MMJC

# MMJCINSIGHTS
## 20 JULY , 2023

# Index



# Is that True?

# Verification of Market Rumours made Mandatory.

## 1. Background

Generally speaking, verification of reported events or information which may have material effect on the listed entity is essential to avoid establishment of a false market sentiment or impact on the securities of the entity. In recent years, a growing influence on market sentiments is being noticed of not just print media, but also television and digital media which sometimes contribute to sudden price movements of specific scrips on stock exchanges based on unverified information about the listed entity. In order to stay contemporary, listed entities need to keep pace with all forms of media, both print and electronic / digital and ensure prompt verification of such rumours, so that they can respond to such rumours quickly before the market price their scrips get impacted by such rumours, one way or another.

## 2. Introduction to the Amendment:

Securities and Exchange Board of India ('SEBI') vide its amendment notification dt: June 14, 2023, amended Regulation 30(11) of Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2023 ['LODR'] and inserted provisos which are mandating rumour verification by certain listed entities as mentioned therein and as elaborated in below paras. These listed entities would now be required to establish a robust mechanism for rumour verification and timely dissemination of accurate information. Considering the fragmentation and cryptic reach of electronic and social media presently, (viz. 1000+ print and digital media means in India and abroad) rumours may be spread in 360 degrees, and it practically stands challenging for a listed entity to respond.

**A.** The **existing provision before the amendment** is stated as follows:

Regulation 30(11) of the LODR: *The listed entity **may on its own initiative** also, confirm or deny any reported event or information to stock exchanges(s).*

Currently (before the amendment becoming effective), rumour verification is a voluntary compliance. But it was applicable to all listed entities and not restricted to certain listed entities. Now SEBI has shifted this compliance requirement from voluntary to mandatory to certain categories of listed entities as mentioned below.

**B.** ***Regulation 30(11) - After Amendment:***

*After sub-regulation 11 the following provisos and Explanations shall be inserted namely:*

Regulation 30(11) of the LODR: *The listed entity **may on its own initiative** also, confirm or deny any reported event or information to stock exchanges(s).*

*"Provided that top 100 listed entities (with effect from October 01, 2023) and thereafter top 250 listed entities (with effect from April 01, 2024) **shall confirm, deny or clarify** any reported **event or information** in the mainstream media **which is not general in nature** and which indicates the **rumours of an impending specific material event or information** in terms of the provisions of this regulation are **circulation amongst the investing public**, as soon as reasonably possible but not later than twenty hours from the reporting event or information.*

*Provided that if the listed entity **confirms the reported event or information**, it shall also provide the **current stage of such reported event or information**.*

*Explanation: The top 100 and 250 listed entities shall be determined on the basis of market capitalization as at the end of the immediately preceding financial year"*

From the above amendment, it can be seen that the requirement to provide any verification on rumours, which was earlier voluntary for all listed entities, has been made mandatory for top 250 listed entities in a phased manner as mentioned in the above-mentioned proviso.

**3. Anomalies and questions relating to rumour verification.**

**a. Specific events or information only needs to be clarified?**

It needs to be highlighted here that what needs to be clarified is rumours relating to specific event or information in the mainstream media. It is not mandatory to confirm or deny or clarify rumours that are general in nature. Question thus arises is how would listed entities be able to demarcate between specific event or information and general information pertaining to a listed entity? For this it would be important for listed entity to evaluate whether majority details of the event or information is being spoken about in mainstream media OR is it only a probability, without any definitive details, which is being discussed in mainstream media? It is not defined or explained what would 'not general in nature' mean? So, this analysis will have to be done by listed entities on a case-to-case basis.

**b. Rumour verification once applicable always applicable?**

Rumour verification is being made applicable to listed entities falling under top 100 and top 250 based on market capitalisation as at the end of immediately preceding financial year. It needs to be highlighted that as per Regulation 3(2) of LODR Regulations "*The provisions of LODR Regulations which become applicable to listed entities on the basis of market capitalisation criteria shall continue to apply to such entities even if they fall below such thresholds.*"

Hence it can be seen that once provisions of particular regulations become applicable on the basis of market capitalisation then it shall continue to remain applicable. So even if a listed entity falls outside market capitalisation of top 250 or 100 in future, then also it will have to continue to comply with same.

**c. Whether it is necessary to 'confirm, deny or clarify and mention specify stage of event' when clarification on market rumours is raised by stock exchange under Regulation 30(10) of LODR Regulations?**

Regulation 30(10) of LODR Regulations specifies that listed entity **shall** provide specific and adequate reply to all queries raised by stock exchange(s) with respect to any events or information. Regulation 30(11) of LODR Regulations provides for voluntary rumour verification by listed entities except for top 100 and top 250 listed entities. Regulation 30(10) uses the word "shall" and it is applicable for all listed entities. So, if clarification on market rumours is raised by stock exchange under Regulation 30(10) of LODR Regulations, then it is mandatory on the part of any listed entity, irrespective of market capitalization, to provide specific and adequate reply to all queries raised by stock exchange(s).

It may be noted that SEBI has added proviso about 'confirm, deny or clarify specific event or information' in Regulation 30(11) and not Regulation 30(10). Hence, in cases where clarification on market rumours is raised by stock exchange under Regulation 30(10) of LODR Regulation, then irrespective of whether the rumour is general or specific is nature, listed entities are bound to provide specific and adequate reply. However, listed entities are not bound to confirm, deny, or clarify about the rumour, unless it is of a specific nature.

Further if the rumour is specific in nature, then irrespective of whether the stock exchange has asked for clarification or not, the top 250 listed entities will need to 'confirm, deny or clarify specific event or information'.

Further there may be scenarios where a listed entity which is not covered in top 250 listed entities may be confirming, denying, or clarifying specific event or information on a voluntary basis. In such cases also, if the listed entity is confirming the rumour, then it is bound to provide the current stage of such event or information, even if it is making this disclosure voluntarily.

**d. Word 'clarify' added as against word 'confirm or deny' under Consultation Paper**

Consultation Paper dt: November 12, 2022, on Review of disclosure requirements for material events or information under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 had proposed to 'confirm' or 'deny' rumours. But in

the amended LODR Regulations, SEBI has now added words 'confirm or deny or clarify' under Regulation 30(11). As per SEBI Board note for its Board meeting dated 29th March 2023, SEBI had received representations stating that a rumour or reported event / information is false from the standpoint of the listed company but would be valid from the standpoint of a third party which listed entity may not be in knowledge of. In such situations listed entities shall be allowed to clarify on the event or information. SEBI acceding to this request added the word 'clarify' under Reg. 30(11) of LODR Regulations.

## 4. Conclusion

On perusing the above measures for rumour verification, it becomes clear that specific provision relating to rumour verification would go a long way in reducing information asymmetry in market.

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# Press Releases to Stock Exchange– Whether material information? Whether UPSI?

## I. Concerns on disclosures by listed entities through Press Release:

Securities and Exchange Board of India ('SEBI') on May 18, 2023, through a consultation paper[1] had proposed changing the definition of Unpublished Price Sensitive Information ['UPSI'] as provided under Regulation 2(1)(n) of SEBI (Prohibition of Insider Trading) Regulations, 2015 ['SEBI PIT']. This proposal was based on certain analysis done by SEBI. SEBI observed that certain listed entities did not have an analytical approach in identifying and disclosing material information to stock exchange. SEBI further observed that many listed entities, on many occasions, had missed to categorise material information as UPSI. This analysis was backed by analysis of 1,100 press releases that were issued by the top 100 listed companies between January 2021 and September 2022. In this analysis it was seen that, out of 1,099 press releases, in 227 instances, there was price movement in the scrip which was more than 2%. However, of these 227 instances, merely 8% (18) press releases were categorised as UPSI by the listed companies.

SEBI highlighted that this meant that if total press releases are considered, only 1.64 per cent of them were categorized as UPSI by the listed companies, which in turn, had hampered its (SEBI's) efforts towards curbing insider trading by the non-categorization of material information as UPSI by the listed companies. If we see the meaning of the term 'Press Release' as per Collins dictionary, it means that *"a press release is a written statement about a matter of public interest which is given to the press by an organization concerned with the matter."* From the definition it can be understood that press releases are mainly meant for media. Press Releases to media would be brief in nature i.e., in the form of news to be given to media for public at large. Such press releases, as it is, cannot be given to the stock exchange. Information to be given to stock exchanges must be in compliance with guidelines given SEBI and Stock Exchanges.

So, there is a need for listed companies to check if press release is in itself or contains any material information or not before releasing the same.

## II. Precedents – Press Releases not being considered as Material Information and UPSI:

In recent past, SEBI has adjudicated a few matters relating to insider trading wherein press releases were issued by listed entities for disclosure of material information and UPSI. SEBI has, in these adjudication orders on insider trading, made remarks regarding practices followed by listed companies of disclosure of material information through press release. In one of the recent cases[2] SEBI Adjudication Officer / contended as follows,

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[1] https://www.sebi.gov.in/reports-and-statistics/reports/may-2023/consultation-paper-on-proposed-review-of-the-definition-of-unpublished-price-sensitive-information-upsi-under-sebi-prohibition-of-insider-trading-regulations-2015-to-bring-greater-clarity-and-uni-_71337.html

[2] In the matter of Zee Entertainment Enterprises Limited ('ZEEL') dated. March 31, 2023

*"I have perused the press releases enclosed by Noticees and observe that the events mentioned in the said press releases are varied and among others, relate to ZEEL's merger with Sony Pictures, corporate information, appointments in ZEEL, etc. A press release is usually carried out to publicise an event considered significant by the company. Press releases may also relate to company's information pertaining to awards received by it, its activities pertaining to Corporate Social Responsibility, etc. which may not necessarily constitute price sensitive information. In the list of press releases provided by the Noticees,* ***it is also observed that certain price sensitive information had been communicated through press release as well.*** *For instance, ZEEL had, for instance, issued a press release announcing their agreements for merger with Sony Pictures Networks India which was a price sensitive information.* ***Therefore, information provided through press releases needs to be assessed to determine whether the information is price sensitive or not…"***

Further in another order, Securities Appellate Tribunal had highlighted concerns on disclosure made in the form of a press release by Edelweiss Financial Services Ltd regarding 100% acquisition by its step down wholly owned subsidiary. It was argued by Edelweiss that this 100% acquisition was neither material information nor price sensitive information. In this case[3] Securities Appellate Tribunal held as follows, *"Moreover, it is a fact that the* ***company did not make the disclosure under Regulation 30 of LODR Regulations giving all details of the financial magnitudes*** *and business volumes and stating that the acquisition, though 100% of a company, is only addition to the fintech having no impact on the business volumes etc…..The above* ***disclosure only talks of 100% acquisition of a company*** *by a subsidiary of Edelweiss which would help grow Edelweiss fixed income advisory business.* ***No caveats are given****; rather certainly the disclosure is clearly as a positive addition to help the business growth of Edelweiss…. Therefore, in our considered view any event like 100% acquisition of a company, irrespective of its value or size is material and liable to bring in UPSI and consequently liable for regulatory compliance under LODR and PIT Regulations"* Stock markets function on disclosure-based regime. Disclosure of correct and adequate information is responsibility of listed companies.

## III. Circulars from Stock Exchanges:

Guidance in form of Circulars have been issued by Stock Exchange **(**Bombay Stock Exchange ['BSE'] and National Stock Exchange ['NSE'])[4] for the language to be used while submitting information**.** BSE and NSE have provided an indicative list of things that need to be kept in mind by listed entities while making disclosures to stock exchanges. Guidelines provided by the stock exchange range from providing concise, truthful, fair, and evidence-based data. Also, stock exchanges have given guidance on content pertaining to specific disclosure viz. receipt of award. It has also been advised to avoid using technical and complex language.

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https://www.sebi.gov.in/enforcement/orders/mar-2023/final-order-in-the-matter-of-zee-entertainment-enterprises-limited_69683.html

[3] Order of SAT in the matter of Edelweiss Financial Services Limited dt: March 24, 2021.

[4] https://www.bseindia.com/markets/MarketInfo/DispNewNoticesCirculars.aspx?page=20210611-28 – BSE circular. https://static.nseindia.com//s3fs-public/inline-files/NSE_guidance_note_11062021.pdf - NSE Circular dt: June 11, 2021

## IV. Conclusion:

Looking at the above guidance being given through Orders by SEBI and SAT and through the guidance issued by stock exchanges, it is very important that how are listed entities handling the issuance of press releases and disclosure of related information to stock exchanges.

Listed entities need to be guided by following points while making submission of information pertaining press releases to stock exchanges:

a. Whether the information is material information warranting disclosure to stock exchange under Regulation 30 read with Schedule III of LODR Regulations?
b. If yes, then the disclosure to be given to stock exchange shall be accompanied by minimum disclosures that are required to be given as per SEBI Circular September 9, 2015, as may be applicable.
c. Disclosures given to stock exchanges shall be in compliance with Guidance provided by BSE and NSE for communication to stock exchanges.
d. If the listed entity is of the view that the information in Press Release is not in the nature of material information under Regulation 30 read with Schedule III of LODR Regulations, then the listed entity needs to ensure that it has adequate justification as to why that information is not material information? and also ensure documentation of such justification in its relevant records.
   Further in such cases, the press release should not be submitted to stock exchanges under the tab of 'Regulation 30' while filing with stock exchanges in XBRL mode.
e. Similarly, the listed entity should be clear on whether the information is in the nature of UPSI? If yes, then all relevant activities under SEBI PIT, like closure of trading window, entries in structured digital database etc., right at the stage of germination of such information.
f. If the listed entity is of the view that the information in Press Release is not in the nature of UPSI, although it may or may not be material information under Regulation 30 read with Schedule III of LODR Regulations, then the listed entity need to ensure that it has adequate justification as to why that information is not in the nature of UPSI?, and also ensure documentation of such justification in its relevant records.

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https://www.taxmann.com/research/company-and-sebi/top-story/105010000000023081/disclosures-by-listed-entities-through-press-release-whether-material-information-whether-upsi-experts-opinion

# Understanding SEBI's Material Event Thresholds: Enhancing Disclosure Standards for Market Integrity

## I. Background:

Regulation 30(1) of Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements), Regulations, 2015 ['LODR Regulations'] requires listed entities to disclose material information to stock exchanges. Regulation 30(4) states the criteria that listed entities should see to determine what would be considered as material information /event. Earlier barring certain events / information which were deemed to be material, determination of whether an information is material or not was left to the listed companies. There was no specified threshold provided for considering information or event as material. Listed Companies were guided by provisions of Clause (i) of sub-regulation 30 (4) of LODR Regulations for determining what was considered as material information.

## II. Rationale of Amendment:

In November 2022, SEBI issued a Consultation Paper for bringing transparency, objectivity and uniformity while disclosing material events or information specified under Regulation 30 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("*LODR Regulations*").

The Consultation Paper underlined the issue(s) observed by SEBI while disclosing the events specified in Para B of Part A of Schedule III upon applying guidelines of materiality. It underlined the fact that many listed entities do not disclose events specified under Para B on the ground that they are not considered as material as per their Materiality Policy framed in terms of the criteria prescribed in regulation 30(4) of LODR Regulations.

Therefore, to bring uniformity in the Materiality Policy of Listed entities, SEBI proposed to introduce a quantitative criterion of minimum threshold for determining materiality of information events for disclosure specified under Para B of Part A of Schedule III based on the value or the expected quantitative impact of the event.
The proposal was accepted and incorporated in LODR Regulations by way of SEBI (Listing Obligations and Disclosure Requirements) (Second Amendment) Regulations, 2023 ("*the Amendment*"). This Amendment shall be effective from July 14, 2023.

## III. Amendment:

Now pursuant to amended Reg. 30(4)(i) of LODR Regulations, ISEBI has prescribed new thresholds as clause (c) in Regulation 30(4)(i) as to what would be considered as material information. Pursuant to Reg. 30(4) of LODR Regulations listed companies shall consider the following criteria for determination of materiality of events/information:

(a) the omission of an event or information, which is likely to result in discontinuity or alteration of information already available publicly; *[existing clause]* or
(b) the omission of an event or information is likely to result in significant market reaction if the said omission came into light at a later date; *[existing clause]*
(c) omission of an event or information, whose threshold value, or the expected impact in terms of value exceeds the lower of the following: ***[newly added clause]***
    1. **two percent of turnover**, as per the last audited Consolidated financial statements of the listed entity;
    2. **two percent of net worth**, as per the last audited Consolidated financial statements of the listed entity, except in case the arithmetic value of the net worth is negative;
    3. **five percent of three-year average of absolute value of profit/loss after tax**, as per the last three audited Consolidated financial statements of the listed entity.
(d) In case where the criteria specified in sub-clauses (a)**,** and (b) and (c) are not applicable, an event/information may be treated as being material if in the opinion of the board of directors of listed entity, the event / information is considered material. *[existing clause]*

Thus, an additional criterion for classifying any event/information as material is introduced in Regulation 30 (4). It may be noted that the events specified in Para A of Part A of schedule III are deemed to be material, irrespective of the value. Hence it can be observed that the above-mentioned criteria are relevant for determination of materiality for the events / information specified in Para B of Part A of Schedule III. Accordingly, listed entities shall consider any event or information specified under Para B as material, if omission of an event or information, whose threshold value, or the expected impact in terms of value exceeds the specified limits of turnover or net worth or profit/loss after tax on consolidated basis (and not on standalone basis). Even if anyone's threshold is getting crossed, then it appears that it shall be deemed to be material.

## IV. Fluctuation in materiality thresholds on annual basis:

Since the new quantitative criteria for determination of materiality thresholds are based on previous years audited consolidated financials, these thresholds would now change every year. Accordingly, the magnitude of events or information to be disclosed to the stock exchange would also change every year. Generally Audited Financial Results would be ready by the end of 60 days after completion every year. So, a question can arise whether till that date, the criteria of materiality would be made on the basis of previous year's consolidated audited financials? It appears so and hence on the date when the annual audited consolidated financial results are approved by the board of directors, the materiality thresholds will change every year.
Further, every year these thresholds would have to be disseminated to the relevant employees in order to help them identify material events.

## V. Materiality Policy

Listed Companies are required to have a policy for determination of materiality as per Reg. 30(4)(ii) of LODR Regulations based on criteria specified in Reg. 30(4)(i), duly approved by its board of directors, and then disclosed on its website. LODR Regulations further states that such policy for determination of materiality shall not dilute any requirements specified under this Regulation 30(4) of LODR Regulation. **Now as Reg. 30(4)(i) is amended** and additional quantitative criteria are prescribed, it is recommended that **policy for determination of materiality of event / information also be amended and updated on website on or before July 14, 2023.**

As per newly inserted second proviso in Regulation 30(4)(ii), policy for determination of materiality shall be framed in a manner to assist relevant employees in identifying potential material event or information which shall be escalated and reported to the relevant Key Managerial Personnel for determining materiality of the event or information and for making disclosure to stock exchange(s). Now SEBI has mandated to make it a part of policy to help employees identify what is material and what is not? This would require percolating materiality thresholds in the organization. This would require extensive and continuous dialogue and engagement with employees.

## VI. Conclusion

This amendment in Regulation 30 of LODR Regulations has triggered a lot of actionable on the part of listed entities. Hence although, at this point of time, lot of listed entities may be busy in annual reports finalization and making preparations for forthcoming annual general meetings, these compliance under Regulation 30 also need to be taken care of and systems be put in place to ensure compliance of these Regulations within the prescribed time frame.

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**In the matter of CG Power and Industrial Solutions Limited - Adjudication order dated April 20,2023**

**FACTS OF THE CASE**

- CG Power and Industrial Solutions Ltd (hereinafter referred to as CG Power/ the Company) filed a corporate announcement with Bombay Stock Exchange (hereinafter referred to as BSE) and National Stock Exchange (hereinafter referred to as NSE) on August 20, 2019, which **disclosed the outcome of its Board meeting held on August 19, 2019**. From the said disclosure, Securities and Exchange Board of India (hereinafter referred to as SEBI) noted that the **total liabilities** of the Company and the CG Power Group might have been **potentially understated** by approximately ₹1053.54 Crore and ₹1,608.17 Crore respectively, as on March 31, 2018 and by ₹601.83 Crore and ₹401.83 Crore, respectively as on April 1, 2017. SEBI also noted that **advances to related and unrelated parties** of the Company and the CG Power Group might have been **potentially understated** by ₹1,990.36 Crore and ₹2,806.63 Crore respectively, as on March 31, 2018 and by ₹1,479.34 Crore and ₹1,331.47 Crore respectively, as on April 1, 2017.

- With this observation SEBI sought information in this matter from the Company in order to examine as to whether there were any violations of the provisions of securities and other applicable laws by the Company and its Directors / Promoters, during the period **2016-2019.** SEBI also had sought responses from the Chairman (Gautam Thapar), past Directors (Madhav Acharya, B. Hariharan) and CFO (V. R. Venkatesh) of CG Power. CG Power then appointed M/s Vaish Associates, an independent law firm to investigate on certain transactions and submitted preliminary Investigation report.

- Subsequently, **SEBI, vide an Interim Order dated September 17, 2019, debarred Gautam Thapar – Chairman, VR Venkatesh - CFO, Madhav Acharya - former director and B Hariharan – former director from buying, selling or otherwise dealing in securities in any manner, either directly or indirectly, till further orders.**

- SEBI further appointed MSA Probe Consulting Private Limited ('hereinafter referred to as MSA / Forensic Auditor') for conducting the forensic audit of the books of accounts of CG Power. Further SEBI confirmed its interim order by passing a final order dt: March 11, 2020, pending receipt of the forensic audit report from MSA.

- MSA vide its forensic audit report suggested to **examine the role** of MD & CEO, Risk and Audit Committee (RAC), Board and other employees of CG Power as well as that of Mr. Ashwin Mankeshwar i.e., Managing Partner of **M/s K. K. Mankeshwar and Co**. (hereinafter referred to as **KKM/ Noticee No. 2**) who was the Statutory Auditor of the Company appointed in 81st Annual General Meeting

of the Company dated September 28, 2018, till January 25, 2020. SEBI further conducted investigation in the matter and observed that M/s **Chaturvedi & Shah** (hereinafter referred to as **CAS/ Noticee No. 1**) was the joint statutory auditor of CG Power along with M/s Sharp & Tannan for the FY 2016-17 and subsequent to its resignation, on April 27, 2018, KKM was appointed as the statutory auditor of CG Power on April 28, 2018 to fill the casual vacancy, who completed the statutory audit of CG Power for the FY 2017-18.

- With regards to Noticee No. 2, SEBI noted from the Investigation Report (IR) that the statutory audit of CG Power for the FY 2018-19 was completed by KKM jointly with SRBC & Co. LLP after CG Power made an announcement in respect of various irregularities in the nature of fraud on August 20, 2019. While reviewing payments made in the past years, the Company came across certain unexplained payments from the Company and its subsidiaries made to KKM as well as association of Mr. Ashwin Mankeshwar, Managing Partner of KKM, as a Director of Blue Garden Estate Private limited ('Blue Garden') and Acton Global Private limited ('Acton'). In this regard, the RAC of CG Power issued a show cause notice to KKM under Section 140(1) of the Companies Act, 2013 and provided KKM with an opportunity of being heard. However, no submissions were made by KKM in respect of the aforesaid show cause notice. SEBI Investigation further observed and alleged that CAS and KKM had been acting against the fiduciary capacity, and that instead of working in the interest of shareholders of CG Power, they facilitated the scheme of cleaning up the books of accounts of CG Power, despite being aware of the irregularities and misstatements in the financial statements of CG Power

**CHARGES LEVIED**

Violation of the provisions of section 12A(a), (b) and (c) of the SEBI Act, 1992 and Regulations 3(b), (c) and (d), 4(1) and 4(2)(f) of the Prohibition of Fraudulent Trade Practices (PFUTP) Regulations, 2003.

**CONTENTIONS BY THE NOTICEES**

**Noticee 1**

1. **Sale of Nashik property and Kanjurmarg Property not known to Noticee:** Noticee 1 was questioned by the Forensic Auditor viz. MSA about the transactions with Blue Garden and Acton. In this regard Noticee 1 submitted that they were unaware of the transactions. Noticee 1 further submitted that transactions of Nashik & Kanjurmarg property were never disclosed to Board of Directors of the Company, filing of charge form pertaining to same was also not done respective Registrar of Companies, guarantees and the undertakings were never routed through meeting of board of directors of the Company. Noticee 1 further stated that management representations provided to them for the financial year 2016-17 were false and misleading.

2. **Netting off amount between two different entities not checked with each journal entry:** On the allegation of netting off amount, Noticee 1 submitted that they had only seen the net amount appearing in the final books of accounts for financial year 2016-2017 and not each individual entry.

3. **CG Power's advanced of Rs 28 crore to Blue Garden was checked:** Noticee 1 stated that they were aware that CG Power had advanced a sum of ₹28 Crore to Blue Garden during the FY 2016-17, so they sought an explanation from CG Power for such advance. CG Power informed that they had made such payment towards consultancy services from Blue Garden. Noticee 1 further stated that they were provided with balance confirmation from Blue Garden and a copy of the agreement dated March 27, 2017 entered by CG Power with Blue Garden for provision of consultancy services. Noticee 1 further submitted that on furnishing of these documents they did not suspect any non-genuineness in this transaction between CG Power and Blue Garden.

**Noticee 2**

1. **Reinstatement of financials and audit opinion:**
   Noticee 2 vide their Independent Auditor's Report dt: August 30, 2019 highlighted that they were informed by the Board of directors of the company that financial statements of earlier financial year 2016-2017 and 2017-2018 have been adjusted due to independent investigation carried out in the Company and that pending outcome of the investigation, the financial statements of 2016-2017 and 2017-2018 and of the year ended March 31,2019 might get revised /restated. Therefore Noticee 2 in their Independent Auditor's Report dt: August 30, 2019 under the heading — **'Basis for disclaimer of opinion'** mentioned that in view of the proposed voluntary revision / restatement of the financial statements of prior years, which may result in revision / restatement of financial statements for the year ended March 31, 2019 and also considering the significance of certain transactions / specific matters described herein below, Noticee 2 were unable to determine the consequential impact of the proposed revisions / restatements and the impact of certain transactions / specific matters on the Standalone Financial Statements as at March 31, 2019.

2. **Concerns on appointment of Mr. Ashwin Mankeshwar, Managing Partner of KKM, as additional director in Blue Garden and Acton**
   Noticee 2 vide reply dated January 15, 2023 stated that Mr. Ashwin Mankeshwar was inducted as an additional director in the Blue Garden and Acton on January 25, 2017 and he resigned from the said companies on March 14, 2017. During this period, he did not attend any meeting of both the companies nor was he privy to any transaction entered into by these companies. No remuneration was drawn by him during the period he was appointed as a director in these companies. Mr. Ashwin Mankeshwar further submitted that his previous directorship was not in conflict with any other laws. Also, no payments were received by him other than in the course of his statutory audit. Hence Noticee 2 submitted that it cannot be stated that they did not act in their fiduciary capacity.

## ARGUMENTS BY SEBI ON CONTENTIONS MADE BY NOTICEE 1

1. **Sale of Nashik property and Kanjurmarg Property not known to Noticee:**
SEBI noted that during the audit period i.e., during 2016-17, the transactions relating to a Nashik Property and a Kanjurmarg Property involving receipts of ₹390 crore by CG Power from Blue Garden and lending of ₹245 crore and ₹145 crore by CG Power to Acton and Avantha Holdings Ltd (hereinafter referred to as AHL) respectively were executed, which were not reflected in the audited financial statements of CG Power. Further said transactions were done without any agreement between CG Power, Blue Garden and Acton. SEBI noted that no approval/consent of Maharashtra Industries Development Corporation was obtained before sale of the Nashik property. Further, the land at Nashik was not a barren unused piece of land but home to a huge and fully operational factory owned by CG Power, which is a major contributor to CG Powers business and provides employment to a large number of people. It was further observed by SEBI that no approval was obtained from the Board of CG Power for the execution of Memorandum Of Understanding between CG power and Blue Garden for transfer of Kanjurmarg property for a consideration amount of ₹498 Crore to which SEBI noted that the aforesaid factors were also not considered by Noticee No.1 in its audit report. SEBI hence stated that arguments of Noticee 1 cannot be sustained. SEBI thereafter stated that fraud done by CG Power involved multiple transactions each amounting to hundreds of crores. Further, the said transactions were done through the banking channel. At the time of preparation of the audit report, Noticee No.1 had access to the bank statements and books of accounts of CG power and also had the right to seek and obtain information and explanations from CG Power to their satisfaction but did not act upon. Rather, Noticee No.1 allowed the said irregularities in above mentioned transactions in its audit report for the FY 2016-17 which shows the involvement of Noticee No. 1 with the company for facilitating it in showing true and fair picture of the financials. Hence SEBI stated that contentions of Noticee 1 cannot be accepted.

2. **Netting off amount between two different entities**
SEBI noted that advances against sale of properties received from Blue Garden to the extent of ₹388 Crore were adjusted by netting off against the amount transferred as loans to Acton and AHL by passing journal entries on March 30, 2017 and March 31, 2017. Also, all the entries of the transactions were made in such a way to net off the assets and liabilities of different entities i.e., debit balance of one entity netted off with credit balance of other entity in the books of account of CG Power which might not show the correct financial position of CG Power. SEBI further stated that in accounting norms, generally the netting of balance i.e., debit and credit of the same entity is permitted and not between the different entities. But in the present matter, the auditor did not raise question on the same and instead certified the same as true and fair in the auditor's report for the year 2016-17, which indicates the auditor's direct involvement on making such entries in the books of accounts of the company. SEBI hence stated that arguments of Noticee 1 cannot be sustained.

3. **CG Power had advanced sum of Rs. 28 crore to Blue Garden**
   SEBI highlighted that the balance confirmation as on March 31, 2017 was signed on behalf of CG power by Mr. Madhav Acharya and on behalf of Blue Garden was signed by Mr. Bhimrao Venkataramana Rao. SEBI further noted that with regard to agreement dated March 27, 2017 which was signed by Mr. Bhimrao Venkataramana Rao on behalf of Blue Garden and Mr. V. R. Venkatesh on behalf of CG Power, Mr.V.R. Venkatesh had never been a director of CG Power. Further, he had taken charge as Chief Financial Officer of CG Power from Mr. Madhav Acharya only on August 11, 2017 i.e., subsequent to the aforesaid agreement stated to have been executed on March 27, 2017. Even Mr. Bhimrao Venkataramana, who had signed the agreement was appointed as a Director of Blue Garden only on April 15, 2017. SEBI therefore observed that the aforesaid facts clearly indicated that the agreement dated March 27, 2017 between CG Power and Blue Garden was created merely to provide some basis to the transactions between CG Power and Blue Garden. SEBI further observed that the agreement was dated only 4 days prior to the end of the FY 2016-17 while the transactions between CG Power and Blue Garden had begun since May 2016. Therefore, SEBI noted that CAS, though admitted to have examined the said transaction, had not examined the aforesaid irregularities, and did not bring out in the audit report for the FY 2016-17. This all clearly indicated that CAS facilitated the company to make such entries in the books of account and hence were aware of the transactions relating to Nashik Property and Kanjurmarg Property involving Blue Garden to facilitate the scheme of cleaning up the books of accounts of CG Power. SEBI hence stated that arguments of Noticee 1 cannot be sustained.

**ARGUMENTS BY SEBI ON CONTENTIONS MADE BY NOTICEE 2**

1. **Reinstatement of financials and audit opinion**
   SEBI stated that Noticee 2 had raised various points with respect to the audit report of 2018-19 submitted by it on August 30, 2019. However no fraudulent transaction were reported in the audit report of 2017-18 during which all the aforesaid fraudulent transactions were carried out by the company. Further SEBI noted that the said audit report was submitted only on August 30, 2019 i.e., after CG Power made an announcement in respect of various irregularities in the nature of fraud on August 20, 2019. SEBI further noted that KKM was appointed by CG Power, immediately after resignation of CAS and without holding any Board Meeting. Further, after its appointment on April 28, 2018, KKM submitted audit report for 2017-18 on May 30, 2018 i.e., almost in a month. In view of the aforesaid facts, SEBI stated that there is no merit in the submissions made by Noticee No. 2 that it highlighted certain points w.r.t. the irregularities in its audit report of 2018-19.

2. **Concerns on appointment of Mr. Ashwin Mankeshwar, Managing Partner of KKM, as additional director in Blue Garden and Acton**
   SEBI mentioned that Memorandum of Understanding between Blue Garden and CG Power for assigning, sale and transfer of rights of Kanjurmarg Property was entered into on February 1, 2017 and the funds amounting to ₹190 Crore received

by Blue Garden as loan from ABFL in this regard were transferred to CG Power on February 16 and 17, 2017. From the same it was clear that it happened during the tenure of Mr. Ashwin Mankeshwar as director in Blue Garden and just after his appointment. Forensic auditor also stated that Blue Garden and Acton were Special Purpose Vehicles, which were incorporated for effecting the transactions relating to Nashik Property and Kanjurmarg Property. SEBI further noted from Forensic audit report that KKM provided multiple services to Avantha Group and received substantial remuneration from them and were quickly appointed as the statutory auditor of CG Power upon resignation of CAS. This indicated KKM's close ties with Avantha Group entities who had been the beneficiaries of the fraudulent transfers from CG Power. SEBI further noted the fact that Mr. Ashwin Mankeshwar did not receive any remuneration from Blue Garden and Acton during the period of January 25, 2017 to March 14, 2017 while he was holding the position of Director in these companies, as also stated by Noticee No. 2 in its contention, actually shows his close proximity with these companies and the nature of transactions in which these companies were involved. SEBI therefore concluded that all above facts clearly establish that Noticee No. 2 was aware of the irregularities and misstatements in the financial statements of CG Power, while issuing the audit report for the FY 2017-18.

**PENALTY**

| Sr.No. | Name of the Noticee | Violation | Penalty amount |
|---|---|---|---|
| 1 | M/Chaturvedi & Shah | Sections 12A(a), (b) and (c) of the SEBI Act, 1992; and Regulations 3(b), (c) and (d), 4(1) and 4(2)(f) of the PFUTP Regulations, 2003 | Rs.5,00,000/- |
| 2 | M/s. K. K. Mankeshwar & Co. | Sections 12A(a), (b) and (c) of the SEBI Act, 1992; and Regulations 3(b), (c) and (d), 4(1) and 4(2)(f) of the PFUTP Regulations, 2003 | Rs.5,00,000/- |

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**Order of the ROC, Gujarat, Dadra & Nagar Haveli dated April 28, 2023**
**In the matter of M/s. Sun Pharmaceutical Industries Limited**

**Facts of the case:**

- M/s. C.J. Goswami & Associates, Practicing Company Secretaries was appointed as Secretarial Auditor ['Secretarial Auditor'] for the financial year 2014-2015, 2015-2016, 2016-2017, 2017-2018 respectively by Board of Directors of M/s. Sun Pharmaceutical Industries limited which is a Company registered under Companies Act ,2013 in the state of Gujarat and having its registered office at SPARC, Tandalja, Vadodara
- An inquiry was conducted of Sun Pharmaceutical Industries limited (hereinafter referred to as 'SPIL/the Company') under Section 206(4) of the Companies Act 2013 ['the Act'] as ordered by Ministry of Corporate Affairs ('MCA') in the affairs of the Company covering the financial years from 2014-15 to 2017-2018.
- In connection to this inquiry, the inquiry officer had issued Show Cause Notice ('SCN') to the Secretarial Auditor on November 10, 2022 in respect of not reporting Aditya Medisales Ltd (hereinafter referred to as 'AML') as related party as per Indian Accounting Standard 24 and Accounting Standard 18 in financial statements of the Company for financial year 2014-2015, 2015-2016, 2016-2017.

**Charges levied:**

- Secretarial Auditor of the Company was alleged to have not reported Aditya Medisales Ltd as related parties as per the requirement of IND-AS 24/ AS-18 in the financial statement of the Company of FY 2014-15, 2015-16 and 2016-17.

**Submissions by Secretarial Auditor:**

- Mr. Chintan Goswami, Proprietor of M/s. C.J. Goswami & Associates, Practicing Company Secretaries submitted that the format of MR-3 i.e., Secretarial Audit report was already prescribed under Section 204 of the Act. As per the scope of secretarial audit as decided by Central Council of Institute of Company Secretaries of India ['ICSI'] at its 226$^{th}$ Central Council meeting, the provisions relating to audit of accounts and financial statement of the company is dealt in the statutory audit and Secretarial Auditor may rely on the reports given by statutory auditor or another designated professional. Therefore, relying on the reports given by M/s SRBC & Co. LLP, Statutory Auditor of SPIL for financial year 2014-15 to 2016-17 ['Reporting Period'] they believed that the Company complied with the provisions of section 133 of the Act regarding compliance with accounting standards.
- Secretarial Auditor further submitted that none of the secretarial audit report issued for Reporting Period stated that financial statements comply with the accounting standards.

- Secretarial Auditor further brought to the kind attention of the Presenting Officer a statement mentioned by Secretarial Auditor in the secretarial audit reports issued for Reporting Period at sr. no. 2 of Annexure 1 of the said reports that, "We have not verified the correctness and appropriateness of financial records and books of accounts of the company"
  Secretarial Auditor further drew attention of the Presenting Officer to the extract of guidance note on undertaking secretarial audit assignments issued by ICSI on May 14, 2018 from (Chapter 1 of Guidance Note on Secretarial Audit) which states that,
  *"The term Secretarial Audit is a mechanism which is connected with the audit of the non-financial aspects of the company.*
  *The object of the Secretarial audit is evaluation and form an opinion and to report to the shareholders whether, the company has complied with applicable laws comprising various statues, rules, regulations, guidelines, followed the board processes and report on the existence of compliance management system.*
  *Third party support and evidences: It would always be helpful to cross verification of the fillings made by the company at MCA, SEBI & other authorities independently. Verification of record and enquiries can also be made with the other statutory auditor and internal auditors and consultants and Independent directors of the company"*
- Secretarial Auditor further submitted that duty cast upon secretarial auditor under relevant standards of auditing and reporting framework had been duly and fully complied. Secretarial Auditor further brought to the kind attention of Presenting Officer, observations/views in the secretarial audit report for the financial year ended March 31, 2016 and March 31, 2017.
- Secretarial Auditor further stated that as per their limited understanding on basis of documents available in public domain in relation to the non-disclosure of transaction with AML the Company had already settled this matter with SEBI. Secretarial Auditor hence sought the details of as to on what grounds this SCN was issued to them? Secretarial Auditor hence prayed for dismissing the allegations of non-compliance /violation of the provision of the act and no penalty ought to be levied.

**Submissions by Presenting officer:**

- The Presenting Officer submitted that inquiry on SPIL was based on a whistle blower complaint in respect of related party transactions, money diversions from SPIL to AML and other group companies of SPIL. As per Section 204 of the Act, the secretarial auditor plays a crucial role in laws for effective compliances. The object of secretarial audit is to evaluate and form an opinion and to report to the shareholders whether company has complied with applicable laws comprising

various statues, rules, regulations, guidelines, followed the board processes and report on the existence of compliance management system.

- Practicing Company Secretaries ('PCS') has the professional duty to provide an unbiased view on compliance status of the company. A PCS should be independent from company being audited. The Secretarial auditor is also expected to ensure that activities of the client company are in accordance with the applicable procedure and that supporting evidence is maintained by company and same is genuine. Presenting Officer further stated that PCS should have examined transactions during the Reporting Period to identify whether any fraud element is present or not?
- Presenting Officer further elaborated in detail the group structure of SPIL. He then stated that Mr. Dilip Sanghvi, Managing Director of SPIL has control over AML. Further highlighting the group structure of SPIL, Presenting Officer highlighted that companies were created between SPIL and AML to hide the director control of
  Mr. Dilip Sanghvi and their relatives in AML.
- Thus, he stated that it has been established that MD of SPIL, Mr. Dilip Sanghvi had control on AML and all other private body corporates were created between SPIL and AML to hide direct control of MD of SPIL. SPIL's RPT with AML exceeded Rs.100 crores which formed material and significant transaction.
- It was further stated that although the shareholder of AML is body corporate, but the main control person of all the body corporates was MD of SPIL, i.e., Mr. Dilip Sanghvi and their family members.
- Further highlighting on business of AML, Presenting Officer stated that AML was the sole distributor of the SPIL since long time in India. All the goods manufactured by SPIL were sold within India through AML. AML was also promoter company of SPIL since year 2001. Also, the promoters of SPIL were the shareholders of AML.
- SPIL and AML were Related party even before the merger of Sanghvi Finance Ltd because as per the scheme of merger filed by the Company before NCLT, the Company itself confirmed that all 22 transferor companies and Sanghvi Finance Pvt ltd are connected with Mr. Dilip Sanghvi who is MD of SPIL.
- Mr. Dilip Sanghvi who is MD of SPIL and also holds more than 2% of AML (directly/indirectly), is therefore related party of AML as per Section 2(76) (v) and (vi) of the Act read with Accounting Standard 18.
- The Presenting Officer further stated that instead of complying his duties as per Guidance notes Secretarial auditor merely relied on Statutory auditor reports. Further replying to the submission of Secretarial Auditor about scope of secretarial audit as per ICSI 226$^{th}$ meeting, Presenting Officer stated that identification of related party under Section 2(76) and Section 188 of the Act fall under the purview of secretarial auditor of the company and non-reporting of AML as related party for Reporting Period falls under the purview of duty of secretarial

auditor as per guidance note of Secretarial audit issued by ICSI. Hence Presenting Officer found Secretarial Auditor of SPIL guilty for violation of section 143(14) read with section 188 & 204 of the Companies Act,2013.

**Penalty as per Section 450 of the Companies act 2013**

| For the Financial year | Name of the auditor's firm | Penalty (In Rs.) | Maximum Penalty (In Rs.) | Penalty Imposed (In Rs.) |
|---|---|---|---|---|
| 2014-2015 | C.J Goswami & Associates, Practicing Company Secretary | 10,000+1000/- per day | 50,000/- | 50,000/- |
| 2015-2016 | | 10,000+1000/- per day | 50,000/- | 50,000/- |
| 2016-2017 | | 10,000+1000/- per day | 50,000/- | 50,000/- |

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**Non-constitution of Nomination & Remuneration committee; ROC penalizes MD and exonerates CS.**

**Introduction:**

The board of directors, being the brain of the Company, is responsible for all decisions taken by the company. In such a scenario, the board has to take assistance of and guidance from the various committees of directors formed by the board itself for its assistance or which are constituted under the Companies Act, 2013. These committees collectively known as "board committees", are responsible for assisting the board in effective performance of functions specified by the board and act as a guide for the decisions to be taken by the board of directors. The Companies Act 2013 ("the Act") requires the listed companies and **unlisted public companies having Paid up capital of Rs 10 crore or Turnover of Rs 100 crore or having aggregate outstanding loans, debentures and deposits exceeding Rs 50 crore or more** to constitute certain committees. One such committee is the Nomination & Remuneration committee ("NRC").

**I. Legal provisions relating to NRC:**

Section 178(1) of the Act requires the companies to form a Nomination and Remuneration Committee which shall be responsible for identification and selection of persons to be appointed as directors and key managerial persons and senior management. The committee shall also recommend the remuneration to be payable to such persons. Section 178 of the Act also clearly specifies the constitution of NRC. Further, sub-section 8 of section 178 says that, if the committee is not constituted as specified, then the company and the officers in default shall be liable for penalties.

**II. ROC order in case of PTC Financial Services Limited:**

There are certain committees like executive committees which are formed to assist the board. But the constitution of some committees like NRC is a legal requirement coming from the Act. Therefore, as mentioned above, non-constitution of committee results in penalty on company. This situation was seen in the ROC Adjudication Order dated 27th June 2023 passed by ROC Delhi in the matter of PTC Financial Services Limited ("the Company").

In this case, the ROC Delhi had imposed penalty on the company and its managing director for not constituting NRC after the same becoming dysfunctional due to vacation of office of a director who was member of NRC also.

**A. Facts of the case**:

The existing NRC of the Company consisted of 3 members, and 2 of them including the chairman of NRC, were independent directors and the third member was the nominee of the holding company (PTC India Ltd). After the holding company revoked its nomination in favor of its nominee director, the said nominee director ceased to be a director in PTC Financial Services Ltd., and hence ceased to be a member of the NRC as well.

Due to this, the minimum number of members required in the NRC went below the statutory limit and hence the NRC was rendered dysfunctional. Thereafter, the board called for a board meeting for reconstitution of committee but the same got cancelled twice. Thereafter, 3 independent

directors of the company resigned and the board meeting could not be held thereafter. As a result, the NRC remained dysfunctional.

**B. Action initiated by RoC:**

The ROC Delhi came to know about this non-compliance in this company from forensic audit report and inspection conducted by SEBI. The ROC therefore sent show cause notice for this non-compliance to the company, its Managing Director ("MD"), its Chief Financial Officer ("CFO") and the Company Secretary ("CS").

**C. Reply by the CFO & CS of the Company:**

The CFO and CS of the Company submitted separate replies and the Company along with its MD submitted a joint reply.
The CFO submitted that he was not aware of all these non-compliances and also that he was not marked in any of the emails exchanged by the directors, hence he could not be held liable.
Further, the CS replied that he had highlighted to the Chairman and the MD of the Company about the non-compliance. These replies given by the CFO and CS were held to be satisfactory and hence they were not penalized.

**D. Reply by the Company and its MD:**

In the joint reply submitted by the Company and its MD, the Company said that it could not convene the board meeting for re-constitution of NRC for the reason that all the independent directors of the company had resigned, and board meeting could not be held in absence of independent directors.

As soon as the independent directors of the holding company were appointed on the board of PTC Financial Services Ltd as independent directors, the board meeting for re-constitution of NRC was held. Therefore, the delay in compliance was due to factors outside the control of the Company.

**E. ROC's decision:**

As mentioned above, the replies given by the CFO and CS of the Company were held to be satisfactory and hence no penalty was imposed on both. However, in case of Company and its MD, ROC held that, *"facts and circumstances in itself clearly demonstrate that the NRC was made dysfunctional and the company and the MD & CEO at its helm did not take swift action to restore normalcy by reconstituting the NRC. Hence, the Company and its MD & CEO failed to comply with the provision of Section 178 of the Act."*

**F. Penalty on company and its managing director:**

Considering the non-compliance of section 178(1), the ROC imposed penalty under subsection 8 of section 178 on the company of RS. 5,00,000 and on its managing director of RS. 1,00,000.

## III. Conclusion:

Other than the penalty for non-compliance of section 178, there is one more point worth observation in this order. That is, this is unique order of ROC wherein the company secretary was able to prove himself not guilty for the reason that he had already highlighted the non-compliance to the managing director and chairman of the Company.

As observed in this order, ROC had sent show cause notice to Company as well as key managerial personnel ("KMP") of the Company as defined in section 2(51) of the Act, i.e., MD, CFO and CS of the Company for the non-compliance with respect to constitution of NRC. The CFO took a view that the constitution of this Committee was not under the purview of his role as a KMP. Whereas the CS pleaded that he had taken efforts to convey the on-going non-compliance to the Chairman and MD of the Company, therefore he had complied with his duty of guiding the board with regard to proper compliance of law. This reply given by the CS of the Company was accepted by the ROC and he was exonerated from the charges of non-compliance. This order highlights that if the company secretary has remained vigilant in the performance of his duty and has pleaded well before the adjudicating officer, he may be able to save himself from the

penalty. Rutuja Umadikar - Research Associate - rutujaumadikar@mmjc.in

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***Failure to allot the shares or refund monies against the money deposited towards purchase of shares is a financial debt under IBC?***

***In the matter of Katepalli Venkateswara Rao (Petitioner) Vs. M/s Bio Green Papers Ltd (Respondent) in the order passed by National Company Law tribunal (NCLT) Hyderabad Bench dated 30 th May 2023***

***Facts of the case:***

- An application was filed u/s 7 of Insolvency and Bankruptcy Code, 2016 (IBC) for initiation of Corporate Insolvency Resolution Process (CIRP) against the *Bio Green Papers Limited* - Corporate Debtor (CD) who had defaulted in the payment of debt of Rs. 1,64,65,891/- which includes Principal and interest.
- *Katepalli Venkateswara Rao* – Petitioner and the Financial Creditor (FC) is in to the business of rending financial services and during the course of business - entered a Memorandum of Understanding (MOU) on 2 April 2018 whereunder it was agreed that CD would allot the shares to FC in the CD in consideration of the FC investing Rs. 1 Crore in the CD in the form of convertible/redeemable preference shares with in a period of maximum one year from the date of payment of the same to CD. And the the said sum would be used for the purpose of the revival and rehabilitation of machinery and working capital needs of the CD.
- The MOU further stated that in the event if CD failed to allot shares in the form of convertible/redeemable preference shares, the CD would repay the amounts paid by the petitioner along with interest @ 18% per annum.
- The CD not only failed to allot the shares to the FC but also failed to repay the invested amount with interest @ 18%. Aggrieved by this – the FC filed the application for CIRP at NCLT.
- The CD in counter filed and admitted that the FC had approached the CD through one Mr. Aveena Gudapati for allotment of Convertible/Redeemable preference shares in the CD but the same could not be allotted to the FC by CD.
- It was agreed by the CD via oral agreement to refund the said amount in 12 quarterly instalments without interest. Contrary to the terms of the oral understanding, the application had been filed.
- The CD sought further time from the FC to clear its dues and the FC orally agreed to grant some more time for repayment of the amount. Despite the understanding, the application was filed by the FC with an ulterior motive to recover the amount which was against the object of the Code.

***Question for Consideration before NCLT:***

***Whether a financial debt as claimed by the Petitioner is due and payable by the Respondent, if so, whether the Respondent defaulted in payment of the same?***

- It was noted that Rs. 1 Crore has been deposited by the FC with the CD for purchase of shares and the shares were not allotted, it was agreed by the CD to refund the said amount in 12 quarterly instalments without interest.
- Therefore, the allotment money has been converted into a debt by the parties as is evident from the contest putforth.
- The said debt was not repaid the default in repayment of the same stands established. Therefore, as existence of debt and its default was established the petition was liable to be **allowed**.
- Accordingly, the petition was admitted and NCLT ordered the commencement of CIRP against the CD.

Interesting point to be noted here is that the pursuant to section 73 of the Companies Act, 2013 (the Act) and Rule 3(c)(vii) of Companies (Acceptance of Deposit) Rules, 2014 - *if any amount is received by the company towards subscription to any securities, including share application money or advance towards allotment of securities and if the securities for which application money or advance for such securities was received could not be allotted within sixty days from the date of receipt of the application money or advance for such securities and such application money or advance if not refunded to the subscribers within fifteen days from the date of completion of sixty days, then such amount would be treated as a deposit..*

*In this case - the CD not only failed to allot the shares against the money deposited towards purchase of shares but also failed to refund the money. And due to which the said amount was considered as debt and the default in repayment was also established.*

*Question to be pondered here is such default would also trigger the non-compliance of deposit provisions under the Act. And as per section 76A of the Act - apart from penalty on the Company and every officer who is in default - every officer of the Company who is in default shall be punishable with imprisonment – how this would be treated in the eyes of laws is also to be looked upon!*

*Further, whether CD would proceed to NCLAT and if yes, under what plea would be another interesting question to follow!*

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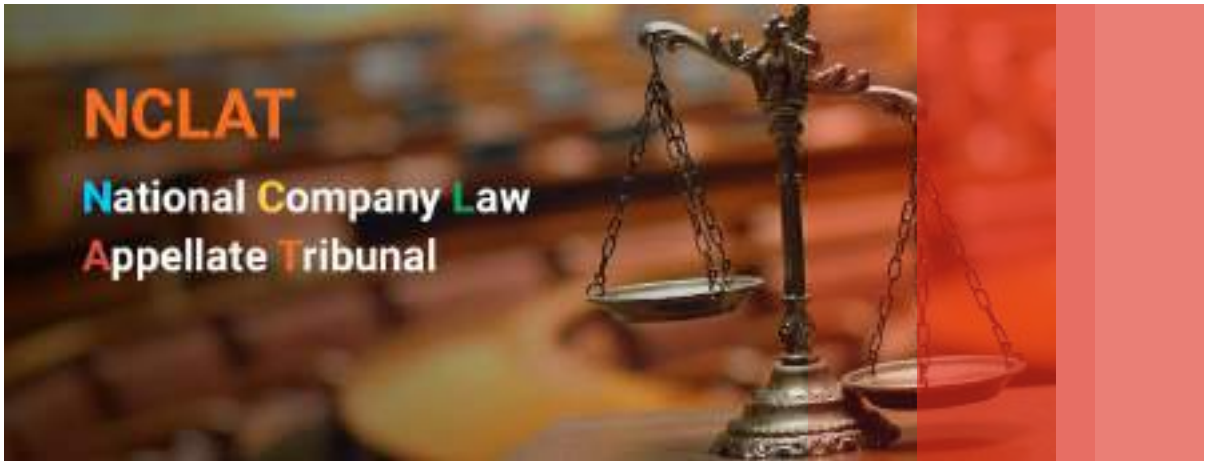

# Ministry of Finance (MOF) pulls reins on International Credit Card Use under LRS back peddled.

## I. Background:

The usage of credit cards has seen a fourfold growth in previous decade. The overall payments done through the usage of credit cards had increased by 27% and 54.3% in terms of volume and value respectively in financial year 2021-22 as per the Reserve Bank of India's annual report for 2021-22. Since April 2020-21, The Reserve Bank of India has been closely monitoring the details of all transactions done via debit/ credit cards/ UPI on a monthly basis through a return filed by all Authorised Dealer banks (AD Banks) called 'FETERS cards.

## II. Exemption regarding transaction limit through international credit cards:

The limits for foreign exchange expenditure/ transactions are prescribed under the Liberalised Remittance Scheme. Individuals' resident in India can avail the foreign exchange facility within the limit of USD 2,50,000 only per financial year under the scheme. Foreign Exchange expenditure beyond the said limit requires prior approval of the Reserve Bank of India (RBI). The Scheme shall not apply to corporates, partnership firms, HUF, Trusts. Rule 7 in Foreign Exchange Management (Current Account Transactions) Rules, 2000 (hereinafter referred to as 'Current Account Rules')

This limit was exempted even for transactions done through international credit cards pursuant to an exemption given in Rule 7 of the Foreign Exchange Management (Current Account Transactions) Rules, 2000 (hereinafter referred to as "Current Account Rules"). This Rule_ provided exemption for obtaining prior approval from Reserve Bank of India for incurring foreign expenditure by way of international credit cards (within or beyond limits as per scheme).

## III. Previous amendment for withdrawal of exemption:

The Ministry of Finance (MOF) had notified Foreign Exchange Management (Current Account Transactions) (Amendment) Rules, 2023 on 16th May 2023 pursuant to which omitted this Rule 7 of Current Account Rules'.

As a result of omission of the said Rule, foreign expenditure incurred using international credit cards beyond prescribed limits of USD 2,50,000 per financial year would have required prior approval from the Reserve Bank of India.

**A. Probable reasons for omission of Rule 7:**

1. The move to amend the current account rules was hinted by the union finance minister in her budget where rate of tax collected at source (TCS) was proposed to increase from 5% to 20% on remittance under Liberalised Remittance Scheme and purchase of overseas tour program package from 1st July 2023 and also removing the threshold of Rs 7 lakh for levy of TCS on remittance under Liberalised Remittance Scheme.

   Omission of Rule 7 could have helped ensure that the credit card payments made are covered under the ambit of applicable LRS limits so that Tax collected at source is not escaped.

2. The high value foreign outflow through International Credit Cards could be watched upon by the Reserve Bank of India and this action taken by Ministry would have led to a decrease in the value of transactions done through international credit cards to some extent.

**B. Impact of the notification dated 16th May 2023 – omission of this exemption:**

The general probable impact of omission of this exemption could be as follows:

1. As a result of the said amendment foreign tours and foreign expenditures using credit cards, foreign travel could increase the cost expenditure by 20%.
2. Also, omission of Rule 7 shall lead to increase in administrative and compliance burden on the Banks as the onus of keeping a track on the international credit card expenditures and collection of TCS shall be on the Banks.
3. Omission of Rule 7 could also bring equity in transactions carried out by international debit and credit cards, as payments using debit cards were considered under LRS limits even earlier.

## IV. Foreign Exchange Management (Current Account Transactions) (Amendment) Rules, 2023 dated 16th May 2023 back peddled:

Considering the criticism from the industry and individual taxpayers, the Ministry of Finance issued notification dated 30th June 2023 for bringing back the exemption as provided by the Current Account Rules earlier, by inserting Rule 7 once again.

The move by the Ministry of Finance to take back the effect caused by the omission of Rule 7 could have been an impact of the criticism received through the comments and suggestions by the stakeholders. As mentioned above, the use of international credit cards beyond prescribed limits under LRS required prior approval and collection of TCS. Such transactions required to be closely watched upon by the Authorised Dealer Banks which led to increased administrative and compliance burden on the AD Banks.

The revised TCS rates are also said to be rolled out from 1st October 2023 as against 1st July 2023 prescribed earlier. The extension could also provide some time to the banking systems and card networks to put in place requisite IT-based solutions and infrastructure required.

## V. Conclusion:

Hence summarising the whole scenario, the ministry has reversed its decision via notification dated 16th May 2023 through further notification dated 30th June 2023, continuing the exemption provided by Rule 7 with respect to obtaining approval of RBI for expenditure incurred through International Credit beyond the LRS limits. **Bringing back exemption under Rule 7 also meant No levying of Tax Collected at Source (TCS) on international credit card spends outside India presently at the moment.**

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