the case may be.

Other modes of recovery

According to Section 28(1), where a certificate has been issued to the Recovery Officer under sub-section (*7*) of section 19, the Recovery Officer may, without prejudice to the modes of recovery specified in section 25, recover the amount of debt by any one or more of the modes provided under this section.

If any amount is due from any person to the defendant, the Recovery Officer may require such person to deduct from the said amount, the amount of debt due from the defendant under this Act and such person shall comply with any such requisition and shall pay the sum so deducted to the credit of the Recovery Officer:

Provided that nothing in this sub-section shall apply to any part of the amount exempt from attachment in execution of a decree of a civil court under section 60 of the Code of Civil Procedure, 1908.

Sub clause 3 states that -

(i) The Recovery Officer may, at any time or from time to time, by notice in writing, require any person from whom money is due or may become due to the defendant or to any person who holds or may subsequently hold money for or on account of the defendant, to pay to the Recovery Officer either forthwith upon the money becoming due or being held or within the time specified in the notice not being before the money becomes due or is held so much of the money as is sufficient to pay the amount of debt due from the defendant or the whole of the money when it is equal to or less than that amount.

(ii) A notice under this sub-section may be issued to any person who holds or may subsequently hold any money for or on account of the defendant jointly with any other person and for the purposes of this sub-section, the shares of the joint holders in such amount shall be presumed, until the contrary is proved, to be equal.

(iii) A copy of the notice shall be forwarded to the defendant at his last address known to the Recovery Officer and in the case of a joint account to all the joint holders at their last addresses known to the Recovery Officer.

(iv) Save as otherwise provided in this sub-section, every person to whom a notice is issued under this sub-section shall be bound to comply with such notice, and, in particular, where any such notice is issued to a post office, bank, financial institution, or an insurer, it shall not be necessary for any pass book, deposit receipt, policy or any other document to be produced for the purpose of any entry, endorsement or the like to be made before the payment is made notwithstanding any rule, practice or requirement to the contrary.

(v) Any claim respecting any property in relation to which a notice under this sub-section has been issued arising after the date of the notice shall be void as against any demand contained in the notice.

(vi) Where a person to whom a notice under this sub-section is sent objects to it by a statement on oath that the sum demanded or the part thereof is not due to the defendant or that he does not hold any money for or on account of the defendant, then, nothing contained in this sub-section shall be deemed to require such person to pay any such sum or part thereof, as the case may be, but if it is discovered that such statement was false in any material particular, such person shall be personally liable to the Recovery Officer to the extent of his own liability to the defendant on the date of the notice, or to the extent of the defendant's liability for any sum due under this Act, whichever is less.

(vii) The Recovery Officer may, at any time or from time to time, amend or revoke any notice under this sub-section or extend the time for making any payment in pursuance of such notice.

(viii) The Recovery Officer shall grant a receipt for any amount paid in compliance with a notice issued under this sub-section, and the person so paying shall be fully discharged from his liability to the defendant to the extent of the amount so paid.

(ix) Any person discharging any liability to the defendant after the receipt of a notice under this sub-section shall be personally liable to the Recovery Officer to the extent of his own liability to the defendant so discharged or to the extent of the defendant's liability for any debt due under this Act, whichever is less.

(x) If the person to whom a notice under this sub-section is sent fails to make payment in pursuance thereof to the Recovery Officer, he shall be deemed to be a defendant in default in respect of the amount specified in the notice and further proceedings may be taken against him for the realisation of the amount as if it were a debt due from him, in the manner provided in sections 25, 26 and 27 and the notice shall have the same effect as an attachment of a debt by the Recovery Officer in exercise of his powers under section 25.

The Recovery Officer may apply to the court in whose custody there is money belonging to the defendant for payment to him of the entire amount of such money, or if it is more than the amount of debt due, an amount sufficient to discharge the amount of debt so due.

The Recovery Officer may, by order, at any stage of the execution of the certificate of recovery, require any person, and in case of a company, any of its officers against whom or which the certificate of recovery is issued, to declare on affidavit the particulars of his or its assets.

The Recovery Officer may recover any amount of debt due from the defendant by distraint and sale of his movable property in the manner laid down in the Third Schedule to the Income-Tax Act, 1961.

Application of certain provisions of Income-tax Act

The provisions of the Second and Third Schedules to the Income-Tax Act, 1961 and the Income-Tax (Certificate Proceedings) Rules, 1962, as in force from time to time shall, as far as possible, apply with necessary modifications as if the said provisions and the rules referred to the amount of debt due under this Act instead of to the Income-tax:

Provided that any reference under the said provisions and the rules to the "assessee" shall be construed as a reference to the defendant under this Act.

Appeal against the order of Recovery Officer

Notwithstanding anything contained in section 29, any person aggrieved by an order of the Recovery Officer made under this Act may, within thirty days from the date on which a copy of the order is issued to him, prefer an appeal to the Tribunal.

On receipt of an appeal under sub-section (*1*), the Tribunal may, after giving an opportunity to the appellant to be heard, and after making such inquiry as it deems fit, confirm, modify or set aside the order made by the Recovery Officer in exercise of his powers under sections 25 to 28 (both inclusive).

Deposit of amount of debt due for filing appeal against orders of the Recovery Officer

Section 30A provides for deposit of amount of debt due for filing appeal against orders of the Recovery Officer. It states that where an appeal is preferred against any order of the Recovery Officer, under section 30, by any person from whom the amount of debt is due to a bank or financial institution or consortium of banks or financial institutions, such appeal shall not be entertained by the Tribunal unless such person has deposited with the Tribunal fifty percent of the amount of debt due as determined by the Tribunal.

Transfer of pending cases

Section 31 stipulates that every suit or other proceeding pending before any court immediately before the date of establishment of a Tribunal under this Act, being a suit or proceeding the cause of action whereon it is based is such that it would have been, if it had arisen after such establishment, within the jurisdiction of such Tribunal, shall stand transferred on that date to such Tribunal:

Provided that nothing in this sub-section shall apply to any appeal pending as aforesaid before any court:

Provided further that any recovery proceedings in relation to the recovery of debts due to any multi-State co-operative bank pending before the date of commencement of the Enforcement of Security Interest and Recovery of Debts Laws (Amendment) Act, 2012 under the Multi-State Co-operative Societies Act, 2002, shall be continued and nothing contained in this section shall apply to such proceedings.

Where any suit or other proceeding stands transferred from any court to a Tribunal under sub-section (*1*),—

(a) the court shall, as soon as may be after such transfer, forward the records of such suit or other proceeding to the Tribunal; and

(b) the Tribunal may, on receipt of such records, proceed to deal with such suit or other proceeding, so far as may be, in the same manner as in the case of an application made under section 19 from the stage which was reached before such transfer or from any earlier stage as the Tribunal may deed fit.

Power of Tribunal to issue certificate of recovery in case of decree or order

Section 31A states that where a decree or order was passed by any court before the commencement of the Recovery of Debts Due to Banks and Financial Institutions (Amendment) Act, 2000 and has not yet been executed, then, the decree-holder may apply to the Tribunal to pass an order for recovery of the amount.

On receipt of an application under sub-section (*1*), the Tribunal may issue a certificate for recovery to a Recovery Officer.

On receipt of a certificate under sub-section (*2*), the Recovery Officer shall proceed to recover the amount as if it was a certificate in respect of a debt recoverable under this Act.

Priority to secured creditors

Section 31A provides that notwithstanding anything contained in any other law for the time being in force, the rights of secured creditors to realise secured debts due and payable to them by sale of assets over which security interest is created, shall have priority and shall be paid in priority over all other debts and Government dues including revenues, taxes, cesses and rates due to the Central Government, State Government or local authority.

Explanation.—For the purposes of this section, it is hereby clarified that on or after the commencement of the Insolvency and Bankruptcy Code, 2016, in cases where insolvency or bankruptcy proceedings are pending in respect of secured assets of the borrower, priority to secured creditors in payment of debt shall be subject to the provisions of that Code.

Will Insolvency and Bankruptcy Code, 2016 prevails over SARFAESI Act, 2002?

In the case of ***Canara Bank v. Sri Chandramoulishvar Spg. Mills (P) Ltd.,*** the NCLAT while referring to Supreme Court's verdict in Innoventive case has ruled that when two proceedings are initiated, one under the Insolvency and Bankruptcy Code, 2016 (the Code) and the other under the SARFAESI Act, 2002, then the proceeding under the Code shall prevail.

The appeal in the case was preferred by the Financial Creditor i.e. Canara Bank against the NCLT's (National Company law Tribunal) order, whereby the application preferred by Operational Creditor under Section 9 of the Insolvency and Bankruptcy Code, 2016 (application for initiation of corporate insolvency resolution process by operational creditor) against the Corporate Debtor i.e. M/s. Sri Chandra Moulishvar Spinning Mills Private Limited was admitted by the Tribunal. The Appellant's main grievance in the case was that he had already initiated proceedings under the SARFAESIAct, 2002 for recovery against the Corporate Debtor.

The NCLAT in view of the issue involved in the case, made reference to Supreme Court's verdict in the case of *Innoventive Industries Ltd. v. ICICI Bank,* whereby the Apex Court was of the view that if the application under Section 9 is complete and there is no 'existence of dispute' and there is a 'debt' and 'default' then the Adjudicating Authority is bound to admit the application.

Thus, NCLAT upheld NCLT's decision and also noted that such action cannot continue as the Code will prevail over SARFAESI Act, 2002.

LESSON ROUND-UP

- Securitisation is the process of pooling and repackaging of homogenous illiquid financial assets into marketable securities that can be sold to investors.
- The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 is enacted with a view to regulate securitisation and reconstruction of financial assets and enforcement of security interest and for matters connected therewith or incidental thereto.
- The SARFAESI Act, 2002 has empowered the Banks and Financial Institutions with vast power to enforce the securities charged to them. The Banks can now issue notices to the defaulters to pay up the dues and if they fail to do so within 60 days of the date of the notice, the banks can take over the possession of assets like factory, land and building, plant and machinery etc.
- Asset Reconstruction Company' means a company registered with Reserve Bank under section 3 of SARFAESI Act for the purposes of carrying on the business of asset reconstruction or securitisation, or both. Section 3 of SARFAESI Act deals with the Registration of Asset Reconstruction Companies.
- Any security interest created in favour of any secured creditor may be enforced, without the intervention of the Court or Tribunal, by such creditor in accordance with the provisions of this Act.
- Any borrower or any other person aggrieved by the action of the secured creditors can file an appeal to the concerned Debt Recovery Tribunal (DRT).
- Any person aggrieved by the order of DRT, may prefer an appeal to the Appellate Tribunal within thirty days from the date of receipt of the order of Debt Recovery Tribunal.
- Section 31 of the Act contains provisions relating to non-applicability of the Act in certain cases. Section 34 provides that no civil court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which a Debts Recovery Tribunal or the Appellate Tribunal is empowered by or under this Act.
- Any person who contravenes the provisions of this Act or of any rules made thereunder shall be punishable with imprisonment for a term which may extend to one year, or with fine, or with both.
- Limitation Act, 1963 is applicable to the claims made under this Act. Section 35 provides that the provisions of this Act shall have effect, notwithstanding anything inconsistent therewith contained in any other law for the time being in force or any instrument having effect by virtue of any such law.

TEST YOURSELF

(*These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation*).

1. What is securitization? Mention the reasons behind the enactment of the SARFAESI Act, 2002?
2. Write a note on Asset Reconstruction Companies citing the measures it can take under section 9 of the SARFAESI Act, 2002.
3. What are the provisions relating to assistance of Chief Metropolitan magistrate or District magistrate for taking possession of a securest asset?
4. Mention provisions relating to 'demand notice' under rule 3 of Security Interest (Enforcement) Rules, 2002.
5. Explain the 'Right to lodge a caveat' under SARFAESI Act, 2002.
6. State the salient features of the Recovery of Debts and Bankruptcy Act, 1993.
7. Explain in brief the procedure for making application to the Tribunal under section 19 of the Recovery of Debts and Bankruptcy Act, 1993.
8. Write a note on the powers of the Tribunal and Appellate Tribunal under the Recovery of Debts and Bankruptcy Act, 1993.

LIST OF FURTHER READINGS

- Bare Act - Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, (SARFAESI) 2002 and Recovery of Debts Due to Banks and Financial Institutions Act, 1993 rules and regulations made thereunder.
- Report of the Committee to Review the Working of Asset Reconstruction Companies, September 2021.

OTHER REFERENCES (Including Websites / Video Links)

- https://rbi.org.in/home.aspx
- https://m.rbi.org.in/scripts/PublicationReportDetails.aspx?UrlPage=&ID=1188

Winding-up by Tribunal under the Companies Act, 2013

Lesson 25

KEY CONCEPTS

■ Winding up ■ Company Liquidator ■ Dissolution ■ Fraudulent preference

Learning Objectives

To understand:

- Grounds of winding up by Tribunal and its petition
- Functions of company liquidators
- Submission of reports to Tribunal

Lesson Outline

- Introduction
- Important changes brought about by IBC
- Winding up by Tribunal : Grounds
- Petition for the Winding-up
- Powers of the Tribunal
- Directions for filing statement of affairs
- Company Liquidators and their appointments
- Removal and replacement of Liquidators
- Submission of the reports by the Company Liquidator
- Advisory Committee
- Submission of periodical reports to the Tribunal
- Powers and duties of the Company Liquidator
- Audit of Company Liquidator's accounts
- Overriding Preferential Payments
- Fraudulent preferences
- Companies (Winding-up) Rules, 2020
- Case Laws
- Lesson Round-Up
- Test Yourself

REGULATORY FRAMEWORK

- Section 59 & 255 of the Insolvency and Bankruptcy Code, 201
- Section 270 to 303 & 324 to 365 of Companies Act, 2013
- Companies (Winding up) Rules, 2020

INTRODUCTION

Winding up is a means by which the dissolution of a company is brought about. The main purpose of winding up of a company is to realize the assets and pay the company's debts expeditiously and fairly in accordance with the law. If any surplus is left, it is distributed among the members in accordance with their rights.

It may be noted that on winding up, the company does not cease to exist as such, except when it is dissolved. Even after the commencement of winding-up, the property and assets of the company belong to the company until the dissolution takes place. On dissolution, the company ceases to exist as a separate entity and becomes incapable of keeping property, suing or being sued. Thus, in between the winding up and dissolution, the legal status of the company continues and it can be sued in the court of law.

> The terms "Winding up" and "dissolution" are sometimes erroneously used to mean the same thing. But, the legal implications of these two terms are quite different and there are fundamental differences between them as regards the legal procedure involved.

The entire procedure for bringing about a lawful end to the life of a company is divided into two stages i.e., 'winding up' and 'dissolution'. Winding up is the first stage in the process whereby assets are realised, liabilities are paid off and the surplus, if any, distributed among its members. Dissolution is the final stage whereby the existence of the company is withdrawn by the law. Dissolution brings about an end to the legal entity of the company.

IMPORTANT CHANGES BROUGHT ABOUT BY THE INSOLVENCY AND BANKRUPTCY CODE, 2016

The Insolvency and Bankruptcy Code, 2016 ('Code') was passed with the objective of consolidating and amending the laws relating to reorganisation and insolvency resolution in a time bound manner for maximization of value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders including alteration in the order of priority of payment of Government dues and to establish an Insolvency and Bankruptcy Board of India, and for other matters connected.

> The Ministry of Corporate Affairs has notified section 255 of the Insolvency and Bankruptcy Code, 2016. Section 255 of the Insolvency and Bankruptcy Code, 2016 amends the Companies Act, 2013, in accordance with the eleventh Schedule of the Insolvency and Bankruptcy Code, 2016.
>
> The Central Government had appointed 15th November, 2016 as the date on which the provisions of section 255 of the Insolvency and Bankruptcy Code, 2016 shall come into force

The Insolvency and Bankruptcy Code, 2016 has made significant amendments to provisions relating to winding up in the Companies Act, 2013. The important ones are discussed below:

Winding up – The expression "winding up" was not defined in the Companies Act, 2013 or in the erstwhile Companies Act of 1956. The eleventh Schedule has added sub-section (94a) to section 2 of the Companies Act, 1956. The definition of "winding up" reads as follows:

> "Winding up" means winding up under the Companies Act, 2013 or liquidation under the insolvency and Bankruptcy Code, 2016, as applicable" [Section 2(94a)]

Voluntary winding up – Provisions relating to voluntary winding up in the Companies Act, 2013 i.e., sections 304 to 323 have been omitted by the insolvency and Bankruptcy Code, 2016. Voluntary liquidation is now dealt with under section 59 of the insolvency and Bankruptcy Code, 2016 read with IBBI (Voluntary liquidation Process) regulations, 2017.

Inability to pay debts – The Insolvency and Bankruptcy Code, 2016 has substituted section 271 of the Companies Act, 2013.

Now after its substitution, section 271 provides the following five grounds where a company may be wound up by a tribunal:

(a) if the company has, by special resolution, resolved that the company be wound up by the tribunal;

(b) if the company has Acted against the interests of the sovereignty and integrity of Iindia, the security of the State, friendly relations with foreign States, public order, decency or morality;

(c) if on an application made by the Registrar or any other person authorised by the Central Government by notification under this Act, the Tribunal is of the opinion that the affairs of the company have been conducted in a fraudulent manner or the company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company be wound up;

(d) if the company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years; or

(e) if the tribunal is of the opinion that it is just and equitable that the company should be wound up.

The following two grounds have been deleted from section 271:

(a) if the company is unable to pay its debts;

(d) if the tribunal has ordered the winding up of the company under Chapter XIIX.

Thus, if a company is unable to pay its debts, creditors canno't file petition in tribunal in for winding up of the Company. However, the Companies Act, 2013 shall continue to govern winding up of companies on various other grounds excluding inability to pay debts.

WINDING UP BY TRIBUNAL UNDER THE COMPANIES ACT, 2013

The Companies Act, 2013 continues to govern winding up of companies on various other grounds excluding inability to pay debts. Sections 270 to 288, Sections 290 to 303, Section 324 and Sections 326 to 365 of Chapter XX of the Companies Act, 2013 contain the provisions relating to winding up of a company.

The Ministry of Corporate Affairs has notified these sections on 7th December, 2016 and these sections have come into force with effect from 15th December 2016.

WHO MAY FILE PETITION FOR WINDING UP

Section 272 lays down that a petition to the tribunal for the winding up of a company shall be presented by –

(a) the company;

(b) any contributory or contributories;

(c) all or any of the persons specified in clauses (a) and (b);

(d) the registrar;

(e) any person authorised by the Central Government in that behalf; or

(f) in a case falling under clause (b) of section 271, by the Central Government or a State Government.

POWERS OF TRIBUNA

According to section 273(1), the tribunal may, on receipt of a petition for winding up under section 272 pass any of the following orders, namely: –

(a) dismiss it, with or without costs;

(b) make any interim order as it thinks fit;

(c) appoint a provisional liquidator of the company till the making of a winding up order;

(d) make an order for the winding up of the company with or without costs; or

(e) any other order as it thinks fit:

Provided that an order under this sub-section shall be made within ninety days from the date of presentation of the petition:

Provided further that before appointing a provisional liquidator under clause (c), the tribunal shall give notice to the company and afford a reasonable opportunity to it to make its representations, if any, unless for special reasons to be recorded in writing, the Tribunal thinks fit to dispense with such notice:

Provided also that the tribunal shall not refuse to make a winding up order on the ground only that the assets of the company have been mortgaged for an amount equal to or in excess of those assets, or that the company has no assets.

Where a petition is presented on the ground that it is just and equitable that the company should be wound up, the tribunal may refuse to make an order of winding up, if it is of the opinion that some other remedy is available to the petitioners and that they are Acting unreasonably in seeking to have the company wound up instead of pursuing the other remedy. [Section 273(2)]

FILING STATEMENT OF AFFAIRS OF THE COMPANY

In case, where the Company fails to file the statement of affairs, the tribunal shall forfeit the right of the company to oppose the petition and right of such directors and officers of the company as found responsible for such non-compliance.

Section 274 lays down that in case, where the Tribunal is satisfied that on a petition that the winding up of the company is to be made out, he may by an order direct the company to file its objections along with a statement of its affairs within thirty days of the order which can be allowed a further period of thirty days in a situation of contingency or special circumstances.

Further, the director or the officer of the company who is in default will be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both.

The complaint may be filed in this behalf before the Special Court by Registrar, provisional liquidator, Company liquidator or any person authorised by the tribunal.

COMPANY LIQUIDATORS AND THEIR APPOINTMENTS

For the purposes of winding up of a company by the tribunal, the tribunal at the time of the passing of the order of winding up, shall appoint an Official Liquidator or a liquidator from the panel maintained under sub-section (1) as the Company liquidator. [Section 275(1)]

The provisional liquidator or the Company liquidator, as the case may, shall be appointed by the tribunal from amongst the insolvency professionals registered under the insolvency and Bankruptcy Code, 2016. [Section 275(2)]

Where a provisional liquidator is appointed by the tribunal, the tribunal may limit and restrict his powers by the order appointing him or it or by a subsequent order, but otherwise he shall have the same powers as a liquidator. [Section 275(3)]

> **"Company Liquidator",**
>
> means a person appointed by the tribunal as the Company liquidator in accordance with the provisions of section 275 for the winding up of a company under this Act. [Section 2(23)].

The terms and conditions of appointment of a provisional liquidator or Company liquidator and the fee payable to him or it shall be specified by the Tribunal on the basis of task required to be performed, experience, qualification of such liquidator and size of the company. [Section 275(5)]

On appointment as provisional liquidator or Company liquidator, as the case may be, such liquidator shall file a declaration within seven days from the date of appointment in the prescribed form disclosing conflict of interest or lack of independence in respect of his appointment, if any, with the tribunal and such obligation shall continue throughout the term of his appointment. [Section 275(6)]

While passing a winding up order, the tribunal may appoint a provisional liquidator, if any, appointed under clause (c) of sub-section (1) of section 273, as the Company liquidator for the conduct of the proceedings for the winding up of the company. [Section 275(7)]

REMOVAL AND REPLACEMENT OF LIQUIDATOR

Section 276 lays down that in case where the reasonable cause being shown and for reasons to be recorded in writing, the tribunal may remove the provisional liquidator or the Company liquidator, on any of the following grounds:

(a) misconduct;

(b) fraud or misfeasance;

(c) professional incompetence or failure to exercise due care and diligence in performance of the powers and functions;

(d) inability to Act as provisional liquidator or as the case may be, Company liquidator;

(e) conflict of interest or lack of independence during the term of his appointment that would justify removal.

Further, in the event of death, resignation or removal of the liquidator the tribunal may transfer the work assigned to him or it to another Company liquidator for reasons to be recorded in writing.

INTIMATION FOR WINDING UP

Aaccording to Section 277, upon the order for appointment of provisional liquidator or for the winding up of a company, the tribunal shall within a period not exceeding seven days from the date of passing of the order give intimation of the appointment to the Company liquidator or provisional liquidator and the registrar.

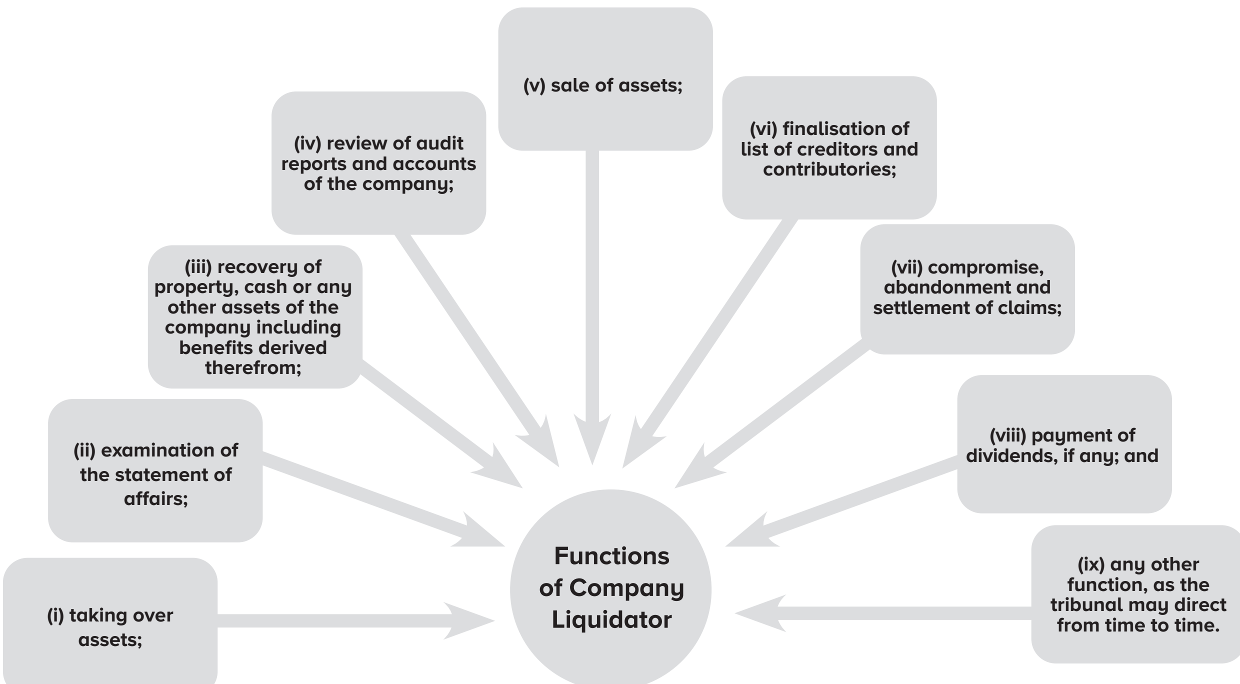
The registrar on receipt of the copy of order of appointment of provisional liquidator or winding up order shall make an endorsement to that effect in his records relating to the company and notify in the Official Gazette that such an order has been made and in the case of a listed company, the registrar shall intimate about such appointment or order, to the stock exchange or exchanges where the securities of the company are listed.

Such winding up order shall be deemed to be a notice of discharge to the officers, employees and workmen of the company, except when the business of the company is continued.

Within three weeks from the date of passing of winding up order, the Company liquidator shall make an application to the tribunal for constitution of a winding up committee to assist and monitor the progress of liquidation proceedings by the Company liquidator in carrying out the function as provided in sub-section (5) and such winding up committee shall comprise of the following persons, namely:—

(i) Official Liquidator attached to the Tribunal;	**(ii) nominee of secured creditors; and**	**(iii) a professional nominated by the tribunal.**

The Company liquidator shall be the convener of the meetings of the winding up committee which shall assist and monitor the liquidation proceedings in following areas of liquidation functions, namely:—



The Company liquidator shall place before the tribunal a report along with minutes of the meetings of the committee on monthly basis duly signed by the members present in the meeting for consideration till the final report for dissolution of the company is submitted before the Tribunal. He shall also prepare the draft final report for consideration and approval of the winding up committee. The final report, so approved by the winding up committee, shall be submitted by the Company liquidator before the tribunal for passing of a dissolution order in respect of the company.

STAY OF SUITS ON WINDING UP ORDER

When a winding up order has been passed or a provisional liquidator has been appointed, no suit or other legal proceeding shall be commenced, or if pending at the date of the winding up order, shall be proceeded with, by or against the company, except with the leave of the tribunal and subject to such terms as the tribunal may impose:

Provided that any application to the tribunal seeking leave under this section shall be disposed of by the tribunal within sixty days. [Section 279(1)]

Nothing in sub-section (1) shall apply to any proceeding pending in appeal before the Supreme Court or a High Court. [Section 279(2)]

> ***Effect of winding up order***
>
> The order for the winding up of a company shall operate in favour of all the creditors and all contributories of the company as if it had been made out on the joint petition of creditors and contributories. [Section 278]

SUBMISSION OF REPORT BY COMPANY LIQUIDATOR

Aaccording to section 281(1), where the tribunal has made a winding up order or appointed a Company liquidator, such liquidator shall, within sixty days from the order, submit to the tribunal, a report containing the following particulars, namely:

(a) the nature and details of the assets of the company including their location and value, stating separately the cash balance in hand and in the bank, if any, and the negotiable securities, if any, held by the company:

Provided that the valuation of the assets shall be obtained from registered valuers for this purpose;

(b) amount of capital issued, subscribed and paid-up;

(c) the existing and contingent liabilities of the company including names, addresses and occupations of its creditors, stating separately the amount of secured and unsecured debts, and in the case of secured debts, particulars of the securities given, whether by the company or an officer thereof, their value and the dates on which they were given;

(d) the debts due to the company and the names, addresses and occupations of the persons from whom they are due and the amount likely to be realised on account thereof;

(e) guarantees, if any extended by the company;

(f) list of contributories and dues, if any, payable by them and details of any unpaid call;

(g) details of trademarks and intellectual properties, if any, owned by the company;

(h) details of subsisting contrActs, joint ventures and collaborations, if any;

(i) details of holding and subsidiary companies, if any;

(j) details of legal cases filed by or against the company; and

(k) any other information which the tribunal may direct or the Company liquidator may consider necessary to include.

The Company liquidator shall include in his report the manner in which the company was promoted or formed and whether in his opinion any fraud has been committed by any person in its promotion or formation or by any officer of the company in relation to the company since the formation thereof and any other matters which, in his opinion, it is desirable to bring to the notice of the tribunal. [Section 281(2)]

The Company liquidator shall also make a report on the viability of the business of the company or the steps which, in his opinion, are necessary for maximising the value of the assets of the company. [Section 281(3)]

The Company Liquidator may also, if he thinks fit, make any further report or reports. [Section 281(4)]

Any person describing himself in writing to be a creditor or a contributory of the company shall be entitled by himself or by his agent at all reasonable times to inspect the report submitted in accordance with this section and take copies thereof or extrActs therefrom on payment of the prescribed fees. [Section 281(5)]

DIRECTIONS OF TRIBUNAL ON REPORT OF COMPANY LIQUIDATOR

The Tribunal shall, on consideration of the report of the Company Liquidator, fix a time limit within which the entire proceedings shall be completed and the company be dissolved:

Provided that the tribunal may, if it is of the opinion, at any stage of the proceedings, or on examination of the reports submitted to it by the Company liquidator and after hearing the Company liquidator, creditors or contributories or any other interested person, that it will not be advantageous or economical to continue the proceedings, revise the time limit within which the entire proceedings shall be completed and the company be dissolved. [Section 282(1)]

The tribunal may, on examination of the reports submitted to it by the Company liquidator and after hearing the Company liquidator, creditors or contributories or any other interested person, order sale of the company as a going concern or its assets or part thereof:

Provided that the Tribunal may, where it considers fit, appoint a sale committee comprising such creditors, promoters and officers of the company as the Tribunal may decide to assist the Company Liquidator in sale under this sub-section. [Section 282(2)]

Custody of Company's Properties

Upon the winding up order made by the tribunal the Company liquidator or the provisional liquidator take into his or its custody or control all the property, effects and Actionable claims to which the company is or appears to be entitled to and take such steps and measures, as may be necessary, to protect and preserve the properties of the company which shall be deemed to be in the custody of the tribunal from the date of the order for the winding up of the company. [Section 283]

Where a report is received from the Company liquidator or the Central Government or any person that a fraud has been committed in respect of the company, the tribunal shall, without prejudice to the process of winding up, order for investigation under section 210, and on consideration of the report of such investigation it may pass order and give directions under sections 339 to 342 or direct the Company Liquidator to file a criminal complaint against persons who were involved in the commission of fraud. [Section 282(3)]

The tribunal may order for taking such steps and measures, as may be necessary, to protect, preserve or enhance the value of the assets of the company. [Section 282(4)]

The Tribunal may pass such other order or give such other directions as it considers fit. [Section 282(5)]

ADVISORY COMMITTEE

The tribunal may, while passing an order of winding up of a company, direct that there shall be, an advisory committee to advise the Company liquidator and to report to the tribunal on such matters as the tribunal may direct. [Section 287(1)]

The advisory committee appointed by the tribunal shall consist of not more than twelve members, being creditors and contributories of the company or such other persons in such proportion as the tribunal may, keeping in view the circumstances of the company under liquidation, direct. [Section 287(2)]

The Company liquidator shall convene a meeting of creditors and contributories, as ascertained from the books and documents, of the company within thirty days from the date of order of winding up for enabling the tribunal to determine the persons who may be members of the advisory committee. [Section 287(3)]

The advisory committee shall have the right to inspect the books of account and other documents, assets and properties of the company under liquidation at a reasonable time. [Section 287(4)]

The provisions relating to the convening of the meetings, the procedure to be followed thereat and other matters relating to conduct of business by the advisory committee shall be such as may be prescribed. [Section 287(5)]

The meeting of advisory committee shall be chaired by the Company liquidator. [Section 287(6)]

POWERS AND DUTIES OF COMPANY LIQUIDATOR

Section 290 of the Companies Act, 2013 lays down that subject to directions by the tribunal, if any, in this regard, the Company liquidator, in a winding up of a company by the tribunal, shall have the power –

(a) to carry on the business of the company so far as may be necessary for the beneficial winding up of the company;

(b) to do all Acts and to execute, in the name and on behalf of the company, all deeds, receipts and other documents, and for that purpose, to use, when necessary, the company's seal;

(c) to sell the immovable and movable property and actionable claims of the company by public auction or private contract, with power to transfer such property to any person or body corporate, or to sell the same in parcels;

(d) to sell the whole of the undertaking of the company as a going concern;

(e) to raise any money required on the security of the assets of the company;

(f) to institute or defend any suit, prosecution or other legal proceeding, civil or criminal, in the name and on behalf of the company;

(g) to invite and settle claim of creditors, employees or any other claimant and distribute sale proceeds in accordance with priorities established under this Act;

(h) to inspect the records and returns of the company on the files of the Registrar or any other authority;

(i) to prove rank and claim in the insolvency of any contributory for any balance against his estate, and to receive dividends in the insolvency, in respect of that balance, as a separate debt due from the insolvent, and rateably with the other separate creditors;

(j) to draw, accept, make and endorse any negotiable instruments including cheque, bill of exchange, hundi or promissory note in the name and on behalf of the company, with the same effect with respect to the liability of the company as if such instruments had been drawn, accepted, made or endorsed by or on behalf of the company in the course of its business;

Professional Assistance to Company Liquidator

The Company liquidator may, with the sanction of the tribunal, appoint one or more chartered accountants or company secretaries or cost accountants or legal prActitioners or such other professionals on such terms and conditions, as may be necessary, to assist him in the performance of his duties and functions under this Act. [Section 291(1)]

Aany person appointed under this section shall disclose forthwith to the tribunal in the prescribed form any conflict of interest or lack of independence in respect of his appointment. [Section 291(2)]

(k) to take out, in his official name, letters of administration to any deceased contributory, and to do in his official name any other Act necessary for obtaining payment of any money due from a contributory or his estate which cannot be conveniently done in the name of the company, and in all such cases, the money due shall, for the purpose of enabling the Company liquidator to take out the letters of administration or recover the money, be deemed to be due to the Company liquidator himself;

(l) to obtain any professional assistance from any person or appoint any professional, in discharge of his duties, obligations and responsibilities and for protection of the assets of the company, appoint an agent to do any business which the Company liquidator is unable to do himself;

(m) to take all such Actions, steps, or to sign, execute and verify any paper, deed, document, application, petition, affidavit, bond or instrument as may be necessary, –

   (i) for winding up of the company;

   (ii) for distribution of assets;

   (iii) in discharge of his duties and obligations and functions as Company liquidator. and

(n) to apply to the tribunal for such orders or directions as may be necessary for the winding up of the company.

EXERCISE AND CONTROL OF COMPANY LIQUIDATOR'S POWER

Sub-section (1) of section 292 lays down that subject to the provisions of this Act, the Company liquidator shall, in the administration of the assets of the company and the distribution thereof among its creditors, have regard to any directions which may be given by the resolution of the creditors or contributories at any general meeting or by the advisory committee.

Any directions given by the creditors or contributories at any general meeting shall, in case of conflict, be deemed to override any directions given by the advisory committee. [Section 292(2)] The Company liquidator

(a) may summon meetings of the creditors or contributories, whenever he thinks fit, for the purpose of ascertaining their wishes; and

(b) shall summon such meetings at such times, as the creditors or contributories, as the case may be, may, by resolution, direct, or whenever requested in writing to do so by not less than one-tenth in value of the creditors or contributories, as the case may be. [Section 292(3)]

Aany person aggrieved by any Act or decision of the Company liquidator may apply to the tribunal, and the Tribunal may confirm, reverse or modify the Act or decision complained of and make such further order as it thinks just and proper in the circumstances. [Section 292(4)]

AUDIT OF COMPANY LIQUIDATOR'S ACCOUNTS

The Company liquidator shall maintain proper and regular books of account including accounts of receipts and payments made by him in such form and manner as may be prescribed. [Section 294(1)]

The Company liquidator shall, at such times as may be prescribed but not less than twice in each year during his tenure of office, present to the Tribunal an account of the receipts and payments as such liquidator in the prescribed form in duplicate, which shall be verified by a declaration in such form and manner as may be prescribed. [Section 294(2)]

The Tribunal shall cause the accounts to be audited in such manner as it thinks fit, and for the purpose of the

Books to be kept by Company Liquidator

The Company liquidator shall keep proper books in such manner, as may be prescribed, in which he shall cause entries or minutes to be made of proceedings at meetings and of such other matters as may be prescribed. [Section 293(1)]

Any creditor or contributory may, subject to the control of the tribunal, inspect any such books, personally or through his agent [Section 293(2)] audit, the Company liquidator shall furnish to the tribunal with such vouchers and information as the tribunal may require, and the tribunal may, at any time, require the production of, and inspect, any books of account kept by the Company liquidator. [Section 294(3)]

When the accounts of the company have been audited, one copy thereof shall be filed by the Company Liquidator with the tribunal, and the other copy shall be delivered to the registrar which shall be open to inspection by any creditor, contributory or person interested. [Section 294(4)]

Where an account referred to in sub-section (4) relates to a Government company, the Company liquidator shall forward a copy thereof –

(a) to the Central Government, if that Government is a member of the Government company; or

(b) to any State Government, if that Government is a member of the Government company; or

(c) to the Central Government and any State Government, if both the Governments are members of the Government company. [Section 294(5)]

The Company liquidator shall cause the accounts when audited, or a summary thereof, to be printed, and shall send a printed copy of the accounts or summary thereof by post to every creditor and every contributory:

Provided that the tribunal may dispense with the compliance of the provisions of this sub-section in any case it deems fit. [Section 294(6)]

PAYMENT OF DEBTS BY CONTRIBUTORY AND EXTENT OF SET-OFF

The Tribunal may, at any time after passing of a winding up order, pass an order requiring any contributory for the time being on the list of contributories to pay, in the manner directed by the order, any money due to the company, from him or from the estate of the person whom he represents, exclusive of any money payable by him or the estate by virtue of any call in pursuance of this Act. [Section 295(1)]

The Tribunal, in making an order, under sub-section (1), may, –

(a) in the case of an unlimited company, allow to the contributory, by way of setoff, any money due to him or to the estate which he represents, from the company, on any independent dealing or contrAct with the company, but not any money due to him as a member of the company in respect of any dividend or profit; and

(b) in the case of a limited company, allow to any director or manager whose liability is unlimited, or to his estate, such set-off. [Section 295(2)]

In the case of any company, whether limited or unlimited, when all the creditors have been paid in full, any money due on any account whatever to a contributory from the company may be allowed to him by way of set- off against any subsequent call. [Section 295(3)]

POWER TO SUMMON PERSONS SUSPECTED OF HAVING PROPERTY OF COMPANY

The Tribunal may, at any time after the appointment of a provisional liquidator or the passing of a winding up order, summon before it any officer of the company or person known or suspected to have in his possession any property or books or papers, of the company, or known or suspected to be indebted to the company, or any person whom the tribunal thinks to be capable of giving information concerning the promotion, formation, trade, dealings, property, books or papers, or affairs of the company. [Section 299(1)]

The Tribunal may examine any officer or person so summoned on oath concerning the matters aforesaid, either by word of mouth or on written interrogatories or on affidavit and may, in the first case, reduce his answers to writing and require him to sign them. [Section 299(2)]

The Tribunal may require any officer or person so summoned to produce any books and papers relating to the company in his custody or power, but, where he claims any lien on books or papers produced by him, the production shall be without prejudice to such lien, and the tribunal shall have power to determine all questions relating to that lien. [Section 299(3)]

Power to order costs

The Tribunal may, in the event of the assets of a company being insufficient to satisfy its liabilities, make an order for the payment out of the assets, of the costs, charges and expenses incurred in the winding up, in such order of priority inter se as the tribunal thinks just and proper. [Section 298]

The Tribunal may direct the liquidator to file before it a report in respect of debt or property of the company in possession of other persons. [Section 299(4)]

If the Tribunal finds that –

(a) a person is indebted to the company, the tribunal may order him to pay to the provisional liquidator or, as the case may be, the liquidator at such time and in such manner as the tribunal may consider just, the amount in which he is indebted, or any part thereof, either in full discharge of the whole amount or not, as the Tribunal thinks fit, with or without costs of the examination;

(b) a person is in possession of any property belonging to the company, the tribunal may order him to deliver to the provisional liquidator or, as the case may be, the liquidator, that property or any part thereof, at such time, in such manner and on such terms as the tribunal may consider just. [Section 299(5)]

If any officer or person so summoned fails to appear before the Tribunal at the time appointed without a reasonable cause, the tribunal may impose an appropriate cost. [Section 299(6)]

Every order made under sub-section (5) shall be executed in the same manner as decrees for the payment of money or for the delivery of property under the Code of Civil Procedure, 1908 (5 of 1908). [Section 299(7)]

Any person making any payment or delivery in pursuance of an order made under sub-section (5) shall by such payment or delivery be, unless otherwise directed by such order, discharged from all liability whatsoever in respect of such debt or property. [Section 299(8)]

EXAMINATION OF PROMOTERS, DIRECTORS, ETC.

As per Section 300(1) of the Act, upon the report of the Company liquidator to the tribunal stating that in his opinion a fraud has been committed by any person in the promotion, formation, business or conduct of affairs of the company since its formation, the tribunal may, after considering the report, direct that such person or officer shall attend before the Tribunal on a day appointed by it for that purpose, and be examined as to the promotion or formation or the conduct of the business of the company or as to his conduct and dealings as an officer thereof.

The Company liquidator shall take part in the examination, and for that purpose he or it may, if specially authorised by the tribunal in that behalf, employ such legal assistance as may be sanctioned by the tribunal. [Section 300(2)]

The person shall be examined on oath and shall answer all such questions as the tribunal may put, or allow to be put, to him. [Section 300(3)]

A person ordered to be examined under this section -

(a) shall, before his examination, be furnished at his own cost with a copy of the report of the Company liquidator; and	(b) may at his own cost employ chartered accountant or company secretaries or cost accountant or legal practitioners entitled to appear before the tribunal under section 432, who shall be at liberty to put to him such questions as the tribunal may consider just for the purpose of enabling him to explain or qualify any answers given by him. [Section 300(4)]

DISSOLUTION OF COMPANY BY TRIBUNAL

When the affairs of a company have been completely wound up, the Company Liquidator shall make an application to the tribunal for dissolution of such company. [Section 302(1)]

The Tribunal shall on an application filed by the Company Liquidator under sub-section (1) or when the Tribunal is of the opinion that it is just and reasonable in the circumstances of the case that an order for the dissolution of the company should be made, make an order that the company be dissolved from the date of the order, and the company shall be dissolved accordingly. [Section 302(2)]

A copy of the order shall, within thirty days from the date thereof, be forwarded by the Company liquidator to the registrar who shall record in the register relating to the company a minute of the dissolution of the company. [Section 302(3)]

If the Company Liquidator makes a default in forwarding a copy of the order within the period specified in sub- section (3), the Company Liquidator shall be punishable with fine which may extend to five thousand rupees for every day during which the default continues. [Section 302(4)]

Arrest of person trying to leave India or abscond

The Tribunal, if satisfied that a contributory or a person having property, accounts or papers of the company in his possession is about to leave India or otherwise to abscond, or is about to remove or conceal any of his property, for the purpose of evading payment of calls or of avoiding examination respecting the affairs of the company, the tribunal may cause – (a) the contributory to be detained until such time as the tribunal may order; and (b) his books and papers and movable property to beseized and safely kept until such time as the tribunal maythink fit. [Section 301]

Keraela High Court in the matter of **[Mathew Philip v. Malayalam Plantation Ltd.]** 1994 held that there are three contingencies for dissolution of company:

(1) When company has been completely wound-up	(2) When the court is of the opinion that liquidator cannot proceed with the winding-up of company for want of funds and assets	(3) When the court is of the opinion that liquidators cannot proceed with the winding-up for any other reason.

FRAUDULENT PREFERENCE

Section 328 of the Companies Act, 2013 deals with fraudulent preference. Sub-section (1) of section 328 provides that where a company has given preference to a person who is one of the creditors of the company or a surety or guarantor for any of the debts or other liabilities of the company, and the company does anything or suffers anything done which has the effect of putting that person into a position which, in the event of the company going into liquidation, will be better than the position he would have been in if that thing had not been done prior to six months of making winding up application, the Tribunal, if satisfied that, such transaction is a fraudulent preference may order as it may think fit for restoring the position to what it would have been if the company had not given that preference.

According to sub-section (2), if the Tribunal is satisfied that there is a preference transfer of property, movable or immovable, or any delivery of goods, payment, execution made, taken or done by or against a company within six months before making winding up application, the Tribunal may order as it may think fit and may declare such transaction invalid and restore the position.

Liabilities and Rights of Certain Persons Fraudulently Preferred

Where a company is being wound up and anything made, taken or done after the commencement of this Act is invalid under section 328 as a fraudulent preference of a person interested in property mortgaged or charged to secure the company's debt, then, without prejudice to any rights or liabilities arising, apart from this provision, the person preferred shall be subject to the same liabilities, and shall have the same rights, as if he had undertaken to be personally liable as a surety for the debt, to the extent of the mortgage or charge on the property or the value of his interest, whichever is less. [Section 331(1)]

The value of the interest of the person preferred under sub-section (1) shall be determined as at the date of the transaction constituting the fraudulent preference, as if the interest were free of all encumbrances other than those to which the mortgage or charge for the debt of the company was then subject. [Section 331(2)]

On an application made to the tribunal with respect to any payment on the ground that the payment was a fraudulent preference of a surety or guarantor, the tribunal shall have jurisdiction to determine any questions with respect to the payment arising between the person to whom the payment was made and the surety or guarantor and to grant relief in respect thereof, notwithstanding that it is not necessary so to do for the purposes of the winding up, and for that purpose, may give leave to bring in the surety or guarantor as a third party as in the case of a suit for the recovery of the sum paid. [Section 331(3)]

The provisions of sub-section (3) shall apply *mutatis mutandis* in relation to transactions other than payment of money. [Section 331(4)]

COMPANIES (WINDING-UP) RULES, 2020

Ministry of Corporate Affairs notified Companies (Winding-Up) Rules, 2020 through Notification No. G.S.R. 46(e) on 24th January, 2020. These rules shall apply to winding-up under the Companies Act 2013. These rules came into force from 1st April, 2020.

The rules are applicable to companies going into winding-up for the circumstances mentioned under section 271 as well as summary procedure for liquidation under section 361 of the Companies Act, 2013. The summary procedure entails appointment of an official liquidator by the Central Government, followed by the official liquidator immediately thereafter taking into his custody all the assets, effects and Actionable claims to which the company is or appears to be entitled, who will then submit a report to the Central Government within 30 days of his appointment. The rules have been divided into 6 parts comprising of 191 rules and 95 forms.

'Winding-up Rules' among other things provide for summary procedure for winding-up of companies having specified thresholds. The winding-up of companies falling within the specified thresholds will henceforth require the approval of the Central Government instead of the National Company Law Tribunal (NCLT).

Notification of these rules is expected to reduce the burden at the level of NCLT as summary procedure for liquidation can now be filed with the Central Government.

> An important feature of these Rules is the summary procedure for liquidation introducedthrough Part V. An important factor for such summary winding-up is that the Central Government will provide required approvals to such companies for the normal winding-up process which is otherwise undertaken throughthe NCLT, thereby reducing the burden on NCLTand greatly shortening the overall winding-uptimelines.

Currently, the proceedings pertaining to voluntary winding up and winding up on the grounds of inability to pay debts are governed by the insolvency and Bankruptcy Code 2016, which provides for time-bound speedy dissolution of a company.

However, winding-up proceedings on the ground other than inability to pay debts continues to be governed by the Companies (Court) Rules, 1959 which were notified nearly 60 years ago by the Supreme Court and required suitable amendments in view of the notification of the Companies Act, 2013 and the Insolvency and Bankruptcy Code, 2016.

Summary Procedure for liquidation

These rules allow following classes of companies to close their business by making a winding-up application to Central Government without going to NCLT.

Companies accepting deposit and having total outstanding deposits	upto Rs.25 lacs*
Companies having total outstanding loan including secured loan	upto Rs.50 lacs*
Companies having total turnover	upto Rs.50 Crores*
Companies with paid-up capital	upto Rs.1 Crore*

**based on latest audited balance sheet.*

- In addition, companies having book value of assets upto Rs.1 Crore (currently specified under section 361(1) (i)) of the Companies Act, 2013, can also approach Central Government for liquidation.
- The provisions of the Rules related to filing and audit of the Company Liquidator's accounts and its procedure (rule 91 to 99 of the rules) and disposing of assets (rule 165 to 167 of the rules) shall be applicable to above class of companies with modification that the word 'Tribunal' shall be considered as 'Central Government'.

Other procedural aspects are as under:

- The rules lay down the process for meeting of creditors and contributories of the company, and specify the scenarios in which creditors can vote.
- The rules make it necessary for all the money lying in the bank account of Company liquidator which is not immediately required for the purposes of winding up, to be invested in government securities or in interest bearing deposits in any scheduled bank.
- The rules lay down the procedure for maintenance of registers and books of accounts by the Company liquidator.
- The rules also outline the procedure for creditors to prove their debts and claims against the company and if the proof of such debt gets rejected by the Company liquidator, there is also a provision and process for creditor to make an appeal to tribunal.

CASE LAWS

Case-1

In the matter of ***'Indiabulls Housing Finance Ltd. v. Shree Ram Urban Infrastructure Ltd.',*** the Indiabulls Housing Finance Ltd. (appellant) had initiated Corporate insolvency resolution Process against Shree Ram Urban Infrastructure Ltd. (Corporate debtor) under Section 7 of the Insolvency and Bankruptcy Code, 2016.

The National Company law tribunal, Mumbai Bench by impugned order dated 18th May, 2018 dismissed the application as not maintainable in view of the fact that the winding-up proceeding against the Corporate Debtor had already been initiated by the High Court of Bombay.

Thus, the issue that fell for consideration before the National Company Law Appellate Tribunal was whether an application under Section 7 of the Code is maintainable when winding-up proceeding against the Corporate debtor has already been initiated?

NCLAT decision

In the said appeal the NCLAT examined judgments governing the issue to hold that the High Court of Bombay has already ordered for winding-up of Corporate debtor, which is the second stage of the proceeding, thus question of initiation of 'Corporate Insolvency Resolution Process' which is the first stage of resolution process against the same Corporate debtor does not arise.

While arriving at its judgment, the NCLAT relied on the case of Forech India Pvt. ltd. Vs. Edelweiss assets reconstruction Company Ltd. & Aanr., wherein the NCLAT observed that if a Corporate insolvency resolution has started or on failure, if liquidation proceeding has been initiated against the Corporate debtor, the question of entertaining another application under Section 7 or Section 9 against the same very Corporate debtor does not arise, as it is open to the 'Financial Creditor' and the 'Operational Creditor' to make claim before the Insolvency Resolution Professional/Official Liquidator.

The NCLAT further opined that once second stage i.e. liquidation (winding-up) proceedings has already been initiated, the question of reverting back to the first stage of Corporate Insolvency Resolution Process or preparation of Resolution Plan does not arise.

In view of the facts of the present case, the NCLAT concluded that as the High Court of Bombay had already ordered winding-up of Corporate debtor and the same has been initiated, therefore, initiation of Corporate Insolvency Resolution Process against the Corporate debtor did not arise.

Case-2

In the matter of ***'Amar Remedies Limited',*** the applicant filed an application before NCLT, Mumbai Bench under section 110 of the Insolvency and Bankruptcy Code, 2016 suppressing the material facts that liquidation order had been passed in a winding-up petition against the corporate debtor.

The NCLAT lt Mumbai Bench observed: "...the corporate applicant suppressed this material fact, knowing it to be material, and filed the petition under section 10 and in contravention of Rule 10 of Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016. The alleged Act of the corporate applicant is punishable under section 77(a) of the Iinsolvency and Bankruptcy Code 2016.

Accordingly, it directed the Registrar of Companies to lodge prosecution against the applicant under section 77(a) of the Code. Iit rejected application with costs of Rs.10 lakh, which shall be paid by the applicant in the account of the Prime Minister's National Relief Fund.

LESSON ROUND-UP

- The Companies Act, 2013 contains provisions relating to winding-up of companies. However, IBC has made substantial changes in these provisions.
- The main purpose of winding-up of a company is to realize the assets and pay the debts of the company expeditiously and fairly in accordance with the law.
- Winding-up means winding-up under the Companies Act, 2013 or liquidation under the Insolvency and Bankruptcy Code, 2016, as applicable.
- The Companies Act, 2013 shall continue to govern winding-up of companies on various other grounds excluding inability to pay debts, which shall be dealt under the Insolvency and Bankruptcy Code, 2016.
- Sections 270 to 288, Sections 290 to 303, Section 324 and Sections 326 to 365 of Chapter XX of the Companies Act, 2013 contain the provisions related to winding up of the company.
- Section 271 of the Companies Act, 2013 contains circumstances under which a company may be wound-up by the Tribunal (NCLT).
- Section 275 contains provisions relating to the appointment of liquidator.
- Section 281 provides the particulars that a report submitted by liquidator shall contain. Section 287 contains provisions relating to the Advisory Committee.
- Section 290 provides for the powers and duties of the Company liquidator.

- The Companies Act, 2013 has only provisions relating to winding-up of solvent companies through the NCLT, and winding-up of unregistered companies.
- The Companies (Winding-up) Rules, 2020 under the Companies Act, 2013 have been notified by the Ministry of Corporate Affairs on 24th January 2020. These Rules have come into force from 1st April, 2020.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).

1. What are the important changes brought about by the Insolvency and Bankruptcy Code, 2016 in the provisions relating to winding-up under the Companies Act, 2013?
2. Discuss with the help of a decided case law whether a profit making company can be wound-up for just and equitable reasons.
3. Eexplain the constitution and role of the Advisory Committee in the winding-up process.
4. Ddiscuss the powers and duties of Company liquidator under section 290 of the Companies Act, 2013.
5. Examine whether a secured creditor is entitled to file a winding-up petition after having obtained a decree from the Debt Recovery Tribunal.
6. Workmen can be heard but they cannot file petition for winding-up of a company. Discuss.
7. Discuss the provisions of Companies (Winding-up) Rules, 2020.

Strike Off and Restoration of Name of the Company and LLP

Lesson 26

KEY CONCEPTS

■ Striking off Company ■ Striking off LLP ■ Restoration of Name

Learning Objectives

To understand:

- Circumstances under which name of the company Struck off from the Register
- Circumstances under which name of the LLP is Struck off from the Register
- Procedure for Striking off the Name
- Procedure for Restoration of the Name

Lesson Outline

- Introduction
- Ways of Striking off of Companies
- Strike off by ROC
- Strike off by the Company
- Striking off the name of the LLP from the Register of LLP
- Procedure of Striking Off
- Liabilities of partners to continue after Strike Off
- Restoration of LLP
- Procedure for making Application to NCLT
- Lesson Round-Up
- Gossary
- Test Yourself
- List of Further Readings
- Other References (Including Websites/Video Links)

REGULATORY FRAMEWORK

- Companies Act, 2013
- Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016
- Limited Liability Partnership Act, 2008
- Limited Liability Partnership Rules , 2009

INTRODUCTION

The Ministry of Corporate Affairs ("MCA") vide Notification dated 26th December, 2016 notified Sections 248 to 252 of the Companies Act, 2013 ("Act") dealing with the provision for Removal of Names of Companies from the Register of Companies ("ROC"). The provisions relating to strike off provide an opportunity to the non working companies to get their names struck off from the records of the ROC. The MCA had also issued the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016 ("Rules") to be effective from the same date i.e. 26th December, 2016 in order to provide procedural aspects of striking off.

WAYS OF STRIKING OFF OF COMPANIES

A company can be struck off by any of the following modes:

- *Suo moto* by the ROC under Section 248(1) of the Act; or
- An application by the company for removal of name/ strike off of company under Section 248(2) of the Act.

A company which is undergoing the process of 'Striking Off' either voluntarily or by an action of the ROC is given the status as 'Striking Off' and the status of the company is changed to 'Dissolved' or 'Liquidated' when affairs of the company are completely wound-up by following the provision of winding-up of company. After dissolution or liquidation, the company ceases to exist.

The provisions of Sections 248 to 252 of the Companies Act, 2013 read with Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016 deal with the removal of names of companies from the Register of Companies.

Legal Framework dealing with the provisions of:

(i) Strike Off by ROC

In case of an existing company which has failed to commence its business within one year of its incorporation or is not carrying on any business or operation for a period of two immediately preceding financial years and has not made any application within such period for obtaining the status of a dormant company under section 455 of the Act or the subscribers to the memorandum have not paid the subscription and a declaration to this effect has not been filed within 180 days of incorporation or it is revealed after a physical verification that the company is not carrying on any business or operations, the Registrar can suo moto after giving notice and opportunity of being heard, strike off the name of the company from the register of companies, and publish notice thereof of the striking off of the name of the company from the register of companies in the Official Gazette and on the publication of this notice in the Official Gazette, the company shall stand dissolved.

(ii) Strike Off by the company

Striking off under Chapter XVIII of the Companies Act, 2013 can also be by way of an application filed by the company with the ROC for removing its name from the Register of Companies on all or any of the grounds mentioned above. A company may file such an application, after extinguishing all its liabilities, by a special resolution or consent of seventy-five percent members in terms of paid-up share capital. On receipt of the application along with necessary fees, the Registrar shall issue a public notice for intimating the general public about the receipt of an application for removal of name of the company and giving a chance to the creditors and general public to submit their objection, if any, to the proposed application. In case no objection is received after the expiry of the time mentioned in the notice, the ROC may proceed to strike off the name of the company from the Register of Companies and shall publish a notice thereof in the Official Gazette. On publication in the Official Gazette of this notice, the name of the company stands struck off with effect from the date mentioned therein and the company shall stand dissolved.

Strike Off by ROC *Suo Motu*

Subject to the provisions of section 248(1) of the Act read with Rule 3 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016, in the following cases, the Registrar can *suo moto* remove the name of the company from the Register:

(a) a company has failed to commence its business within one year of its incorporation or;

(b) a company is not carrying on any business or operation for a period of two immediately preceding financial years and has not made any application within such period for obtaining the status of a dormant company under section 455 of the Companies Act, 2013; or

(c) the subscribers to the memorandum have not paid the subscription which they had undertaken to pay at the time of incorporation of a company and a declaration to this affect has not filed within 180 days of its incorporation under section 10A(i). This provision is applicable to companies incorporated after 02nd November, 2018 ; or

(d) the company is not carrying on any business or operations as revealed after the physical verification carried out under section 12(9) of the Act.

Before removal of the name of the company from the Register, the ROC is required to send a notice in Form STK 1 to the company and all the directors of the company, of his intention to remove the name of the company from the register of companies. Such a notice should contain the reasons for which the name of the company is to be removed from the Register of Companies. Such a notice should be sent to all the directors of the company at the addresses available on record, by registered post with acknowledgement due or by speed post. On receipt of such a notice, the company and all the directors of the company are required to send their representations along with copies of the relevant documents, if any, explaining the reasons as to why the name of the company should not be removed from the Register of Companies. Such representations should be given within a period of thirty days from the date of the notice.

Procedure to be followed by ROC for striking of the name of the company on suo motu basis:

Service of notice by ROC
Reply to the notice from the company
Consideration of the representation made by the company
Publication of notice of strike off by the ROC
Intimation to regulatory authorities
Striking off / Removal of the name of the company
Provision for realisation of amount due
Notice of dissolution of the company by the ROC

1. **Service of notice by ROC:** The ROC is required to send a notice in Form STK 1 to the company and all the directors of the company, of his intention to remove the name of the company from the Register of

Companies. Such a notice shall contain the reasons on the basis of which the name of the company is to be removed from the Register of Companies. Such a notice should be sent to all the directors of the company at the addresses available on record, by registered post with acknowledgement due or by speed post.

2. **Reply to the Notice from the company:** On receipt of such a notice, the company and all the directors of the company, are required to send their representations along with copies of the relevant documents, if any, explaining the reasons as to why the name of the company should not be removed from the Register of Companies. Such a representation should be given within a period of thirty days from the date of the notice.

3. **Consideration of the representation made by the company:** The ROC will consider the representation made by the company and all the directors of the company. If the ROC is not satisfied with the representation made by the company and its directors, it may proceed to strike off the name of company.

4. **Publication of notice of strike off by ROC:** The notice for removal of the name of the company should be in form STK 5 for the information of the general public and should be:

   (i) placed on the official website of the Ministry of Corporate Affairs on a separate link established on such website in this regard;

   (ii) published in the Official Gazette;

   (iii) published in Form No. STK 5A in English language in a leading English newspaper and at least once in vernacular language in a leading vernacular language newspaper, both having wide circulation in the State in which the registered office of the company is situated.

   Such a publication is required to be given for the information of the general public in order to enable the general public to give their objections, if any, to the proposed removal / striking off of name of the companies from the Register of Companies and requiring them to send their objection to the ROC within thirty days from the date of publication of the notice.

5. **Intimation to regulatory authorities:** Intimation about the proposed action of removal or striking off the names of company should be sent to the Income-tax authorities, central excise authorities and service-tax authorities having jurisdiction over such a company. Such intimation should be given to enable the authorities to give their objections, if any. Such objections are required to be given within a period of thirty days from the date of issue of the letter of intimation.

6. **Striking off / Removal of the name of the company:** After expiry of thirty days from the date of issue of the letter of intimation, if there are no objections received within thirty days from the general public or respective authority and unless cause to the contrary is shown by the company, the ROC can proceed to strike off or remove the name of the company from the Register of Companies.

7. **Provision for realisation of amount due:** The ROC before passing an order for Striking off / Removal of the name of the company should satisfy himself that sufficient provision has been made for s realisation of all amount due to the company and for the payment or discharge of its liabilities and obligations by the company within a reasonable time. The ROC can obtain necessary undertakings from the managing director, director or other persons in charge of the management of the company. Notwithstanding the undertakings, the assets of the company shall be made available for the payment or discharge of all its liabilities and obligations even after the date of the order removing the name of the company from the Register of Companies.

8. **Notice of dissolution of the company by the ROC:** After the expiry of the time mentioned in the notice, the ROC can strike off the name of the company from the Register. The notice of striking off the name of the company from the Register of Companies and its dissolution should be published in the Official Gazette in Form STK 7 and the same should also be placed on the official website of the Ministry of Corporate Affairs. The company shall stand dissolved on the publication of this notice in the Official Gazette.

Strike Off by Way of Filing an Application by the Company

Strike off provisions gives a choice or an option to non working companies to remove its name from the Register of Companies. There are many companies which are registered with ROC but due to various reasons they are not operative. The strike off gives an option to such companies to apply to ROC for removal of their name from the Register of Companies. The procedure of this exit is now governed under section 248(2) of Companies Act, 2013 read with Rule 4 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016. This act is a speedy way to close down a company being non–operational over a period of time.

Subject to the provisions of section 248 (2) of companies Act 2013 read with Rule 4 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016, the company can on its own file an application for removal of name of company from the Register of companies.

Type of Companies which cannot be removed under these provisions, viz., Section 248(1) & (2) of the Act:

(i) Listed Companies;

(ii) Companies registered under section 8;

(iii) Companies having charges which are pending for satisfaction;

(iv) Companies whose application for compounding is pending for compounding of offences committed by the company or any of its officers in default;

(v) Companies against which any prosecution for an offence is pending in any court;

(vi) Vanishing Companies;

(vii) Companies that have been delisted due to non-compliance of listing regulations or listing agreement or any other statutory laws;

(viii) Companies where inspection or investigation is ordered and being carried out or actions or such order are yet to be taken up or were complete but prosecutions arising out of such inspection or investigation are pending in the court;

(ix) Companies which have accepted public deposits which are either outstanding or the company is in default in repayment of the same;

(x) Companies where notices under section 234 of CA 1956 or 206 or 207 of the CA 2013 have been issued by the Registrar or Inspector and reply thereto is pending or report under section 208 is pending or where any prosecution arising out of such inquiry or scrutiny, if any, is pending with the court.

A company through its board of directors, can file an application for removal of name of company from the Register of Companies on the following grounds:

(a) Where a company has failed to commence its business within one year of its incorporation; or

(b) Where a company is not carrying on any business or operation for a period of two immediately preceding financial years and has not made any application within such period for obtaining the status of a dormant company under section 455 of the Companies Act, 2013; or

(c) the subscribers to the memorandum have not paid the subscription which they had undertaken to pay at the time of incorporation of a company and a declaration to this effect has not been filed within 180 days of its incorporation. This provision is applicable to companies incorporated after 02nd November, 2018; or

(d) the company is not carrying on any business or operations as revealed after the physical verification carried out under section 12(9).

Before making an application to the ROC for removal of the name of the company, the board of directors of the company shall take all the steps necessary in order to extinguish all its liabilities. Approval of the shareholders by way of special resolution or consent of seventy five percent members in terms of paid up share capital is also required to be taken for filing an application to the ROC for the removal of the name of the company from the Register of Companies. In the case of a company regulated under a Special Act, approval of the regulatory body constituted or established under that Act shall also be obtained and enclosed with the application.

Situations in which a company cannot apply for strike off under Section 248(2) of the Act:

The Company shall not make any application for the strike off of the company, if at any time in the previous 3 months, the company has done any of the below mentioned activities:

i. Has changed its name; or

ii. Has shifted its registered office from one State to another; or

iii. has made a disposal for value of property or rights held by it, immediately before cesser of trade or otherwise carrying on of business, for the purpose of disposal for gain in the normal course of trading or otherwise carrying on of business; or

iv. has engaged in any other activity except the one which is necessary or expedient for the purpose of making an application under that section, or deciding whether to do so or concluding the affairs of the company, or complying with any statutory requirement; or

v. has made an application to the Tribunal for the sanctioning of a scheme of compromise or arrangement and the matter has not been finally concluded; or

vi. is being wound up under Chapter XX of the Companies Act, 2013 or under the Insolvency and Bankruptcy Code, 2016.

An application for striking off the name of the company under Section 248(2) of the Act shall be withdrawn by the company or rejected by the ROC as soon as the above stated conditions are brought to notice. In case of violation of the above provision, the company shall be punishable with fine which may extend to one lakh rupees.

Procedure of striking off of the name of the company by way of an application to ROC

The board of directors of the company shall follow the following procedure for removal of name of the company from the Register of Companies maintained by the ROC:

(i) Call and hold Board Meeting to pass Board resolution for the purpose of striking off of the name of the company from the Register maintained by the ROC, subject to the approval of the shareholders of the company, and to authorize any director to file an application and for fixing date, time and venue for the Extraordinary General Meeting of the shareholder.

(ii) After passing of Board resolution, if there is any liability in the company, the company will set off / pay all its liabilities.

(iii) Every director of the company should sign and execute indemnity bond duly notarised by every director in Form STK 3 and Affidavit in Form STK 4. In case director is a foreign national or non-resident Indian, the documents should be notarized or apostilled or consularised.

(iv) Company should get the statement of accounts in Form STK-8 containing the assets and liabilities of the company made up to a day, not more than thirty days before the date of application. Such a statement should be certified by a Chartered Accountant.

(v) General Meeting should be held on the day, date, time and venue as fixed earlier for passing of the special resolution.

(vi) Within thirty days from the date of the passing of the special resolution in the General Meeting or after obtaining consent, company should file MGT-14.

(vii) Approval of concerned authorities is required in case of a company regulated by any other authority.

(viii) Thereafter, an application for removal of the name of the company shall be made in Form STK-2 along with the fee of ten thousand rupees.

Application for Removal of Name of Company

Rule 4(1) of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016 provides that an application for removal of name of a company under sub-section (2) of section 248 shall be made to the Registrar, Centre for Processing Accelerated Corporate Exit in Form No. STK-2 along with fee of ten thousand rupees.

Provided that the company shall not file an application unless it has filed overdue financial statements under section 137 and overdue annual returns under section 92, up to the end of the financial year in which the company ceased to carry its business operations:

Provided further that in case a company intends to file the application after the action under subsection (1) of section 248 has been initiated by the Registrar, it shall file all pending financial statements under section 137 and all pending annual returns under section 92, before filing the application:

Provided also that once notice under sub-section (5) of section 248 has been issued by the Registrar for publication pursuant to the action initiated under sub-section (1) of section 248, a company shall not be allowed to file the application under this sub-rule.

Rule 4(2) provides that every application under sub-rule (1) shall accompany a no objection certificate from appropriate Regulatory Authority concerned in respect of following companies, namely: -

(i) companies which have conducted or conducting non-banking financial and investment activities as referred to in the Reserve Bank of India Act, 1934 or rules and regulations thereunder;

(ii) housing finance companies as referred to in the Housing Finance Companies (National Housing Bank) Directions, 2010 issued under the National Housing Bank Act, 1987;

(iii) insurance companies as referred to in the Insurance Act, 1938 or rules and regulations thereunder;

(iv) companies in the business of capital market intermediaries as referred to in the Securities and Exchange Board of India Act, 1992 or rules and regulations thereunder;

(v) companies engaged in collective investment schemes as referred to in the Securities and Exchange Board of India Act, 1992 or rules and regulations thereunder;

(vi) asset management companies as referred to in the Securities and Exchange Board of India Act, 1992 or rules and regulations thereunder;

(vii) any other company which is regulated under any other law for the time being in force.

As per Rule 4(3), the application in Form STK 2 shall be accompanied by -

(i) indemnity bond duly notarised by every director in Form STK 3;

Provided that in case of a -

(a) Government company in which the entire paid up share capital is held by the Central Government, or by any State Government or Governments or by the Central Government and one or more State Governments; or

(b) subsidiary of a Government company, referred to in clause (a), in which the entire paid up share capital is held by that Government company, a duly notarised indemnity bond in Form STK-3A shall be given by an authorised representative, not below the rank of Under Secretary or its equivalent, in the administrative Ministry or Department of the Government of India or the State Government, as the case may be, on behalf of the company.

(ii) a statement of accounts in Form No. STK-8 containing assets and liabilities of the company made up to a day, not more than thirty days before the date of application and certified by a Chartered Accountant;

(iii) An affidavit in Form STK 4 by every director of the company;

(iv) a statement regarding pending litigations, if any, involving the company.

Rule (3A) states that the Registrar, Centre for Processing Accelerated Corporate Exit established under sub-section (1) of section 396, shall be the Registrar of Companies for the purposes of exercising functional jurisdiction of processing and disposal of applications made in Form No. STK-2 and all matters related thereto under section 248 having territorial jurisdiction all over India.

According to Rule (4) of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016:

(a) Where the Registrar, on examining the application made in Form STK-2, finds that it is necessary to call for further information or finds such application or any document annexed therewith is defective or incomplete in any respect, he shall inform to the applicant to remove the defects and re-submit the complete Form within fifteen days from the date of such information, failing which the Registrar shall treat the Form as invalid in the electronic record, and shall inform the applicant, accordingly.

(b) After the re-submission of the Form or document, if the Registrar finds that the Form or document is defective or incomplete in any respect, he shall give further time of fifteen days to remove such defects or complete the Form, failing which the Registrar shall treat the Form as invalid in the electronic record and shall inform the applicant, accordingly.

(c) Any re-submission of the application in Form STK-2 made prior to the commencement of the Companies (Removal of Names of Companies from the Register of Companies) Amendment Rules, 2022 shall not be counted for the purposes of reckoning the maximum number of re-submissions of such Form.

Manner of Filing of Application

As per Rule 5 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016:

(1) The application in Form STK 2 shall be signed by a director duly authorised by the Board in their behalf.

(2) Where the director concerned does not have a registered digital signature certificate, a physical copy of the form duly filled in shall be signed manually by the director duly authorised in that behalf and shall be attached with the Form STK 2 while uploading the form.

Form to be Certified

Rule 6 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016 provides that the Form STK 2 shall be certified by a Chartered Accountant in whole time practice or ***Company Secretary in whole time Practice*** or Cost Accountant in whole time practice, as the case may be.

Manner of Publication of Notice

According to Rule 7of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016:

(1) The notice under sub-section (1) or sub-section (2) of section 248 shall be in Form STK 5 or STK 6, as the case may be, and be-

(i) placed on the official website of the Ministry of Corporate Affairs on a separate link established on such website in this regard;

(ii) published in the Official Gazette;

(iii) published in English language in a leading English newspaper and at least once in vernacular language in a leading vernacular language newspaper, both having wide circulation in the State in which the registered office of the company is situated.

Provided that in case of any application made under sub-section (2) of section 248 of the Act, the company shall also place the application on its website, if any, till the disposal of the application.

Provided further that the publications of notice under clause(iii) of this sub-rule, in respect of cases falling under sub-section (1) of section 248 shall be in Form No. STK 5A.

(2) The Registrar of Companies shall, simultaneously intimate the concerned regulatory authorities regulating the company, viz, the Income-tax authorities, central excise authorities and service-tax authorities having jurisdiction over the company, about the proposed action of removal or striking off the names of such companies and seek objections, if any, to be furnished within a period of thirty days from the date of issue of the letter of intimation and if no objections are received within thirty days from the respective authority, it shall be presumed that they have no objections to the proposed action of striking off or removal of name.

Manner of Notarisation, Appostilisation or Consularisation of Indemnity Bond and declaration in case of Foreign Nationals or Non-Resident Indians

Rule 8 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016 provides that if the person is a foreign national or non-resident Indian, the indemnity bond, and declaration shall be notarised or appostilised or consularised.

Notice of Striking Off and Dissolution of Company

Rule 9 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016 states that the Registrar shall cause a notice under subsection (5) of section 248 of striking off the name of the company from the register of companies and its dissolution to be published in the Official Gazette in Form STK 7 and the same shall also be placed on the official website of the Ministry of Corporate Affairs.

Liabilities of directors, managers, officers and members to be continue

The liability, if any, of every director, manager or other officer who was exercising any power of management, and of every member of the company dissolved under section 248(5) of the Act, shall continue and may be enforced as if the company had not been dissolved.

List of STK forms

Sr. No	Name of Form	Purpose	Governed by
1	Form STK-1	Notice by ROC for removal of name of a company from the Register of Companies.	Section 248(1) of the Companies Act,2013& rule 3 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016.
2	Form STK-2	Application by company to ROC for removing its name from register of Companies.	Section 248(2) of the Companies Act, 2013 & Rule 4(1) of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016.
3	Form STK-3	Indemnity Bond (to be given individually or collectively by every director).	Pursuant to clause (i) of sub-rule (3) of rule 4 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016.
4	Form STK-4	Affidavit (to be given individually by every Director).	Section 248(2) of the Companies Act, 2013 & clause (iii) of sub-rule (3) of Rule 4.
5	Form STK-5	Public Notice	Section 248(1) & (4) of the Companies Act, 2013 & rule 7 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016.

Sr. No	Name of Form	Purpose	Governed by
6	Form STK-5A	Public Notice	Section 248(1) & (4) of the Companies Act, 2013 & rule 7(1) of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016.
7	Form STK-6	Public Notice	Section 248(2) & (4) of the Companies Act, 2013 & rule 7 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016.
8	Form STK-7	Notice of Striking Off and Dissolution.	Section 248(5) of the Companies Act, 2013 & rule 9 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016.

Restoration of the company

The ROC can *suo moto,* after issuing the notice under section 248(1) of the Act, strike off the name of the company. It may so happen that the name of the company may be struck off from the Register of Companies by the ROC even though the company is active company due to non-filing of reply to the said notice. In such a case, the directors of such a company have no option but to approach National Comapny Law Tribunal ("NCLT") by making an appeal for the restoration of the name of the company in the Register of Companies maintained by the ROC. The legal provisions related to restoration of name of the struck off companies are given in Section 248 to 252 of the Act read with Rule 87A of the NCLT (Amendment) Rules, 2017 and the Companies (Removal of Name of Companies from the Register of Companies) Rules, 2016.

Appeal to NCLT for restoration of the name of the company

Any person aggrieved by the order of the ROC may file an appeal before the Tribunal within 3 years of the order passed by ROC and if the Tribunal is of the opinion that the removal of name of company from the Register is not justified in view of the absence of any of the grounds on which the order was passed by the ROC, it may pass an order for restoration of the name of the company in the Register of Companies after giving a reasonable opportunity of making representations and of being heard to the ROC, the company and all the persons concerned.

Application to NCLT by ROC for restoration of the name of the company

The ROC may, within a period of three years from the date of passing of the order dissolving the company under section 248, file an application before the Tribunal seeking restoration of name of such company, if it is satisfied that the name of the company has been struck off from the Register of Companies, either inadvertently or on the basis of incorrect information furnished by the company or its directors.

Application to NCLT for restoration of the name of the company by Company or any member or creditor or workmen:

The Tribunal, on an application made by the company, member, creditor or workman, aggrieved by the company having its name struck off from the Register of Companies, before the expiry of 20 years from the publication in the Official Gazette of the notice of dissolution of the company, if satisfied that:

(a) the company was, at the time of its name being struck off, carrying on business or in operation; or

(b) otherwise it is just that the name of the company be restored to the Register of Companies, may order the name of the company to be restored to the Register of Companies. Further, the Tribunal may also pass an order and give such other directions and make such provisions as deemed just for placing the company and all other persons in the same position as nearly as may be as if the name of the company had not been struck off from the Register of Companies.

A copy of the order passed by the Tribunal shall be filed by the company with the ROC within thirty days from the date of the order and on receipt of the order, the ROC shall cause the name of the company to be restored in the Register of Companies and shall issue a fresh certificate of incorporation.

In the case of *Vbuiltfine Properties Private Ltd(Appellant) vs. Registrar of Companies, Mumbai (Respondent) Company Appeal (AT) No.27 of 2023,* the appellant's name was struck of from the register of companies and an appeal for restoration of the name was filed by the Appellant before the NCLT. By the impugned order under challenge, NCLT directed the ROC Mumbai to restore the name of the company i.e., Vbuiltfine Properties Pvt Ltd, to the register of Registrar of Companies with imposition of cost of Rs. 5,00,000/- Appellant challenged the imposition of this huge cost.

National Company Law Appellate Tribunal in its judgement dated August 18, 2023 inter alia observed that ongoing through the aforesaid order it is difficult to infer as to under what circumstances the company petition was allowed and direction was issued for restoration of the name of the company along with imposition of costs.

It is evident from the impugned order that the company petition was preferred under Section 252(1) of the Companies Act, 2013. However, since the date of striking off the name of the company is not mentioned. It is difficult to infer as to whether the petition was filed within three years from the striking off the name of the company or not. The order does not reflect any plausible reason for passing an order for restoration. Similarly, nothing has been indicated as to under what circumstances the cost of Rs.5 lakhs was imposed.

On examination of aforesaid provision, it is evident that from the date of striking off the name of the company from the register of Registrar of Companies, one can prefer an appeal within a period of three years from the date of striking off the name of the company. In the order impugned date of striking off under Section 248(5) of Companies Act, 2013 has not been mentioned. On examination of the impugned order, it is evident that though date of striking off was not mentioned, the appeal was preferred after four years. The order on this issue appears to be completely vague. Moreover, if the NCLT was exercising its jurisdiction under Section 252(3) of the Companies Act, 2013, in such situation the appellant was required to satisfy the NCLT that on the date of striking off the company, the company was carrying on business or in operation. There was third condition for passing of the restoration order in case it was otherwise just for restoring the name of the company.

The order does not meet either of the three criteria under Section 252(3) of the Act. Moreover, since the appeal was preferred under Section 252(1) of the Companies Act, 2013 the learned NCLT was required to examine the appeal strictly in accordance with the provision under Section 252(1) of the Companies Act, 2013. In absence of exact date of striking off it would be difficult to approve the impugned order. Moreover, learned NCLT has imposed cost of Rs. 5 lakhs but no plausible reason has been given for imposing such cost. In such view of the matter, we are left with no option but to set aside the order and remit back the matter to the NCLT for passing order afresh after affording opportunity to both the parties i.e., Appellant and ROC.

STRIKING OF THE NAME OF THE LIMITED LIABILITY PARTNERSHIP (LLP) FROM THE REGISTER OF LIMITED LIABILITY PARTNERSHIPS

Similar to the provision of section 248 to 252 of the Companies Act, 2013 read with Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016 dealing with the provision for Removal of Names of Companies from the Register of Companies, Section 75 of the Limited Liability Partnership Act, 2008 read with Rule 37 of the Limited Liability Partnership Rules, 2009 deals with the provision for striking off the name of the Limited Liability Partnership from the Register of limited liability partnerships.

The Ministry of Corporate Affairs ("MCA") had amended Limited Liability Partnership Rules, 2009 by introducing the Limited Liability Partnership (Amendment) Rules, 2017 with effect from 20th May, 2017. With this amendment, LLP Form 24 has been introduced by the MCA to allow easy closure of a LLP by making an application to the ROC for striking off the name of LLP.

Legal Framework

In case of an existing LLP which is not carrying on any business or operation for a period of one year or more, it can make an application in Form 24 to the ROC, with the consent of all partners of the limited liability partnership for striking off its name from the register. Similarly, where the Registrar has reasonable cause to believe that a limited liability partnership is not carrying on business or its operation, in accordance with the provisions of this Act for a period of two years or more, the name of limited liability partnership may be struck off from the register of limited liability partnerships by ROC by taking suo moto action for striking off the name of the LLP. However, before striking off the name of the LLP by the ROC, the ROC shall give reasonable opportunity of being heard to the limited liability partnership and all its partners.

Strike Off by the ROC on suo moto basis

Subject to the provisions of section 75 of the Limited Liability Partnership Act, 2008 read with Rule 37 of Limited Liability Partnership Rules, 2009 as amended from time to time, the ROC can *suo moto* remove the name of the LLP from the Register in case a limited liability partnership is not carrying on any business or operation for a period of two years or more and the ROC has reasonable cause to believe the same. In such a case, the ROC can *suo moto* take the action for striking off the name of the LLP.

Procedure to be followed by the ROC for striking of the name of the LLP on suo moto basis:

Service of Notice by the ROC to the LLP
Reply to Notice
Consideration of the representation made
Publication of Notice
Striking off of the name of the LLP
Provision for realisation of amount due
Notice of dissolution of the LLP

1. **Service of notice by the ROC to the LLP:** Before striking off the name of the LLP, the ROC is required to send a notice to the LLP and all the partners of the LLP of his intention to remove the name of the LLP from the Register of LLP. Such a notice shall contain the reasons for which the name of the LLP is to be removed from the Register.

2. **Reply to Notice:** On receipt of such a notice, the LLP and all the partners of the LLP are required to send their representations along with copies of the relevant documents, if any, explaining the reasons as to why the name of the LLP should not be removed from the Register. Such a representation should be given within a period of one month from the date of the notice.

3. **Consideration of the representation made:** The ROC will consider the representation made. If the Registrar is not satisfied with the representation made by the LLP and its partners, it may proceed to strike off the name of LLP.

4. **Publication of Notice:** The Notice shall be placed on the website of the Ministry of Corporate Affairs for the information of the general public for the period of one month. Such publication is required to be given for the information of the general public in order to enable the general public to give their objections, if any, to the proposed striking off of name of the LLP from the Register and requiring them to send their objection to the ROC within one month from the date of publication of the notice.

5. **Striking off of the name of the LLP:** After the expiry of the time limit of one month and unless cause to the contrary is shown by the LLP, if there are no objections received, the ROC can proceed to strike off the name of the LLP from the Register of LLP.

6. **Provision for realisation of amount due:** The ROC before passing an order for striking off of the name of the LLP should satisfy that sufficient provision has been made for the realization of all amount due to the limited liability partnership and for the payment or discharge of its liabilities and obligations by the limited liability partnership within a reasonable time. The ROC can obtain necessary undertakings from the designated partner or partner or other persons in charge of the management of the limited liability partnership. Notwithstanding the undertakings, the assets of the limited liability partnership shall be made available for the payment or discharge of all its liabilities and obligations even after the date of the order removing the name of the limited liability partnership from the Register.

7. **Notice of dissolution of the LLP:** After the expiry of the time mentioned in the notice of one month for receiving objections from the general public, the ROC can strike off the name of the LLP from the Register and publish notice thereof in the Official Gazette. The LLP shall stand dissolved on the publication of this notice in the Official Gazette.

Strike Off by Way of Filing an Application by the LLP

Subject to the provision of section 75 of the Limited Liability Partnership Act, 2008 read with Rule 37 of the Limited Liability Partnership Rules, 2009, where a limited liability partnership is not carrying on any business or operation for a period of one year or more, such a LLP can make an application for purpose of suo moto striking off the name of the LLP.

Procedure of striking off of the name of the LLP by way of an application to ROC:

1. Calling and holding the meeting of the partners of LLP for making an application in Form 24 for the striking off of the name of the LLP and authorizing the partner to make the application to ROC. The consent of all partners of the limited liability partnership should be obtained before making an application to the ROC for striking off of the name of the LLP.
2. All the pending filings including the Annual Filing of Form 8 and Form 11 up to the end of the financial year in which the limited liability partnership ceased to carry on its business or commercial operations should be completed before making of an application for striking off of the name of the LLP.
3. Approval of concerned authorities should be obtained in case of a LLP regulated by any Special Law.
4. All the Designated Partners of the LLP must execute an affidavit, either jointly or severally, as mentioned as point 5(d) below. Thereafter, an application for striking of the name of the LLP shall be made in Form 24 along with fees as prescribed and along with following documents:
   (a) a statement of account disclosing nil assets and nil liabilities, certified by a Chartered Accountant in practice made up to a date not earlier than thirty days of the date of filing of Form 24.
   (b) copy of acknowledgement of latest Income tax return, where the limited liability partnership has carried out any business and has filed such a return.
   (c) copy of the initial limited liability partnership agreement, if entered into and not filed, along with changes thereof in cases where the LLP has not commenced business or commercial operations since its incorporation.
   (d) an affidavit signed by the designated partners, either jointly or severally, to the effect,—
      (i) that the Limited Liability Partnership has not commenced business or where it commenced business, it ceased to carry on such business from (dd/mm/yyyy);
      (ii) that the limited liability partnership has no liabilities and indemnifying any liability that may arise even after striking off its name from the Register;
      (iii) that the Limited Liability Partnership has not opened any Bank Account and where it had opened, the said bank account has since been closed together with certificate(s) or statement from the respective bank demonstrating closure of Bank Account;
      (iv) that the Limited Liability Partnership has not filed any Income-tax return where it has not carried on any business since its incorporation, if applicable.

(e) Copy of the initial limited liability partnership agreement, if entered into and not filed, along with changes thereof in cases where the Limited Liability Partnership has not commenced business or commercial operations since its incorporation.

(f) Copy of detailed application- mention full details of LLP plus reasons for closure.

(g) Copy of Authority to Make the Application- Duly signed by all the Partners.

The date of cessation of commercial operation is the date from which the Limited Liability Partnership ceased to carry on its revenue generating business and the transactions such as receipt of money from debtors or payment of money to creditors, subsequent to such cessation will not form part of revenue generating business.

5. **Publication of Notice:** The Notice shall be placed on the website of Ministry of Corporate Affairs for the information of the general public for the period of one month.

6. **Striking off of the name of the LLP:** After the expiry of the time limit of one month and unless cause to the contrary is shown by the LLP, if there are no objections received, the ROC can proceed to strike off the name of the LLP from the Register of LLP.

7. **Provision for realisation of amount due:** The ROC, before passing an order for striking off of the name of the LLP, should satisfy that sufficient provision has been made for the realization of all amount due to the limited liability partnership and for the payment or discharge of its liabilities and obligations by the limited liability partnership within a reasonable time. The ROC can obtain necessary undertakings from the designated partner or partner or other persons in charge of the management of the limited liability partnership. Notwithstanding the undertakings, the assets of the limited liability partnership shall be made available for the payment or discharge of all its liabilities and obligations even after the date of the order removing the name of the limited liability partnership from the Register.

8. **Notice of dissolution of the LLP:** After the expiry of the time mentioned in the notice of one month and if the application filed by the company is found acceptable, the concerned ROC can strike off the name of the LLP from the Register and publish notice thereof in the Official Gazette. The LLP shall stand dissolved on the publication of this notice in the Official Gazette.

Liabilities of Partners to be continued after Striking Off

The liability of all designated partners of the limited liability partnership would continue and may be enforced as if the limited liability partnership had not been dissolved.

Power of the Tribunal to wind up

Nothing in these provisions shall affect the power of the Tribunal to wind up a limited liability partnership, the name of which has been struck off from the Register of LLP.

Restoration of the LLP

The ROC can *suo moto* after issuing the notice under section 75, strike off the name of the LLP. In such a case, it may happen that the name of the LLP may be struck off even though the LLP is active, but the ROC removed the name of the LLP from the Register, either inadvertently or due to incorrect information furnished by the LLP or its partners.

In such a case, there is no relief provided in the Limited Liability Partnership Act, 2008 or in the Limited Liability Partnership Rules, 2009 to restore the name of the LLP in the Register, hence, the partners of such a LLP have to approach the jurisdictional High Court by filing writ petition under Article 226 of the Constitution of India for restoration of the name of the LLP in the Register of LLP.

LESSON ROUND-UP

- The Registrar has suo moto power to remove the name of the company and LLP from the Register after complying with the provisions of law. With a view to enable the defunct company / LLP to remove their name from the Register, the provisions are made for such companies / LLP, providing an exit scheme. Such companies / LLP can apply to the Registrar for striking off their name from the Register.
- The provisions of section 248 to 252 of the Companies Act 2013 provide an easy exit to companies and are much speedy as compared to other modes of winding up under the Companies Act, 2013. Even though the company can easily dissolve through this mode and get its name removed from the ROC's Register, the liabilities of every director, officer and members of the company continue and may be enforced in the same manner as if the company had not been dissolved. In addition, by providing restoration provisions, the company which has been struck off may get a chance to restore its name in the Register and acquire 'active' status with the permission of NCLT within 20 years of being struck off.

GLOSSARY

Defunct company : A company which has failed to commence business operations within one year from the date of registration without any proper reason, which is beyond the control ofthe company or where a company has no assets or liabilties. Again, if a company is not filling its balance sheet for many years, then also it will be termed as a defunct company.

Vanishing Company : A company, registered under the Act or previous company law or any other law for the time being in force and listed with Stock Exchange which has failed to file its returns with the Registrar of Companies and Stock Exchange for a consecutive period of two years, and is not maintaining its registered office at the address notified with the Registrar of Companies or Stock Exchange and none of its directors are traceable.

Cessation of commercial operation : It is the date from which the Limited Liability Partnership ceased to carry on its revenue generating business and the transactions such as receipt of money from debtors or payment of money to creditors, subsequent to such cessation will not form part of revenue generating business.

TEST YOURSELF

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Discuss in brief the law to strike off the name of the company on its own accord.
2. State the power of Registrar of Companies to strike off the name of the Company.
3. State the grounds on which the name of a struck off company can be restored.
4. Discuss in brief the law to strike off the name of LLP on its own accord. State the power of Registrar of Companies to strike off the name of the LLP.
5. State the power of the NCLT to restore the name of the struck off LLP.

LIST OF FURTHER READINGS

- Companies Act, 2013
- Insolvency and Bankruptcy Code, 2016 (Bare Act)

OTHER REFERENCES (Including Websites / Video Links)

- https://ibbi.gov.in
- https://mca.gov.in

WARNING

Regulation 27 of the Company Secretaries Regulations, 1982

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PROFESSIONAL PROGRAMME

CORPORATE RESTRUCTURING, VALUATION & INSOLVENCY

GROUP 2 • PAPER 6

(This test paper is for practice and self-study only and not to be sent to the Institute)

Time Allowed: 3 Hours ***Maximum Marks: 100***

Answer ALL questions

PART I: CORPORATE RESTRUCTURING (40 MARKS)

Question No. 1

Kumar Farms Private Limited (hereinafter referred to as "KFPL" and/or "Transferee Company") is a private limited company incorporated and existing under the provisions of the Companies Act, 2013. The entire shareholding (100%) of KFPL is held by the Singhania Family comprising Mr. Ajay, Mrs. Vinay and Mr. Abhishek. KFPL and the Singhania Family are part of the Promoter and Promoter Group of PPAP Limited (hereinafter referred to as "PPAP / Target Company"), a company whose shares are listed on the Stock Exchanges i.e., BSE and NSE. The entire Promoter and Promoter Group holding in PPAP is 64.52% as of June 30, 2023. Copy of Shareholding Pattern of PPAP as disclosed under Regulation 31 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (hereinafter referred to as "SEBI (LODR) Regulations, 2015") for the Quarter ending 30th June 2023.

Out of the Promoter and Promoter Group shareholding of PPAP, KFPL holds 13.28% and shareholders of KFPL viz. Mr. Ajay (27.62%), Mrs. Vinay (3.81%) and Mr. Abhishek (7.16%) are also classified as "Promoter" for more than 3 years. Their consolidated/aggregate shareholding in the PPAP/Target Company is 51.87%. Presently, KFPL is in the process of considering a Scheme of Amalgamation and Arrangement ("Scheme") of below mentioned 10 entities ("Transferor Companies") with KFPL i.e., the Transferee Company:

S. No.	Name	Shareholding Percentage in PPAP/ Target Company as of June 30, 2020	Current Shareholding Percentage in PPAP/ Target Company	Shareholder whether classified as "Promoter" or not
1	NiFoods Private Limited	1.03%	1.05%	Promoter
2	Advance Private Limited	1.56%	1.58%	Promoter
3	Dealtrade Private Limited	1.04%	1.06%	Promoter
4	Littlestar Private Limited	1.39%.	1.41%	Promoter
5	Sri Lehra Private Limited	3.91%	3.98%	Promoter
6	Commosales Limited	NIL	NIL	Promoter
7	Icon Private Limited	NIL	NIL	Promoter
8	Ginius Private Limited	NIL	NIL	Promoter
9	Arhaan Private Limited	NIL	NIL	Promoter
10	Ajay Holdings Private Limited	NIL	NIL	Promoter
	Total	**8.93%**	**9.08%**	

100% of the shareholding of all the aforesaid companies is directly or indirectly held by Mr. Ajay, Mrs. Vinay and Mr. Abhishek. Furthermore, all the aforesaid 10 entities are included in the Promoter and Promoter Group of PPAP. With a view to consolidate the entities so as to eliminate the chain holdings and attain a leaner and more efficient structure from a long-term perspective it is proposed to merge the 10 Transferor Companies with the Transferee Company i.e., KFPL through a Scheme of Amalgamation and Arrangement ("Scheme") under section 230 to 232 of the Companies Act, 2013 ("Act") read with applicable provisions of the Act.

All the Transferor Companies shall stand dissolved pursuant to the proposed Scheme and the entire business and whole of the undertaking of the Transferor Companies, including, without any limitation all the assets and properties of the Transferor Companies, including but not limited to all stocks, assets, investments of all kinds (including shares, scrips, stocks, bonds, debenture stocks, units) shall get transferred to KFPL. Thus the 9.08% shares held by the Transferor Companies in PPAP will stand transferred to KFPL. The same will result in an increase in the holding of KFPL in the Promoter capacity in PPAP from 13.28% to 22.36%. Pursuant to the Scheme, there will be no change in the shareholding percentage of the Singhania Family in KFPL, who will continue to hold 100%. Further, there will be no change in the percentage of Promoter and Promoter Group shareholding of PPAP, which will remain at 64.52%.

As per the Scheme, the entire consideration paid for the amalgamation would be discharged by KFPL by way of the issue of its shares to Mr. Ajay, Mrs. Vinay and Mr. Abhishek. No portion of the consideration would be discharged in the form of cash/cash equivalent.

In view of the above facts, answer the following with reasons:

(i) Whether the proposed transfer of shares from one promoter entity to another, qualifies as normal transfer within the 5% limit as well as inter se transfer not amounting to seeking exemption under Regulation 10 of the SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011?

(ii) Whether normal disclosures under Regulations 29 any other compliance have to be made by the Promoter while filing of forms under Regulation 10 of SEBI (SAST) Regulations, 2011.

(iii) The inter-se transfer of shares among promoter groups though permitted under SEBI (SAST) Regulations, 2011, will it be affecting the proposed preferential offer under SEBI (ICDR) Regulations, 2018?

(iv) Discuss whether the threshold limits for acquisition of shares / voting rights, beyond which an obligation to make an open offer is triggered?

(5 marks each)

Attempt all parts of either Q.No.2 or Q.No.2A

Question No. 2.

(a) Mr. "X" a member of ABC Limited holding 8% of shareholding in the company raised several legal issues pertaining to methodology of the valuation of concerned companies, adequacy of swap ration of 15:1, violation of Section 230 of Companies Act, 2013 in the scheme of amalgamation, challenged to market approach method of valuation and other illegalities which tantamount to Oppression & Mis-Management of the Appellants minority shareholders. Discuss whether Mr. "X" is eligible to raise objection in the scheme of amalgamation.

(b) Every scheme of amalgamation of a Bank is sanctioned under the Banking Regulation Act and aims at securing larger public interest and health of the banking industry. Comment.

(c) Amalgamation is unlike the winding up of a corporate entity, in the case of amalgamation, the outer shell of the corporate entity is undoubtedly destroyed; it ceases to exist. Comment.

(d) Whether Companies Act, 2013 empowers the National Company Law Tribunal to dispense with the meeting of shareholders in Amalgamation? Discuss the scope and ambit of the jurisdiction of the Tribunal while exercising its power in sanctioning the scheme of amalgamation.

(5 marks each)

OR (Alternate question to Q.No.2)

Question No. 2A

(a) PCBL Limited ("Acquirer") is a public listed company. The Acquirer is currently engaged in the following businesses: (i) manufacture and sale of carbon black, and (ii) manufacture of green power. The Acquirer is one of the largest manufacturers of carbon black in India and is a strong global player with a significant customer base in over 50+ countries.

ACP Private Limited ("Target") is a private limited company, with its registered office located in Pune, Maharashtra. The Target is a leading specialty chemicals company, engaged in the manufacture of: (i) water treatment chemicals with key products such as: (a) phosphonates, (b) biodegradable chelating agents, (c) polymers, (d) biocides; and (ii) water treatment chemicals used for scale and corrosion control such as: (i) imidazolines, and (ii) quats, used in oil and gas production.

The Acquirer proposes to acquire 100% equity share capital of the Target from the existing shareholders of the Target. Post the Proposed Combination, the Target will be a wholly-owned-subsidiary of the Acquirer. The Proposed Combination is notifiable to the Hon'ble Competition Commission of India under Section 5(a) of the Competition Act, 2002.

The Proposed Combination will enable the Acquirer to enter the global specialty segments of (i) water treatment chemicals, and (ii) oil and gas chemicals. The Proposed Combination will result in the Target becoming a part of the PCBL Limited, allowing it to access a larger pool of resources, aiding its expansion and growth strategies. Additionally, the Proposed Combination will provide the existing shareholders of the Target an attractive exit opportunity. The Acquirer & Target activities do not exhibit any horizontal, vertical, or complementary overlaps in any of the plausible relevant markets in India.

In view of the above, answer the following:

(i) Whether the Proposed Combination is required to be notified under the green channel route in terms of Regulation 5A and Schedule III of the Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011? Discuss briefly the Green Channel Route.

(ii) In accordance with international best practices, the Competition Commission of India allows for informal and verbal consultation with its staff/ case team prior to filing of notice for a proposed combination in terms of sub section (2) of section 6 of the Competition Act, 2002 ("Act") read with regulations 5 and 5A of Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011. Discuss briefly the Pre-Filing Consultation with Competition Commission of India.

(iii) Discuss the factors that the Competition Commission of India may be taken into account while deciding whether any combination is Appreciable Adverse Effect in Competition (AAEC).

(5 marks each)

(b) The Board of directors of ABC Ltd., a small company is considering to merge with BRQ Ltd., another small company. The Board wants the merger to be fast and seeks your opinion about the conditions to be complied in this respect. Render your opinion based on the provisions of Companies Act, 2013.

(5 marks)

PART II: VALUATION (20 MARKS)

Question No. 3

(a) Assume ABC Manufacturing Company is projected to generate the following cash flows over the next five years:

Year 1: Rs. 500,000

Year 2: Rs. 600,000

Year 3: Rs. 700,000

Year 4: Rs. 800,000

Year 5: Rs. 900,000

The discount rate for ABC Manufacturing Company is determined to be 10%.

Calculate the Present Value (PV) of Cash Flows & Determine the Terminal Value

(b) ABC Tech Solutions is a fast-growing technology company specializing in software development and IT services. The company was founded five years ago and has experienced rapid revenue growth and a strong customer base. The management team is exploring options for fundraising and needs to determine the valuation of the business.

Key Information:

1. Financial Performance:

Year 1: Revenue - $2 million, Net Income - $500,000

Year 2: Revenue - $3 million, Net Income - $800,000

Year 3: Revenue - $5 million, Net Income - $1.2 million

Year 4: Revenue - $7 million, Net Income - $1.8 million

Year 5: Revenue - $10 million, Net Income - $2.5 million

2. *Industry Analysis:*

Comparable companies in the same industry are trading at an average Price-to-Earnings (P/E) ratio of 15x.

The average Enterprise Value-to-Revenue (EV/Revenue) multiple is 2.5x.

3. *Discount Rate:*

10% The discount rate represents the required rate of return considering the risk associated with the investment.

Calculate Average Net Income & Present Value (PV) of Earnings Value.

(5 marks each)

Question No. 4

(a) Discuss the Core Principles of Valuation needs to be followed by Valuers in the process of Amalgamation.

(b) Examine the three Principle Business Valuation Approaches such as Market Approach, Income approach & Asset Approach.

(5 marks each)

PART III: INSOLVENCY(40 MARKS)

Question No. 5.

(a) Mr. “A”, Mr. “B” & Mr. “C” are home buyers, who had opted for allotment in a real estate project of the XYZ Limited. Aggrieved by the delay in the completion of the project, Mr. “A”, Mr. “B” & Mr. “C” approached the State Real Estate Regulating Authority (RERA) which by its orders upheld this entitlement to refund amounts deposited by the, together with interest. In the meantime, proceedings under the Insolvency and Bankruptcy Code, 2016 were initiated against XYZ Limited. In the course of proceedings after due consultations by the Committee of Creditors, a resolution plan was presented to the Adjudicating Authority.

In that plan, a distinction was made between home buyers, who had opted or elected for other remedies such as i.e., applying before the RERA and having secured orders in their favor, and those who did not do so. Home buyers who did not approach authorities under Real Estate Development Authority Act, 2016 were given the benefit of 50% better terms than that given to those who approached RERA or who were decree holders. Mr. “A”, Mr. “B” & Mr. “C” appeal before the Adjudicating Authority; their applications were rejected by the adjudicating authority. Their appeals too were unsuccessful before the NCLAT. Consequently, they have approached Supreme Court.

In view of the above facts, answer the following with reasons:

(i) Whether home *buyers are financial creditors under the IBC?*

(ii) Whether a single homebuyer has the right to initiate an insolvency process against the defaulting builder company under IBC?

(5 marks each)

(b) Discuss the parameters to be met with respect to Group Insolvency Approach in Corporate Insolvency Resolution Process (CIRP) Framework.

(c) Section 95 to Section 100 of the Insolvency and Bankruptcy Code, 2016 are unconstitutional as they violate Article 14 and Article 21 of the Constitution. Comment.

(5 marks each)

Attempt all part of either Q. No. 6 or Q. No. 6A

Question No. 6

(a) The statutory obligation and duty of the resolution professional and liquidator is very clear in the IBC(Code). Section 30 of the Code mandates a resolution professional to examine every resolution plan to be in compliance with the requirements mentioned therein and section 25(2)(i) cast upon him the duty to present all resolution plans at the meetings of the committee of creditors. While during the liquidation process, Regulation 33(3) of the Liquidation Regulations casts an obligation on the liquidator not to proceed with sale of assets and approach AA for necessary directions, if he is of the opinion that there is possible collusion. Resolution Professional and Liquidator should not draw a parallel between the process of submission of resolution plans in the insolvency resolution process with the e-auction process during the liquidation process.

In view of the above, answer the following:

(i) An insolvency professional must not conceal any material information to the IBBI or to the Adjudicating Authority. Critically examine.

(ii) An insolvency professional or liquidator should not itself acquire, directly or indirectly, any of the assets of the debtor, nor knowingly permit any relative to do so. Critically examine.

(iii) When can a liquidator apply for avoidance of preferential transaction?

(5 marks each)

(b) Commercial Wisdom of Committee of the Creditors (CoC) is paramount under the Insolvency and Bankruptcy Code, 2016. Comment.

(5 marks)

OR (Alternate question to Q. No. 6)

Question No. 6A

(a) For the purposes of the Indian insolvency ecosystem, the possibility of cross border insolvency arises when an Indian company has foreign liabilities, assets or operations or when a foreign company has Indian liabilities, assets or operations. For assets, the term “foreign” generally indicates the presence of assets and operations in a foreign jurisdiction. For instance, cash holdings in a bank account in a foreign country, a production facility or an office in a foreign country and so on. However, foreign assets may also take intangible forms, not always be linked with physical presence or human interventions.

In view of the above, answer the following:

(i) How IBC enables Liquidator to relies the assets in a foreign jurisdiction. Discuss.

(ii) Discuss the scope of UNCITRAL Model Law on cross border insolvency.

(5 marks each)

(b) State the eligibility criteria for Pre-packaged Insolvency Resolution Process under IBC.

(c) Discuss the procedure to be followed by Registrar of Company for striking of the name of the company sue motu basis.

(5 marks each)

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