THE CENTRE FOR CORPORATE LAW
NATIONAL LAW UNIVERSITY ODISHA

#IN SIGHTS

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INSOLVENCY & BANKRUPTCY LAW

Insolvency and Bankruptcy Board of India ("IBBI") issues guidelines for members of the Committee of Creditors ("CoC"). [Link]

The IBBI has issued guidelines for the CoC ("**Guidelines**") in the insolvency resolution process under the Insolvency and Bankruptcy Code, 2016 ("**Code**"). These Guidelines outline the responsibilities of the CoC to ensure a fair and time-bound resolution of insolvency of the Corporate Debtor ("**CD**"). The CoC comprises financial creditors of the debtor company/CD. The CoC is responsible for choosing the successful resolution applicant for acquiring the corporate debtor and running it as a going concern.

Under the Guidelines, the members of the CoC are expected to maintain integrity and objectivity while making informed decisions relating to the CD. The CoC is also required to maintain impartiality and disclose relevant conflicts of interest. Members of the CoC shall ensure that they are abreast of the provisions of the Code and any other applicable regulations. This standard of knowledge must also apply while nominating representatives to meetings of the CoC.

The Guidelines further impose fiduciary duties on the CoC pertaining to cooperation, proactive information sharing, confidentiality, and active participation in the insolvency process. It also deems CoC members responsible for contributing to maintaining the viability of the CD by facilitating procedures essential to the smooth functioning of the CDs.

Earlier the above-stated responsibilities of the CoC were neither laid down explicitly nor considered while upholding the commercial wisdom of CoC. Recently, the Delhi High Court ("**HC**"), in *Kunwer Sachdev v. IDBI Bank*, earmarked the necessity of clear guidelines laying down the responsibilities of CoC while exercising its commercial wisdom.

These Guidelines are aimed to serve as guardrails within which the CoC could exercise its commercial wisdom. However, the Guidelines are not mandatory but recommendatory and lack any consequences for its non-compliance

A creditor can file for Corporate Insolvency resolution process ("CIRP") against a CD for remaining debt after the insolvency resolution process against the corporate guarantor [*BRS Ventures Investments v SREI Infrastructure Finance Ltd*]. [Link]

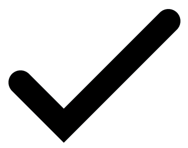
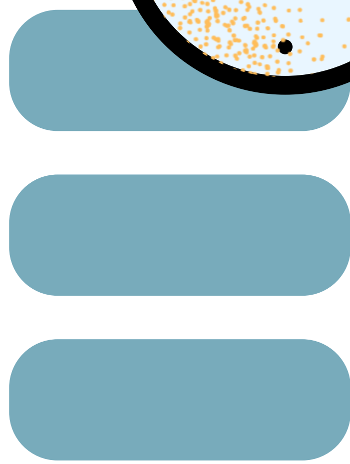
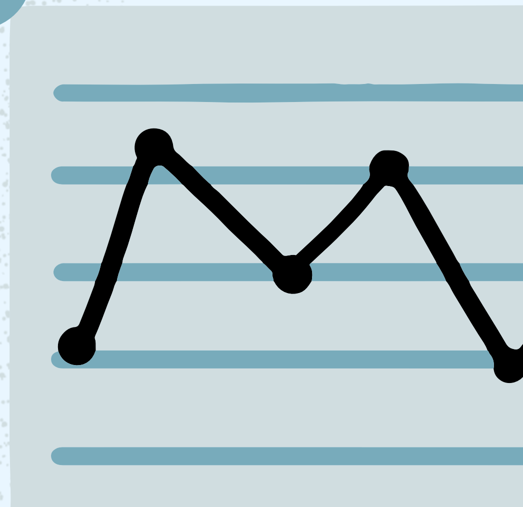
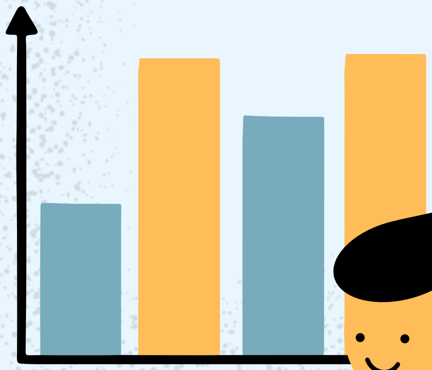
In the present ruling, the Supreme Court ("**SC**") refused to bar a creditor from filing a Corporate Insolvency Resolution Process ("**CIRP**") against a CD for balance debt even after insolvency resolution had taken place against the corporate guarantor. In this case, the creditor initiated an insolvency resolution process against the corporate guarantor for part of the debt against the CD and approved a resolution plan to the effect.

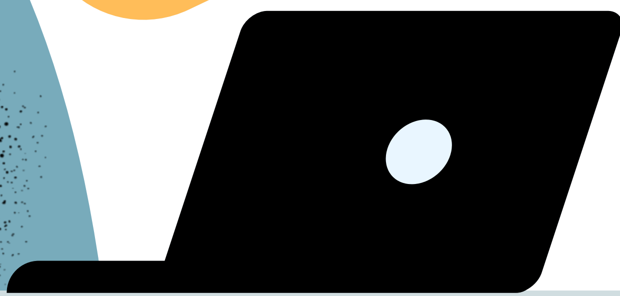
The creditor initiated a CIRP against the CD under Section 7 of the Code for the remaining debt. In response, the CD appealed to the SC, challenging its maintainability. Here, the primary issue addressed by the Court is whether CIRP could be instituted against the CD after acceptance of the resolution plan concerning the corporate guarantor. The court upheld that approval of the resolution plan by the creditor discharging a corporate guarantor does not discharge the CD from repayment of the remaining debt.

The present judgment complements the *Lalit Kumar Jain v. Union of India* case, wherein the SC held the liability of the guarantor and debtor to be co-extensive. In this case, the Court referred to and interpreted Section 128 of the Indian Contract Act, 1872 ("**ICA**") while deciding the liability of a guarantor when CIRP has already been instituted against CD.

In the present case, the SC upheld the above interpretation of the provisions of the ICA, while relating them to the co-extensive liabilities of a guarantor and CD under the Code.

SECURITIES LAW



Securities and Exchange Board of India ("SEBI") proposes to expand the scope of "connected persons" and "relative" in the SEBI (Prohibition of Insider Trading) Regulations, 2015 ("PIT Regulations"). [Link]

In a significant move to rationalize and expand the regulatory scope of the definitions of "connected person" and "relative" under the PIT Regulations, SEBI has released a consultation paper. This proposal stems from SEBI's observation that certain individuals, not currently classified as "connected persons," may still have access to unpublished price-sensitive information ("**UPSI**") due to their close associations. Essentially, a "connected person" refers to someone whose relationship with a company is likely to give them access to UPSI.

SEBI has proposed two key changes: *first*, to broaden the definition of "connected person" by drawing parallels to the definition of "related party" under the Companies Act, 2013; and second, to rationalize the definition of "relative" in line with the Income Tax Act, 1961 ("**IT Act**").

Additionally, the proposed changes introduce six new categories of "deemed connected persons," including firms where a connected person is a partner, individuals whose advice a connected person regularly follows, corporations where boards or managers act under the instructions of a connected person, individuals sharing a residence with a connected person, those with material financial ties to a connected person, and Hindu Undivided Families where the Karta or any member is a connected person or relative. These deemed connected persons, when charged under the PIT Regulations, will bear the burden of proving they did not possess UPSI.

Currently, PIT Regulation defines a "connected person" as someone associated with a company in any capacity during the six months before a relevant act, particularly those in positions likely to provide possession of or access to UPSI.

SEBI's proposed amendments thus, aim to expand the scope of "connected persons" to reduce insider trading risks. Aligning the definition of "relative" with the IT Act streamlines corporate compliance, but the broader scope and vague definitions like "material financial relationship" and "customarily is accustomed to acting" may lead to challenges, allowing SEBI to charge individuals without providing access to UPSI.

To avoid discouraging fair market activities, effective guidelines and enforcement measures are essential. The consultation process will be crucial in refining these changes without imposing undue burdens on listed companies or individuals.

SEBI mulls new asset class to bridge the gap between Mutual Funds ("MFs") and Portfolio Management Services ("PMS"). [Link]

In order to offer greater flexibility to high-risk investors and bridge the gap between MFs and PMS, SEBI has proposed the introduction of a new asset class/product category ("**NAC**"). This NAC aims to provide investors with a regulated investment product that comes with a larger ticket size, focusing on reducing the proliferation of unregistered and unauthorized investment products.

The NAC is proposed to be under the SEBI(MF) Regulations, 1996 structure but with distinct features to differentiate it from traditional MF schemes. It includes a minimum investment threshold of INR 10 lakh, and the registration process for NAC will follow the existing MF registration procedures, involving both in-principle and final approval stages.

Additionally, asset management companies ("**AMCs**") will be allowed to offer "investment strategies" under a pooled fund structure, similar to MFs, with SEBI defining the types of strategies, such as long-short equity funds and inverse exchange-traded funds

Moreover, NAC will be permitted to take derivative exposure beyond hedging purposes, with other proposed relaxations including increased limits on single issuer debt securities and ownership of paid-up capital carrying voting rights.

This new asset class is intended to fill the current gap between existing investment products, which range from MF schemes with low ticket sizes aimed at retail investors to PMS with a minimum investment of Rs. 50 lakhs and Alternative Investment Funds ("**AIFs**") require a minimum of Rs. 1 crore.

SEBI's consultation paper thus, aims to offer retail investors access to strategies like long-short equity funds and inverse exchange-traded funds.

However, the introduction of NAC may lead to a reshuffling of AUM between traditional MF schemes and NAC, as investors currently in MFs might opt for the NAC. Additionally, tax efficiency is expected to be a key factor attracting high-net-worth individuals and ultra-high-net-worth individuals to this new investment opportunity if the taxation of NAC aligns with that of the MF as it could offer a more tax-efficient alternative to Category III AIFs, which do not currently enjoy pass-through status.

Moreover, to protect retail investors often vulnerable to losses or abuse, SEBI could introduce additional certification for those managing NACs. While the consultation paper aims to merge the benefits of AIF and PMS, unclear taxation and certification requirements could lead to market misuse, undermining SEBI’s preventive efforts.

COMPANY LAW

Variable Capital Companies ("VCCs") introduced in the union budget 2024-25. [Link]

While presenting Union Budget 2024-25, the finance minister announced the formation of Variable Capital Companies ("**VCCs**") in India which is based on the Sahoo Committee report of October 2022. VCC, as the name suggests, enables distinct sub-pools with varying investment objectives, investors, and asset classes, all under a unified board and management structure. It functions as an umbrella AIF, comprising distinct sub-pools under a single umbrella entity. It can be incorporated as a company or a Limited Liability Partnership ("**LLP**").

A VCC enables distinct sub-pools with varying investment objectives, investors, and asset classes, all under a unified board and management structure. For example, a single VCC can operate a hedge fund and a private equity fund under the same roof, something that is not possible under the AIF model due to these funds falling under different categories of AIFs. VCCs will operate as an umbrella entity operating multiple funds with separate or one fund manager. Alternatively, a VCC can operate as a separate investing entity without any sub-fund. In VCCs, the capital is not static, that is to say, the investor has the option to withdraw capital based on the satisfaction of certain conditions.

In the current scenario, in an AIF, the fund is positioned above the fund manager, who oversees the investments. When the fund sells its investment in a company, the proceeds come to the fund and are then paid off to the investors by the fund manager. Often, an investment management company must establish multiple entities to invest in various asset classes. Further, as stated above, each fund must be registered separately under the SEBI (AIF) Regulations, 2012.

A VCC will significantly reduce compliance requirements compared to AIFs, providing greater flexibility for pooling funds and repatriating profits. It will also allow a single entity to run different types of funds. The VCC framework allows for flexible payout structures, permitting customized dividends and capital gains based on the performance of individual sub-funds.

Foreign investment rules amended to include the transfer of shares by a swap of securities. [Link]

On August 16, 2024, the Government of India through the Ministry of Finance notified the Foreign Exchange Management (Non-debt Instruments) (Fourth Amendment) Rules, 2024 ("**Amendment**") which proposed certain key amendments to the Foreign Exchange Management (Non-debt Instruments) Rules, 2019 ("**NDI Rules**").

Rule 9A, which has been introduced in this amendment, allows the following structure:

- Issue of equity instruments by an Indian company in exchange for equity capital of a foreign company
- Secondary share swaps involving the transfer of equity instruments between foreign investors and an Indian company
- Secondary share swaps involving the transfer of equity instruments by an Indian company in exchange for equity capital of a foreign company and equity instruments of another Indian company.

Prior to this amendment, Indian companies could issue new shares in exchange for acquisition of shares in a foreign company; or an Indian company could transfer shares which are already held by some other foreign investor in exchange for acquisition of shares of the transferee foreign company. These shares of the transferee company can be newly issued or be already available in the secondary market.

However, what was not possible is a simple transfer of shares (already available in the domestic secondary market) of an Indian company in exchange for shares of a foreign company.

This amendment is expected to provide an impetus to the investors for entering into cross-border share swap arrangements. Share swaps are the most preferred way of exercising M&A deals especially for the larger ones. This amendment is expected to facilitate global expansion of Indian companies via mergers, acquisitions and other strategic initiatives which would enable them to reach new markets. These changes will also enhance India's attractiveness as a destination for foreign capital.

ARBITRATION LAW

SC: Arbitration can proceed despite full settlement [*SBI General Life Insurance Co. Ltd. v. Krish Spinning Mills Ltd*]. [Link]

In its recent ruling, the Hon'ble SC clarified the issue of accord and satisfaction and the enforceability of arbitration agreements after a full and final settlement between the parties.

The dispute in this case arose after the parties reached a full and final settlement, with one party later seeking to invoke the arbitration clause. SBI General Life Insurance, the appellant in this case, argued that the settlement precluded arbitration, while Krish Spinning Mills, respondent in this case, contended that the arbitration clause remained valid.

Accordingly, the SC addressed the dispute and framed three key issues. The first was whether a full and final settlement automatically invalidates an arbitration agreement. The second concerned the scope of judicial scrutiny under Section 11(6) of the Arbitration and Conciliation Act, 1996 ("**A&C Act**"). The third issue was whether national courts can interfere with the jurisdiction of arbitral tribunals before the tribunal has had the opportunity to address the matter.

Upon hearing both sides, the SC held that accepting a full and final settlement does not necessarily preclude the invocation of an arbitration clause unless the settlement explicitly lapses the arbitration agreement.

Further, the scope and standard of judicial scrutiny under Section 11(6) of the A&C Act should be limited to examining the prima facie existence of an arbitration agreement. It stated that courts must avoid delving into the merits of the dispute, including the conformity of the accord and satisfaction test, leaving such matters to the arbitrator.

Lastly, it emphasized that the negative aspect of the competence-competence doctrine restricts national courts from interfering with matters related to the jurisdiction of the arbitral tribunal before the tribunal itself has had the opportunity to address them.

Before this ruling, the judicial approach to "accord and satisfaction" involved a more intrusive approach by the referral courts. They often evaluated whether a settlement truly discharges the contract and whether it would prevent further arbitration, potentially undermining the efficiency of the arbitration process.

This ruling aligns with the pro-arbitration stance of the Indian judiciary and helps ensure that the tribunal's authority is not undermined by premature judicial scrutiny. This decision marks a significant development in arbitration law by emphasizing the need for clarity in settlements. This ruling is expected to influence how future settlements and arbitration clauses are drafted and interpreted, thereby ensuring that parties' rights are preserved.

SC: Arbitral Tribunals cannot award compound interest without specific agreement [*D. Khosla and Company v. Union of India*]. [Link]

The Hon'ble SC in this case examined and clarified the authority of arbitral tribunals to award compound interest under the A&C Act. It held that courts generally lack the authority to award interest on interest unless specifically provided by a statute or unless specifically agreed upon by the parties.

This appeal stemmed from an arbitral award passed in 1997 that directed the Union of India, respondent in this case, to pay 12% simple interest for the pre-award period and 15% simple interest post-award until payment to D. Khosla and Co, who were the appellant in this case.

Soon after, the appellant raised the matter in court and argued that the 12% interest should be included in the principal for calculating 15% post-award interest, effectively creating a compound interest scenario. However, the principal civil judge and the high court ruled against awarding compound interest.

A similar stance was taken by the SC. It scrutinised the validity of the award and held that the tribunal had overstepped its authority. The SC in holding so examined Section 31(7) of the A&C Act and digressed from the general principle of awarding interest on the principal amount to compensate for delayed payments.

It referred to various provisions under the Indian Arbitration Act, 1940, and the Interest Act, 1978, and concluded that courts generally lack the authority to award interest on interest unless specifically provided by a statute or unless specifically agreed upon by the parties.

Since no such agreement existed in the present case, the tribunal's award was deemed beyond its authority. This portion of the award related to interest on interest was set aside while the remainder was upheld.

In contrast, the SC's decision in *Oriental Structural Engineers Pvt. Ltd. v. State of Kerala* demonstrated a different position on awarding interest in arbitration. The tribunal had then awarded compound interest despite a gap in the contract regarding the interest rate. It had upheld the tribunal's decision and emphasised that silence did not imply a zero-interest rate and awarding interest as a valid compensatory measure.

The stance taken explicitly underscores the arbitral tribunals' duty to adhere to statutory provisions and agreements between the parties and also further clarifies the boundaries of awarding interest. Arbitration agreements may now see more precise terms related to interest to avoid ambiguity and ensure fair outcomes. Overall, this ruling serves as a critical reference for defining the scope of arbitral powers and promoting consistency in arbitration practices.

COMPETITION LAW

Gauhati HC quashes Competition Commission of India ("CCI") proceedings against Star Cement Limited and other cement companies over alleged cartelization [*Star Cement v. CCI and Others*]. [Link]

Recently, the Gauhati HC quashed the proceedings initiated by the CCI on the ground that they were passed without fulfilling the precondition under Section 26(1) of the Competition Act, 2002 ("**the Act**"), i.e., without arriving at prima facie finding. The case involved accusations of violations under Sections 3 and 4 of the Act, which deal with anti-competitive agreements and abuse of dominant position by a company, respectively.

The factual matrix of this case is that an investigation was initiated by the CCI which was initiated in response to a case filed by the Assam Real Estate and Developer Association and Shri Rajesh Prasad, IAS, Commissioner & Secretary, Govt. of Assam, alleging that three major cement manufacturing companies, including Star Cement Ltd., had been indulging in anti-competitive activities by entering into anti-competitive agreements.

CCI after their investigation formed an opinion that Star Cement ("**the company**") and some other cement manufacturing companies by seeking to stifle competition in the market through collusive practices have indulged in anti-competitive activities. This opinion was based on the fact that there appeared to be a simultaneous increase in prices among the cement manufacturers, with the price of cement in Assam rising around the same time.

CCI directed the Director General ("**DG**") to investigate this matter. The DG directed Star Cement to furnish various information but the company did not adhere to the directions. In furtherance, the DG imposed a penalty of Rs. 5,00,000/- for non-compliance. The company had applied for review of such order but it was rejected by CCI.

Aggrieved by this order, it filed a writ petition before the Gauhati HC. To prove a violation of Section 3 of the Act, there must exist "an agreement" entered into by the cement companies, which directly or indirectly determines the purchase or sale price.

The court held that, in the absence of uniform price increases by the three cement companies, it cannot be reasonably inferred that any agreement was entered into.

Thus, the information received does not disclose the existence of the prima facie case as regards contravention of the provisions of Section 3 and/or 4 of the Act, and since the same is a sine qua non for CCI to direct the investigation, the decision of the CCI in directing investigation without fulfilment of the said mandatory pre-condition was held to be without jurisdiction and is therefore, null and void.

This judgment may result in heightened scrutiny of regulatory actions, mandating that such actions are supported by strong and substantial initial evidence. It may have broader implications for similar cases where the CCI's investigatory authority is challenged on procedural grounds. This decision may encourage more parties to seek judicial review of CCI investigations, in the hope of securing relief from protracted and burdensome inquiries. It could also lead to increased litigation and further delays in CCI's decision-making process, potentially extending the timeline of future investigations and outcomes.

MISCELLANEOUS

Capital Gains tax under the new budget 2024-2025. [Link]

The Union Budget has proposed some significant changes in the annual budget for the financial year 2024-2025 in the capital gains framework. The key changes include the removal of indexation benefits on the sale of real estate property, an increase in the taxation of equity funds, and the sale of stocks. Tax on Short- Term Capital Gain ("**STCG**") and Long-Term Capital Gains ("**LTCG**") has also been changed as well and the holding period for the classification of assets under the same has also been modified. This has been done to make the taxation process more uniform.

Removal of Indexation Benefit

If a real estate property is sold after a period of 24 months it is qualified as LTCG. While the government has removed the indexation benefit from the capital gains on the sale of property, it has also reduced the tax on it from 20% to 12.5%. Assets bought prior to April 1, 2001, will still continue to get the benefit of indexation.

By an amendment in the Finance Bill, the government allowed resident individuals and Hindu undivided families to either opt for a 12.5% LTCG tax rate without indexation benefit or a 20% LTCG tax rate with indexation benefit for property purchased before July 23, 2024. This was done to provide some respite to real estate investors. However, this relief is not available to non-residents, companies, LLPs, and partnership firms.

Indexation benefit allowed the difference between the purchase and sale price of a property to be adjusted according to the Cost Inflation Index set by the government, during the period the property was owned. This helped in reducing the impact of inflation on taxable profits from property sales.

The impact of this change is not uniform for all the sellers. While for most of the sellers and homeowners, it would mean letting go of the indexation benefit and paying more tax, some sellers might end up paying less tax. This would be the case if the property value has increased more than the inflation rate.

For real estate transactions, reducing the tax on LTCG from 20% to 12.5% would increase the liquidity in property transactions.

As most of the property sellers end up buying new property, they can offset the capital gains from the sale under Section 54 of the IT Act. However, it is also expected that this new change will decelerate the resale of property and undoubtedly result in more use of cash in the real estate business.

Changes in Taxation of LTGC

The government will now tax all financial and non-financial assets under LTGC at 12.5%. Previously, LTCG from listed equity was taxed at 10% while non-listed equity attracted a higher rate of 20%, under the new framework both of them will be taxed uniformly.

The required holding period for all assets except for listed securities is 24 months and above to qualify as long-term assets. For listed securities, the same is 12 months and above. The government has increased the exemption limit on LTCG from 1 lakh to 1.25 lakh to offset the increase in tax to some extent.

Changes in Taxation of STCG

The budget has also hiked the tax on STCG for listed equity shares from 15% to a staggering 20%. Meanwhile, other financial and non-financial assets underheld for the short term will be taxed in accordance with the slab rate.

Further, the holding period for classification under long-term and short-term there will be only under two categories 12 months and 24 months, unlike the previous third category of 36 months.

To conclude, even though the budget has increased the tax on LTCG and STCG it has nudged the investors to hold assets for a longer period and has discouraged speculative trading. Investors will now need to reassess and modify their investment and trading strategies to adapt to the new tax rates and maximize their returns.

Union government abolishes angel tax in union budget 2024-2025. [Link]

The finance minister Ms. Nirmala Sitharaman announced the abolition of angel tax while introducing the union budget 2024-2025. Clause 23 of the Finance Bill will render the angel tax ineffective from April 1, 2025. It was abolished for all classes of investors to promote startup culture and boost innovation.

Angel tax as it is generally known was a tax introduced by the government in 2012 as a tax on "income from other sources" with the aim of curbing money laundering happening due to undervaluation of shares. It was covered under Section 52(2)(viib) of the IT Act with a tax rate of 30.9%. It is levied on the excess amount of share premium over and above the fair market value ("FMV") of shares issued by unlisted companies (especially startups) on raising capital from investors.

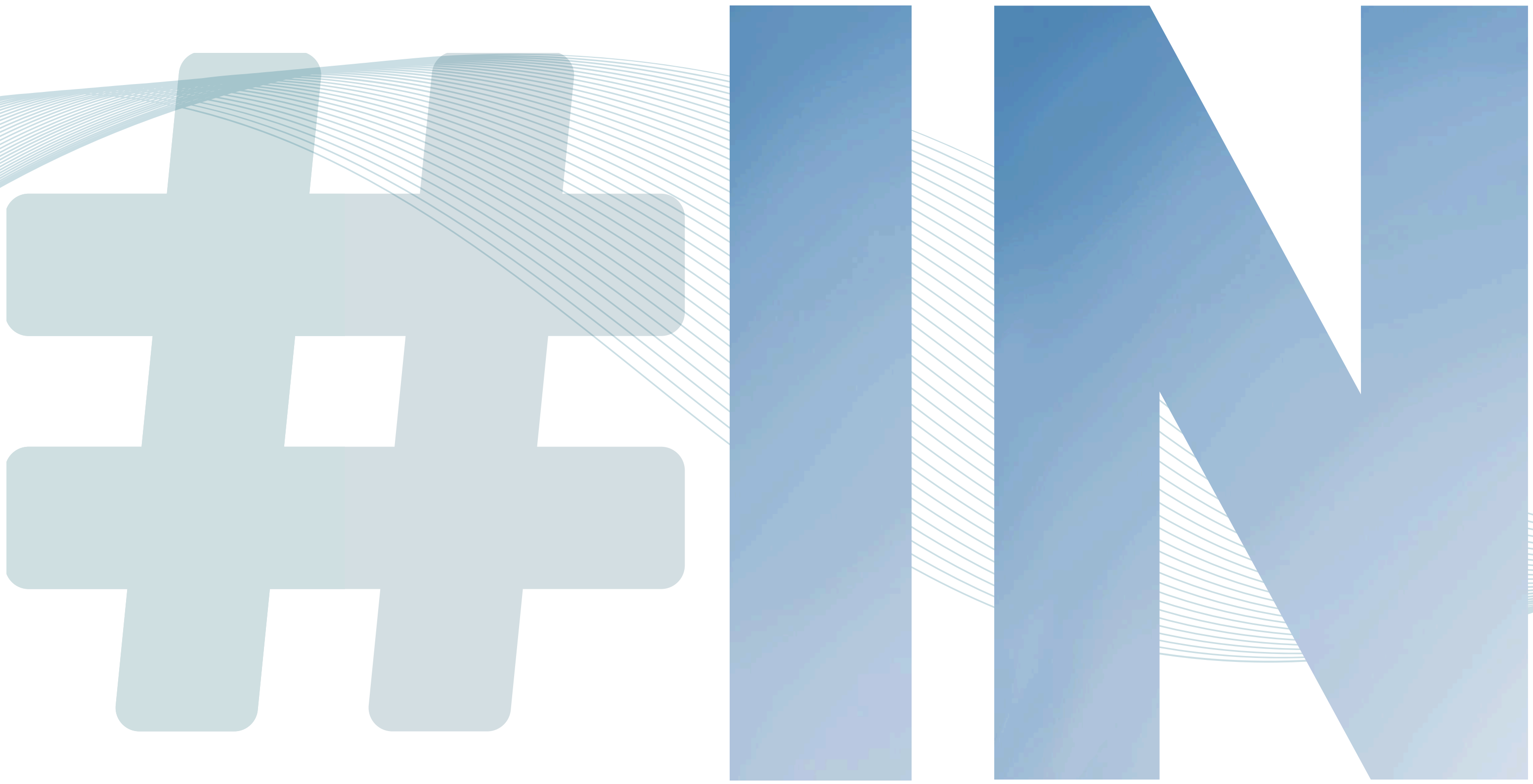
Angel tax was originally applied only to investments made by residents. Under this section, it was further inapplicable if the consideration for the issue of shares was given by a venture capital company, a venture capital fund, a specified fund, or a class of investors notified by the Central Government.

In addition to that, there were certain additional exemptions that were provided by the government over the years, in 2019 the government allowed startups to claim a 100% exemption under section 80-IAC of the IT Act. The criteria for the same is as follows:

- The startups should be recognized by the Department for Promotion of Industry and Internal Trade under notification G.S.R 127(E) released in 2019;
- The aggregate amount of their paid-up share capital should be less than 25 crores;
- Their yearly turnover should not be more than 100 crores in any of the past fiscal years;
- The FMV evaluation of these startups should be done by a certified merchant banker.

Initially, when the tax was introduced, it was not applicable to non-resident investors, they were included under its ambit through the Finance Act, 2023 which came into effect on April 1, 2024. Now with the abolishment of angel tax for all classes of investors including non-resident investors, the government has returned to its original intention of promoting foreign financial investment in India.

This move has a significant impact on the startup culture in India, as it is intended to increase entrepreneurial growth in India. It provides much-needed relief and ease of doing business to innovative startups. This does raise other concerns regarding money laundering and the generation of black money through such investments as some people might exploit the new system by investing their undisclosed, untaxed money into startups at higher than actual values. Thus, it is important to closely monitor these funds and ensure transparency to prevent illicit activities from happening.



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