CGRF SandBox™

January 2021
Volume 2 | Issue 1

CGRF™ CREATE & GROW RESEARCH FOUNDATION

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குறள்: 594
ஆக்கம் அதர்வினாய்ச் செல்லும் அசைவிலா
ஊக்க முடையா னுழை.

Thirukural: 594
Wealth will find its own way to the man of unfailing energy.

From the Editor's Desk

Dear Readers

Wish you a very bright, prosperous and Covid-free Happy New Year 2021!!!

2020 - A year with a humongous challenge to the existence of mankind has been consigned to history, finally. Well, it's a big sigh of relief that vaccines are getting approved. Hopefully a sizeable chunk of vulnerable population is expected to be inoculated in the months to come beginning from January 2021.

In this backdrop, India has been leading from the front in the revival of the economy. Efforts put in by the Government have come in for praise while at the same time distress calls keep coming for rescuing certain segments which have been deeply hurt by the pandemic.

Role of Banks in the recovery path

A big impetus has been given to infuse liquidity in the system through various schemes of lending by the banking sector. As earlier reported in this column, ECLGS (Emergency Credit Line Guarantee Schemes) have gone to a greater extent to help the MSME sector to restore businesses. While the priority for the banks was to offer a life-line, there is a lingering concern that after the Covid-19 dust settles, more bad assets might crop up unless the quality of loan assets is closely monitored. Diligence at every point is essential during the life cycle of the borrowing entities.

Due Diligence

In this context, it is very relevant to refresh ourselves with the concept of **"diligence"** which was ushered in by RBI in 2009. Vide its Circular Ref: DBOD.No. BP.BC. 110/08.12.001/2008-09 dated 10th February 2009, RBI mandated a due diligence for lending under consortium arrangement / multiple banking arrangement. The objective was to strengthen the information sharing system amongst banks in respect of borrowers enjoying credit facilities from multiple banks. The banks were required to obtain regular certification by a professional, preferably a Company Secretary, regarding compliance with various applicable statutory compliances.

Much water has flowed after 2009. Since then, the kind of changes that have happened in the compliances landscape is mind-boggling. Companies Act, 2013 came into existence from 2014. Several amendments have been made to the Act pursuant to the industry representations for ease of doing business. Huge shift in digital transactions and integration of different limbs of the Government (like GST, Income Tax, banking transactions) have strengthened the monitoring aspect. Considering many alarming instances of delinquencies in repayment of even large scale lendings, this area of due diligence has to be strengthened. So, what's ailing the system which has been introduced by RBI as early as in the year 2009? Some steps have been taken by the Institute of Company Secretaries of India and an Exposure draft of the ICSI Guidance Note has been circulated in May 2018.

(Image Source website)

Do we have an answer?

Should the tools of "due diligence" be sharpened in tune with the changing times? Could identification of certain "hot-spots" help the lenders to get fore-warned? Should not the experience gained over the last decade enable the professionals to give more meaningful diligence reports to lenders? Should not some more important items like "status of pledge of promoters' shares" be covered in the diligence report? Whether the lenders respond in time to the distress signals reported in these diligence reports? These are the interesting questions which came up before Team CGRF.

In fact, I am glad to share that CGRF was recently entrusted with a few "limited due diligence" assignments and perhaps the concerns in our mind got fortified. Result: some interesting suggestions to revamp the diligence reporting system which have been shared elsewhere in this issue of CGRF SandBox. We invite valuable comments from the readers from Banks / Corporates / Professionals as well.

CGRF SandBox Team wishes its readers a healthy and vibrant 2021. Difficult times demand dedication and focus. We are sure the New Year would bring in new hopes and opportunities!!

Yours truly
S. Rajendran

Analysis of "Diligence Report" As mandated by RBI

(S. Srinivasan, Senior partner
SR Srinivasan & Co LLP)

Background

More than a decade back there was *inter alia* a strong move by the Reserve Bank of India (RBI) for monitoring more effectively the lending by Commercial Banks to Corporate Borrowers which were enjoying credit facilities either through an arrangement of consortium of banks or through multiple banking. RBI issued initially a notification in this regard vide RBI/2008-2009/183 DBOD No. BP. BC.46/ 08.12.001/2008-09 September 19, 2008.

The notification was a result of RBI withdrawing regulatory prescriptions regarding conduct of consortium / multiple banking / syndicate arrangements in October, 1996. Central Vigilance Commission, Government of India, then in the light of frauds involving consortium/multiple banking arrangements which had taken place, had expressed concerns on the working of Consortium Lending and Multiple Banking Arrangements in the banking system.

The Commission had attributed the incidence of frauds mainly to the lack of **effective sharing of information about the credit history and the conduct of the account of the borrowers among various banks.** The RBI was then made to take notice that there was need for improving the sharing/dissemination of information among the banks about the status of the borrowers enjoying credit facilities from more than one bank. Accordingly, the banks were encouraged to strengthen their information flow about the borrowers enjoying credit facilities from multiple banks. The RBI, therefore introduced *inter alia* three formats for strengthening the information sharing as under:

(i) At the time of granting fresh facilities, a declaration to be obtained from the corporate borrower about the credit facilities already enjoyed by them from other banks **in Annex I.**

(ii) An information exchange about the conduct of the borrowers' accounts with other banks in the format given **in Annex II** at least at quarterly intervals.

(iii) Obtain regular certification by a professional, preferably a Company Secretary, regarding compliance of various statutory prescriptions that are in vogue, as per specimen given **in Annex III.**

For the purpose of our discussion, we shall focus only on Annex III. The notification no. RBI/2008-2009/183 DBOD No. BP. BC.46/ 08.12.001/2008-09 September 19, 2008 cited earlier, with some amendments, was finally superseded and came to rest with issue of RBI notification DBOD.No. BP.BC.110 / 08.12.001/2008-09 dated 10.2.2009. Therefore, a format of a diligence report in the form of Annex III to the notification was framed fixing the responsibility of obtaining such a report titled as "Diligence Report" (DR) on the lending banks through its leader in the consortium or any of the members or through any of the players in the multiple banking arrangement.

Diligence Report applicable to cooperative banks and specified financial institutions also

This exercise of obtaining the report was extended to all Primary Urban Co-operative Banks vide RBI Notification No.RBI/2008-2009/382/UBD.PCB.No. 49/13.05.000/2008-09 dt. 12.2.2009 as also to specified financial institutions such as EXIM Bank, NABARD, NHB and SIDBI vide RBI Notification No. RBI/2009-2020/116/DBOD No. FID.FIC.5/01.02.00/2009-10 dated 5.8.2009.

Conditions for issue of Diligence Report

RBI vide the above notifications stipulated the following conditions:-

1. The borrowing unit must be a corporate borrower;
2. The total exposure of the corporate borrower must be Rs. 5.00 Crores and above irrespective of whether the facilities enjoyed were fund based or non-fund based.
3. The diligence report has to be signed preferably by a Practising Company Secretary (PCS) or a Practising Chartered Accountant or a Practising Cost Accountant the latter two set of professionals being added later on from demands of IBA. It would be pertinent to note that at the end of the format of DR prescribed suggests that a PCS certifies the report.
4. The periodicity of the report was fixed as twice a year, i.e. for the six months ended 30th September and for six months ended 31st March of each year.

Furthermore, the Institute of Company Secretaries of India has issued its guidelines for attestation services by Practising Company Secretaries and by its amended resolution passed the Central Council at 254th meeting held on 1.9.2018, has mandated that only those practising company secretaries who are peer reviewed are eligible to issue this report.

Contents of the Diligence Report

Having noted the purpose of introducing the DR and the parameters under which it should be issued, we shall now dwell on the contents of the DR.

The DR in Part I contains 25 points which the Practising Company Secretary (PCS) needs to examine and comment. Under Part II of Annexure III RBI has spelt out certain suggestions and directions to the certifying professional The RBI's prescribed format is appended. It may be noticed that 17 items out of the 25 in Part I relates to the Companies Act. The format was prescribed when the Companies Act, 1956, was in force. It appears that no attempt has been made by the RBI to revamp the format even after a decade after its original prescription and particularly in view of the Companies Act, 2013, replacing the earlier Act.

ICSI, however, vide its comprehensive Exposure Draft of Guidance on Diligence Report dated 18 May 2018 has made an attempt to improve upon the contents to give additional guidance to the PCS to be followed while conducting the audit. It has taken into account the structural changes like enactment of companies Act, 2013, replacement of Listing Agreement with SEBI LODR 2015 and secretarial audit while finalising the Exposure draft and has suggested modifications to the existing format of the Diligence Report which needs to be addressed by the RBI. The Exposure Draft is very comprehensive and is available on the web Link at https://www.icsi.edu/media/webmodules/EXPOSURE_DRAFT_OF_ICSI_GUIDANCE_ON_DILIGENCE_REPORT_1_140518.pdf.

Suggestions on additional coverage in the Diligence Report

While the effort made by the core group of the task force of ICSI in bringing out the Exposure Draft is laudable, perhaps more items could have been suggested for implementation such as the impact of the findings of the audit committee on Vigil Mechanism in accordance with the provisions of section 177(9) of the Companies Act, 2013, read with Rule 7 of the Companies (Meetings of Board and its Powers) Rules, 2014.

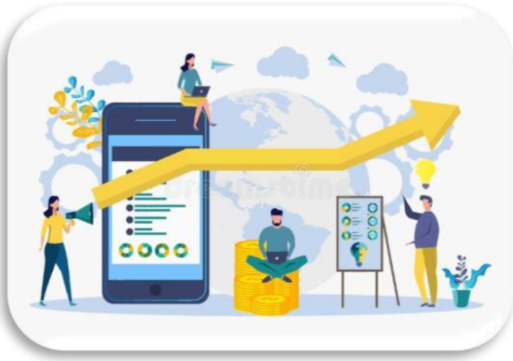
While the Exposure Draft has suggested reporting on pledge of promoters' shares, the pledge of shares of the borrowing company as security for loans sought for the benefit of other persons including group companies does not find a place.

It is not enough for the lending institutions to know whether there has been an amendment to the Memorandum of Association (MoA) / Articles of Association (AoA). Attention must be drawn by the PCS to the absence of any provision or inadequacy in any provision in the MoA /AoA which has an impact on the powers of the company to borrow or provide guarantee or security itself, particularly, where securities are offered for loans not relating to the company.

Suggestion - Board and independent directors to take note of Diligence Reports

It would have been appropriate for the core group of the task force set up for improving the DR to suggest placing of the duly certified DR before the Audit Committee or the Board preferably at its first meeting in the first quarter and the third quarter so that any qualifications by the PCS comes to the notice of Board and in particular to the notice of the Independent Directors.

Section 134(3) of the Companies Act, 2013, may be suitably amended to incorporate the Board's response to the qualifications of the PCS in its report after first drawing reference to the Diligence Reports themselves. It would not be a bad idea to direct the PCS or any certifying professional to share the periodical reports with the statutory auditors and the secretarial auditors within a time frame.



(Image source website)

Way Forward

But what remains to be done by RBI, the Commercial Banks, Primary Urban Cooperative Banks and the specified FIs, is to collect statistics since its inception as to how many borrowing units have facilities of Rs.5 Crores or more, how many have obtained the Diligence Reports and their periodicity, how many reports had qualifications therein by the PCS and what steps these lending institutions have taken to correct themselves in the light of the reports, etc.

From what appears in the last decade or more there has been a lackadaisical attitude on the part of the lending institutions to obtain the DR. It is not enough if a law is enacted or a notification is issued. For any non-compliance of the law or directions of RBI, there must be a penal consequence vested on the lending banks/FIs and its officers responsible for monitoring the account which is sadly lacking in the aforesaid RBI notifications.

Since the analysis of every item of the DR of the RBI notification read with the Exposure Draft will be a voluminous exercise, the author reserves his liberty to publish the same in the subsequent issues of SandBox.

Annexure I- Minimum information to be declared by borrowing entities to banks while approaching for finance under multiple banking arrangements

A. Details of borrowing arrangements from other banks (institution wise)

I. Name and address of bank/institution	
II. Purpose for which borrowed	
III. Limit sanctioned (full details to be given, e.g. working capital / demand loan/ term loan / short term loan)/ foreign currency loan, corporate loan / line of credit / Channel financing contingent facilities like LC, BG, DPG (I & F) etc. Also, state L/C bills discounting/project wise finance availed)	
IV. Date of sanction	
V. Present outstanding	
VI. Overdues position, if any	
VII. Repayment terms (for demand loans, term loans, corporate loans, project - wise finance)	
VIII. Security offered (complete details of security both primary and collateral including specific cash flows assigned to project wise finance/loan raised & personal/ corporate guarantee, to befurnished)	
IX. Requests for facilities which are under process	

[The information to be given for domestic and overseas borrowings from commercial banks, Financial Institutions and NBFCs]

B. Miscellaneous Details

i. CPs raised during the year and current outstanding	
ii. Details of financing outside banking system e.g. L/C Bills discounting	
iii. Main and allied activities with locations	
iv. Territory of sales and market share	
v. Details of financial aspects incl. DSCR Projections wherever applicable as per requirement of bank – Imp. Financial covenants, if any, agreed to/accepted with other lenders.	
vi. CID A/cs, within/outside financing Banks, being operated, if any	
vii. Demands by statutory authorities / current status thereof	
viii. Pending litigations	
ix. A declaration authorizing the bank to share information with other financing banks	

Annexure II -revised format under multiple banking arrangement credit information exchange

PART I (BIO DATA)	
I. Borrowing party's name and address	
II. Constitution	
III. Names of Directors / Partners	
IV. Business activity • Main • Allied	
V. Names of other financing Banks	
VI. Net worth of Directors/Partners	
VII. Group affiliation, if any	
VIII. Data on associate concerns, if banking with the same bank	
IX. Changes in shareholding and management from the previous report, if any	
PART II (FINANCIAL)	
I. IRAC Classification	
II. Internal Credit rating with narration	
III. External Credit rating, if any	
IV. Latest available Annual Report of the borrower	As on --------
PART III (EXPOSURE DETAILS)	
I. Type of credit facilities, e.g. working capital loan / demand loan / term loan / short term loan / foreign currency loan, corporate loan / line of credit / Channel financing, contingent facilities like LC, BG & DPG (I & F) etc. Also, state L/C bills discounting / project wise finance availed).	
II. Purpose of loan	
III. Date of loan facilities (including temporary facilities)	
IV. Amount sanctioned (facility wise)	
V. Balance outstanding (facility wise)	
VI. Repayment terms	
VII. Security offered • Primary • Collateral • Personal / Corporate Guarantees • Extent of control over cash flow	
VIII. Defaults in term commitments / lease rentals / others	
IX. Any other special information like court cases, statutory dues, major defaults, adverse internal / external audit observations.	
PART IV	
I. Conduct of funded facilities (based on cash management/ tendency to overdraw)	
II. Conduct of contingent facilities (based on payment history)	
III. Compliance with financial covenants	
IV. Company's internal systems & procedures	
V. Quality of management	
VI. Overall Assessment	

Annexure III – Part I

Format of Diligence Report on Governance for Banks Diligence Report

To
The Manager,
___________________ (Name of the Bank)

I/We have examined the registers, records, books and papers of............... Limited having its registered office at…………………… as required to be maintained under the Companies Act, 1956 (the Act) and the rules made thereunder, the provisions contained in the Memorandum and Articles of Association of the Company, the provisions of various statutes, wherever applicable, as well as the provisions contained in the Listing Agreement/s, if any, entered into by the Company with the recognized stock exchange/s for the half year ended on………… In my/our opinion and to the best of my/ our information and according to the examination carried out by me/us and explanations furnished to me/us by the Company, its officers and agents. I/ We report that in respect of the aforesaid period:

1. The management of the Company is carried out by the Board of Directors comprising of as listed in Annexure …., and the Board was duly constituted. During the period under review the following changes that took place in the Board of Directors of the Company are listed in the Annexure …., and such changes were carried out in due compliance with the provisions of the Companies Act, 1956.
2. The shareholding pattern of the company as on.............. Was as detailed in Annexure …………. During the period under review the changes that took place in the shareholding pattern of the Company are detailed in Annexure…….
3. The company has altered the following provisions of (i) The Memorandum of Association during the period under review and has complied with the provisions of the Companies Act, 1956 for this purpose. (ii) The Articles of Association during the period under review and has complied with the provisions of the Companies Act, 1956 for this purpose.
4. The company has entered into transactions with business entities in which directors of the company were interested as detailed in Annexure….........
5. The company has advanced loans, given guarantees and provided securities amounting to Rs. .... to its directors and/or persons or firms or companies in which directors were interested, and has complied with Section – 295 of the Companies Act, 1956.
6. The Company has made loans and investments; or given guarantees or provided securities to other business entities as detailed in Annexure…. and has complied with the provisions of the Companies Act, 1956.
7. The amount borrowed by the Company from its directors, members, financial institutions, banks and others were within the borrowing limits of the Company. Such borrowings were made by the Company in compliance with applicable laws. The breakup of the Company’s domestic borrowings were as detailed in Annexure ….
8. The Company has not defaulted in the repayment of public deposits, unsecured loans, and debentures, facilities granted by banks, financial institutions and non-banking financial companies.
9. The Company has created, modified or satisfied charges on the assets of the company as detailed in Annexure…. Investments in wholly owned Subsidiaries and/or Joint Ventures abroad made by the company are as detailed in Annexure ……
10. Principal value of the forex exposure and Overseas Borrowings of the company as on ………… are as detailed in the Annexure under.
11. The Company has issued and allotted the securities to the persons entitled thereto and has also issued letters, coupons, warrants and certificates thereof as applicable to the concerned persons and also redeemed its preference shares/debentures and bought back its shares within the stipulated time in compliance with the provisions of the Companies Act,1956 and other relevant statutes.
12. The Company has insured all its secured assets.
13. The Company has complied with the terms and conditions, set forth by the lending bank/financial institutions at the time of availing any facility and also during the currency of the facility.
14. The Company has declared and paid dividends to its shareholders as per the provisions of the Companies Act, 1956.
15. The Company has insured fully all its assets.

16. The name of the Company and or any of its Directors does not appear in the defaulters' list of Reserve Bank of India.
17. The name of the Company and or any of its Directors does not appear in the Specific Approval List of Export Credit Guarantee Corporation.
18. The Company has paid all its statutory dues and satisfactory arrangements had been made for arrears of any such dues.
19. The funds borrowed from banks/financial institutions have been used by the company for the purpose for which they were borrowed.
20. The Company has complied with the provisions stipulated in Section 372A of the Companies Act in respect of its Inter Corporate loans and investments.
21. It has been observed from the Reports of the Directors and the Auditors that the Company has complied with the applicable Accounting Standards issued by the Institute of Chartered Accountants in India.
22. The Company has credited and paid to the Investor Education and Protection Fund within the stipulated time, all the unpaid dividends and other amounts required to be so credited.
23. Prosecutions initiated against or show cause notices received by the Company for alleged defaults/offences under various statutory provisions and also fines and penalties imposed on the Company and or any other action initiated against the Company and /or its directors in such cases are detailed in Annexure…..
24. The Company has (being a listed entity) complied with the provisions of the Listing Agreement.
25. The Company has deposited within the stipulated time both Employees' and Employer's contribution to Provident Fund with the prescribed authorities.

Note: The qualification, reservation or adverse remarks, if any, are explicitly stated may be stated at the relevant paragraphs above place(s).

Place:	
Date:	

Signature:	
Name of Company Secretary/Firm:	
C.P.No:	

Part II

CERTIFICATIONS OF BORROWAL COMPANIES BY CHARTERED ACCOUNTANTS / COMPANY SECRETARIES/ COST ACCOUNTANTS

(i) Terms of reference for stock audit are to be spelt out clearly by the Banks, so that the Chartered Accountants can give focused attention to such areas.
(ii) End-use verification of funds lent, if certified by Statutory Auditors, will be a good comfort to the Banks.
(iii) As Banks quite often deal with unlisted companies, disclosure requirements for such companies above a specific turnover may be made akin to those for listed companies, viz. consolidated balance sheet, segmental reporting etc. Information on large shareholding also will be useful.
(iv) Further, the following additional certification either from Chartered Accountant or Company Secretary or Cost Accountants may also be thought of :-
   a) Company Directors not figuring in defaulters list (RBI/ECGC)/wilful defaulters list etc.)
   b) Details of litigation above a specified cut off limit.
   c) A specific certificate, probably from the Company Secretary, regarding compliance with Sec. 372 (a) of the Companies Act.
   d) Details of creation/ modification/satisfaction of charges on the assets of the company, position regarding insurance, show cause notices received, finds and penalties awarded.
(v) As regards rotation of Auditors, for the sake of operational convenience, it is suggested they may be changed once every 5 years instead of every 3 years.
(vi) In order to avoid concentration, group companies may have different Statutory/ Internal Auditors in case group turnover exceeds Rs.100 crore

Amended provisions relating to registration of creation, modification and satisfaction of charges under the Companies Act, 2013 – Bankers' perspective

CGRF Bureau

Preamble:

Registration of charges (read: encumbrances) created or modified or satisfied on the assets, tangible or intangible, of a company assumes greater significance in the current context of recovery of over dues by lenders.

It may be noted that in the event of the defaulting company going into liquidation, no charge created by the company shall be taken into account by the liquidator unless it is duly registered under the provisions of Sec.77 of Companies Act, 2013. In simpler terms, if the charge created or modified is not registered with the Registrar of Companies, the secured creditor shall lose his status of a "secured creditor" and shall become an "unsecured creditor" in the event of liquidation of the company.

Amended provisions with effect from 2nd November 2018

The Companies (Amendment) Ordinance, 2018 ("Ordinance") promulgated by the President of India with effect from 2nd November 2018 has ushered in quite a few significant steps in the realm of governance of the corporates. This Ordinance was later on repealed by Companies (Amendment) Second Ordinance dated 12.1.2019 which was eventually again repealed by Companies (Amendment) Act, 2019.

In this amendment, a radical shift in the thinking process of the Government has come to the fore in respect of registration of charges. Set in the context of proliferation of non-performing assets of the banking sector and the far-reaching inroads made by the Insolvency and Bankruptcy Code, 2016, these changes in respect of the time-limit for registration of charges merit a closer analysis for a better understanding by the lenders for ensuring prompt compliance.

Needless to say, registration of charges by corporates serves an important purpose of disclosing to the larger world the debt profile of the corporate and the securities committed by the corporate to the lenders. The Ministry of Corporate Affairs (MCA) portal – www.mca.gov.in) provides an immediate window to the lenders on the debts contracted by a corporate, their terms and conditions and whether such debts have been satisfied by way of repayment.

Time-lines for registration of creation or modification or satisfaction of charges

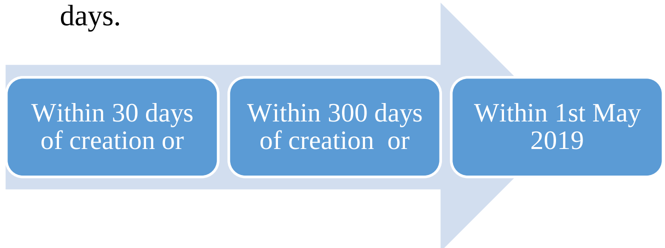
Section 77 of the Companies Act, 2013 casts a duty on every company which is creating a charge within or outside India on its property or assets or any of its undertakings, whether tangible or otherwise, and situated in or outside India, to seek registration of the particulars of the charge signed by the company and the charge-holder together with the instruments, if any, creating such charge in Form CHG-1 or CHG-9. Form CHG-1 is specified in the case creation of securities in respect of borrowings other than debentures. Form CHG-9 is specified in the case of creation of security in respect of debentures.

Such registration of charge has to be done within thirty days of its creation.

In case there is a failure to register the creation or modification within thirty days as stated above, the amended provisions pave way for an extended period for registration with financial implication in the form of additional fees and advalorem fees as explained below:

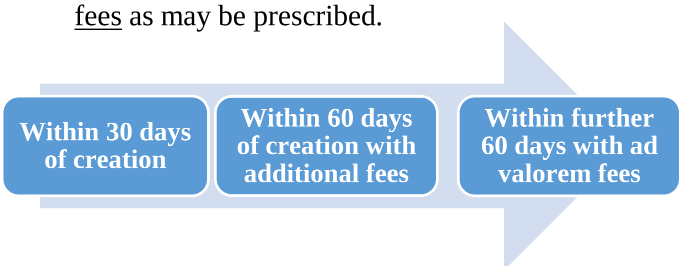
- **In case of charges created or modified prior to 2nd November 2018 -**

  The registration should be done within 300 days of such creation or within 6 months from the date of commencement of Companies (Amendment) Act 2019 – i.e. within 1st May 2019. Additional fees will be levied for the delay beyond the first period of 30 days.



- **In case of charges created or modified on or after 2nd November 2018 -**

  The registration should be done within 60 days of such creation with additional fees or within a further period of 60 days after payment of such ad valorem fees as may be prescribed.



For the purposes of a better understanding of the amendments brought in, it would be essential to have a comparative glimpse of the provisions that existed prior to the amendment as well as the amended provisions as per the diagrammatic presentation given below:

Changes in provisions relating to registration of Creation Modification or Satisfaction of charges Consequent to the Companies (Amendment) Act, 2019 with effect from 2nd Nov. 2018:

Provisions that existed prior to the amendment wef 2nd Nov. 2018	Provisions as applicable after the amendment wef 2nd Nov. 2018	
Sec.77	**Sec.77**	
Creation or modification of a charge has to be registered within 30 days of such creation or modification (normal fees applicable)	Creation or modification of a charge has to be registered within 30 days of such creation or modification (normal fees applicable)	
If not registered within the said 30 days, such creation or modification can be registered	If not registered within the said 30 days, such creation or modification can be registered as per the following manner depending upon when the event of creation or modification of charge took place as shown below:	
	Date of Creation or modification prior to 2nd Nov.2018	**Date of Creation or modification on or after 2nd Nov.2018**
within a further period of 270 days, with additional fees	A further period of 270 days is allowed to register the creation or modification of charge	A further period of 30 days is allowed to register the creation or modification of charge
If not registered within the abovesaid period,	**If not registered within the abovesaid period, then,**	
	Registration has to be done within a period of 6 months from the date of the Ordinance, i.e. 2nd Nov. 2018 with such additional fees as may be prescribed.	A further period of 60 days is allowed to register the creation or modification of charge with such ***ad valorem*** fees as may be prescribed.
The company may seek condonation of delay under Sec.87.	**No provision available for seeking condonation of delay under Sec.87**	

Condonation of delay in registration not available

It could be clearly seen that prior to the amendment, the second proviso to Sec.77(1) was giving an exit route if a company failed to register a charge within the extended period of 300 days from the date of creation. It mandated that if registration is not made within a period of three hundred days of such creation, the company shall seek extension of time in accordance with Sec.87.

Under the provisions of Sec.87 that existed prior to the Ordinance, it was possible to get the approval of the Central Government for extension of time for filing the particulars of charge or to rectify any omission or misstatement in the particulars of charge or modification or satisfaction of charge.

In contrast to this, the amended second proviso to Sec.77 (1) does not contain the words "the company shall seek extension of time in accordance with Sec.87". The omission of this particular phrase is conspicuous and appears well intended because if one visits Sec.87 after the amendment, one could see that the provisions that existed for the Central Government to approve extension of time for filing of particulars of charge have been omitted.

A closer reading of the provisions of Sec.87 prior to the Ordinance and after the Ordinance would make it abundantly clear that the Government wants to remove the provisions relating to condonation of delay in respect of creation or modification of charge whereas it wanted to retain those provisions which relate to satisfaction of charge or rectification in respect of a misstatement of the particulars of charge.

Therefore, it is loud and clear that the provisions relating to condonation of delay are no more applicable, having been dropped by the amendment wef 2nd Nov. 2018.

When the lender (charge-holder) can make an application for registration of charge?

In several cases, the borrower company does not take the pains to register the creation or modification of a charge. This puts the lender at risk in the event of liquidation of the company. Sec.77 (3) provides a warning to this effect.

> Sec.77 (3): Notwithstanding anything contained in any other law for the time being in force, no charge created by a company shall be taken into account by the liquidator appointed under this Act or the Insolvency and Bankruptcy Code, 2016, as the case may be, or any other creditor unless it is duly registered under sub-section (1) and a certificate of registration of such charge is given by the Registrar under Sec.77 (2).
>
> Sec.77 (4): Nothing in sub-section (3) shall prejudice any contract or obligation for the repayment of the money secured by a charge.

Therefore, an unregistered charge shall not be taken into account by the liquidator or any other creditor unless the charge is duly registered under Sec.77 (1) and a certificate of registration of such charge is given by the Registrar under Sec.77 (2).

In this context, it would be relevant to note that Sec.78 provided a relief to the person in whose favour the charge is created by the company.

> Sec.78: Where a company fails to register the charge within the period of thirty days referred to in sub-section (1) of section 77, without prejudice to its liability in respect of any offence under this Chapter, the person in whose favour the charge is created may apply to the Registrar for registration of the charge along with the instrument created for the charge, within such time and in such form and manner as may be prescribed and the Registrar may, on such application, within a period of fourteen days after giving notice to the company, unless the company itself registers the charge or shows sufficient cause why such charge should not be registered, allow such registration on payment of such fees, as may be prescribed.
>
> Provided that where registration is effected on application of the person in whose favour the charge is created, that person shall be entitled to recover from the company the amount of any fees or additional fees paid by him to the Registrar for the purpose of registrar of charge.

It could be seen here that the provisions of Sec.78 have not been amended. Hence, a person in whose favour a charge is created, is still having a right to make an application to the Registrar, in the event of the company failing to register the charge within the period of 30 days as referred to in Sec.77(1), after the expiry of the said 30 days.

Provisions relating to satisfaction of charge:

Sec.82 and 83 of the Companies Act, 2013 deal with reporting of satisfaction of charge. These sections have not been amended. Be that as it may, it would be useful to have a quick glance on the provisions in this regard.

1. A company shall give intimation to the Registrar in the prescribed Form CHG-4 of the payment or satisfaction in full of any charge registered under this Chapter, within a period of 30 days from the date of such payment or satisfaction.

2. The Registrar, may, on an application by the company or the charge-holder, allow such intimation of payment or satisfaction to be made within a period of three hundred days of such payment or satisfaction on payment of such additional fees as may be prescribed.

3. If such satisfaction of charge is not intimated within the period of 300 days specified above, the provisions of Sec.87 can be invoked by the company. The amended provisions of Sec.87 as already dealt with in this article continue to provide shelter although the process of condonation of delay has to be applied for in Form CHG-8 along with Form CHG-4 and after obtaining the order of the Regional director, the order will have to be filed with the Registrar in Form INC-28 for registering the satisfaction of charge.

4. Sec.83 empowers the Registrar to make entries of satisfaction and release in absence of intimation from the company, on evidence being given to his satisfaction with respect to a registered charge. The Registrar shall inform the affected parties within thirty days of making an entry in the register of charges.

It would be in the interest of the company to promptly intimate the Registrar of the satisfaction of a charge. It also serves out information to the larger world that the encumbrance which existed earlier has been fully satisfied. Lenders stepping into a corporate with exclusive securities would always insist on a satisfaction of all prior charges in respect of such securities.

Extension due to Covid-19 pandemic for filing CHG-1 or CHG-9

Taking due note of the difficulties faced due to Covid-19 pandemic, Scheme for relaxation of time for filing the forms related to creation or modification of charges was notified by MCA vide General Circular No.23/2020 dated 17th June 2020 and General Circular No.32/2020 dated 28th September 2020.

As per these Circulars, where the date of creation or modification of charge is before 1st March 2020 but the timeline for filing such form had not expired as on 1st March 2020 or the timeline for filing such forms falls on any date between 1st March 2020 and 31st December 2020, the period of time from 1st March 2020 to 31st December 2020 or such shorter period shall be considered as relaxation of time and the counting of number of days after 29th Feb. 2020 shall start from 1st January 2021. Applicable normal fee shall be charged excluding the period of 1st March 2020 to 31st December 2020, counting the days from 1st Jan. 2021 till the date of filing the form plus the days lapsed from the date of creation/modification of charge till 29th Feb. 2020.

The above scheme shall not apply in respect of filing of Form CHG-4 for satisfaction of charges.

Conclusion:

On the whole, the intention of the Government has been made very clear that the registration of charges created or modified by a company is a matter of serious import and there cannot be indefinite time given to a corporate to disclose the security interest created by it.

The lenders should take utmost caution in ensuring the creation or modification of charge is properly registered with the Registrar of Companies. As one of the signatories to the Form CHG-1 or CHG-9 is the lenders themselves, it is all the more essential for them to ensure that the terms specified in the Form like extent and operation of charge, nature of security interest, etc. are properly mentioned.

Any subsequent lenders will be put on notice by the charges already registered, thus giving them valuable information to take a prudent decision on providing further credit lines to the corporates.

MCA Update on 31st December 2020

Stakeholders may please note that there is no change in the additional fee logic of eform MGT-7 and AoC-4/AOC-4 XBRL/AOC-4 CFS/AOC-4 NBFC for the FY 2019-20 w.e.f 01st January 2021 since extension was provided to all the companies for conducting AGM and not for filing the form. Hence, the due date of form filing shall be computed based on the actual date of AGM or due date/extended due date of AGM as the case may be. Post 31st December 2020, additional fee shall be applicable from the actual date of AGM or due date/extended due date of AGM + 30/60 days as the case may be and Rs.100 per day shall be charged starting from such day even if such date falls prior to 31st December 2020.

The curious case in NCLAT of V. Padmakumar Vs. Stressed Assets Stabilization Fund

N. Nageswaran
Insolvency Professional

The roller coaster ride in deciding whether or not the debt entered in the balance sheet of a company will amount to acknowledgment of debt for deciding the time frame for initiating insolvency proceedings seems to be continuing with the five-member bench headed by Acting Chairperson Justice Bansi Lal Bhat upholding the view that such entries in the balance sheet will not amount to acknowledgement of debt as specified under Limitation Act.

Before proceeding further to understand the arguments that were put for and against in the matter, for sake of clarity, the provisions of the related section is provided below:

Section 18 of the Limitation Act, 1963

Effect of acknowledgment in writing.—

1) Where, before the expiration of the prescribed period for a suit of application in respect of any property or right, an acknowledgment of liability in respect of such property or right has been made in writing signed by the party against whom such property or right is claimed, or by any person through whom he derives his title or liability, a fresh period of limitation shall be computed from the time when the acknowledgment was so signed.
2) Where the writing containing the acknowledgment is undated, oral evidence may be given of the time when it was signed; but subject to the provisions of the Indian Evidence Act, 1872 (1 of 1872), oral evidence of its contents shall not be received. Explanation.—for the purposes of this section,—
    a) an acknowledgment may be sufficient though it omits to specify the exact nature of the property or right, or avers that the time for payment, delivery, performance or enjoyment has not yet come or is accompanied by a refusal to pay, deliver, perform or permit to enjoy, or is coupled with a claim to set-off, or is addressed to a person other than a person entitled to the property or right;
    b) the word “signed” means signed either personally or by an agent duly authorised in this behalf; and
    c) an application for the execution of a decree or order shall not be deemed to be an application in respect of any property or right.

The Facts of the case:

A Term Loan of Rs. 600 crores was sanctioned by the 'Industrial Development Bank of India' ('IDBI') t to 'M/s. Uthara Fashion Knitwear Limited' (‘Corporate Debtor’) secured by hypothecation of plant and machinery... The account was classified as a "Non-Performing Asset" on 29th May, 2002. Thereafter, IDBI assigned the loan to Stressed Assets Stabilization Fund (SASF)'- ('Financial Creditor') who filed an application u/s 7 of the Insolvency and Bankruptcy Code, 2016 ("Code") for initiation of 'Corporate Insolvency Resolution Process' (‘CIRP’) against the Corporate Debtor in NCLT, Chennai. . The Adjudicating Authority (National Company Law Tribunal), Division Bench, Chennai, by its impugned order dated 21st November, 2019 admitted the application for CIRP.

An Appeal was preferred over the Order by Mr.V.Padmakumar, Director and member of the suspended board of the CD before NCLAT. The contention was that application under Section 7 was barred by limitation, on the account of the Corporate Debtor having been declared as an NPA in the year 2009 and the decree obtained in the year 2013 on a suit filed by Financial Creditor against the Corporate Debtor for Recovery of Debt u/s 19 of Recovery of Debts due to Banks and Financial Institutions Act, 1993 (‘RDDBFI’) cannot change the position. The Hon’ble Members of the Tribunal raised the query whether after the suit is decreed the non-payment thereafter amounts to “committed default” in terms of Section 3(12) of IB Code for the first time and in terms of Article 137 of the Limitation Act 1963 for the purpose of filing application under Sec 7 of the Code the three years would commence from the date of default in terms of decree.

The matter was referred to a larger bench with the following as the main issues for consideration:

a) Whether the limitation period commences from the date of the amount falling due and payable or whether a fresh limitation period commences from the date of decree of any suit for recovery of debt.
b) Whether reflection of debt in a Balance Sheet of the 'Corporate Debtor' prepared pursuant to Section 92 of the Companies Act, 2013 amounts to acknowledgment of debt.

The judgment

The five member NCLAT bench took note of the decision of the two-member Bench of NCLAT in the case of Sh.G.Eswara Rao vs Stressed Assets Stabilisation Fund which held that the entries in the Company’s Balance

Sheet cannot be considered as an acknowledgement of debt under Section 18 of the Limitation Act 1963.

Reiterating the same view, the majority decision of NCLAT, which was rendered by a 4:1 majority, ruled that *entry in balance sheet/ annual return, which is required to be prepared to comply with statutory requirements*, *cannot be treated to be an acknowledgement under Section 18 of the Limitation Act.* Incidentally, it is to be noted that Justice S J Mukhopadhaya was a member of both the two member and five member Benches

The NCLAT held that, since the account of the 'Corporate Debtor' was declared NPA on 31st October, 2002 and that the decree was passed on 19th June, 2009/31st August, 2009, NCLAT held that the application under Section 7 filed by Financial Creditor against the Corporate Debtor was barred by limitation and was not maintainable. Thus, setting aside the impugned order dated 21st November, 2019 passed by the Adjudicating Authority (National Company Law Tribunal), Division Bench, Chennai.

Decision of Hon'ble Supreme Court in the matter of Veer Gurjar case

In the matter of Babulal Vardharji Gurjar Vs Veer Gurjar Aluminium Industries Pvt Ltd & another, NCLAT confirmed the orders passed by NCLT, Mumbai for commencement of CIRP on the CD. The contention of the appellant was that the Section 7 application was debarred by limitation. When the matter was appealed, the Hon'ble Supreme Court discussed various factors leading to the inescapable conclusion that the application made under Section 7 of the Code in the month of March 2018, seeking initiation of CIRP in respect of the corporate debtor with specific assertion of the date of default as08.07.2011, is clearly barred by limitation for having been filed much later than the period of three years from the date of default as stated in the application. The Court accepted the arguments that the debt shown in the balance sheet does not revive the limitation period of three years as applicable to the IBC under Article 137 of the Limitation Act for the reasons that the debt as shown in the balance sheet is not covered by Section 18 of the Limitation Act; and even otherwise, Section 18 of the Limitation Act cannot revive the "default" relevant for IBC and could only revive limitation

With respect to the cause of action. Also, that Section 18 of the Limitation Act could revive limitation in some cases but not for every remedy which is separate and distinct; and when limitation period of three years under Article 137 of the Limitation Act, in relation to the application under Section 7 of the Code, starts from the date of default, acknowledgment of the debt in the balance sheet will not give any fresh date of default because default occurs only once and cannot be continuing. The court also accepted the argument that the alleged proposal for OTS, if at all made on 31.07.2018, cannot revive the date of default as per declaration of NPA on 08.07.2011 nor does it attract Section 18 of the Limitation Act.

Thus, it was concluded, at least as far as cases under IBC are concerned, the date of declaring NPA should be reckoned while calculating the period of limitation for filing applications under the Code.

(Image source website)

The curious turn

In the month of September 2020, a three member NCLAT bench which heard the case of Bishal Jaiswal Vs. Asset Reconstruction Company (India) Ltd, suggested, with great respect, reconsideration of the judgment by the 5-member Bench of NCLAT in the case of V.Padmakumar vs Stressed Assets Stabilisation Fund in the light of various courts including the Hon'ble Supreme Court deciding that the mentioning of a debt in the balance sheet/annual return of a company tantamount to acknowledgement of debt and hence will revive the debt for the purpose of calculation of limitation period.

The latest judgement of the five member NCLAT Bench

The five-member Bench headed by Justice Bansi Lal Bhat, Chairperson of NCLAT *has* held on 22nd Dec 2020 that reflection of debt in the balance sheet could not be considered as an acknowledgment of debt under Section 18 of the Limitation Act. The bench proceeded to call the reference by the three member Bench that it was inappropriate, in competent and misadventure.

Conclusion

Interestingly, NCLAT has, every single time till now, achieved to come up with a new line of thinking to attract Supreme Court's attention. The Padmakumar case decision has all the ingredients to summon Supreme Court's attention again.

Independent Director – an important player in good corporate governance.

Jincy Jose, CS (Professional)
CGRF Research Scholar

The recent cases like Satyam scam, Tatas vs Cyrus Mistry, IL & FS case, etc. are the popular examples of the corporates with lack of transparency, mutual understanding/ trust and good corporate governance culture in the organisation. The Companies Act 2013 has accordingly brought the revised provisions with regard to independent directors.

Companies Act 2013 read with Schedule IV specifies the code of conduct of an independent director for corporates - a person of integrity with relevant experience who is neither a promoter nor related to any. It also outlines that the person have limits to receiving financial benefits for their role.

However, the role of independent director is far significant than those specified in the Act. Independent directors as the name suggest are expected to be independent from the management and act as the trustees of shareholders. Independent directors are the key players in good corporate governance of a Company. They contribute to the Company's growth, succession planning, innovative ideas, projects, etc. through their analytical skills and expertise. Their appointment criteria itself defines how critical and important they are to the Company. The Board appoints an independent director after due scrutiny of his/her qualification, expertise, experience and abilities which are used as weapons during the time of need and crisis.

Now the question arises that why should companies have the impetus to keep an independent director had it not been mandated. Independent directors contribute to increase the corporate credibility among competitors and thereby increase the shareholder confidence in the Company. The Companies need to understand that it's not only the bare requirement of the law that the Company appoints an independent director but the value additions they make to the Company is important. During the good times they create credibility for the company and in bad times they manage risk. Independent directors scrutinise and analyse the important issues of the Company like Company's codes, policies, the appointments of Key Personnel and provide their suggestions, opinions and judgements to the Board through various committees formed under the Act. Their views and suggestions bring independence to the Company's decision making which is the most important factor in good corporate governance. The independent directors also critically analyse the Company's performance with the future goals and help in setting realistic targets for each year.

Independent directors play a vital role in determining appropriate remuneration to the executive directors, key managerial personnel and senior management of the Company. The Listed Company / public limited Companies are required to constitute Nomination and Remuneration Committee for the deciding and recommending the remuneration and commission to executive and non- executive directors of the Board. These committees consist of majority independent directors. In case of listed entity the SEBI (Listing Obligation Disclosure Requirements), 2015 (SEBI LODR 2015) requires that the Nomination and Remuneration committee shall consist of all the independent directors. This brings transparency and better decision making in the Company with regard to recommendation of the remuneration and other benefits, if any.

Another major role of an independent director is to safeguard the interest of minority shareholders which is a matter of conflict in many corporates. In a conflicting situation, it is the independent directors who play a vital role and whose judgements are recorded in the minutes of the meeting for review of the regulators/ external parties. The Secretarial Standards requires that the opinions, views, assent/ decent to any resolution are to be noted in the minutes of the meeting which is the sign of good corporate governance.

The various Committees formed by the Company under the Companies Act, 2013 and SEBI LODR 2015 like Audit Committee, Nomination and Remuneration Committee and Stakeholders Relationship Committee requires the Chairman of the Committee to be an independent director. Also the Companies Act requires that the Chairman of these committees to compulsorily attend the Annual General meeting of the Company. This is another important aspect of the corporate governance wherein the independent director is available to the stakeholders of the Company for addressing their queries and grievances.

Companies Act 2013 also requires that independent directors of the company shall hold at least one meeting in a financial year, without the attendance of non-independent directors and members of management where they will discuss and review the performance of the non-independent directors of the Company and the Board as a whole, review the performance of the Chairperson of the company, taking into account the views of executive directors and non- executive directors, and assess the quality, quantity and timeliness of flow of information between the company management and the Board. All these matters discussed at the meeting and minuted in the minutes books are available to the statutory auditors and regulators for review whenever asked for. These matters hence bring in transparency to the Company's performance as a whole thereby reflecting the all-around corporate governance levels maintained in the Company.

There is mandatory evaluation of independent directors every year which enhances their overall performance, skills and abilities. This evaluation determines that every independent director has acted in the best interest of the Company and in full independence which enables to widen the scope of the company's corporate governance.

Hence, independent directors are of paramount importance to the management of the Company as they offset the management deficiencies, strengthen the controls, balance the management deficiencies and bring in ethical behavior and harmonize the conflicts of stakeholders thus bringing in good corporate governance culture in the company. The Company is thus required to understand the roles and duties of the independent director and appoint an efficient person for a valuable contribution towards the overall management of the Company.

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in 'MS Word'.

Do You Know?

Government extended due dates for filing IT and GST Returns

Ministry of Finance, Department of Revenue vide press release dated 30th December 2020 extended the due date for furnishing of GST, Income Tax Returns and Audit Reports for AY 2020-21 due to the outbreak of COVID – 19.

S.No	Basis of Compliance	Original Due Date	Extended Due Date as on 24th October 2020	Extended Due Date as on 30th December 2020
1	Return of Income (in case of TP Audit) AY 2020-21	30.11.2020	31.01.2021	15.02.2021
2	Return of income (Company Assesse) AY 2020-2021	31.10.2020	31.01.2021	15.02.2021
3	Return of income (where audit is mandatory) AY 2020-2021	31.10.2020	31.01.2021	15.02.2021
4	Return of income (in case of a partner in a firm whose audit is mandatory) AY 2020-2021	31.10.2020	31.01.2021	15.02.2021
5	Return of income (in any other case) AY 2020-2021	31.07.2020	31.12.2020	10.01.2021
6	Filing of tax audit report and all other reports AY 2020-2021	30.09.2020	31.12.2020	15.01.2021
7	Annual Return u/s 44 of the CGST Act, 2017	31.12.2020	-	28.02.2021

Can a company's debt be recovered from its directors/ shareholders?

Prof R. BalaKrishnan FCS, Pune

1. Company debts

All Companies - listed public companies, unlisted public companies including closely held companies and private companies may borrow money from banks and financial institutions and also from Individuals for running their business. When the company defaults in making the payment as per the terms then the recourse to the lender is to take legal action by taking the necessary course of action. Upon taking the legal course of action, the courts issues necessary orders for recovering the debts from the company by way of Decree.

2. Can the money payable by company be recovered from its directors or a shareholder

The crucial question arises in anybody's mind is as to whether the debts due from the company be recovered by enforcing a decree or court order, from the director of the company or from the company's shareholders. By and large, many people believe that a company director is personally liable to make the payment of the debt due from the company

Let us examine the above and run a thorough check with reference to the relevant laws applicable to a company relating to debt recovery.

3. Company is a separate legal personality and independent from the shareholders

In the famous case of Salomon v Salomon – a popular landmark case under the UK Companies Act 1897 {1896} UKH: 1 {1897} AC 22 - the House of Lords, unanimously ruled that, as the company incorporated by Salomon transferred his business of boot making is an independent artificial person with its rights and liabilities appropriate to itself, and that "the motives of those who took part in the promotion of the company are absolutely irrelevant in discussing what those rights and liabilities are".

Based on the Salomon case, the legal fiction of "corporate veil" between the company and its owners/controllers was firmly created and the legal fiction of corporate veil, stood established, which enunciates that a company has a legal personality separate and independent from its shareholders. Therefore, any rights, obligations or liabilities of a company are discrete and different from its shareholders. The shareholders are responsible only to the extent of their unpaid capital contribution by them in the corporate entity which is known as "limited liability"

The ruling in the Salomon case remains predominant and continues to underpin English Company Law and the Indian Company law is based on the English Company law.

4. Lifting the corporate veil

The corporate veil is nothing but an imaginary barrier that separates the company from the owners of the company and also the people who manages the company. With reference to a company, a company is an independent legal entity than its owners (i.e. shareholders) and the directors of the company. The advantage of this is the liability of the owners are limited to the extent of their shareholding. However in the real sense, it is the persons who form the association that carry out the business on behalf of the company which is incorporated as a separate entity. In the fiction of law, a corporation is a distinct entity but in reality, it is an association of persons who are in fact the beneficiaries of the corporate personality. Hence, the attribution of legal personality on incorporation is a privilege given to the companies by the framework of law.

In exceptional circumstances such as fraud / façade, the law would trigger the invocation of the piercing the corporate veil and go beyond the corporate entity and find out who are the real people involved who committed the fraud / façade. However, these exceptional circumstances are not much exhaustive and again it is left to the regulators to their discretion and interpretation. The regulator would examine and, then decide such cases based on case-to case analysis and its gravity.

5. Personal liability in case of sole proprietary firm

In case of a sole proprietary firm run by an individual, since the individual is doing his business under a trade name but the business belongs solely to him and hence the individual is liable for the debts due by the firm as the firm is nothing but trading done by the individual under a trade name. The above view is confirmed by the Honourable Apex Court of India in the case of criminal appeal relating to Shankar Finance and Investments vs State of Andhra Pradesh and others (2009) AR SC 422 decided in the year 2009 and in another case of criminal appeal relating to Milind Shripad Chandurkar vs Kalim M Khan (2011) 4 SCC 275 decided in 2011.

6. Personal liability in case of Partners in a partnership firm

There are two types of Partnerships which are in place in our country as under:-

1. The Partnership Act 1932 which came into force on October 1, 1932.

2. Limited Liability Partnership (LLP) Act, 2008 which came into force for most part, on 31st March, 2009 followed by its Rules on 1st April, 2009.

6.1 Personal liability in case of Partners under the Partnership Act 1932

Partners have unlimited personal liability for partnership liabilities under this Act. Partners are jointly liable on all contracts entered by the partnership firm. The partners are jointly and severally liable for all torts committed by one of the partners or by a firm's employee (s) within the scope of the partnership's business. In this case, the debt owned by the partnership firm is payable by the partners personally.

6.2 Personal liability in case of Partners under the Limited Liability Partnership (LLP)

The Limited Liability Partnership is an incorporated Partnership formed and registered under Limited Liability Partnership Act, 2008 with limited liability and perpetual succession similar to a company which is incorporated under Companies Act 2013. The limited liability protects the member's personal assets from the liabilities of the business and LLP's are a separate legal entity to the members and it is deemed to be a legal person having its corporate ownership. In case of LLP, the liability of the partners are limited and hence the debt owed by the LLP is not payable by the partners personally.

7. Personal liability in case of company incorporated under the Companies Act 2013

As discussed earlier, a company is an artificial legal person equal to a natural person and enjoys the legal entity of its own. The shareholders and owners of the company who are the contributors to the company's capital do not get involved in running the organization and looking after the day-to-day operation. The shareholders in turn appoint company Directors as their representative to run the organization delegating the necessary powers to the directors and these directors are collectively called the Board or Board of Directors.

The directors act as agent of a company and company being an independent legal entity. The Directors are not personally liable for contracts entered by the Directors on behalf of the Company. Since the shareholders have delegated the necessary authority to the Board of Directors, the Directors themselves do not have any independent authority to make a contract on behalf of the Company. Hence the Directors are not personally liable for contract entered by them which is on behalf of the Company and the liability is solely on the Company which enjoys its own personality as decided in Solomon case.

If the directors having no authority, but still they entered into a contract on behalf of the company, even then, the directors are not personally liable for the contract entered by them. However, the Directors may be liable for damages for breach of an implied warranty or authority. Yet, if the Directors have duly acted on behalf of the company, they are never required to be personally liable to the contracting party. This holds good even if the company failed to carry out the contract which is due to the fault of the directors.

8. Recovery of debt / dues by Creditors from the company

The dues / debts could only be recovered by the creditors against the assets of the Company and definitely not personally against the directors as discussed. In the normal course of business, the company could have entered into contract for the following:-

(a) Purchase of goods and services from the suppliers for day-to-day operations
(b) Purchase of capital goods or any other assets or facilities for carrying out certain project / expansion etc.
(c) Dues of workmen or employees towards their wages / remuneration
(d) Debts / dues arising out of various contracts entered by the company
(e) Statutory dues to the regulators such as Custom duty, Goods and Services Tax (GST), Income Tax etc.

All the above dues / debt could only be recovered from the assets owned by the company for payment / recovery. No creditors could recover the debts / dues from a company from the directors / shareholders of the company. If the company authorized some of its employees or appointed specifically authorized persons for its dealing, the creditors cannot hold them personally liable for the dues of the company. All the above people have acted on behalf of the company and hence, the company alone is responsible in making the payment.

9. Various court judgments / pronouncements on this matter

Various Courts of India have pronounced judgements spelling out that a decree / judgement / order passed against a limited company cannot be enforced against its shareholders. Let us have a look at some of the judgments in this respect.

9.1 Judgement by Kerala High Court

In the case of Ramachandran Vs State of Kerala MANU /KE/0055 / 1983, the Honourable Kerala High Court held that the Managing Director (of Revathy Exports Private Limited) is not liable unless and otherwise provided by special law. This case was for the dues by the company towards the payment of sales tax and the Court held that the Managing Director is not a defaulter for arrears of tax due from the company.

9.2 Judgment by Punjab & Haryana High Court

It was held by the Punjab & Haryana High Court in the case of HS Sidana Vs Rajesh Enterprises (1993) 11 CLA 248 that where there was a decree for recovery of sums due to a bank from a company in a suit against the company and its Managing Director, the liability to discharge the decretal amount was that of the company and not of the Managing Director.

9.3 Judgement by Madhya Pradesh (MP) High Court

The MP High Court in the case of Vimalchand vs Arora Distillery Private Limited MNU/MP/0232/2009 has observed that:-

> "I am of the view that a decree passed against a private company which being a distinct legal entity, it cannot be executed against its Managing Director or Directors and the Directors cannot be held personally liable".

10. Some of the judgments confirming that the company is a distinct legal entity

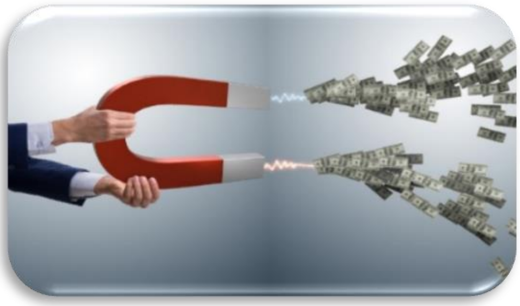
There are umpteen number of cases which categorically spelled out the directors are not personally liable for the debt / dues by the company. One may note the following:-

(a) Registered Company is a distinct legal entity than its Directors. The fact that the Directors have shares in the company is no ground to hold that the decree obtained against the Company would be binding on the Directors or that it can be executed against their personal property
(Pravinchand Parakh vs. Navratanmal nahata and others by MP High Court)

(b) After considering the judgments of various High Courts has held that a Company is a legal entity by itself and it can sue or can be sued as a legal entity and any dues from the company has to be recovered only from the company and not from its Directors.
(K. S. Narasimhan vs. Commercial Tax Officer Kuralagam Annexe, Chennai - High Court of Madras)

(c) The Honorable Supreme Court of India held in the case of Vodafone International Holdings BV vs. Union of India (2012) 6 SCC 613

> "The approach of both the corporate and tax laws, particularly in the matter of corporate taxation, generally is founded on the separate entity principle, i.e., treat a company as a separate person. The Indian Income Tax Act, 1961, in the matter of corporate taxation, is founded on the principle of the independence of companies and other entities subject to income-tax. Companies and other entities are viewed as economic entities with legal independence vis-à-vis their shareholders/participants".



(Image Source website)

11. Circumstances when directors are personally liable

The directors can be held personally liable in cases where the directors have furnished personal guarantee in respect of any borrowing / loan to the Bank or financial institution or any other lender or to a supplier of goods and or services. In such circumstances, the liability of the director would continue even after the director ceases to hold the office of the director in the company as his personal guarantee is furnished.

12. Conclusion

In view of the forgoing discussion, we can conclude that debt / dues payable by a company under any judgment, decree of Court, Tribunal or Quasi-Judicial Authority so payable by the company cannot be recovered from managing director, whole time director, executive director, independent director or ordinary Director or shareholders or employees or any authorized person of the company.

bona vacantia

Property to which no one has a claim; included within the term are the property of dissolved corporations and the residuary estate of persons who have died intestate without relatives entitled to succeed.

A Glimpse into Labour Law reforms in progress

Lakshmi Sankara Raman, CS

Introduction:

Large number of Central and State legislations relating to the most important resource –Manpower – enacted in the last 100 years made "ease of doing business" a far cry. These legislations were primarily aimed to protect the interest of labour during those years when organised labour was not existing. The Governments were forced to step in to prevent large scale exploitation.

However, after the opening up of economy and large scale industrialization, the shackles imposed by these laws were a drag on foreign investments. Coming from a regime of "Hire and Fire", the multinational companies were facing the wrath of multitude of pro-labour legislations. In order to attract global investments, successive Governments tried their hand to reform the labour laws.

Attempts were made to simplify the laws and bring in a uniform legislation. Labour laws being a sensitive subject, the reforms initiatives faced arduous headwinds in the last few decades.

The Bills introduced in the Parliament since 2017 were referred to Parliamentary Standing Committee on Labour. Taking due note of the reports from the Committee, the Bills proposing to put together the numerous labour laws into four distinctive Codes, were finally passed by both the Houses of Parliament and received Presidential assent.

Title of the Code	Presidential Assent received on
Code on Wages	8th August 2019 *(Notified in Gazette on 8th Aug.2019)*
Industrial Relations Code	28th September 2020 *(Notified in Gazette on 29th Sept. 2020)*
Code on Social Security	----do----
Occupational Safety, Health and Working Conditions Code	----do----

The Acts enacted earlier to regulate various areas relating to wages, industrial relations, PF, ESI, etc. were subsumed into the Codes as per the details given below:

S.No.	Title of the Code under which the old Acts were subsumed	No. of Sections	Acts that existed prior to introduction of New Labour and Industrial Code
1	Code on Wages, 2019	69	1. Payment of Wages Act, 1936 2. Minimum Wages Act, 1948 3. Payment of Bonus Act, 1965 4. Equal Remuneration Act, 1976
2	Industrial Relations Code, 2020	104	1. Trade Unions Act, 1926 2. Industrial Employment (Standing Orders) Act, 1946 3. Industrial Disputes Act, 1947
3	Code on Social Security, 2020	163	1. Employees' Provident Funds and Miscellaneous Provisions Act, 1952 2. Employees' State Insurance Act, 1948 3. Employees' Compensation Act, 1923 4. Employment Exchanges (Compulsory Notification of Vacancies) Act, 1959 5. Maternity Benefit Act, 1961 6. Payment of Gratuity Act, 1972 7. Cine – workers Welfare Fund Act, 1981 8. Building and Other Construction Workers" Welfare Cess Act, 1996 9. Unorganized Workers Social Security Act, 2008

4	Occupational Safety, Health and Working Conditions Code, 2020	143	1. Factories Act, 1948 2. Mines Act, 1952 3. Dock Workers (Safety, Health and Welfare) Act, 1986 4. Building and Other Construction Workers (Regulation of Employment and Conditions of Service) Act, 1996 5. Plantations Labour Act, 1951 6. Contract Labour (Regulation and Abolition) Act, 1970 7. Inter-State Migrant Workmen (Regulation and Employment and Conditions of Service) Act, 1979 8. Working Journalist and Other Newspaper Employees (Conditions of Service and Miscellaneous Provisions) Act, 1955 9. Working Journalist and Other Newspaper Employees (Conditions of Service and Miscellaneous Provision) Act, 1955 10. Working Journalist (Fixation of rate of Wages) Act, 1958 11. Motor Transport Workers Act, 1961 12. Sales Promotion Employees (Condition of Service) Act, 1976 13. Beedi and Cigar Workers (Conditions of Employment) Act, 1966 14. Cine-Workers and Cinema Theatre Workers (Regulation of Employment) Act, 1981

It is clearly specified in Section 1(3) of each of the Codes that they shall come into force on such date as the Central Government may by notification in the Official Gazette appoint and different dates may be appointed for different provisions of the Code and any reference in any such provision to the commencement of this Code shall be construed as a reference to the coming into force of that provision.

(Image Source website)

The Central Government exercising the powers conferred by sub-section (3) of Section 1 of the Code of Wages, 2019 read with Section 14 of the General Clauses Act, 1897 has notified on 18th December 2020 that the date of publication of this notification in the Official Gazette as the date on which the following provisions of the said Code shall come into force, namely:-

S. No.	Provisions of the Code
1.	Sub-sections (1), (2), (3), (10) and (11) of Section 42 (to the extent they relate to the Central Advisory Board);
2.	Clauses (s) and (t) of Sub-section (2) of Section 67 (to the extent they relate to the Central Advisory Board);
3.	Section 69 [to the extent it relates to Sections 7 and 9 (to the extent they relate to the Central Government) and Section 8 of the Minimum Wages Act, 1948 (11 of 1948)].

The Draft Rules (Central) have also been notified in respect of the above four Codes, as detailed below.

S.No.	Title of the Code	Title of the Draft Rules	Particulars of issue
1.	Code of Wages, 2019	The Code on Wages (Central) Rules, 2020	GSR 432 (E) dt. 7.7.2020
2.	Industrial Relations Code, 2020	The Industrial Relations (Central) Rules, 2020	GSR 684 (E) dt. 29.10.2020
3.	Code on Social Security, 2020	The Code on Social Security (Central) Rules, 2020	GSR 713 (E) dt. 13.11.2020
4.	Occupational Safety, Health and Working Conditions Code, 2020	Occupational Safety, Health and Working Conditions (Central) Rules, 2020	GSR 729 (E) dt. 29.11.2020

It may be noted that once the Rules are finalized, the provisions will come into effect.

An elaborate discussion on the important aspect of these Codes and the respective Draft Rules will be shared with the readers in the forthcoming issues of Sandbox.

Will Registration of Trade Marks protect your unique value proposition?

Sheeba Nair. K, CS
CGRF Research Scholar

Introduction

Registration of Trade Marks and Unique Value Proposition:

The terms Registration of Trade Marks and Unique Value Proposition are two different aspects adopted by an entrepreneur to book a space in market untouched by competitors. Both complement each other. But whether Registration of Trade Marks will act as a tool to protect one's Unique Value Proposition is to be critically analysed based on facts and circumstances of cases. In this article, an attempt has been made to address some of the features of the Captioned phrase - Registration of Trade Marks and Unique Value Proposition, individually, so that a conclusion on whether a legal tool extends legal protection for a marketing strategy, can be arrived at.

Interpretation

Unique Value Proposition – A Marketing Strategy
Unique Value Proposition is a marketing strategy that explains how a customer will be exclusively benefited out of purchase of products or brand offered by a business unit. It is a statement of superiority one's products/brands as compared to that of a competitor. The customer should be able to apply his mind in making a decision as to why he should opt for a particular brand or product. Hence Unique Value proposition may be described as one of the decision-making tools of a customer.

Registered vs Unregistered Trade Mark- Legal protection

Registration of Trade Mark can be considered as a tool to give legal protection for a Trade Mark. But registration of a Trade Mark is not mandatory as per the Laws of the Country. A registered trademark is protected under the Trade Mark Act, 1999, and the Owner of a registered trade mark, can seek legal remedy of infringement under Trade Marks Act to defend the competitors for unauthorised use of the mark. Moreover, application for Registration or a Registered Trade Mark in the home country is the base criteria for filing International Application under Madrid Protocol. At the same time, an unregistered trademark owner gets protection under the Common Law.

Hence, it is inferred that, protection is available for both Registered and Unregistered owners of a Trade Mark, but the owner of a Registered Trade Mark enjoys an upper hand in terms of prima facie validity in all legal proceedings, establishing proof of validity, country wide protection of the Trade Mark etc.

Registration of Trade Mark-Whether Actually A Boon

There are certain instances wherein the Registration of Trade Mark need not be a saviour.

(Image Source Website)

For instance, a well-known mark, is a category, wherein even if, the mark is not registered, it will get legal protection. In case of a well-known trade mark, it can be stated that for a trademark to be granted protection in India, it is not necessary that the mark owner has his business in India or its trademark is registered within India. Thus, the particular provision relating to well-known Trade Marks in Trade Marks Act, provide for the concept of trans-border reputation of trade mark and the same is very well stated in the case of Daimler Benz vs Hybo Hindustan [AIR 1994 Del 2369]. Hence, it's the business, turnover and the brand value, that over rules here. The image that comes to common man's mind on hearing of a brand, which is the result of the Unique Value Proposition that Brand has infused in to a person, is the prime factor that determines a well-known Trade Mark. The Owner of a well-known trade mark may seek legal protection restricting an entity or an individual from using its Brand name even for products, which do not fall under the Category of well-known mark and not dealt by them. The reasonable justification lies in the fact that there is chance that Public will assume the products of such entity or an individual, to be related to be coming under the Business of the Owner of well-known mark and is very well stated in the case of Rolex Sa v. Alex Jewellery Pvt. Ltd. & Ors. [2009 (41) PTC 284 (Del.)] Cases Courtesy-mondaq.com

Another instance is prior use of the Mark. Date of use is very vital in determining the legal protection extended to the Trade Mark. As per the provisions of the Trade Mark Act 1999, even if a Trade Mark is unregistered, but its use date is prior to that of the use date or Registration date of the Registered Trade Mark, whichever is earlier, then the Owner of the Registered Mark cannot prevent the Proprietor of the Unregistered Mark from using the Mark, provided there has been a continuous use of the Trade Mark and also the there is a huge volume of sales by the Proprietor of the Unregistered Mark. Hence, in the above scenario, law will not be a saviour to the Owner of the Registered Mark. Some of the aspects as discussed hereinabove is specifically interpreted in the Case Law - Peps Industries Private Limited Vs. Kurlon Limited (Delhi High Court) - Case Courtesy- mondaq.com.

Conclusion

Registration of Trade Mark is indeed an important aspect to be considered by an entrepreneur in designing a Business Model. Registered Trade Mark creates an intangible asset i.e., Intellectual Property for an organisation, which can be commercialised. Unique Value Proposition is a marketing message and also a tool for commercialisation. It is a broader term and Trade Mark is only one of the aspects of Unique Value Proposition. As stated earlier, both complement each other.

Based on the facts mentioned hereinabove in this Article, Registration of Trade Mark is only one of the aspects that will help in protection of Unique Value Proposition and the same shall also be analysed on the basis of facts of each case. Sole registration of Trade Mark will not extend complete protection to one's Unique Value Proposition.

Suspension of initiating CIRP proceeding against Corporate Debtor upto 24th March 2021

The Ministry of Corporate Affairs vide its Notification No.S.O. 4638(E) dated 22nd Dec. 2020 has further extended the suspension for initiating corporate insolvency resolution process against Corporate Debtors for a further period of 3 months till 24th March 2021, for any default arising on or after 25th March, 2020.

In view of the above, CIRP cannot be initiated against a Corporate Debtor, for any default arising on or after 25th March 2020 upto 24th March 2021.

Role of Independent Directors in good corporate governance

CS. Darshak Thaker, LLB, B.Com
CGRF Research Scholar

The Companies Act 2013 envisages a much bigger role for independent directors as independent directors are seen as the crucial interface between promoters/ management on the one hand and the minority shareholders/stakeholders on the other.

To justify the role of Independent Directors which plays an important role in promoting good corporate governance are as follows:

The independent directors shall:

- Help in bringing an independent judgement to bear on the Board's deliberations especially on issue of strategy, performance, risk management, resources, key appointments and standards of conduct;
- bring an objective view in the evaluation of the performance of board and management;
- scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance ;
- satisfy themselves on the integrity of financial information;
- controls and the systems of risk management are robust and defensible;
- safeguard the interests of all stakeholders, particularly the minority shareholders;
- balance the conflicting interest of the stakeholders;
- Determine appropriate levels of remuneration of executive directors, key managerial personnel and senior management and have a prime role in appointing and where necessary recommend removal of executive directors, key managerial personnel and senior management.
- Moderate and arbitrate in the interest of the company as a whole, in situations of conflict between management and shareholders interest;
- Assist the board in achieving consensus on important issues;
- Bring a degree of objectivity to the board's deliberations in monitoring executive management;
- Work with CEOs to prioritise issues, set the agenda and enable it to focus on substantive issues;
- Determining remuneration/ appointment & removal of executive directors, key managerial personnel and senior management;
- Bring an objective view in the evaluation performance of board and management;
- Safeguard the interests of all stakeholders, particularly the minority shareholders;
- Play the role of a facilitator outside the board room especially on contentious issues;
- Ensures that board conversations do not veer in the direction of certain unwanted topics/ individual preferences;
- Undertake appropriate induction and regularly update and refresh their skills, knowledge and familiarity with the company;
- Ascertain and ensure that the company has an adequate and functional vigil mechanism and to ensure that the interests of a person who uses such mechanism are not prejudicially affected on account of such use;
- Report concerns about unethical behaviour, actual or suspected fraud or violation of the company's code of conduct or ethics policy;

With this growth of business interest, there is a rise in expectation that Indian companies would abide by the highest standards of corporate governance in a manner clearly demonstrable to the investors.

Also the objectives of the corporate governance cannot perhaps be effectively met without the inclusion of independent directors, and this become more compelling in the context of a burgeoning economy with unprecedented amounts of funds flowing into companies from within and outside the country.

The board is a group of individuals and we all have frailties. Only the collective conscience on independent and executive directors can ensure proper governance.

The high profile scandals being Enron, WorldCom has brought into focus the lack of commitment of board towards shareholders and expressed greater concern over the role of independent directors towards monitoring the policies undertaken by management is in sync with long-term strategic objectives of company. Independency of independent directors will assist in connecting the management's interests with that of shareholders' and improve the quality of judgement in decision-making. Also since independent directors will be individuals unknown to the management, an objective analysis of firm's performance will ensure good corporate conduct and governance practices across the globe.

Conclusion:

To assume that only independent directors can ensure governance is myth. Good governance is what is right rather than what can be justified as being right.
Independent Directors have a key role to play.

Case Studies
Independent Directors Role

- ✓ Essar Energy raised capital through an IPO on LSE at a price of 420 Pence in April 2010. Currently the stock price is around 66 pence. Earlier this month a group firm Essar Global Fund Limited offered shareholders 70 pence a share to allow the family to buy back 22% in the company it does not own. A five member committee of independent directors appointed by the Ruia family, constituted to look at the offer by EGFL rejected it outright saying that the offer does not take into account the company's long term growth prospects- clearly it's uncharacteristic. Independent directors in India do not act this way. They saw their duty towards all shareholders not just the controlling one;
- ✓ When Swiss building material giant Holcim proposed to more than double the royalty fee from its Indian subsidiary, some independent board directors strongly opposed the move. The matter was referred to Audit Committee which recommended the proposal for shareholders' approval. Although 80% of the minority shareholders voted against, the resolution sailed through because Holcim was a majority shareholder in ACC and Ambuja Cement;
- ✓ Nestle board increased royalty from 3.5 to 4.5% of sales over a five year period starting 2014. Investors were not satisfied. They questioned the role of two independent directors on the Nestle India board. Nestle board had 8 directors. 4 executive and 4 independent. With the executive directors recusing themselves from voting. All the independent directors voted in favour of hike in royalty. Investors say 2 independent directors do not fit the definition of independent because one director has been on the board for 34 years and other for 20 years.

Jus scriptum

is Latin for "written law". By "written law" the Romans meant not only laws derived from legislation but also laws based on any written source.

Companies (Amendment) Act, 2020 – Some of the provisions notified on 21st Dec 2020

The readers may recollect that the Companies Act, 2013 was amended on 28th September 2020 in an attempt to de-criminalise several offences.

Out of total 66 Sections in the Companies (Amendment) Act, 2020, 46 Sections have now been notified on 21st December 2020. Majority of the Sections notified are for decriminalising the offences by replacing penalty with the fines and imprisonment prescribed earlier, such as imprisonment prescribed for officers in default for various non-compliances like default in compliance with Section 8 of the Act, contravention in issue of prospectus, buy –back of shares, non-compliance with provisions of Audit Committee and Nomination and Remuneration Committee etc. The de-criminalisation has been done to promote ease of doing business and to relax punishments for defaults and non-compliances in technical nature.

One of the notable amendment coming into effect is given below:

Amendment in Section 441(5) – Compounding of certain offences:

Prior to amendment, non-compliance with any order made by the Tribunal or the Regional Director or any officer authorised by the Central Government on compounding of offences was punishable with imprisonment as well as fine. However, post amendment the **imprisonment** and **fine** have been omitted and the following provision has been made:

"If any officer or other employee of the company who fails to comply with any order made by the Tribunal or the Regional Director or any officer authorised by the Central Government under sub-section (4), the maximum amount of fine for the offence proposed to be compounded under this section shall be twice the amount provided in the corresponding section in which punishment for such offence is provided."

Personal Guarantor to Corporate Debtor
(Insolvency Resolution Process)
Application by a Creditor under Sec.95 of IBC – A flow chart
Stage I

B. Mekala
Insolvency Professional

1st Day
Demand Notice to be issued in "Form B" to Guarantor-- Sec.95

15th Day
Filing of Application in "Form C" with AA (Failure by the debtor to pay the debt within a period of 14 days of notice)
Interim Moratorium starts-- Sec.96

29th/32nd Day
Appointment of RP -- Sec.97

35th Day
Applicant shall provide copy of the application to RP--Rule 9--(β) & to IBBI

42nd Day
Submission of Report to AA by RP recommending for approval or rejectingof the Application--Sec.99

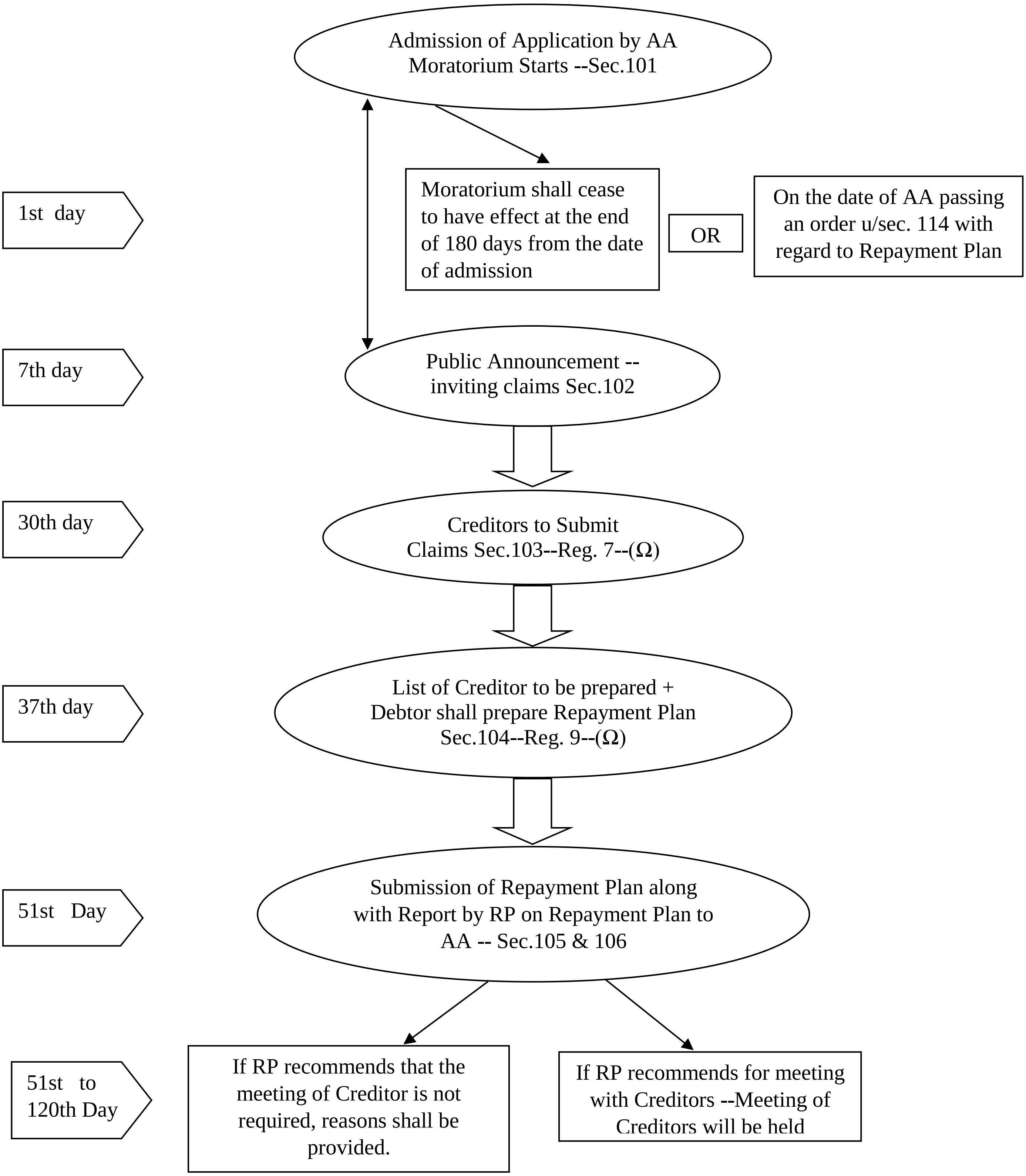
Withdrawal of application in "Form D" --Rule 11--(β)

Before Approval

56th Day
If Admitted (Sec.100)
-will proceed to Stage II
If rejected-the applicant may proceed to file application for Bankruptcy
Of the guarantor within 3 months of the date of order passed by AA

With 90% of the creditors agreeing after approval

Stage II


Admission of Application by AA
Moratorium Starts --Sec.101
1st day
Moratorium shall cease to have effect at the end of 180 days from the date of admission
OR
On the date of AA passing an order u/sec. 114 with regard to Repayment Plan
7th day
Public Announcement -- inviting claims Sec.102
30th day
Creditors to Submit Claims Sec.103--Reg. 7--(Ω)
37th day
List of Creditor to be prepared + Debtor shall prepare Repayment Plan Sec.104--Reg. 9--(Ω)
51st Day
Submission of Repayment Plan along with Report by RP on Repayment Plan to AA -- Sec.105 & 106
51st to 120th Day
If RP recommends that the meeting of Creditor is not required, reasons shall be provided.
If RP recommends for meeting with Creditors --Meeting of Creditors will be held

RP shall submit the Report of the meeting of the Creditors --Sec.113

↓

Secured Creditors (SC) shall be entitled to participate and Vote in the meeting provided SC forfeit their rights to enforce the security interest during the period of Repayment Plan or shall submit an affidavit that his right to vote is only in respect of the unsecured part of the debt--Sec.110

↓

120th Day

RP shall file Repayment Plan (approved by 3/4th in value of Creditors present and voting in the meeting) with AA--Sec.111

↓

Orders of NCLT--Repayment Plan Sec. 114 & 115

Approval of the Repayment Plan --Leads to Implementation

Rejection of the Repayment Plan --Leads to Entitlement to file application for Bankruptcy

Insolvency and Bankruptcy for Individuals and Partnership Firms--Sec.78 to 187 of Insolvency and Bankruptcy Code.
(Ω) --Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Personal Guarantors to Corporate Debtors) Regulations, 2019
(β) --IIRP Rules--Insolvency and Bankruptcy (Application to Adjudicating Authority for Insolvency Resolution Process for Personal Guarantors to Corporate Debtors) Rules, 2019

AA-Adjudicating Authority
Rule 3(e) of IIRP Rules ((β) --"guarantor" means a debtor who is a personal guarantor to a corporate debtor and in respect of whom guarantee has been invoked by the creditor and remains unpaid in full or part;

CGRF Legal Team
M. Savitha Devi, Advocate

Action Ispat Power Pvt. Ltd.
Vs
Shyam Matallics and Energy Ltd.
Decided on 15.12.2020
(Supreme Court – Full Bench)

Discretion of the company court to transfer winding up proceedings before it to the Tribunal.

An application for winding up filed under the Companies Act, 1956 pending before the Company Court was ordered and an official liquidator was appointed directing to proceed with the liquidation process. Thereafter, State Bank of India had filed an application before the NCLT under Section 7 of the Insolvency and Bankruptcy Code, 2016. Citing that proceedings have been initiated under the IBC before NCLT, an application seeking transfer of the winding up petition before the Delhi High Court to the NCLT was sought by State Bank of India. The Company Court had allowed the petition for transfer of the winding up proceedings.

On an appeal, the Division Bench of the Delhi High Court confirmed the order passed by the Single Judge. Thereafter an appeal was preferred before the Hon'ble Supreme Court. An argument was made that, once a winding up order had been passed by the Company Judge, winding up proceedings alone must continue before the High Court and parallel proceedings under the Code cannot continue.

Arguments by the Attorney General was that fifth proviso to Section 434(1)(c) of the Companies Act, 2013 makes it clear that a discretion is vested in the Company Court to transfer winding up proceedings to the NCLT without reference to the stage of winding up. Even post admission, if no irreversible steps have been taken, then a combined reading of the fifth proviso to Section 434(1)(c) and Section 238 of the Code would lead to the result that the winding up proceeding be transferred to the NCLT, as not only is the Code a special enactment with a non-obstante clause which would, in cases of conflict, do away with the Companies Act, 2013.The judgment of the Hon'ble Apex Court in **Swiss Ribbons** that winding up is the last resort after all efforts to revive the company has failed emphasises the above.

The Hon'ble Supreme Court observed that as far as transfer of winding up proceedings are concerned, the Code left the proceedings relating to winding up of companies to be transferred to NCLT at a stage as may be prescribed by the Central Government. This was done through the introduction of the Companies (Transfer of Pending proceedings) Rules, 2016 w.e.f 15.12.2016. Rules 5 and 6 of the abovesaid rules referred to 3 types of proceedings, where, all proceedings at the stage of pre-service of notice of the winding up petition would stand transferred to the NCLT compulsorily. This would lead to a post-notice and pre-admission of winding up petitions, where parallel proceedings would continue under both statutes, leading to a most unsatisfactory state of affairs. Therefore the Fifth proviso to section 434(1)(c) of the Companies Act, 2013 was introduced, which is not restricted to any particular stage of a winding up proceeding as has been pointed out in **M/s Kaledonia Jute & Fibres Pvt. Ltd. v. M/s Axis Nirman & Industries Ltd. & Ors.**, 2020 SCC OnLine SC 943.

Therefore, what follows as a matter of law is that even after a winding up petition is admitted and the Official Liquidator is appointed to take over the assets of a company sought to be wound up, discretion is vested in the Company Court to transfer the winding up petition to the NCLT. The question that arose in the present case before the Hon'ble Apex Court is as to how such discretion to be exercised needs.

Chapter XX of the Companies Act, 2013 deals with winding up of companies exclusively. When a petition to wind up a company is made before the Tribunal, the Tribunal is given powers under Section 273 to dismiss it; to make any interim order as it thinks fit; to appoint a provisional liquidator of the company till the making of a winding up order; to make an order for the winding up of the company; or to pass any other order as it thinks fit.

The Supreme Court has answered as follows:

"Given the aforesaid scheme of winding up under Chapter XX of the Companies Act, 2013, it is clear that several stages are contemplated, with the Tribunal retaining the power to control the proceedings in a winding up petition even after it is admitted. Thus, in a winding up proceeding where the petition has not been served in terms of Rule 26 of the Companies (Court) Rules, 1959 at a pre- admission stage, given the beneficial result of the application of the Code, such winding up proceeding is compulsorily transferable to the NCLT to be resolved under the Code. Even post issue of notice and pre admission, the same result would ensue. However, post admission of a winding up petition and after the assets of the company sought to be wound up become in custodia legis and are taken over by the Company Liquidator, section 290 of the Companies Act, 2013

would indicate that the Company Liquidator may carry on the business of the company, so far as may be necessary, for the beneficial winding up of the company, and may even sell the company as a going concern. So long as no actual sales of the immovable or movable properties have taken place, nothing irreversible is done which would warrant a Company Court staying its hands on a transfer application made to it by a creditor or any party to the proceedings. It is only where the winding up proceedings have reached a stage where it would be irreversible, making it impossible to set the clock back that the Company Court must proceed with the winding up, instead of transferring the proceedings to the NCLT to now be decided in accordance with the provisions of the Code. Whether this stage is reached would depend upon the facts and circumstances of each case."

Having stated above the Hon'ble Apex Court has gone ahead and upheld the concurrent finding of the Company Court and the Division Bench that the discretion vested in it by the 5th proviso to section 434(1)(c) has been exercised correctly while observing that "*despite the fact that the liquidator has taken possession and control of the registered office of the appellant company and its factory premises, records and books, no irreversible steps towards winding up of the appellant company have otherwise taken place.*"

Apya Capital Services Private Limited
Vs.
Guardian Homes Private Limited
(NCLAT) (8.12.2020)

Appellant was aggrieved of dismissal of its application filed under Section 9 of IBC by the AA vide impugned order of NCLT, Mumbai Bench on the ground that there was a clear deficiency in the service provided by the Appellant and there was no debt as claimed by the Appellant.

Hon'ble NCLAT allowed the appeal and directed the NCLT to admit the application holding that,

"*On merits of the case, we are of the considered opinion that the Adjudicating Authority has landed in error in holding that there was no 'debt' as claimed by the Appellant and there was 'deficiency in service' provided by the Appellant. The findings recorded by the Adjudicating Authority are grossly erroneous and same cannot be supported. Once the liability in respect of Rs. 75 lakh was admitted and the same was not discharged by the Corporate Debtor, dispute in regard to quantum of debt would be immaterial at the stage of admission of application under Section 7 (Sec 7 mentioned in quoted portion is a clerical error) unless the debt due and payable falls below the minimum threshold limit prescribed under law. The impugned order is liable to be set aside as the same is unsustainable.*"

The Adjudicating Authority was directed to admit the application of Appellant under Section 9 of the 'I&B Code' after providing an opportunity to the Respondent-Corporate Debtor to settle the claim of Appellant, if it so chooses and to pass all consequential directions as a sequel thereto.

Seroco Lighting Industries Pvt. Ltd.
Vs.
Ravi Kapoor, RP for Arya Filaments Pvt. Ltd. & Ors.
(NCLAT) (10.12.2020)

Resolution Plan once submitted cannot be withdrawn as there is no provision in IBC which allows the withdrawal of the approved Resolution Plan

A Resolution Plan was provided by the Promoters of the Corporate Debtor (an MSME sector) was approved by the CoC, therefore an Application was filed by the RP u/s 30(6) of the code, with a prayer to approve the CoC approved Resolution Plan submitted by the Resolution Applicant (Promoters), u/s 31of the Code. In the same matter, subsequently the Resolution Applicant (Promoters) filed an IA seeking the Hon'ble NCLT to permit them to revise their CoC approved Resolution Plan stating reasons that their Resolution Plan was filed based on the Information Memorandum which was published 2 years ago and that the they - Resolution Applicant (Promoters) were unaware of the CD's current financial condition pursuant to Lockdown situation due to Covid-19.

The Application filed by the RP was allowed by the Hon'ble NCLT approving the Resolution Plan and the IA filed by the Resolution Applicant (Promoters) to modify/ withdraw their Resolution Plan, was disallowed with cost, by a common order.

The IA was disallowed on the basis of *Kundan care products Vs. Amit Gupta, RP& Ors. Wherein it was held that the Resolution Plan once submitted cannot be withdrawn as there is no provision in IBC which allows the withdrawal of the approved Resolution Plan.* Further it was also taken note that, being an MSME unit, the Resolution Applicant who are the Promoters of the CD were allowed u/s 29A of the Code to submit their Resolution Plan.

The Resolution Applicant (Promoters) filed an Appeal against the order of the Hon'ble NCLT disallowing their prayer to revise their Resolution Plan.

The Hon'ble NCLAT upheld the order of the Hon'ble NCLT stating that Successful Resolution Applicant cannot be permitted to withdraw the approved Resolution Plan coupled with the fact that the RA is a Promoter and is well aware of the financial health of the CD. Thus the Appeal was dismissed however considering the economic slowdown due to Covid-19 outbreak, the Hon'ble NCLAT waived off the cost imposed by the Hon'ble NCLT.

Committee of Creditors of Rosewood Trexim Pvt. Ltd. through Resolution professional (NCLAT) (15.12.2020)

Exclusion of period for which the Resolution professional was immobilized as a victim of COVID 19 from the CIRP period of 180 days.

An application was filed before the Adjudicating Authority (AA) seeking exclusion of time period lost during the CIRP of the corporate debtor due to lockdown imposed due to Covid-19 pandemic. The said application was dismissed by the AA. An appeal was preferred by the Committee of Creditors of the CD through the RP before the Appellate Authority on the ground that the RP had fallen sick leading him to go into self-isolation and thereafter having been tested positive for Covid-19, which has affected the progress of the CIRP.

Considering the facts and circumstances of the case and the efforts taken by the RP even while he was under self-isolation, and thereafter the CoC having unanimously resolved to approach the AA for seeking exclusion of the period lost due to the lockdown and the condition of the RP, the Appellate Authority allowed the appeal seeking exclusion of time lost during CIRP from 15.03.2020 till 04.10.2020 (RP was tested negative for Covid-19 on 02.10.2020) excluding 203 days from the 180 days period in addition to allowing extension of CIRP period by 90 days, thereby setting aside the order of dismissal passed the Adjudicating Authority.

Mohan Lal Jain in the capacity of Liquidator of Kaliber Associates Pvt Ltd.
vs.
Lalit Modi &Ors.
(NCLAT) (16.12.2020)

AA cannot abdicate its power provided under statutory provision and refer a matter to MCA / Investigating Agency.

The liquidator in the instant case had filed an application before the AA invoking the provisions of Ss. 43 and 66 of the Insolvency and Bankruptcy Code, 2016 for taking action in regard to preferential transactions and fraudulent/ wrongful trading, however, the same has been disposed by NCLT on the grounds that it would be beyond the scope of powers of the Adjudicating Authority to look into the transactions which attract the provisions of Sections 43/66 of the I&B Code and explanation of the opposite party, if required, can be offered to the Investigating Agency.

NCLAT had overruled the decision of the AA on the basis of the dictum of the Apex Court in the matter of *Embassy Property Developments Pvt. Ltd. vs. State of Karnataka and Ors.*, stating that it is abundantly clear that allegations of preferential transactions as also fraudulent trading/ wrongful trading carried on by the Corporate Debtor during the insolvency resolution can be inquired into by the Adjudicating Authority. NCLAT had thus directed the AA will inquire into such alleged dealings in accordance with law with expedition, preferably within two months.

Mr Rajnish Jain, the promoter, stakeholder and Managing Director of Suspended Board of Directors
Vs.
Manoj Kumar Singh – IRP
(NCLAT) (18.12.2020)

"Resolution Professional or Committee of Creditors cannot reclassify the status of a creditor"

The appeal was preferred by the promoter, stakeholder and Managing Director of Suspended Board of Directors of CD against the order of the Hon'ble NCLT, Allahabad Bench, (herein after referred to as 'Adjudicating Authority' or 'AA') whereby the AA had rejected the Application filed by Appellant under Section 60(5) of IBC and declared 'BVN Traders', as a 'Financial Creditor' under Sec 5(7) of the Code and 'Debt' as 'Financial Debt' under Sec 5(8)(f) of the Code.

The brief facts of the case are as follows:

Earlier IRP recognised Claim of the 'BVN Traders' as a Financial Creditor. Against this, an application by the MD of suspended Board of Director of the CD was filed, where the RP in his reply has opined that BVN Traders is not Financial Creditor. Therefore AA passed an order directing the IRP to place the issue before CoC.

Acting as per directors of the Adjudicating Authority, the RP called the Meeting of 'CoC' the CD (M/s Jain Mfg. (India) Private Limited) 'CoC' in its meeting held on 30th August 2019 passed the Resolution '*that M/s BVN Traders be treated as 'Financial Creditor*'.

Subsequently AA by its order dated 23rd January 2020 rejected the Company Application on the ground that the CoC has voted in majority in favour of BVN Traders as "financial creditor" and thus Suspended Management as well as RP has no locus to challenge the commercial wisdom and decision of CoC with regard to determination of Respondent as financial Creditor.

However, the 'CoC' in its meeting held on 14th February 2020 again discussed the proposed Resolution of RP, for not considering M/s BVN Traders as a 'Financial Creditor'. The CoC accepted the proposed Resolution and passed with its majority that 'M/s BVN Traders is not a 'Financial Creditor'.

Subsequently the CoC in its meeting held on 18th February 2020 passed a *Resolution 'to eliminate the name of M/s BVN Traders from the list of 'Committee of Creditors'***.**

Pursuant to the above, the Appellant had approached the Hon'ble NCLAT on the ground that the AA has erred in facts and law in holding that 'M/s BVN Traders is a 'Financial Creditor', which is mainly based on decision of the CoC, though it was not empowered to decide whether 'BVN Traders is a Financial or Operational Creditor.

The issues that arose for Consideration before the Hon'ble NCLAT are:

(i) Whether the Committee of Creditors constituted under Section 21 of IBC, could determine that M/s BVN Traders' is a 'Financial' or 'Operational' Creditor?

The CoC has no role in deciding the status of a creditor either as 'Financial' or 'Operational' Creditor and such a decision of CoC can never be treated as an exercise under its Commercial wisdom. It is a matter of applying the law of I&B Code, and if such factor is left to CoC, there would be a serious conflict of interest, as the present matter itself shows.

It cannot be a matter of voting, and choice as discretion is not relevant. During the CIRP, the IRP collates the Claim, and after that, the 'Committee of Creditors' is formed under Section 18 of the Code. After the formation of the 'Committee of Creditors', only the aggrieved person can agitate the same and that too, only before the Adjudicating Authority.

The CoC was not empowered to adjudicate the issue that has cropped up in the present case, i.e. whether M/s BVN Traders' is a 'Financial' or 'Operational' Creditor. Such adjudication is beyond the scope of consideration of the CoC.

(ii) Whether the Resolution Professional could reclassify the status of a creditor from 'Financial' to 'Operational Creditor' based on the expert opinion despite that the Adjudicating Authority had taken a contrary view?

The IRP after collation of claims and formation of CoC is not entitled to suo-moto review or change the status of a creditor from Financial to Operational Creditor and vice-versa. Updating list and review are different acts. If RP was aggrieved, he should have moved the AA.

The RP cannot arbitrarily on its own overturn earlier decision, to change the status of a creditor from Financial Creditor to Operational Creditor.

Under the duties of RP under Section 25 of IBC 'to maintain an updated list of Claim, he cannot change the status of an existing creditor on his own. But to maintain an updated list of claims the IRP/RP is authorised to add to existing claims or admit or reject further claims received collating them and thus update the list of creditors accordingly.

It is also necessary to mention that core duty of IRP is to receive, collate and verify claims which cannot be further delegated to 'Committee of Creditors', who in turn cannot be allowed to do the same in purported exercise of Commercial Wisdom.

The RP erred to reclassifying the status of a creditor from 'Financial' to 'Operational Creditor', based on the alleged expert opinion despite that the AA took a contrary view.

(iii) Whether the Order of the Adjudicating Authority in upholding that ' BVN Traders' is a Financial Creditor based on the majority decision of Committee of Creditors is valid?

As per Section 5(8) of the Code, the critical requirement of the financial debt is disbursal against the 'Consideration for the time value of money, which included the events and modes of disbursement and enumerated in sub-clauses.

BVN Traders disbursed the debt against the Consideration for the time value of money. It is reiterated that the Appellant Company had raised the said amount from the BVN Traders to meet its working Capital Requirement. Hence the BVN Traders is a Financial Creditor within the meaning of 5(7) and 5(8) of the Code.

BVN Traders disbursed money in the form of fund transfer made towards the purpose of working capital of funding.

It was concluded that to qualify as a 'Financial Creditor' a basic element of disbursal to the Corporate Debtor, of amount against the Consideration of time value of money, needs to be found in the genesis of any debt being claimed as 'financial debt' before it could be treated so, under Section 5(8) of the IBC".

It was held that the transaction involved in the present case meets the root ingredients/basic element of 'financial debt' within the meaning of the Code

Accordingly, upholding the decision of the AA it was held that the BVN Traders is a Financial Creditor within the meaning of Section 5(7) of the Code, and the debt in question is a "financial debt" within the meaning of Section 5(8) of the Code.

Bishal Jaiswal
Vs
Asset Reconstruction Company (India) Ltd. & Anr
(NCLAT) (22.12.2020)

It may be recalled that in our October issue, while discussing the court orders, we reported the above case whereby a reference was made by the three-member Bench to reconsider the decision in V Padamakumar vs Stressed Assets Stabilization Fund (SASF) & Anr. [Bishal Jaiswal vs ARC LTd & Ors, regarding acknowledgment of debt under Section 18 of the Limitation Act, 1963.

It is now reported that the five-member Bench of the Hon'ble NCLAT has turned down the reference by the three-member Bench to reconsider their decision, thereby upholding their view that with regard to initiation of CIRP proceeding the reflection of debt in the balance sheet could not be considered as an acknowledgment of debt under Section 18 of the Limitation Act, 1963.

Kotak Mahindra Bank Limited
Vs.
Committee of Respondents Creditors of Jai Hind Projects
(NCLAT) (23.12.2020)

"Claims cannot be admitted after the approval of a Resolution Plan"

The appeal was filed by the Appellant claiming that they were not informed of the approval of the Resolution Plan by the CoC and hence could not submit their claim and its proof in time. The appeal was filed by the appellant, a Secured Creditor/Financial Creditor of L&T Finance under deed of assignment. The Appellant claimed that the Appellant has to recover dues from the Corporate Debtor – Jai Hind Projects Ltd. It was stated that they were not informed of the approval of Resolution Plan by the CoC and hence could not submit their claim and its proof in time.

The Hon'ble NCLAT dismissed the appeal and held that,

"Considering the fact that the Resolution Plan was already approved on 19th March, 2020 and the Appellant filed claim on 15th June, 2020, keeping in view provisions of IBC (Insolvency & Bankruptcy Code, 2016), we don't think that it is a matter, where things can be undone. The proceedings for CIRP are proceedings which are initiated with Public Notice and Resolution Plan takes its own time to get passed. The claims are to be filed in response to Public Notice which RP/IRP issued. In such contingency, after the Resolution Plan has already been approved in March, 2020, fresh claim cannot be entertained in June, 2020."

Jay Overseas Pvt Ltd
Vs
Mr. George Samuel Resolution Professional of Jason Decor Pvt Ltd. (NCLAT) (23.12.2020)

There is no harm in making an attempt to save the CD from liquidation by CoC.

Jay Overseas Pvt Ltd, a resolution applicant, had submitted its resolution plan for Jason Decor Pvt Ltd. and the same was rejected by the CoC on 11.11.2020. Since there was no viable resolution plan, CoC had passed a resolution for liquidation, and an application for liquidation was filed on 24.11.2020 and is pending before the Adjudicating Authority. The resolution applicant had revised its resolution plan and sought direction upto the Members of the COC to reconsider the revised offer with a further prayer to direct the RP to convene the meeting, when there is no COC. However, the AA had rejected the application stating it to be premature and not maintainable as CIRP period has already been expired and never approached the Resolution Professional directly while a liquidation application is already pending before the tribunal. NCLAT in the instant appeal, had set aside the order of the tribunal by stating that the resolution plan may be processed by the Resolution Professional as required by the provisions of IBC and if in order Resolution Professional will take steps to place the same, before 'Committee of Creditors'. The 'Committee of Creditors' may consider the revised Resolution Plan and it will be for the 'Committee of Creditors' whether or not to accept the Resolution Plan, and if rejected may take further suitable decision regarding liquidation.

State Bank of India
Vs
Dolphin Offshore Enterprise (India) Limited
(NCLT – Mumbai) (04.12.2020)

It is not necessary to record reasons by the Committee of Creditors (CoC) for replacing the IRP/RP.

An application was filed by one of the Financial Creditors seeking replacement of IRP. The Financial Creditor has 74.79% voting share in the CoC. The CoC in its 3rd meeting resolved to replace the IRP and appoint Mr. Dinesh Kumar Aggarwal as the Resolution professional (RP). The said Resolution was voted in favor by 92.44% CoC.

The Applicant has enclosed the copy of the Resolution, voting result as well as the written consent of the proposed RP in Form AA of the Regulation 3(IA) of the IBBI Regulation, 2016. Following the judgement of Hon'ble NCLAT in *Bank of India Vs. Nithin Nutritions Pvt. Ltd.* observed that "It relates to matter of replacing the IRP, reading section 22 with section 27 of IBC, **it is not necessary for Committee of Creditors (CoC) to record reasons for replacing the IRP/RP and it is not necessary for the AA to call for reasons or decide whether there are sufficient reasons**." The Application was thereby allowed and the RP was called on to make all endeavours to complete the resolution process expeditiously within the stipulated period.

Do you Know?

Vide amendment dated 24th December 2020 of Companies (Incorporation) Rules, 2014, the facility of extending the reservation of names obtained using web service SPICe+ has been provided. Therefore, upon payment of fees to the Registrar of Companies, the duration of names reserved can be extended upto a maximum of 40 days as given below:

Fees to be paid (Rs.)	Extension in Days	Remarks
1,000	20	The payment has to be made before expiry of 20 days from date of approval of the name.
2,000	20	The payment has to be made before expiry of 40 days from date of approval of the name.
OR		
3,000	40	The payment has to be made before expiry of 20 days from date of approval of the name.

Fake invoices under Goods and Services Tax

T.Vinod Kannan
Practicing CMA, Qualified Independent Director

In recent times, we heard that the GST Intelligence Department had conducted nationwide concerted drive against GST fake invoice frauds in Nov'20 and arrested 104 unscrupulous persons for illegally availing or passing on input tax credit (ITC) fraudulently through fake entities and fly-by-night firms and circular trading. In this back drop, we have made an attempt to go much deeper into this matter to analyze the purpose of these frauds, steps taken by the department to tackling the fake invoices & to create awareness for the corporates, MSMEs & banks about the same. Let's discuss the issue in detail.

Mens rea of fake invoice:

Whereas the *mens rea* for the use of such fake invoices appears to be fraudulent availment /encashment of ITC credit, the unscrupulous entities engaged in this also defraud other authorities such as Banks by inflating turnovers, laundering of money etc.

Fake invoice & ways of using it:

Invoices without actual supply of goods or services (SoGS) or payment of GST – Fake Invoice. Three ways in which such fake invoices could be misused in GST regime are as follows:

i. Issue of invoices without SOGS where payment of tax is made by way of ITC which is not available to the issuer of invoice. In such cases, there is no receipt of goods or credit by the issuer of invoice. He merely issues invoice and shows payment of tax by non-existent ITC. This results in actual loss of revenue where the buyer of the invoice avails inadmissible credit which is used for payment of tax. There has also been instance where no GST has been paid even by ITC by the issuers of the fake invoice.

ii. Issue of invoices by persons where the invoice is issued to one person and the goods are diverted to some other person. The person who purchases invoices may utilize the credit for payment of taxes at the time of export of goods and claim refund of the said tax paid, resulting in loss of revenue.

iii. Routing of invoices through a series of shell companies/dummy companies and transfer of ITC from one company to another in a circular fashion to increase the turnover. In such cases, there is no SOGS and thereby availment of credit based on such invoices gets hit by the provisions of Rule 16 of the CGST Act, 2017, which stipulates that the conditions that to avail credit, the buyer should have an invoice on which tax has been paid and he should have received the goods. In such cases, availment of credit without receipt of goods is inadmissible and utilization of such credit for actual regular supplies results in loss of revenue and financial accommodation. In such cases, unscrupulous traders are utilizing the GSTN System to create invoices, fake e-way bills showing movement of goods etc., to defraud the revenue and the banking system.

Potential motives:

1. Evasion of GST on taxable output supplies by availing undue ITC, Saving GST (cash) by payment of tax liability using undue ITC & Clandestine supply without invoices and without payment of taxes
2. Converting excess ITC into cash by transferring of ITC to those who can utilize it, shifting ITC from exempted supplies to taxable supplies, Encashment of ITC by way of IGST refund or unutilized ITC refunds
3. Inflating turnover for the purpose of availing higher Credit Limit/ Overdraft from Banks, obtaining bank loans, improving valuations for IPO or sale of stake &Obtaining contracts including Government contracts
4. Booking fake purchases for getting Income-tax benefits by showing reduced profit margins and higher expenses & avoiding payment of Income-tax by reducing net profit
5. Cash generation/ diversion of company funds

Features of a few cases which were detected by the department:

1. Huge availment of ITC in shorter time.
2. Fabrication of Invoices.
3. E-way bills without corresponding filing of returns.
4. Large number of GSTIN entities spread over States.
5. Some of the entities would fall under the jurisdiction of the CGST authorities while the connected entities fall under the jurisdiction of the State authorities.
6. Floating of dummy firms, addresses are often incorrect/incomplete and the details revealed in the registration forms are often false.
7. Dummy companies with verifiable facts but no assets or means to do business; they act as surrogate for other large companies to camouflage their activities.
8. Connivance with transporters to get bogus bilty/consignment note.
9. Fly-by-night operators are used to get GSTIN and generate large number of tax invoices and e-Way bills in the first few months and disappear.
10. Encashment of ITC availed on fake invoices by obtaining IGST/ITC refunds especially in case of exports.
11. Supplies made and GST collected but not paid i.e. GSTR-1 is filed but GSTR- 3B is not filed. In some cases both GSTR-1 and GSTR-3B are not filed.

Strategies of the department to tackle fake invoices:

Some of the key elements of risk profiling to check such GST frauds by the department has been listed.

1. Scrutiny/Verification of registered taxpayers through risk profiling and verification for early identification of fraudsters indulging in fake invoices.
2. Historically tax evasion prone sectors.
3. Maintenance of offence database of those figuring in frauds to prevent their re- entry in the System.
4. Some of the risk indicators of such persons or activities done by them or commodities traded by them or patterns behind their activities are as under:
   a) Multiple registrations on same PAN.
   b) Common email, common mobile numbers, common address, common authorised signatory, common promoters etc.
   c) A person whose registration application is rejected or a person whose registration is cancelled may apply again for registration.
   d) Live registration against the said PAN with the CGST jurisdiction where offence has been booked by SGST authorities.

Department's standard operating procedure to detect and tackle "fake invoice" fraud:

Identification: Identification of entities who generate "fake invoices" is the first step in curbing this menace. This method also involves identification of generators and users. To identify the generators of fake invoices the following risk parameters are used.

1. Multiple GSTIN registrations for a given address
2. Multiple GSTIN for a given PAN
3. GSTIN using incomplete or wrong addresses

4. Tax payers using sensitive commodities
5. Common e-mail, common mobile nos, common address, common authorised signatories, common promoters for multiple GSTIN.
6. Mismatch between the premises declared and the volume of goods transacted.
7. Mis-match between the quantum or transactions and the e-way bills generated. If there are no e-way bills or less e-way bills generated compared to details of transactions as per the GSTR.
8. PAN involved in any "fake invoice" fraud or any other GST frauds appear as either in GSTR1A or GSTR 2A.
9. Abnormal ITC utilisation (for example above 95%).

Identification also involves the users of fake invoices because, this is where the real concern rests. The user can utilise the fraudulent credit for payment of supply of goods or services. The item number "8 and 9" above will help in identifying the potential users of credit accumulated through fake invoices.

Investigation: The primary aim of investigation is to establish that there was no actual supply of goods or services by the supplier to prove that they issued "fake invoices". This will be achieved by following steps.

1. Search of all premises declared to prove the lack of or inadequacy of manufacturing facility of the declared goods.
2. Other indicators like consumption of electricity, water etc. mismatch with the declared quantum of goods manufactured.
3. Lack of facility and space to handle the quantum of goods traded.
4. Suppliers of invoices do not have any premise for dealing with the goods
5. The inputs and input services required for provision of certain services not existing.
6. Lack of valid clearances / licences / permissions from any other authorities which are required to deal in any manner with either inputs or final products or intermediate products, input services or output services.
7. Lack of required agreements between the entities.
8. Lack of e-way bills
9. Fake vehicle numbers shown in e-way bills or invoices.
10. Comparing the details supplied to other agencies like Income Tax, Registrar of companies
11. Mismatch with the details available for vehicles from RTO office.

Recent steps by the department:

In furtherance to the above steps, department has taken few more steps in the recent days to curb this menace.

1. Registration against Aadhaar authentication or Physical verification by the department officials.
2. Sector specific analysis in GSTN database through Artificial Intelligence tools.
3. Introduction of GSTR 2B
4. Mandated e-invoicing for the taxpayers with aggregate turnover exceeding Rs. 100 Cr. (in any preceding financial year from 2017-18 onwards).
5. Auto Population of E-Invoice in GSTR 1.
6. Importing Invoices from E-way bill site to GSTR 1.
7. Blocking of E-way bill facility in case of failure in furnishing of GSTR 3B / GST CMP 08 returns for 2 months.
8. Auto populated GSTR 3B from GSTR 1 & GSTR 2B.

(Image Source Website)

It has been clearly pointed out the department was taking serious steps through various tools in the GSTN to detect these frauds at the earliest. Likewise, bankers, MSMEs & Corporates should not fall under these traps of fake invoices. Necessary recovery proceedings like attachment of property, bank accounts, etc. will be initiated by the department against the generators & potential users. Hence, the users need to be very cautious to prove the authenticity of their credit.

Now, the bankers need to be very cautious while lending with these new initiatives by the department. It looks like department will initiate recovery actions faster than the bankers with the better analytical tools. In coming days, banks may insist the borrowers to submit the reconciliation statement of GST returns with Income Tax returns, reconciliation of ITC utilisation, percentage of e-invoices, percentage of e-way bill supplies, etc. to safeguard their lending. This article is written to spread the awareness of fake invoices to the readers who in-turn spread the same to their borrowers / vendors for a better & growing economy.

Leadership Language or Leadership is Language?

S.Rajendran

All other things being equal, an organization with a good management has an edge over its peers. A good management is a result of good leadership. Studies on leadership cases have hogged the limelight time to time. A Fortune-500 CEO in cloud nine or a once-respected corporate falling from grace and disappearing into thin air do carry leadership stories.

Recently I came across an interesting book:

Leadership is Language
(The hidden power of what you say – and What you don't.)
Author: L. David Marquet

The author deals with the two important elements of all human activities: doing and thinking.

In the industrial age, the focus and urgency was on getting things done. There was not much time to think. "Thinking" was done by a chosen few who were not "doing". In other words, doers and deciders were different. All that is history now. In the changed context of globalization and service-oriented organizations becoming large value creators, the equation has changed. "For organizations to survive, the doers must also be the deciders".

More precise account of what is doing and what is thinking is very lucidly explained by the author as below:

> **"Our interaction with the world is doing.**
> **Improving our interaction with the world is thinking.**
>
> **Proving and performing is doing.**
> **Growing and improving is thinking.**
>
> **A focused, exclusive, driving, proving mindset is best for doing.**
>
> **An open, curious, seeking, improving mindset is best for thinking."**

A fair share of both doing and thinking is required for creating a resilient, adoptive and agile environment for more profitable and fulfilling engagement.

The new leadership roles, as clearly contrasting the old age regimen, are highlighted by the author as below:

1. **Control the clock instead of obeying the clock.**
2. **Collaborate instead of coercing.**
3. **Commitment rather than compliance.**
4. **Complete defined goals instead of continuing work indefinitely.**
5. **Improve outcomes rather than prove ability.**
6. **Connect with the people instead of conforming to your role.**

The author goes on to highlight that the language used by the leader should be one of seeking, eliciting more involved role play rather than coercing a single word answer like "yes" or "no". Look at the following examples for a leadership language in contrast to the industrial age language:

"Get it done!"	**"How do you see it?"**
"Make it happen."	**"How ready are we for this?"**
"Let's finish this."	**"What can we do better?"**
"Are we on track?"	**"What did we learn?'**

The author introduces the concept of "Team Language Coefficient (TLC)" as an excellent indicator of the power gradient in an organization. The share of voice – that is who speaks more in an organization – is indicated by the TLC. If the leader says 100% of the words and no one else says anything, the share of voice is completely skewed. A more balanced share of voice would lead to more team thinking and better decision outcomes.

The major contribution and involvement of the team has to be inspired by the leadership. This is quoted as the "wisdom of the crowd" rather than "wisdom of the loud".

"We need to always remember that the organization is perfectly tuned to deliver the behavior and people's behaviors are the perfect result of the organization's design."

(Image Source website)

"As individuals, we should embrace our responsibility for being the best we can do within the design of the organization. But as leaders, our responsibility is to design the organization so that individuals can be the best versions of themselves."

Leadership language has to be very clear in order to ensure that the team has clarity of how it should proceed. Therefore leadership is language.

The principles suggested by the Author have profound value in maximizing contribution by any team in any organization. Had they been followed by the Captain of the American Container Cargo Ship "El Faro", the precious lives of 33 mariners on board the vessel could have been saved from a furious hurricane in 2015 in Atlantic Ocean.

Your Feedback Matters

Just had time to go through. As always, very relevant contents. Article on “Smart Trust” is quite interesting.

- Mr. S. Kalyanaraman, Director of TTK Pharma Ltd.

Article on Role of CoC & its commercial wisdom is a quite useful topic for bankers, RPs to decide the resolution Plans. Kudos to the legal team to cover the judgements delivered on 24th Nov 2020 & 26th Nov 2020 (especially for Venus Recruiters case)

- Mr. T. Vinod Kannan, CMA

Am happy to receive this magazine containing some many articles. Good job Keep it up.

- CA Mr. Madhu Desikan

Thanks a lot for sharing

- Prof. R. Balakrishnan, FCS

Thank you for sharing the same

- Mr. K. Sampath Kumar, GM, CAG, SBI

Your Publication SandBox is extremely efficient in knowledge sharing. Great Initiative.

- Mr. Robin Mukhopadhyay, CEO
Haldia Petrochemicals Ltd

Query raised by Mr. Ravindra Sathyamurthy on the provisions of the Companies Act, 2013

Query No: 1

As per Sec.151 of Companies Act, 2013, a Small Shareholders' Director has a maximum tenure of 3 years. If he qualifies for appointment of independent director, he may be considered as independent director. In case he is considered as independent director then whether his term of office will be for 3 years or 5 years?

Response:

Sec.151 of Companies Act, 2013, states that a listed company may have one director elected by such small shareholders in such manner and with such terms and conditions as may be prescribed.

For the purposes of Sec.151, small shareholder mean a shareholder holding nominal value of not more than Rs.20,000/= or such other sum as may be prescribed.

Rule 7 of Companies (Appointment and Qualifications of Directors) Rules, 2014 provide the terms and conditions of appointment of small shareholders' director.

Rule 7(4) says:

"Such director shall be considered as an independent director subject to, his being eligible under sub-section (6) of section 149 and his giving a declaration of his independence in accordance with sub-section (7) of section 149 of the Act.

Rule 7(5) (b) says that such director's tenure as small shareholders' director shall not exceed a period of three consecutive years; and
Rule 7(5)(c) says that on the expiry of the tenure, such director shall not be eligible for re-appointment.

Rule 7(6)(c) says that "A person appointed as small shareholders' director shall vacate the office if the director ceases to meet the criteria of independence as provided in sub-section (6) of section 149.

Further, Rule 7(9) says that a small shareholders' director shall not, for a period of three years from the date on which he ceases to hold office as a small shareholders' director in a company, be appointed in or be associated with such company in any other capacity, either directly or indirectly.

A combined reading of all the above provisions imply that a small shareholders' director can be considered as an independent director if he meets the eligibility criteria for an independent director. This provision enables a company to simultaneously comply with the requirement of appointing an independent director if he is found to be eligible as per Sec.149 (6).

However, to be in sync with the provisions that a small shareholders' director cannot hold the position for more than three years and again considering the provision of Rule 7(9), he cannot continue to be associated with the same company as an independent director. Therefore, the appointment as independent director can be for a term of only 3 years co-terminus with the term as small shareholders' director.

Having said this, it is worth mentioning here that though Sec.149 (6) carves out some exceptions or threshold in the eligibility criteria for independent directors, the words used by Rule 7(9) are more restrictive in the sense that a small shareholders' director shall not be appointed or associated with the company in any other capacity either directly or indirectly after he ceases to hold office as a small directors' shareholder.

Query No: 2

The Companies Act, 2013 states that an alternate director may be appointed by way of a circular resolution. Can an additional director, nominee director and casual vacancy director also be appointed by way of a circular resolution?

Reply:

As per Sec.161 of the Companies Act, 2013, the nominee director, alternate director and additional director may be appointed by the Board of Directors of a company if authorised by the Articles of Association of the Company.

Therefore, additional director and nominee director may be appointed by the Board of Directors by way of a circular resolution as well.

However, as per Sec.161(4) of the Companies Act, 2013 the casual vacancy of a director appointed by the company in the general meeting may be filled by the Board of Directors at a meeting of the Board. This provision insists that such appointment has to be done by the Board of Directors at the meeting of the Board and not by way of circular resolution.

CGRF wishes the SandBox readers and their family

A VERY HAPPY PONGAL!!!

CREATE & GROW
RESEARCH FOUNDATION

CGRF Research Scholars

We are glad to share with the esteemed readers that CGRF advertised in newspapers on 14th December 2020 for enrolling interested research scholars for undertaking various research activities as a part time avocation. 26 Applications were received. The research scholars were requested to share a two page article on any of the topics given to them.

16 Participants submitted their articles and out of them, the articles shared by the following three research scholars were chosen for publishing in SandBox January 2021 issue.

S. No	Name	Place	Topic
1	Jincy Jose	Kerala	Independent Director – an important player in good corporate governance. Justify the role of independent directors
2	K. Sheeba Nair	Kerala	Will registration of Trade Marks protect your unique value propositions?
3	Darshak Thaker	Gujarat	Independent Director – an important player in good corporate governance. Justify the role of independent directors

With immense pleasure, we are carrying these three contributions in this issue of SandBox. We are hopeful more research publications would be forthcoming in the months ahead on topics of importance. We are happy to share the details of all other contributors:

S. No	Name	Place	Topic
4	C M Eswara Prasad	Chennai	1. When is the company said to have abused its dominant position in the market under Competition Law? 2. A resolution professional is vested with the powers of the Board of the corporate director during the CIRP. What are the likely pitfalls when he is discharging his role in a large running organisation?
5	CS Victor J. Uruvath	Thrissur	Independent Director "An important player in good corporate governance"
6	S. Rukmani	Chennai	Will registration of Trade Marks protect your unique value propositions?
7	S. Ranjani	Chennai	Recovery Road in Bankers Journey – DRT-SARFAESI-IBC
8	K. Rajasekhar	Hyderabad	Role of RBI
9	N. Nagendra	Bangalore	Role of Independent director
10	Rajesh Reddy	AP	Independent Director – an important player in good corporate governance. Justify the role of Independent directors
11	Arthi R	Bangalore	CoCs enjoy and unquestionable authority in a CIRP. Is it true?
12	K V Lakshmi	Chennai	Independent Director – an important player in good corporate governance. Justify the role of Independent directors
13	Akhil Nagendra Bachu	Hyderabad	Role of RBI in reviving the economy post the Covid – 19 turbulence.
14	Farahnaz Jabbar	Chennai	IBC is not a recovery tool
15	Sanofar A	West Bengal	Do you think women can play a more progressive role in ensuring good corporate governance? If so, how?
16	G Sri Vidya	Chennai	Independent Director – an important player in good corporate governance. Justify the role of Independent directors

CGRF offers online/class-room Awareness/Training sessions on Corporate Laws, IBC and other Commercial Laws

We are glad to share with you that CREATE & GROW RESEARCH FOUNDATION (CGRF) is a premier, not-for-profit research organization established as a Section 8 Company under the Companies Act, 2013. CGRF has been organizing seminars and Awareness programs on IBC and various other corporate laws to bankers, corporate professionals, faculty members of Universities, Colleges, Legal Professionals, Students, Government Organizations like EPFO, ESIC, Income Tax, GST, etc.

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- **Insolvency & Bankruptcy Code 2016**
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- **Excellence in Management**
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- **Proxy Advisory Services for Institutional shareholders**

We have rich expertise on the abovesaid commercial laws with practical exposure in several industries. Our association with all the major banks gives an edge to provide professional training on practical aspects. We also provide classroom training for students on latest developments in business environment, regulatory domain and challenges faced, etc. Online sessions are also available for 2 hours / 4 hours.

Our training sessions to various educational institutions, bankers and Government departments have been received well with appreciable improvement in recognizing importance of updating knowledge in relevant fields.

Call for more information: Ms. Priya Karthick - Contact No: 044 - 2814 1604

CREATE & GROW RESEARCH FOUNDATION
2nd Floor, Evalappan Mansion, No.188/87,
Habibullah Road, T.Nagar, Chennai - 600 017
(Near Kodambakkam Railway Station)
Phone: 044 2814 1604 | Mobile: 94446 48589 / 98410 92661
Email: create.and.grow.research@gmail.com
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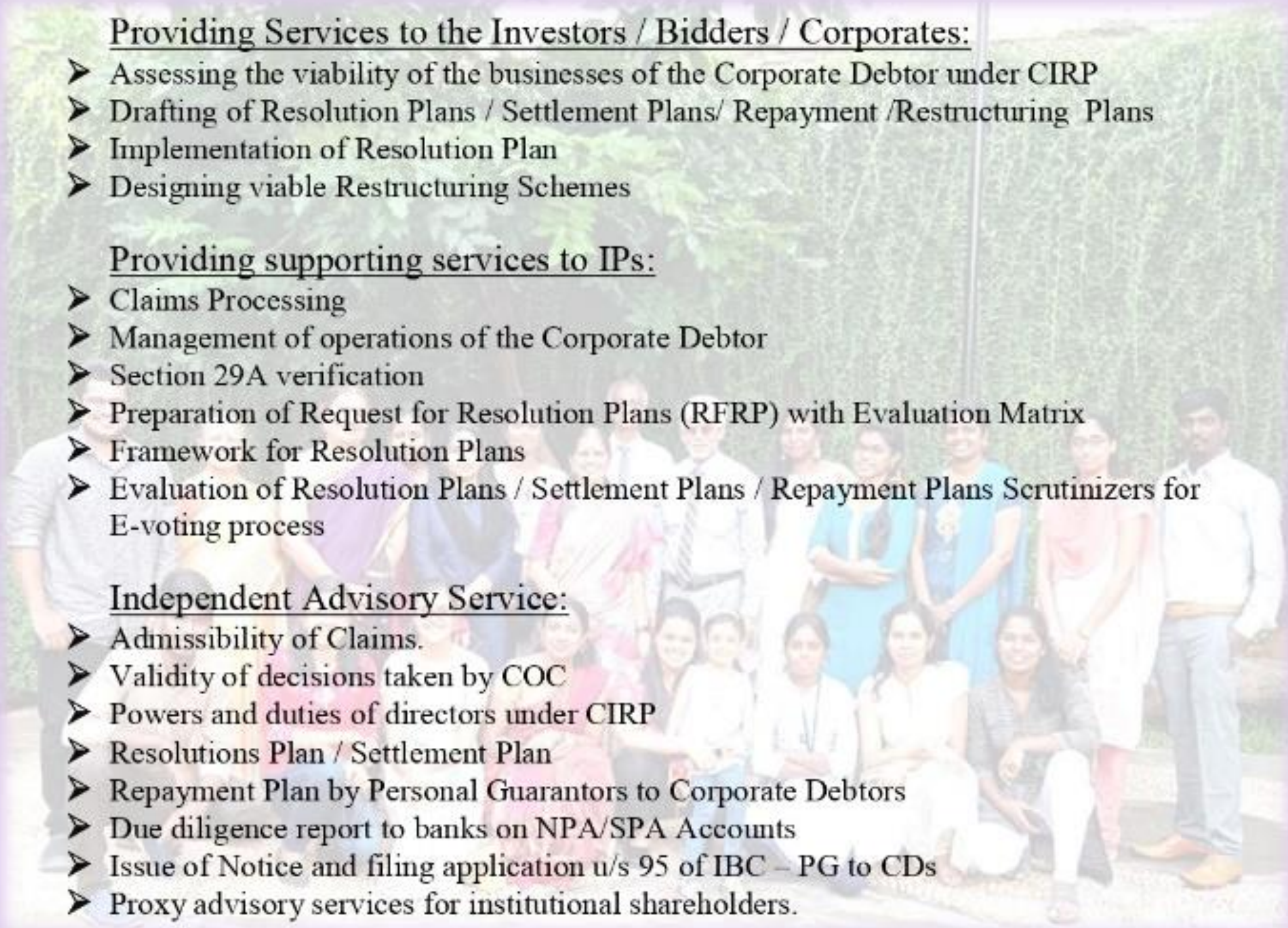
OUR SERVICES



Providing Services to the Investors / Bidders / Corporates:

- Assessing the viability of the businesses of the Corporate Debtor under CIRP
- Drafting of Resolution Plans / Settlement Plans/ Repayment /Restructuring Plans
- Implementation of Resolution Plan
- Designing viable Restructuring Schemes

Providing supporting services to IPs:

- Claims Processing
- Management of operations of the Corporate Debtor
- Section 29A verification
- Preparation of Request for Resolution Plans (RFRP) with Evaluation Matrix
- Framework for Resolution Plans
- Evaluation of Resolution Plans / Settlement Plans / Repayment Plans Scrutinizers for E-voting process

Independent Advisory Service:

- Admissibility of Claims.
- Validity of decisions taken by COC
- Powers and duties of directors under CIRP
- Resolutions Plan / Settlement Plan
- Repayment Plan by Personal Guarantors to Corporate Debtors
- Due diligence report to banks on NPA/SPA Accounts
- Issue of Notice and filing application u/s 95 of IBC – PG to CDs
- Proxy advisory services for institutional shareholders.

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CREATE & GROW RESEARCH FOUNDATION

2nd Floor, Evalappan Mansion, No.188/87, Habibullah Road,
T.Nagar, Chennai - 600 017. (Near Kodambakkam Railway Station)
Phone: 044 2814 1604 | Mob: 94446 48589 / 98410 92661
Email: createandgrowresearch@gmail.com
Website: www.createandgrowresearch.org