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July 2018

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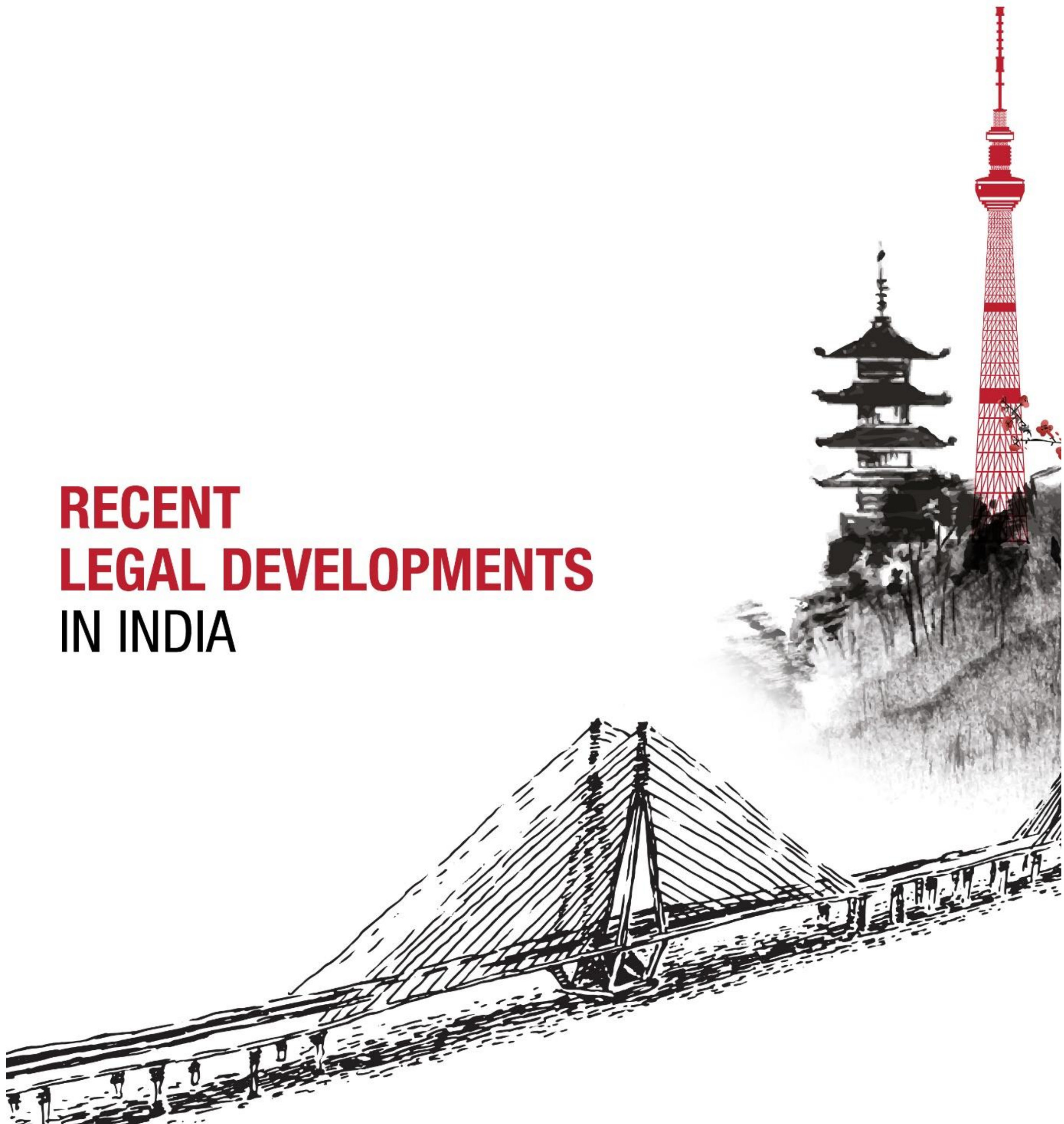

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Our clients generally structure sophisticated corporate & financial transactions or may be involved in complex litigation & dispute resolution proceedings.

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2018年7月

1. **外国からの直接投資**

1.1. **RBIは単一のマスターフォームを導入し、インド企業から受け取ったすべての外国投資を報告します。**

インド準備銀行(**RBI**)は**回覧状**を発行し、単一のマスター・フォーム(**SMF**)を導入して、インドにおける様々なタイプの外国投資に関する既存の報告基準を統合しました。

SMFの目的は、企業名、企業識別番号、入国ルートやセクター・キャップを含む全ての外国投資の詳細など、インド企業の共通の詳細を照合することであると思われます。SMFのドラフトフォーマットに加え、FC-GPR、FC-TRS、InVi、DI、DRR、CN、ESOP等のフォーマットもSMFでは簡略化されています。

1.2. **単一マスター・フォーム・-オンライン・アプリケーション導入の第一段階**

オンライン・アプリケーションFIRMSの第一段階(viz、Entity Master)は、RBIが導入しました。Entity Masterのユーザーマニュアルがオンラインで閲覧できるようになりました。Entity Masterは、6月28日(午後1時)から2018年7月12日に、一般に公開され、データ入力ができるようになります。これらの指示に従わないインド企業は、外国投資(間接外国投資を含む)を受けることができず、非準拠企業として取り扱われます。

1.3. **外国ポートフォリオ投資家(FPI)による債務への投資**

残存期間が1年未満の社債に対するFPIによる投資は、当該外国投資家の社債保有総額の20%の上限が設けられています。カテゴリーの異なる債券に対する20%の投資基準は、継続的に適用されます。投資が20%を超える場合、FPIは6ヶ月以内に保有比率を20%未満に引き下げなければなりません。

2. **コーポレート・コマーシャル**

2.1. **SEBI、上場企業の倒産処理を促進するため、上場廃止・買収規則を改訂**

2018年5月31日、インド証券取引委員会(**SEBI**)は、SEBI(株式および買収)2011年規則(「**株式公開買付け規則**」)およびSEBI(株式上場廃止規則)2009年規則(「**上場廃止規則**」)の修正(まとめて「**修正**」とする)を通知しました。本修正は、2016年**倒産法**の規定に基づき、会社倒産処理手続中の上場会社(**会社債務者**)の取得を促進するために行われたものです。

上場廃止規則

国内会社法審判所(**NCLT**)が**決議案**を承認した場合の、商法に基づく企業倒産処理手続の対象である上場会社の株式の上場廃止については、上場廃止規則は適用されないものとします。

株式公開買付け規則

公開会社株式の取得に際して公開買付を行う義務を規定し、非公開株式の最大75%以上の取得を制限する株式公開買付け規則第3条が改正されました。

現在、NCLTによる決議案の承認に基づき、社債権者の解決権を取得した申込者は、当該社債権者の75%以上の株式を承継することができます。

2.2. **2006年会社改正(会計基準)規則**

企業省は、2006年会社改正規則(会計基準)を、会社改正規則(会計基準)2018年改正規則(**AS規則**)として改正しました。この改正により、AS規則の附属書中の「会計基準(AS)11」パラグラフ32は、累積利益の本国送金による非一体的海外事業からの送金は、投資の返還を構成しない限り、処分の一部を構成しないようにされました。

2.3. **2009年有限責任事業組合規則の改正**

中央政府は2009年有限責任事業組合規則を改正し、2013年会社法に基づき取得したDINをLLP法の適用上十分とすることにより、DPINを取得するための別個の出願の必要性を排除しました。

3. **課税**

3.1. **損害賠償予定に対する物品役務税**

物品およびサービス税(**GST**)は、特定のサービスに関連して履行された契約の履行遅延または不履行に対して課される予定損害賠償金に適用されるという事前の裁定のもと、最近Maharashtra Authority for Advanced Ruling(**AAR**)が開催されました。

予定損害賠償金の支払いは、GST法附則IIの5(e)に該当する「*役務の提供*」としてGSTの対象とされており、「行為を差し控える義務、行為若しくは事態を容認する義務、又は行為を行う義務に合意すること」を規定している。

4. **倒産法**

インド大統領は、2018年6月6日に、住宅購入者を金融債権者と分類し、意思決定基準を変更し、企業倒産処理中に保証人に対する手続きがモラトリアムの範囲内または範囲外にあるかどうかを明確にする、2016年**倒産法**を改正する、2018年破産法条例(**条例**)を公布しました。

1. FOREIGN DIRECT INVESTMENT

1.1. RBI INTRODUCES A SINGLE MASTER FORM TO REPORT ALL FOREIGN INVESTMENT RECEIVED BY INDIAN ENTITIES

INTRODUCTION

On June 7, 2018, the Reserve Bank of India[1] (the "**RBI**") issued a circular (the "**Circular**"),[2] introducing a single master form (the "**SMF**") to integrate the existing reporting norms for various types of foreign investment in India. In this regard, it may be relevant to mention that 'foreign investment' is defined in the Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations 2017 (the "**TISPRO Regulations**"),[3] as any investment made by a person resident outside India, on a repatriable basis, in the capital instruments of an Indian company or to the capital of a limited liability partnership (an "**LLP**").

DATA INPUT UNDER THE ENTITY MASTER FORM AND REPORTING UNDER THE SMF

Interface to input data

Prior to implementing the SMF, the RBI will provide an interface to Indian entities to input data, in a specified format, on the total foreign investment received by them. This interface will be available from June 28, 2018 to July 12, 2018 (the "**Interface Window**"), on the website of the RBI, www.rbi.org.in.

Indian entities[4] with any existing foreign investment are required to provide such information to the RBI in an entity master form, which is annexed to the Circular as Annex 1 (the "**Entity Master Form**").[5] The Entity Master Form will provide a portal for Indian entities to report details of their business activities, and the total direct and indirect foreign investment received by them. It appears that the Interface Window will be the only period within which Indian entities can enter the data required under the Entity Master Form.

PURPOSE OF THE SMF

The purpose of the SMF appears to be the collation of common details of an Indian entity, such as the name of the entity, its corporate identification number, and details of all foreign investment, including the entry route and sectoral cap applicable to it. The SMF, for which the draft format is provided in the Circular as Annex 2,[6] will have to be filed online. The final form, when hosted, will be available as part of the Master Direction – Reporting under **Foreign Exchange Management Act, 1999.**[7] Along with the draft format of the SMF, formats of the following forms have also been uploaded in Annex 2:

[1] *Reserve Bank of India or **RBI** is the central bank of India. Its primary responsibility is to regulate the monetary policy of the Indian economy.*

[2] *Foreign Investment in India - Reporting in Single Master Form A.P (DIR Series) Circular No.30*, available at https://rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=11297.

[3] This definition was incorporated in Regulation 2(xviii) of the TISPRO Regulations, which were introduced on November 7, 2017. The TISPRO Regulations are available at https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11161&Mode=0.

[4] An '*Indian entity*' has been defined in Regulation 2(xxv) of the TISPRO Regulations as an Indian company (including a start-up) or an Indian LLP.

[5] The Entity Master Form is available at https://rbidocs.rbi.org.in/rdocs/content/pdfs/194NT070618_A1.pdf.

[6] The draft format of the SMF is provided in Annex 2 of the Circular, available at https://rbidocs.rbi.org.in/rdocs/content/pdfs/194NT070618_A2.pdf.

[7] The Master Direction on Reporting under FEMA is available at https://rbi.org.in/Scripts/BS_ViewMasterDirections.aspx?id=10202.

- **Form FC-GPR**: Issue of capital instruments by an Indian company to a person resident outside India;
- **Form FC-TRS:** Transfer of capital instruments between a person resident outside India and a person resident in India;
- **Form LLP-I:** Foreign direct investment in an LLP through capital contribution and profit shares;
- **Form LLP-II:** Disinvestment or transfer of capital contribution and profit shares in an LLP;
- **Form ESOP:** Issue of employee stock options, sweat equity shares or shares against the exercise of employee stock options by an Indian company to an employee resident outside India;
- **Form CN:** Issue or transfer of convertible notes;
- **Form DRR:** Issue or transfer of depository receipts;
- **Form DI:** Reporting of downstream investment or indirect foreign investment in a company or an LLP; and
- **Form InVi:** Reporting of investment by a person resident outside India in an investment vehicle.[8]

These forms are currently required to be filed in relation to foreign investment in India, under the Foreign Exchange Management Act, 1999 ("**FEMA**") and the regulations made thereunder. However, the format of these forms appears to have been simplified in the SMF. The directions under the Circular have been issued under Section 10(4)[9] and Section 11(1)[10] of FEMA, and do not seek to overrule any permissions or approvals required under any other law. The Circular also states that authorized dealer category-I banks ("AD Banks") may bring the contents of the circular to the notice of their customers or constituents.

ATTACHMENTS TO THE SMF

Apart from the common details to be provided in the SMF, the draft format of the SMF also includes formats of the following documents, which are required to be attached to the simplified forms mentioned in paragraph 2.2 above:[11]

(a) **Shareholding pattern of the relevant Indian entity**

All Indian entities filing the SMF are required to provide their shareholding pattern along with the relevant details under the applicable forms.

(b) **Declaration to be filed by the authorized representative of the Indian entity**

This declaration is in relation to the Indian entity's compliance with laws such as FEMA, the Prevention of Money

[8] An *'investment vehicle'* has been defined in Regulation 2(xxix) of the TISPRO Regulations as an entity registered and regulated under the relevant regulations framed by Securities and Exchange Board of India or any other authority designated for the purpose, and includes (i) Real Estate Investment Trusts (REITs) governed by the Securities and Exchange Board of India (REITs) Regulations, 2014; (ii) Infrastructure Investment Trusts (InvIts) governed by the Securities and Exchange Board of India (InvIts) Regulations, 2014; and (iii) Alternative Investment Funds (AIFs) governed by the Securities and Exchange Board of India (AIFs) Regulations, 2012.

[9] Section 10(4) of FEMA, available at https://chemexcil.in/uploads/FEMA_1999.pdf : *"An authorised person shall, in all his dealings in foreign exchange or foreign security, comply with such general or special directions or orders as the Reserve Bank may, from time to time, think fit to give, and, except with the previous permission of the Reserve Bank, an authorised person shall not engage in any transaction involving any foreign exchange or foreign security which is not in conformity with the terms of his authorisation under this section."*

[10] Section 11(1) of FEMA, available at https://chemexcil.in/uploads/FEMA_1999.pdf : *"The Reserve Bank may, for the purpose of securing compliance with the provisions of this Act and of any rules, regulations, notifications or directions made thereunder, give to the authorised persons any direction in regard to making of payment or the doing or desist from doing any act relating to foreign exchange or foreign security."*

[11] The relevant attachments are available on pages 24, 25 and 26 of the Circular.

Laundering Act, 2002 and the Unlawful Activities (Prevention) Act, 1967.

(c) **Certificate from the company secretary of the Indian entity**

The format of this certificate has been annexed to the SMF, and requires the company secretary of the relevant Indian entity to certify that the entity has complied with FEMA and the regulations made thereunder, and with the Companies Act, 2013 or the Limited Liability Partnership Act, 2008.

(d) **Certificate indicating the manner of arriving at the price**

This certificate must be obtained from:

1. a merchant banker or chartered accountant registered with the Securities and Exchange Board of India, indicating the manner of arriving at the price of the shares issued to the persons resident outside India; or

2. a chartered accountant, cost accountant or approved valuer from the panel maintained by the Central Government, indicating the manner of arriving at the fair price of the capital contribution or profit shares issued to the persons resident outside India.

(e) **All other necessary documents as applicable to the issue**

Although the Circular states that 'all other necessary documents applicable to the issue' are to be attached to the SMF, it does not provide any details on which documents are deemed necessary.

(f) **Declaration by the non-resident transferor or transferee**

This declaration is in relation to the accuracy of the details provided in the SMF, and compliance with FEMA and the regulations made thereunder.

OTHER RELEVANT DETAILS TO BE PROVIDED

Other key details required to be reported in the SMF are highlighted below.

(a) When reporting any fresh issuance of shares, details such as the nature and particulars of the issue and the foreign investors, the amount received in tranches for the issuance of partly paid shares or share warrants, the fair value of shares, and the pre-determined conversion formula for compulsorily convertible shares or debentures, or for share warrants, are to be provided.

(b) When reporting a transfer of shares in an Indian entity, details such as the nature of the transfer, particulars of the buyer and seller, mode of payment, indemnity arrangement and pricing are to be provided, and the relevant extracts of the transfer agreement are to be enclosed in the SMF.

(c) For an LLP receiving foreign investment through capital contribution or profit shares, details of the foreign investor and remittance are to be provided.

(d) For any issuance of employee stock options, sweat equity shares or shares against the exercise of employee stock options by an Indian company to an employee resident outside India, the relevant scheme of the employee stock options is to be attached, and particulars of the issue are to be provided.

(e) When reporting a transfer of shares with payment by way of deferred consideration, details of the tranches, escrow arrangement and indemnity arrangement are to be inserted.

(f) When reporting convertible notes, details of the repayment, conversion, remittance and transfer of the convertible notes are required to be inserted.

(g) When reporting a transfer of capital instruments or convertible notes from a non-resident to a resident, the acknowledgement letter for the initial

investment by the non-resident is required to be enclosed.

(h) When reporting any issuance or transfer of depository receipts, particulars of the custodian, issuance, securities, conversion ratio, sponsor and listing are to be provided.

(i) When reporting any indirect foreign investment or downstream investment in an Indian entity, particulars of the investor, investment and securities are to be provided.

(j) When reporting foreign investment in an investment vehicle, details of the investment vehicle, investor, remittance and issue are to be provided.

IMPLICATION OF NON-COMPLIANCE

The Circular is especially crucial, given that Indian entities not complying with the prerequisite of entering data within the Interface Window will not be able to receive foreign investment, including indirect foreign investment, and will be considered non-compliant with FEMA and regulations made thereunder.

INDUSLAW VIEW

The intention of the RBI's Circular, introducing the Entity Master Form along with abridged and relatively simple forms required for reporting under the TISPRO Regulations, appears to be to simplify the process of reporting for Indian entities, but also to crack down on historic round-tripping transactions, potential money laundering and other historic violations of FEMA.

While the formats of the various forms and their attachments provided with the SMF appear to be simpler than the currently subsisting formats of the reporting forms, the Circular clearly has retrospective effect and provides a narrow window of opportunity for compliance. The Interface Window, from June 28, 2018 to July 12, 2018, is just 15 (fifteen) days long.

Not only has the RBI given short notice to all Indian entities to be ready with the requisite information, it has provided an exceptionally short period of time for thousands of Indian entities to file this information.

Further, Indian entities that may have defaulted in filing any of the forms that the SMF intends to replace, will likely face the herculean task of making all relevant filings before the end of the Interface Window.

Further, the likelihood of Indian entities being unaware of the requirements of the Circular is fairly high. The RBI has only given AD Banks the option to inform entities of this crucial change.

Given that any non-compliance with the directions of the Entity Master Form and the Circular will lead to an Indian entity being disqualified from receiving foreign investment in the future, the narrow Interface Window is likely to trigger objections.

Although an extension of the Interface Window is certainly necessary, it is unclear whether the RBI will permit or issue such an extension. It is also unclear if the AD Banks will be penalized for not informing their customers, constituents and stakeholders of this change in time, though it is unlikely, given that they are not mandatorily required to notify their customers.

Further, although the Circular is fairly clear on the implication of non-compliance with the directions; disqualification of all defaulting Indian entities from receiving any foreign investment, whatsoever is a disproportionate penalty for minor

violations. This is especially confounding, given the Indian government's hitherto liberal stance on foreign investment.

Whether the RBI decides to widen the Interface Window, or provide other relaxations, remains to be seen. Until then, it is advisable for all Indian entities and other stakeholders to prepare to make the necessary disclosures within the existing Interface Window.

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1.2. SINGLE MASTER FORM – FIRST PHASE OF AN ONLINE APPLICATION INTRODUCED

Further to the RBI announcement that the extant reporting structures of various types of foreign investment in India will be integrated into a Single Master Form (the "**SMF**"), the first phase (viz., the Entity Master) of an online application FIRMS, has been introduced. The User Manual for the Entity Master has been made available online.

The core announcement in this regard, was made by the RBI on June 07, 2018.

The Entity Master will be available to the public for data entry between June 28 (at 1:00 pm) and July 12, 2018. Indian entities not complying with these instructions will not be able to receive foreign investment (including indirect foreign investment) and will be treated as non-compliant with Foreign Exchange Management Act, 1999 (the "**FEMA**") and regulations made thereunder and liable for action as laid in FEMA or the regulations made thereunder.

The full text of the notification from RBI is available at:

https://rbi.org.in/Scripts/femaview.aspx?femaid=64

1.3. INVESTMENT BY FOREIGN PORTFOLIO INVESTORS (FPI) IN DEBT

The RBI capped investments by foreign portfolio investors ("**FPI**") in shorter maturity corporate bonds, three days after it eased rules on purchases of Indian securities by foreigners. The central bank said that investment by an FPI in corporate bonds with residual maturity of below one year is capped at 20% of that foreign investor's total holding of corporate securities.

The 20% investment norm on bonds across categories is applied on a continuous basis, RBI said. At any point in time, all securities with residual maturity of less than one year will be reckoned for the 20% limit, regardless of the maturity of the security at the time of purchase by the FPI.

In case the investment is above 20%, the RBI said that FPIs must bring down the holding to below 20% within six months, starting Tuesday. Until then, FPIs are barred from buying bonds with less than at least one-year maturity either through fresh purchases or through roll-down of investments with a current tenor of more than one year.

The full text of the notification from RBI is available at:

https://rbidocs.rbi.org.in/rdocs/notification/PDFs/NT199035211F142484DEBA657412BFCB17999.PDF

1.4. WITHDRAWAL OF EXEMPTIONS GRANTED TO GOVERNMENT OWNED NBFCs

It has been decided by the RBI to make the NBFC regulations applicable to Government NBFCs as per the timeline indicated in the annexure to this circular. Government NBFCs that are already complying with the prudential regulation as per the road map

submitted by them shall continue to follow the same.

Note: Government owned companies, as defined under Clause (45) of Section 2 of the Companies Act, 2013 (Section 617 of the Companies Act, 1956) and registered with the Reserve Bank of India as NBFCs, are currently exempt from:

(a) Sections 45-IB and 45-IC of the RBI Act, 1934;

(b) Master Direction - Non-Banking Financial Company - Systemically Important Non-Deposit Taking Company and Deposit Taking Company (Reserve Bank) Directions, 2016 and Master Direction - Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016 (except provisions contained in paragraph 23 of these Directions).

(c) Master Direction - Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 2016 (except provisions contained in paragraph 36, 37 and 41 of these Directions).

The full text of the notification from RBI is available at:

https://rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=10586

2. CORPORATE AND COMMERCIAL

2.1. SEBI AMENDS DELISTING AND TAKEOVER REGULATIONS TO FACILIATE INSOLVENCY RESOLUTION FOR LISTED COMPANIES

INTRODUCTION

The regulator of Indian securities market, the Securities and Exchange Board of India[12] ("**SEBI**") on May 31, 2018, notified amendments to the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (the "**Take-Over Regulations**") and the SEBI (Delisting of Equity Shares) Regulations, 2009 (the "**Delisting Regulations**") (collectively, the "**Amendments**"). The Amendments have been carried out to facilitate the acquisition of public listed companies undergoing the corporate insolvency resolution process ("**Corporate Debtors**") under the provisions of the Insolvency and Bankruptcy Code, 2016 (the "**Code**").

THE AMENDMENTS

The Delisting Regulations

The Delisting Regulations shall not be applicable to the delisting of equity shares of public listed companies that are the subject of the corporate insolvency resolution process under the Code, where the National Company Law Tribunal (the "**NCLT**") has approved a resolution plan (a "**Resolution Plan**").

The exemption is however, subject to the Resolution Plan providing for the following:[13]

(a) a specific procedure to complete the delisting of equity shares;

(b) an exit to the public shareholders of the Corporate Debtor at a specified price, not lower than the liquidation price (in distributing any proceeds from the sale of the liquidation assets in accordance with the order of priority provided under Section 53 of the Code), or, if the promoters or other shareholders of the Corporate Debtor are provided a higher exit price, such higher exit price; and

[12] *The Securities and Exchange Board of India or **SEBI** was established to protect the interests of investors in securities and to promote the development of, and to regulate the securities market in accordance with the provisions of the Securities and Exchange Board of India Act, 1992.*

[13] Regulation 3 of the Delisting Regulations.

(c) the details regarding the delisting along with the justification of the exit price should be disclosed to the stock exchange within a period of one day from the date of approval of the Resolution Plan.

Previously, the Delisting Regulations[14] provided for certain embargos for the listing of securities, which had been delisted pursuant to the provisions of the Delisting Regulations. These Delisting Regulations have been amended to provide that henceforth, an application for listing of delisted equity shares may be made in respect of a Corporate Debtor.

Take-Over Regulations

Regulation 3 of the Take-Over Regulations, which provides for the obligation to make an open offer while acquiring the shares of public listed companies and restricts an acquirer to acquire more than the maximum non-public shareholding of 75%, has been amended.

Now, successful applicants acquiring the resolution shares of a Corporate Debtor, pursuant to approval of the Resolution Plan by the NCLT, can take-over more than 75% shareholding of the Corporate Debtor.

INDUSLAW VIEW

To facilitate the corporate insolvency resolution process for listed companies, SEBI amended the Take-Over Regulations in August 2017, essentially exempting resolution applicants from having to make an open offer under Regulations 3 and 4 of the Take-Over Regulations.

Further, the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (the "**ICDR Regulations**"), were also amended to exempt such insolvent listed companies from following the process for preferential allotment under Chapter VII of the ICDR Regulations.

The Amendments (to the Take-Over Regulations and the Delisting Regulations), essentially perfect the process, permitting the resolution applicant to acquire the entire listed company.

The exemption from the Delisting Regulations requires that public shareholders should at least be paid the liquidation value after payment to all other stakeholders pursuant to the waterfall applicable in case of liquidation.

However, once a company has reached a stage where it can no longer pay off its debts or carry on its operations, it implies that the capital of the company has eroded with the shares of the company having lost their value.

Further, even if one is to look at the liquidation waterfall, the equity shareholders of a Corporate Debtor are paid only after all the other stakeholders of the Corporate Debtor have been paid out of the liquidation proceeds.

It is unlikely that a resolution applicant will have to pay any money to acquire the public shareholding of the Corporate Debtor, where the liquidation value of the Corporate Debtor is essentially zero, or if there would be no money left after making payments pursuant to the liquidation waterfall.

The Amendments which were much awaited and if read together with the earlier amendments to the Take-Over Regulations and the ICDR Regulations, provide a comprehensive and clear legal framework to facilitate the take-over of public listed companies undergoing the

[14] Regulation 30 of the Delisting Regulations.

insolvency resolution process, enabling resolution applicants to frame Resolution Plans with more certainty.

Authors: Ran Chakrabarti | Harman Walia

2.2. AMENDMENT TO THE LIMITED LIABILITY PARTNERSHIP RULES, 2009

The Central Government has amended the Limited Liability Partnership Rules, 2009, to substitute two sub-rules (1) and (4) in Rule 10, to state that a DIN obtained under the Companies Act, 2013, will be sufficient for obtaining the DPIN to be appointed as a designated partner under the LLP Act. Further, any change in the particulars of the applicant who has been allotted a DIN or DPIN can be made in Form DIR-6 under the Companies (Appointment and Qualifications of Directors) Rules, 2014.

Previously, Rule 10 of the LLP Rules, 2009, stated that a person who is to be appointed as a designated partner will have to make an application in Form 7 to obtain a DPIN.

The amendment has eliminated the need for filing of a separate application to obtain a DPIN by allowing a DIN, obtained under the Companies Act, 2013, to be sufficient for the purposes of the LLP Act.

DIN can be used in place of the DPIN for a designated director under the LLP Act.

The full text of the amendment is available at:

http://www.mca.gov.in/Ministry/pdf/LLPAmndRule1206_13062018.pdf

3. TAXATION

3.1. GOODS AND SERVICES TAX ON LIQUIDATED DAMAGES

INTRODUCTION

The Maharashtra Authority for Advanced Ruling (the "**AAR**") recently held in an advance ruling that goods and services tax ("**GST**") is applicable on liquidated damages imposed on delayed performance or non-performance of contracts executed in relation to certain services.[15] The decision comes in response to the application (the "**Application**") for advance ruling made by the Maharashtra State Power Generation Company (the "**Applicant**") under section 97 of the Central Goods and Services Act, 2017 (the "**GST Act**").

THE RULING

Under section 97 and section 100 of the GST Act, any person may obtain an advance ruling from the relevant authorities (the Authority for Advance Ruling and/or the Appellate Authority) on one or more questions in relation to the supply of goods or services (or both) being undertaken or proposed to be undertaken by such applicant.

Pursuant to the Application, the Applicant had, among other things, sought clarification from the AAR on whether the recovery of liquidated damages from a contractor, would amount to a 'supply' of goods or services under the GST Act and consequently attract GST.

The AAR ruled that the consideration amount and liquidated damages are two different parts of a transaction and

[15] https://mahagst.gov.in/sites/default/files/ddq/GST-ARA%20ORDER_MAHA%20STATE%20POWER%20GEN%20CO%20LTD.pdf

cannot be considered a consolidated 'supply of service'.

Further, the AAR held that an adjustment of the original consideration to the extent of liquidated damages is a mere facilitation in terms of accounting, which should not affect the valuation of the services involved.

However, it was further held that the impugned liquidated damages constituted income of the Applicant against bearing the delay or non-performance by the contractor and hence, should be construed a deemed 'supply of service' by the Applicant under entry 5(e) of Schedule II to the GST Act, attracting GST at the rate of 18% (eighteen percent) as ***Other Services***.

INDUSLAW VIEW

The payment of liquidated damages has been held subject to GST as a '***supply of service***' falling under entry 5(e) of Schedule II to the GST Act, which covers "agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act".

In our view, payment of liquidated damages is not consideration for the recipient of the services to refrain from any act or tolerate any act. Instead, liquidated damages are paid as compensation for the losses arising from a breach.

It is worthwhile to note that an identical provision was found in section 66E (e) of the Finance Act, 1994. However, legal commentators were divided on the question of whether service tax was chargeable on liquidated damages under the previous regime.

The levy of GST is based on the component of 'supply', which we do not find in the case of liquidated damages. The AAR has taken an extremely aggressive view to consider the tolerance of delay or the failure to deliver services by a service provider or contractor to be a ***'supply of service'***. Parties to an agreement do not agree for a breach of the contract, but for the performance of the contract. Liquidated damages are a genuine pre-estimate of damages to be imposed in order to deter breach, which should not be considered a consideration for a default or a breach. Therefore, we take the view that this ruling is likely to be challenged in the near future.

For any flow of amounts to be considered within the phrase "agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act", there should be an explicit consideration and intent for any waiver, forbearance or tolerance.

A classic example of such consideration is a fee paid against non-compete. The same reasoning cannot make sense in the case of liquidated damages. The payment or deduction of liquidated damages is not a desired outcome of a contract and does not discharge the contractor from its obligations under the agreement.

Hence, a distinction should be made between the two circumstances, that is, circumstances where the outcome is desirable or intended by the parties and circumstances where such event is not desired or intended by the parties.

Lastly, the AAR has held that the facts of each agreement need to be observed for determining the applicability of GST on liquidated damages. If this ruling is not challenged in the future, it will go a long way in casting an impact on agreements of all kinds, especially agreements in the infrastructure sector where liquidated damages are very common.

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4. INSOLVENCY AND BANKRUPTCY CODE

INTRODUCTION

The President of India promulgated the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018 (the "**Ordinance**") on 6 June 2018 to amend the Insolvency and Bankruptcy Code, 2016 (the "**Code**"), which amongst other things, categorizes homebuyers as financial creditors, amends decision making thresholds and clarifies whether proceedings against guarantors fall within or outside of the moratorium during the corporate insolvency process. The Ordinance has immediate effect and was introduced primarily to address some of the issues arising from the interpretation and implementation of the Code. We discuss some of the key amendments that the Ordinance introduces below.

THE AMENDMENTS

Categorization of Home Buyers as Financial Creditors

An explanation has been incorporated in the definition of 'financial debt'[16] to clarify that any amount raised from an allottee for a real estate project shall have the commercial effect of borrowing.

As a result, homebuyers will now be treated as 'financial creditors' and form a part of the committee of creditors of a corporate debtor (the "**CoC**") and play a part in the decision-making process, determining the corporate insolvency resolution process of a corporate debtor, including whether to accept or reject a resolution plan. The classification as a 'financial creditor' also enables homebuyers to initiate the corporate insolvency resolution process.

Initiation of insolvency resolution process by Operational Creditors

Unlike 'financial creditors' who can initiate the insolvency resolution process by directly filing the application with the National Company Law Tribunal (the "**NCLT**"), on the occurrence of a *default*, 'operational creditors' were first required to deliver a demand notice *or* invoice to the corporate debtor, who had 10 days to either pay off the debt or notify the creditor of the existence of a dispute and provide a record of the pendency of the suit or arbitration proceedings filed *before* the receipt of the notice.

The Ordinance waters down the requirement for the corporate debtor to provide evidence of any pending suit or arbitration proceeding and essentially clarifies that an operational creditor will be barred from filing an application for initiating the insolvency resolution process if a dispute exists but is yet to be filed before the courts or an arbitration tribunal. Earlier, operational creditors were also required to file a certificate from their bankers, to certify that no amounts had been received from the corporate debtor to satisfy the 'operational debt'[17]. Such certificate has now been made optional and is to be filed only if available.

Approval of shareholders for initiation of insolvency resolution process by corporate applicant

Previously, for a corporate applicant (the corporate debtor itself or persons in control or management) to file an application for initiation of the insolvency resolution process, there was no requirement to obtain shareholders' approval.

[16] Section 5(8)(f) of the Code.

[17] Section 9(3)(c) of the Code.

Section 10 of the Code has been amended to provide that a special resolution approving the filing of the application by the corporate applicant is now a pre-requisite.

The Ordinance has taken into consideration the circular issued by the Ministry of Corporate Affairs in October 2017 and the Ordinance amends the Code to provide that such approvals normally required from shareholders under the Companies Act, 2013 (or any other law in force) should be deemed given for the purposes of implementation of the resolution plan.[18]

Voting thresholds for decision making by the CoC

All important decisions of the CoC were previously approved by a vote of 75% of the voting shares. Such decisions include the extension of time period for completion of the insolvency resolution process, approval or rejection of the resolution plan and replacement of the insolvency professional. The amendment has now lowered the threshold to 66%.[19]

However, for permitting the withdrawal of an application for initiation of the insolvency resolution process, once the application has been admitted by the NCLT, the threshold has been kept at 90% of the voting share of the CoC.[20]

It may be noted that previously there was no provision under the Code enabling the *withdrawal* of the application *after* admission by the NCLT. Under Rule 8 of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016, the NCLT could only permit the withdrawal of an application on a request by the applicant *before* its admission.

Applicability of moratorium to guarantors

Putting to rest various conflicting judgments of the NCLT as well as the National Company Law Appellate Tribunal (the "**NCLAT**") and the High Courts,[21] the amendment has settled the issue of whether the provisions of Section 14 relating to the moratorium are to apply to the corporate debtor and its assets alone or to the assets of guarantors of the corporate debtor as well. The amendment has categorically clarified that the assets of guarantors are outside the purview of Section 14 and no moratorium would be applicable on such assets.

Streamlining Section 29A of the Code

To streamline Section 29A, the Ordinance has brought about a slew of changes, some of which are discussed below:

(a) Financial entities[22] having accounts, or an account of a corporate debtor under its control, or of which it is a promoter, and which have been classified as non-performing assets ("**NPAs**") have been permitted to submit resolution plans if they are not a related party to the corporate debtor. Further, the term 'related party' has been defined to exclude financial entities who are financial creditors of the corporate debtor and are a related party of the corporate debtor solely because of

[18] Explanation to Section 30(2) of the Code.
[19] Sections 12, 22, 27, 28, 30(4) of the Code.
[20] Section 12A of the Code.
[21] Alpha and Omega Diagnostics (India) Ltd. v. Asset Reconstruction Company of India - NCLAT, New Delhi, Company Appeal (AT) (Insolvency) No. 116/2017; Sanjeev Shriya v. State Bank of India - 2017 (9) ADJ 723; State Bank of India v. V. Ramakrishnan and Veeson Energy Systems - NCLAT, New Delhi, Company Appeal (AT) (Insolvency) No. 213/2017.
[22] Asset reconstruction companies, scheduled banks, Alternate investment funds, overseas financial institutions, investment vehicles, foreign institutional investors, foreign portfolio investors and foreign venture capital investors.

conversion of their debt into equity or instruments convertible into equity;

(b) Resolution applicants who hold an account, or accounts of a corporate debtor under its control or of which it is a promoter, and which have been classified as an NPA, and which was acquired pursuant to the insolvency resolution process under the Code, then such resolution applicants would not be disqualified from submitting a resolution plan, for a period of 3 years from the date of approval of the resolution plan pursuant to which the NPA was acquired;

(c) Resolution applicants who have been the promoters or are in control of a corporate debtor in which a preferential, undervalued, extortionate, or fraudulent transaction has taken place, would be eligible to submit a resolution plan provided that such transactions occurred prior to the acquisition by the resolution applicant of such corporate debtor and under the provisions of the Code, or pursuant to a scheme or plan approved by a financial sector regulator or a court. Further, the resolution applicant should not have in any way contributed to the aforesaid transactions; and

(d) Resolution applicants, who have provided a guarantee to a creditor in respect of a corporate debtor against which an application has been admitted under the Code, were previously barred from submitting a resolution plan. The Ordinance clarifies that for such resolution applicant to be disqualified; such guarantee should have been invoked by a creditor and should remain unpaid whether in part or in full.

Consents and approvals

Although the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations set out that the resolution plan may provide details for obtaining relevant approvals from government authorities to implement the plan,[23] there was no outer limit to obtain such approvals.

Under the Ordinance, such approvals are required to be obtained by the resolution applicant within a period of one year from the date of approval of the resolution plan or such time period as specified in the relevant law, whichever is later.

Limitation Act to apply to the Code

Settling the position on the applicability of the Limitation Act, 1963 (the "**Limitation Act**") to proceedings under the Code, the Ordinance provides that the Limitation Act shall be applicable on proceedings and appeals filed under the Code.[24]

Relaxation for MSMEs

The Ordinance provides that the promoters of corporate debtors who are micro, small and medium enterprises (commonly known as "**MSMEs**") would be eligible to submit a resolution plan for the revival of the MSME.[25]

INDUSLAW VIEW

Interpreting and implementing the Code raised a number of complicated issues for consideration, and the Ministry of Corporate Affairs constituted the Insolvency Law Committee (the "**ILC**") with the mandate to make recommendations on such issues.

The ILC submitted its report at the end of March 2018 and based on the

[23] Regulation 37 http://ibbi.gov.in/webadmin/pdf/legalframwork/2018/Apr/word%20copy%20updated%20upto%2001.04.2018%20CIRP%20Regulations%202018_2018-0411%2016:12:10.pdf

[24] Section 238A of the Code.

[25] Section 240A of the Code.

recommendations of the ILC, the Code was amended by the Ordinance, to address many of those issues.

Classifying home buyers as *financial creditors* and as a result, providing them with a right to initiate the insolvency resolution process as well as decision-making power on the CoC, is underpinned by an innovative definition of 'financial debt'. Amounts raised from homebuyers are used to finance real estate projects and in some cases the amounts advanced by homebuyers could be more than the debt availed from the banks.

Whilst the classification of homebuyers as a 'financial creditor' seems to be an equitable solution, it will not go without consequence. The bankability of real estate development projects and lender concerns may see interest rates rise on loans to developers, or otherwise, lenders may require a greater equity contribution to the project, additional costs which are likely to be passed on to the consumer.

Critically, although homebuyers have been classified as 'financial creditors', no amendment has been made to the Code to clarify whether homebuyers would be treated as secured or unsecured creditors when it comes to the distribution of proceeds arising from the sale of assets in the event of liquidation of the corporate debtor.

It is therefore unclear whether homebuyers will rank pari passu with secured financial creditors in a liquidation scenario. Comments in the media seem to suggest that such status may be subject to agreement between the developer and the homebuyer in any agreement for purchase, though due to the inequality of bargaining power, it's unlikely that homebuyers will be afforded secured financial creditor status in such agreements.

Further, it remains to be seen as to how homebuyers will agree instructions for any representative at the meetings of the CoC. Potentially, in the case of a large project developer becoming insolvent, there could be thousands of homebuyers to consider.

The clarification that operational creditors will be barred from filing applications initiating the insolvency resolution process, even if an ongoing dispute has not yet reached the stage where it has been taken to the courts (or is the subject of arbitration) is in line with a recent decision of the Supreme Court of India.[26]

This is broadly intended to mitigate operational creditors filing on vexatious grounds. However, on the flip side of the coin, should operational creditors be restricted when the same rules don't apply to financial creditors, and, particularly in cases, where the operational debt is larger than some of the financial debt provided by financial creditors?

Nevertheless, it could be the case that a dispute may arise only a few days before an application is filed for initiation of the insolvency resolution process and therefore, constitute a dispute even if it has not yet reached the courts or the arbitral tribunal. Further, even the law of limitation allows for a considerable time between the occurrence of a dispute situation arising and the filing of a case.

Relaxing the requirement of a certificate from a financial institution is sensible, removing an unnecessary impediment

[26] Mobilox Innovations Private Limited v. Kirusa Software Private Limited - Civil Appeal No. 9405 of 2017.

for the operational creditor. Obtaining a certificate from a financial institution could be problematic for a number of reasons, especially where the creditor has a number of bank accounts, together with question marks over the format for such certificate. Further, what would happen when operational creditors have bank accounts in jurisdictions other than India: foreign banks are not considered to be financial institutions under the Code.[27]

Requiring prior approval of the shareholders by way of a special resolution to trigger an application by the corporate applicant for initiating the insolvency resolution process, underlines the importance and interest of the shareholders of the corporate debtor. The insolvency resolution process obviously has far reaching implications on the corporate debtor and its shareholders, who are last in line in any statutory liquidation distribution. It is therefore imperative that shareholder consent is obtained in such cases.

The lowering of the threshold for decision making by the CoC should further the objective of promoting the resolution of corporate debtors and use liquidation as a last resort.

Clarifying that the moratorium will not apply to the assets of the guarantor re-affirms the underlying principle of contract that the liability of the debtor and the guarantor is co-extensive, joint and several. The creditor has the right to enforce its right against either of the parties or both.

If the moratorium extended over the assets of the guarantor, it could lead to a situation whereby shareholder guarantors recklessly drive the corporate debtor towards the insolvency resolution process, knowing that their assets are immune from enforcement.

The eligibility criteria for resolution applicants under Section 29A of the Code (introduced by the Insolvency and Bankruptcy Code (Amendment) Act, 2018 on November 23, 2017) have raised a great deal of debate. Pursuant to the introduction of Section 29A, various resolution plans and applicants have been caught in a quagmire and much litigation has been filed in relation to the eligibility of such applicants.

This has led to delays in the resolution process itself and has had unintended consequences by limiting the scope of those persons eligible to submit resolution plans. Although Section 29A has been amended and amongst other things, *relaxes* the provisions about pure play financial entities, certain other amendments could have been brought in to further streamline the provision by defining the term '*any other person acting jointly or in concert*'.

MSMEs hold an important position in the Indian economy and the market for potential resolution applicants is much narrower than other corporate entities. The Ordinance therefore recognizes that in such circumstances, its shareholders may be the only class of person who are likely to be resolution applicants.

Generally, it is important to consider that only certain provisions of Section 29A of the Code have been relaxed and promoters are still ineligible if they are willful defaulters or undischarged insolvents.

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[27] Section 3 (14) of the Code.

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