

MMJCINSIGHTS

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When Machines Read the Fine Print: How AI is Transforming the DRHP Review Process in India

“Every prospectus ends with a quiet disclaimer from SEBI—it checks if disclosures are complete, not if they’re entirely true. But as AI enters the scene, it opens up a bold possibility: can technology help us do both, and do it faster than ever before?”

The Draft Red Herring Prospectus (DRHP) is the lifeblood of any IPO. A 400+ page document detailing a company’s financials, business risks, promoter background, litigation, and future plans. For investors, it’s a window into the company. For SEBI and stock exchanges, it’s a regulatory maze that must be navigated carefully to ensure no material misstatement goes unnoticed.

Enter AI: BSE’s Bold Move

In June 2025, the BSE quietly rolled out an AI-driven DRHP screening system for its SME IPO platformⁱ. To initiate the AI-driven pre-check, merchant bankers are first required to create an account with the Exchange and obtain secure access to a designated SFTP (Secure File Transfer Protocol) folder. Once access is granted, they can upload the draft offer document (DRHP) directly to this secure environment. Upon upload, the Exchange’s AI system is triggered to begin its analysis. The tool reviews the document and generates a downloadable report highlighting sections that may need revision. This allows merchant bankers to refine the draft proactively before formally filing it with the Exchange. It’s important to note that this AI-based pre-check is purely advisory in nature; the Exchange still undertakes a full, manual review of the DRHP once it is officially submitted. Instead of waiting for formal observations after filing, merchant bankers now have the opportunity to fine-tune the document in advance, making the final submission smoother, quicker, and more aligned with regulatory expectations.

The Bigger Picture: SEBI’s AI Roadmap

BSE isn’t alone. SEBI, too, has been experimenting with AI in IPO document reviews. At the Securing Financial Stability Amid Global Spill overs event on February 16, 2024 SEBI Whole-Time Member Ananth Narayan Saidⁱⁱ, Securities and Exchange Board of India has started using artificial intelligence (AI) for the first level of scrutiny of draft red herring prospectuses (DRHPs). The regulator has piloted ChatGPT-like tools to perform first-level parsing of DRHPs, helping its officers focus on deeper, more nuanced analysis. It’s also pushing for standardized, template-based DRHP formats, where key data fields can be auto-validated using machine logic.

This transformation is not just about speed. It’s about structural change moving from a world of narrative-heavy, loosely formatted disclosures to a regime of clean, comparable, machine-readable filings.

And SEBI isn’t stopping there.

Audio, Video & QR Codes: The DRHP Goes Multimediaⁱⁱⁱ

In a move to democratize IPO access for retail investors, SEBI is now mandating audio-visual summaries of DRHPs short 5–8-minute explainers in English and Hindi,

highlighting the risks, objects of issue, and business model. These will be hosted online and accessible via QR codes, making the document less intimidating and more digestible.

Imagine scanning a QR code on your phone and getting a crisp voiceover summary of the IPO you're considering powered by AI, verified by humans.

This is not just disclosure. It's communication.

Beyond IPO disclosures, SEBI has also begun embracing artificial intelligence more broadly to enhance its surveillance and regulatory functions across the capital markets. By deploying AI-powered algorithms capable of processing vast volumes of structured and unstructured data in real time, SEBI has strengthened its ability to detect unusual trading patterns, potential market manipulation, and insider trading with far greater precision. In parallel, the regulator has implemented advanced data analytics systems that assess historical market data, news, media sentiment, and behavioural patterns to perform predictive analysis. These tools enable SEBI not just to respond to misconduct swiftly, but to anticipate and prevent potential threats before they escalate. Together, these initiatives reflect a strategic shift toward more proactive, technology-driven supervision where AI helps regulators move from reactive enforcement to pre-emptive oversight.^{iv}

Where This is Headed

The DRHP review of tomorrow will likely be:

- Template-driven, minimizing ambiguity
- AI-screened, reducing human fatigue
- QR-enabled, enhancing investor access
- Multi-lingual, broadening reach
- And above all, real-time, allowing for regulatory agility.

This is not speculation. This is India's IPO future being built in real-time.

The Road Ahead for AI in IPO Disclosures

a) Rethinking Regulatory Process:

The use of AI in reviewing DRHPs isn't just about speed or automation it represents a deeper shift in how we think about regulation itself. What BSE has piloted and SEBI is exploring goes beyond technology. It's a rethinking of how we can make the regulatory process smarter, faster, and more inclusive. But let's be clear: this is just the start.

b) From Review Tools to Real-Time Drafting Assistants:

Right now, these AI tools are primarily helping at the initial stage screening documents, flagging issues, and helping merchant bankers prepare better submissions. That alone is a big leap forward. But imagine what happens when these systems evolve into full-fledged assistants embedded within the drafting process itself. They could help issuers catch missing disclosures as they type, suggest compliant wording, and ensure consistency across the document. That's not just convenient it could significantly raise the quality and comparability of DRHPs across the board.

c) Post-Listing monitoring:

Looking beyond the IPO stage, AI could also help in post-listing monitoring. With companies making ongoing disclosures under the LODR Regulations, AI systems could spot missed deadlines, unusual financial trends, or even detect gaps in corporate governance practices allowing exchanges and regulators to act early.

Conclusion

Of course, with all this potential comes responsibility. AI isn't magic it reflects the data and design choices behind it. That's why strong governance is critical. We need audit trails, version control, transparency, and above all, human judgment to remain in the loop. If done right, AI won't replace trust it'll help build it.

So, as we look ahead, one thing is clear: AI in capital markets is not just about enforcement. It's about enabling better compliance, better decisions, and ultimately, a better marketplace.

This article is published on Taxmann. The link for the same

<https://www.taxmann.com/research/company-and-sebi/top-story/105010000000026797/when-machines-read-the-fine-print-how-ai-is-transforming-the-drhp-review-process-in-india-experts-opinion>

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ⁱ <https://www.bseindia.com/markets/MarketInfo/DispNewNoticesCirculars.aspx?page=20250617-3>

ⁱⁱ <https://www.moneycontrol.com/news/business/markets/sebi-using-ai-for-preliminary-scrutiny-of-ipo-documents-says-ananth-narayan-12290321.html>

ⁱⁱⁱ https://www.sebi.gov.in/legal/circulars/may-2024/audiovisual-av-presentation-of-disclosures-made-in-public-issue-offer-documents_83569.html

^{iv} <https://www.ijnrd.org/papers/IJNRD2404397.pdf>



"SEBI Ups the Ante: Enhanced Corporate Governance for High-Value Debt Listed Entities"

Securities and Exchange Board of India ('SEBI') vide its amendment notification Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Amendment) Regulations, 2025 ['LODR amendment'] dt: March 27, 2025, notified provisions for High Value Debt Listed Entities ['HVDLE']. HVDLE means an entity who has its listed non-convertible debt securities listed on a recognized stock exchange having outstanding principal value of rupees one thousand crore or more as on March 31. These provisions have become effective from the date of notification in the official gazette (i.e. March 27, 2025']

Reasonable time period for compliance with provisions by HVDLE:

As provisions relating to HVDLE are made effective immediately the question that arises is whether any reasonable time period is there with HVDLE for compliance with provisions of law. Hon'able High Court of Kerala in case of KK Balakrishna **Pisharody V. Kerala State Electricity Board and Others**, dt: **November 6, 1987**, held that, "*When no time limit is fixed, provisions has to complied with reasonable time. Reasonable time depends upon the facts and circumstances of each case*". Further as per Law Lexicon the term 'Reasonable Time' is defined to be so much time as is necessary, under the circumstances, to do conveniently what the contract or duty requires should be done in a particular case.

What is reasonable time of compliance would depend on compliance requirement for each provision of LODR amendment. It may also differ for each regulation. Listed entities hence need to ensure compliance with LODR amendment provisions within a reasonable timeframe as may be applicable.

Analysis of LODR amendment:

Below is the analysis on the applicability of revised provisions:

1. Increase in threshold of non-convertible debt securities for identification of HVDLE: Till now entities having their outstanding principal value of non-convertible debt securities listed worth Rs 500 crore or more were considered as HVDLE irrespective of whether its specified securities (viz. equity shares or anything convertible into equity) have been listed or not. Entities having their outstanding principal value of non-convertible debt securities listed worth Rs 500 crore or more were required to comply with corporate governance provisions (viz. regulation 15 to 27 and relevant provisions of schedule V of LODR) of Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements), Regulation, 2015 ['LODR'] on 'comply' or 'explain' basis till March 31, 2025.

SEBI has now vide its LODR amendment, notified that an entity would be considered as HVDLE, irrespective of the fact whether its specified securities are listed or not, if it has outstanding principal value of non-convertible debt securities listed worth Rs 1000 crore or more as on March 31ⁱ. So, if as on March 31, 2025, an entity has non-convertible debt securities listed worth Rs 1000 crore or more then it will be considered as HVDLE for FY 25-26. SEBI has further stated that

entities having their specified securities listed and their outstanding principal value of non-convertible debt securities of Rs 1000 crore or more listed, shall also be considered as HVDLE.

2. Provisions applicable for HVDLE: Once an entity is categorized as HVDLE it will have to comply with corporate governance provisions. If a HVDLE already has its specified securities (viz. equity shares or any security convertible into equity shares) listed on recognized stock exchange then it needs to comply with regulation 15 to regulation 27 of LODRⁱⁱ. If an entity does not have its specified securities listed on a recognized stock exchange then it will have to comply with newly added chapter VA of LODR. This demarcation has created ease and prevented overlap for entities that have their equity and their non-convertible debt securities listedⁱⁱⁱ.

Entities need to monitor their non-convertible debt securities issued and listed on stock exchanges. SEBI has now specified that once an entity crosses the limit of 1000 crores in value of its principal outstanding non-convertible debt securities listed then it will have to ensure compliance within six months from the date of provisions becoming applicable^{iv}.

3. Sunset clause: SEBI has provided ease by bringing in sunset clause of applicability of corporate governance provisions to HVDLE.

SEBI has stated that once the provisions of chapter VA of LODR become applicable to a HVDLE, will continue to remain applicable till the value of principal outstanding non-convertible debt securities is 1000 crore or more. An HVDLE whose value of principal outstanding listed non-convertible debt securities reduces and remains below 1000 crores for three consecutive financial years may cease compliance with provisions of chapter VA. SEBI has specified that the computation of three consecutive financial years would start from April 1, 2025 (i.e. end of FY 25-26)^v

For entities who have their specified securities listed will not be able to cease compliance with provisions of regulation 15 to 27 of LODR even if its principal outstanding non-convertible debt securities reduces and remains below 1000 crores for three consecutive financial years, if corporate governance provisions under regulation 15 to 27 of LODR continue to remain applicable to it due to its paid up equity share capital exceeding rupees 10 crore and net worth exceeding rupees twenty five crore as on the last of date of previous financial year.

4. Time limit for ensuring compliance with LODR: No time limit is provided by SEBI for compliance with provisions of chapter VA or regulation 15 to 27 as the case may be by HVDLE. HVDLE need to ensure compliance with effect from March 27, 2025 (i.e. date of notification of LODR amendment) or as soon as reasonably possible. SEBI in its board of directors note discussing amendment to LODR dt: March 27, 2025, has stated that corporate governance provisions were applicable on 'comply or explain basis' till March 31, 2025 for entities having their principal high value debt of Rs 500 crore or more. Hence sufficient time is already given to

entities having their principal outstanding of non-convertible debt securities exceeding 1000 crore also to ensure compliance with the provisions of LODR^{vi}.

So, if an entity has principal outstanding of non-convertible debt securities listed as on March 31 worth Rs 1000 crore or more then it will have to ensure compliance as on March 27, 2025 or as soon as reasonably possible.

E.g. If an entity crosses threshold of 1000 crore in value of principal outstanding non-convertible debt in the month of September 2025, then it will have to ensure compliance with applicable provisions within a period of six months (i.e. by March 2026). To ensure compliance would mean revisiting managerial remuneration, related party transactions prior approval, board composition etc. as per LODR or chapter VA of LODR norms.

5. Transition of compliance: Entities having their principal outstanding non-convertible debt securities worth Rs 500 crore or more was required to ensure compliance with provisions of regulation 15 to 27 of LODR till March 31, 2025. Entities having their non-convertible debt securities listed of outstanding value (Principal value) of Rs 500 crore or more as on March 31, 2025, will not be considered as high value debt listed entities. Hence these entities shall cease to ensure compliance with corporate governance provisions with effect from March 27, 2025 (i.e. date of notification of amendment to LODR).

Conclusion :

Applicability of corporate governance provisions with clarity is now the reality. With this applicability clarity it would be definitely easy for HVDLE to ensure compliance with applicable provisions.

Amendment to LODR can be accessed at following link:

https://www.sebi.gov.in/legal/regulations/mar-2025/securities-and-exchange-board-of-india-listing-obligations-and-disclosure-requirements-amendment-regulations-2025_93156.html

ⁱ Reg. 15(1A) of LODR

ⁱⁱ Explanation 5 to reg 15(1A) of LODR

ⁱⁱⁱ Reg 62C(1) of LODR

^{iv} 1st proviso to reg. 62C(1) of LODR

^v Explanation to reg 62C(2) of LODR

^{vi} https://www.sebi.gov.in/sebi_data/meetingfiles/dec-2024/1735215423736_1.pdf



Foreign Contributions Under the Clock: The Changing Validity Landscape of FCRA Permissions

1. Introduction:

The Ministry of Home Affairs (MHA) has introduced significant regulatory changes under the Foreign Contribution (Regulation) Act, 2010 (FCRA), by notifying new validity limits for organizations granted prior permission to receive foreign contributions. The period for receiving foreign funds is now capped at three years, while the utilization period is restricted to four years, replacing the earlier open-ended regime. This move aims to streamline foreign funding oversight, enforce uniform compliance timelines, and enhance transparency in the management of foreign contributions.

2. Prior Permission under FCRA:

The Foreign Contribution (Regulation) Act, 2010 (FCRA) was enacted to regulate the acceptance and utilization of foreign contributions or hospitality by individuals, associations, and companies. Its primary purpose is to ensure that foreign funds are used in a manner consistent with national interest and do not compromise the sovereignty and integrity of India.

Under Section 11(1) of the Act, an individual or organization not already registered under FCRA can receive foreign contributions only after obtaining prior permission from the Ministry of Home Affairs (MHA). This provision is especially relevant for :

- Newly formed organizations, not having complete 3 years of operations required to be fulfilled for obtaining registration under 11(2),
- Organizations planning to undertake a specific project with foreign funding,
- Individuals or entities engaging in activities of definite cultural, economic, educational, religious, or social nature.

Key Features of Prior Permission:

- Granted for a specific source of funding.
- Applicable to specific project(s) or activity(ies).
- Requires adherence to utilization and reporting norms as per FCRA and related rules.

3. MHA Public Notice Dated 7th April 2025: Introduction of New Validity Periods:

On 7th April 2025, the Ministry of Home Affairs, through its Foreigners-II Division (FCRA), issued Public Notice No. IF21022/36(0025)/2025/FCRA-II introducing new norms related to the validity period for receipt and utilisation of foreign contribution under prior permission:



Highlights of the Public Notice:

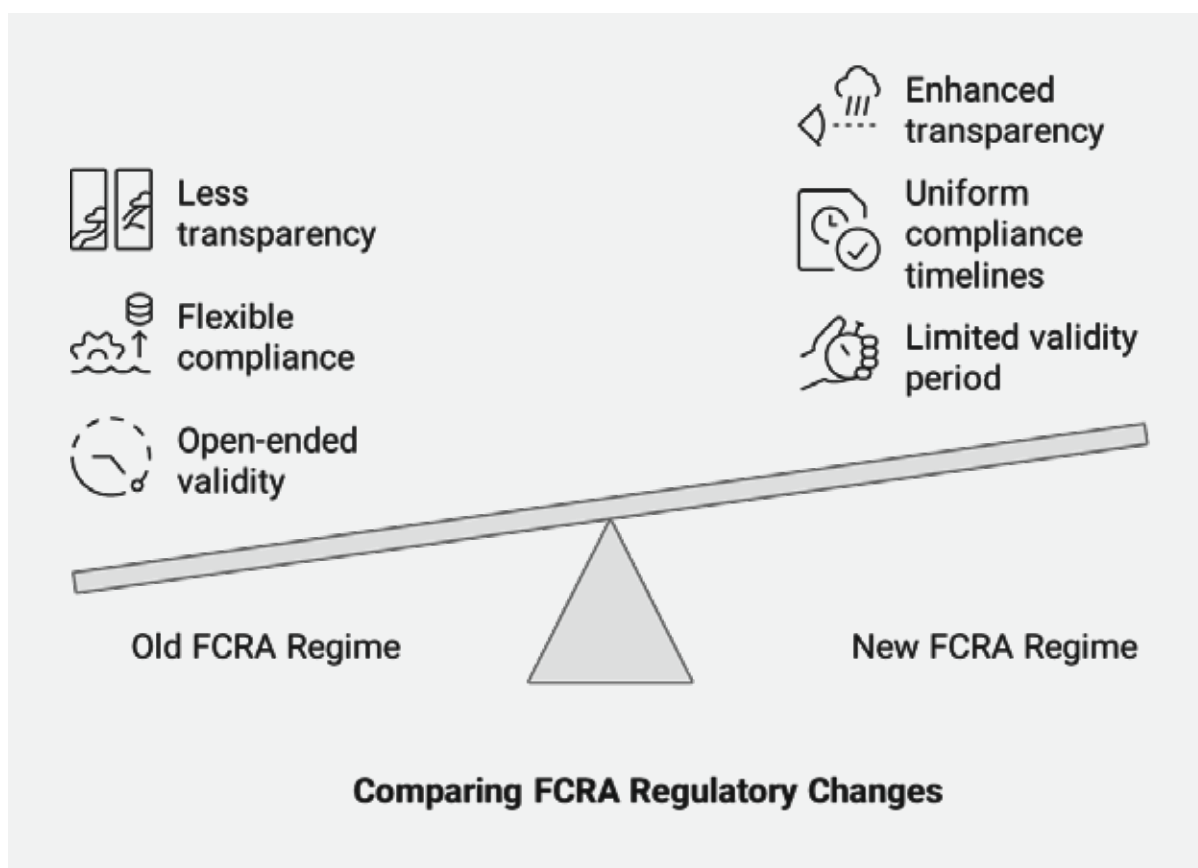
- Validity for Receiving Foreign Contribution:

The validity period for receiving foreign contributions shall be three years, commencing from the date on which the application for prior permission is approved by the Ministry of Home Affairs

- Validity for Utilization of Foreign Contribution:

The foreign contribution sanctioned shall be utilized within a period of four years from the date on which the Ministry of Home Affairs grants approval to the application

This amendment has been brought into effect by exercising powers under Section 46 of the FCRA, 2010, which empowers the Central Government to issue such directions to ensure proper implementation of the Act.



4. Effect of the Public Notice: Uniformity and Predictability :

The implications of the public notice for applicants and grantees for prior permission under FCRA shall include:

- Brings clarity and consistency in validity terms.

The introduction of fixed timelines eliminates inconsistencies and case-specific variations that often existed in the prior permission process. Organizations now operate within a clearly defined window for both fund receipt and utilization. This

consistency simplifies legal compliance and improves internal planning and documentation.

- Eases regulatory tracking by enforcement and audit agencies.

Uniformity in validity periods facilitates streamlined regulatory supervision. Authorities such as the MHA and auditing agencies can now more effectively monitor compliance, ensuring timely use of funds and easier detection of any deviations or violations. This also aids in better data collection, reporting, and governance.

- Encourages timely execution of foreign-funded projects.

The new framework compels recipient organizations to initiate and complete their projects within a defined timeframe, thereby avoiding delays, fund stagnation, or misallocation. Projects must now be designed with a sharper focus on timeline discipline, ensuring that the intended social, educational, cultural, or developmental impacts are achieved without undue delay.

- Organizations must now plan and implement projects within a defined period, avoiding indefinite holding of funds.

Entities seeking prior permission will now need to align their project design, budgeting, execution strategy, and reporting cycles with the standardized validity periods. This leads to better planning and discourages indefinite holding or diversion of funds beyond the approved scope or duration.

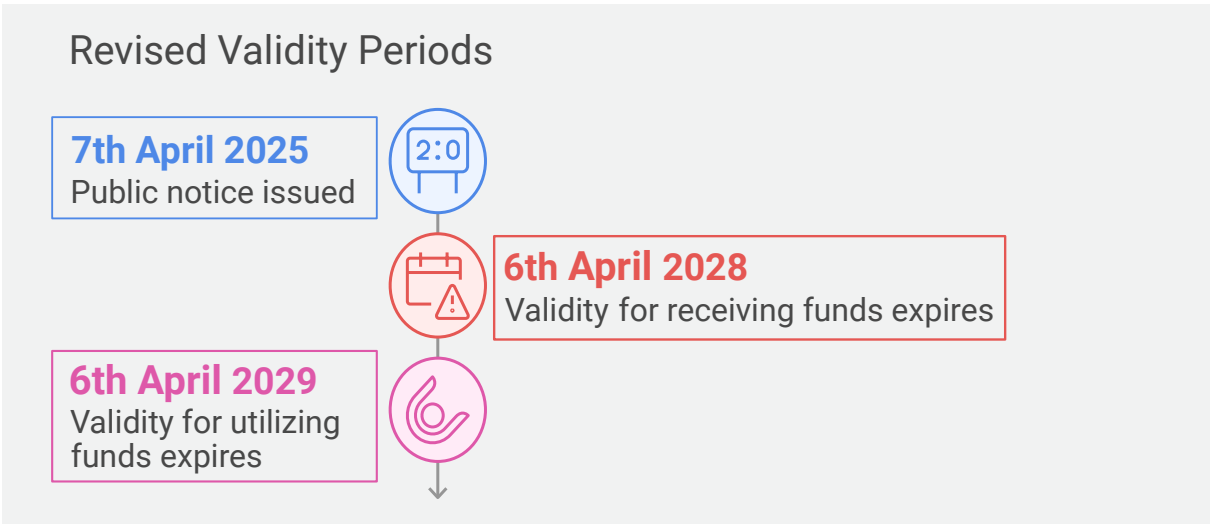
5. Impact on Entities That Received Prior Permission Before 7th April 2025:

For organizations that had obtained prior permission before the date of this notice, the MHA has provided a transitional provision to ensure continuity and clarity.

Recalculation of Validity Periods:

If the remaining duration of the project/activity (as approved under prior permission) is more than 3 years from the date of the notice (i.e., beyond 7th April 2028), the validity for receiving and utilizing foreign funds will now be recomputed as follows:

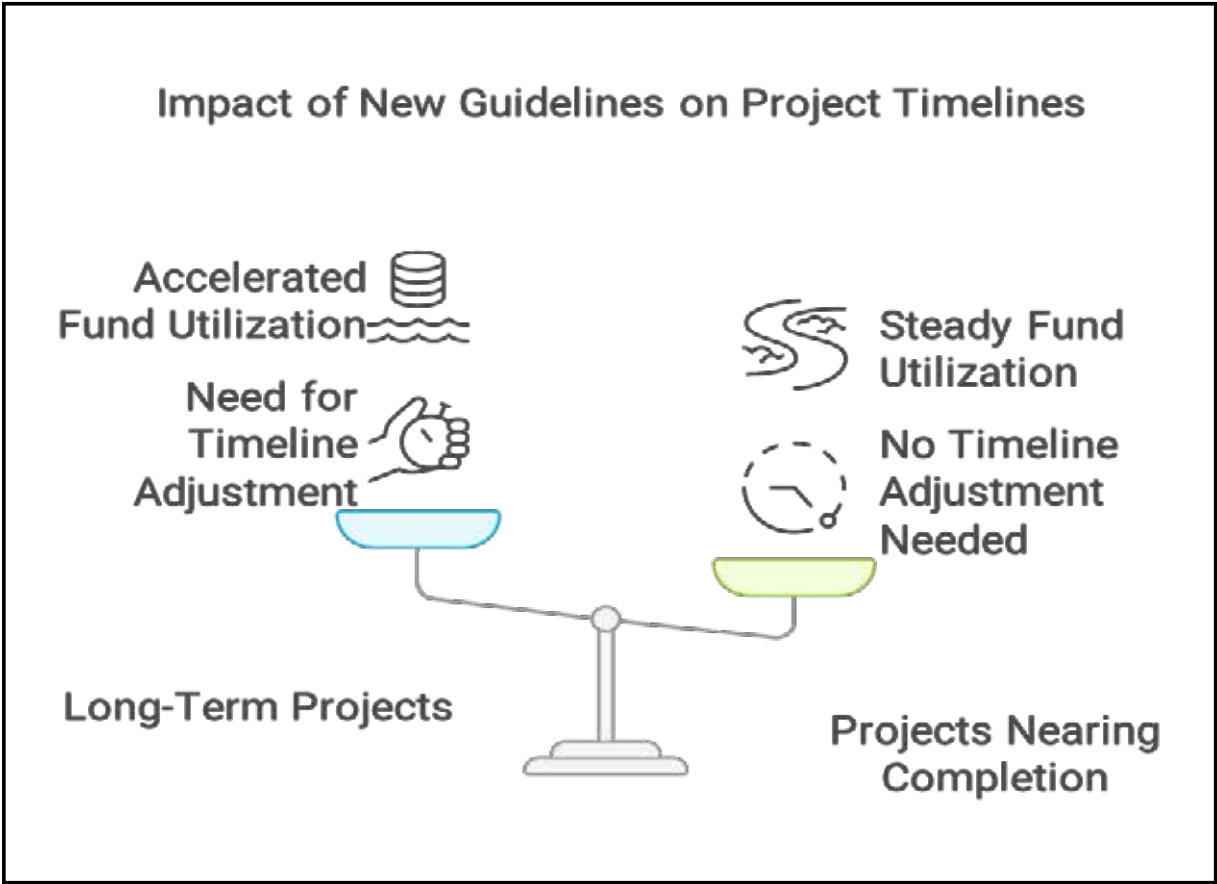
Purpose	Revised Validity
Receiving Foreign Contributions	Valid up to 6th April 2028 (3 years from the date of public notice)
Utilization of Foreign Contributions	Valid up to 6th April 2029 (4 years from the date of public notice)



This ensures that older projects with longer timelines are brought in line with the new uniform standards, without disrupting those nearing completion.

Illustrative Practical Examples

Example	Project Details	Impact Based on New Guidelines	Outcome
1. Long-Term Project Still in Early Phase	NGO received prior permission in Oct 2022 for a 6-year water conservation project	<ul style="list-style-type: none">• As of date of public notice/ notification, 3.5 years remain• Validity to receive funds recalculated to 6th April 2028• Utilization allowed up to 6th April 2029	NGO must accelerate fund inflow and project execution to comply with the revised limits
2. Project Nearing Completion – No Major Impact	Trust received prior permission in June 2021 for a 5-year education program ending May 2026	<ul style="list-style-type: none">• As of public notice/ notification, only 1 year remains• Project not affected by new limits due to short remaining timeline	Trust can continue operations as planned; no recalibration needed



Key Takeaways for Organizations :

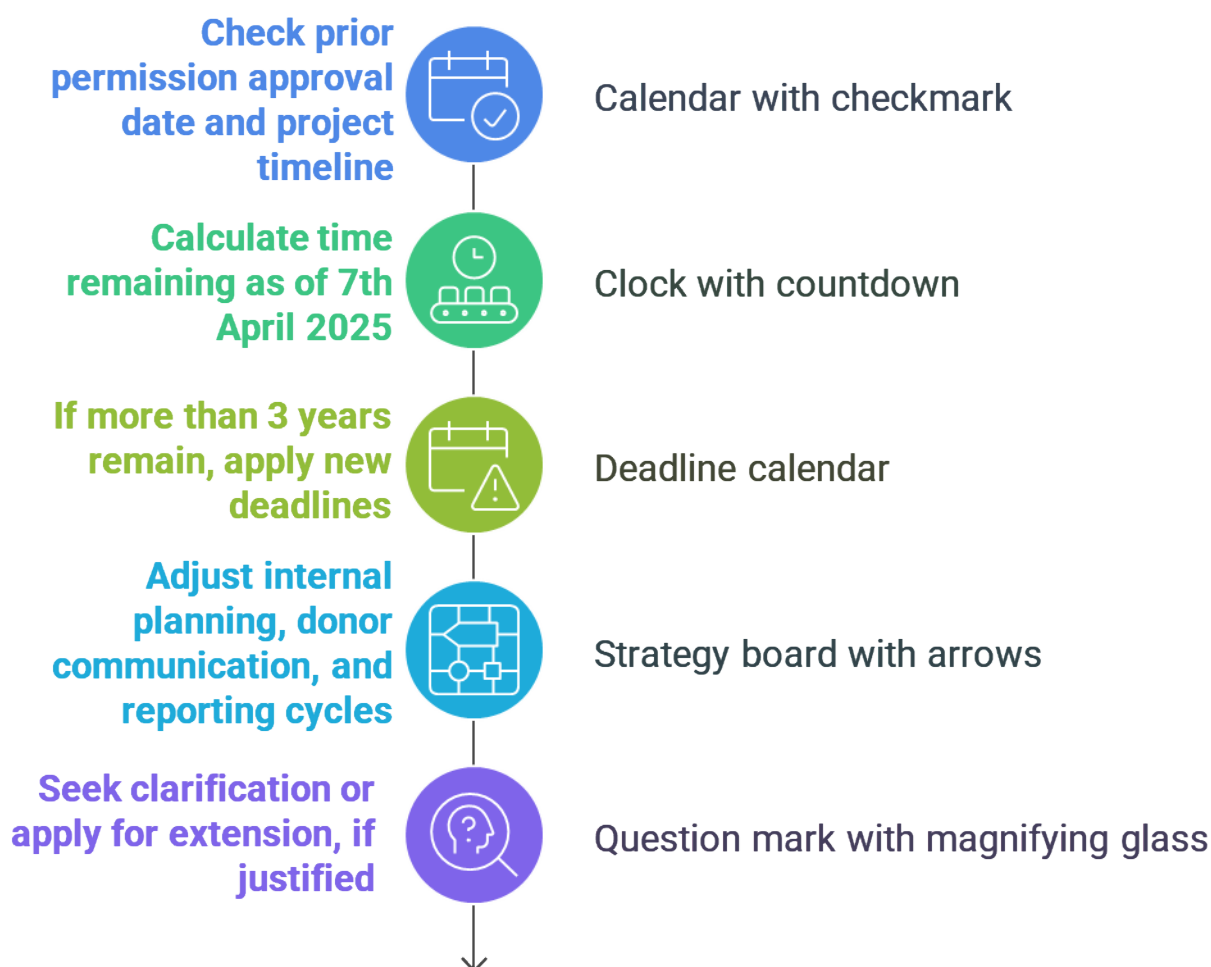
- Entities with older prior permissions that still have long project durations remaining will need to re-align their timelines according to the new framework.
- This change avoids indefinite fund flows and aligns all existing approvals with a clear and consistent policy structure.
- Organizations should review their original approvals, check the remaining project period, and, if needed, adjust their fundraising and activity schedules to ensure compliance.

Action Points for organisations having received prior permission under FCRA and have unutilised foreign contribution:

- Check your prior permission approval date and project timeline.
- Calculate how much time remains as of 7th April 2025.
- If more than 3 years remain, apply the new deadlines for receiving and using funds.
- Adjust internal planning, donor communication, and reporting cycles accordingly.
- Seek clarification or apply for extension, if justified, on a case-by-case basis



Navigating FCRA Compliance: Key Action Points



6. Consequences in Case of Contravention

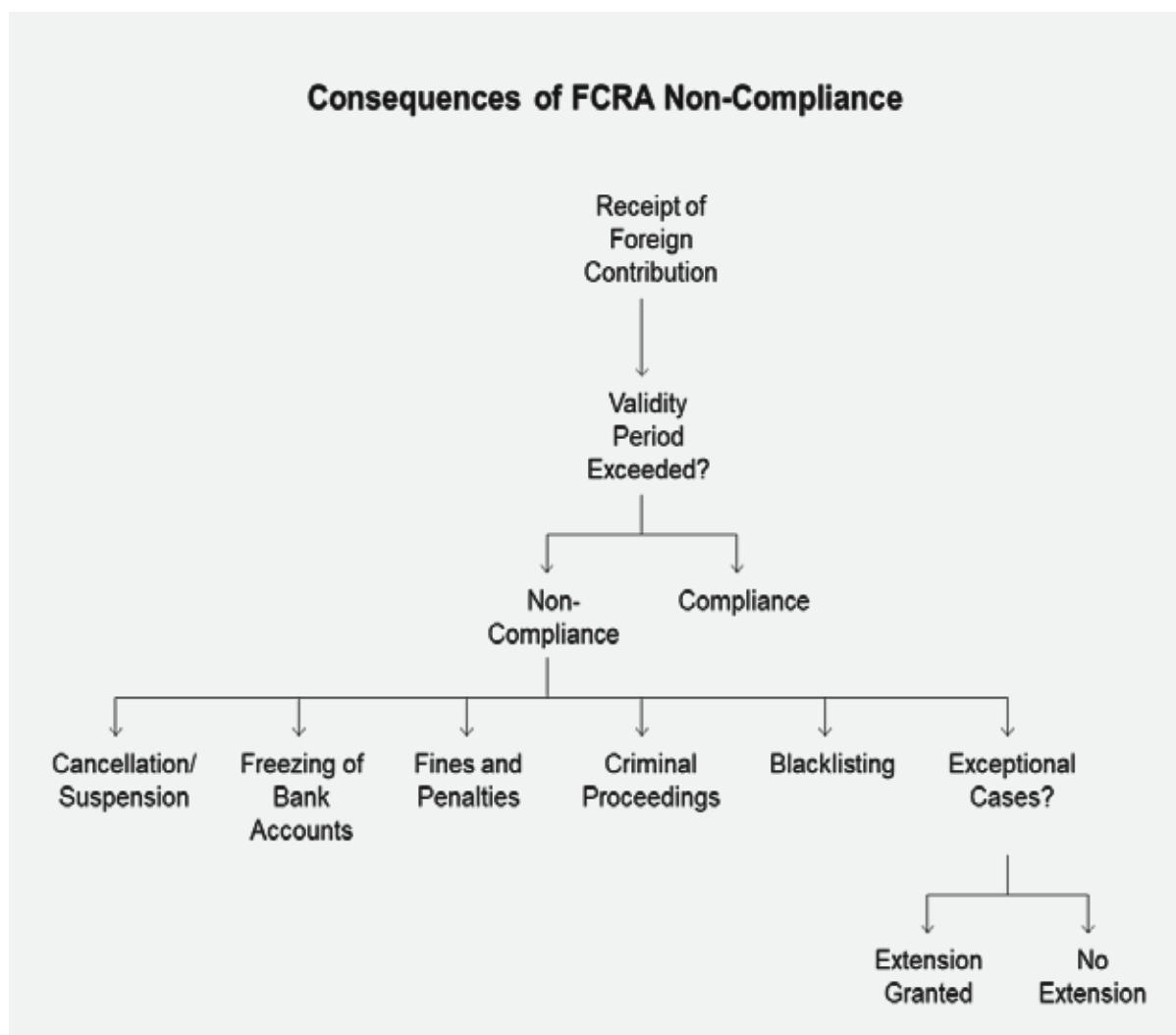
The Ministry has clarified that any receipt or utilization of foreign contribution beyond the specified validity periods, unless expressly approved, may be considered non-compliant with the provisions of the FCRA, 2010

Possible Penal Actions:

1. **Cancellation or Suspension** of FCRA registration or prior permission.
2. **Freezing of bank accounts** holding foreign contribution funds.
3. **Imposition of fines and penalties** as per Section 35 to 39 of the Act.
4. **Initiation of criminal proceedings**, where applicable.
5. **Blacklisting** of the organization, barring it from receiving foreign funds in the future.

However, the notice also provides flexibility in exceptional cases:

The Competent Authority in the Ministry of Home Affairs may grant an extension of the validity period on a case-to-case basis, depending on the merits of the proposal and justifications offered by the organization.



Conclusion:

The Ministry of Home Affairs' public notice dated 7th April 2025 appears to be a timely response to recurring instances where organizations either failed to receive foreign contributions after obtaining prior permission or did not utilize the received funds in accordance with the approved objectives and timelines. A notable example highlighting the need for regulatory tightening is the recent NCLT order in the matter of LBR Foundation India, dated 4th March 2025, which underscored the importance of proper fund management and compliance under the FCRA.

Against this backdrop, the Ministry's decision to introduce standardized validity periods for receiving and utilizing foreign contributions marks a significant step toward strengthening the FCRA regulatory framework. It reflects the government's intent to enhance accountability, promote timely implementation of foreign-funded projects, and ensure that foreign contributions are used strictly for their intended purposes.

Organizations and individuals relying on prior permission under FCRA must take immediate steps to:

- Review their approvals and current project timelines,
- Assess compliance risks, and
- Apply for extensions, if necessary.

This article is published in Taxguru. The link to the same is as follows

<https://taxguru.in/corporate-law/mha-introduces-validity-limits-fcra-foreign-contributions.html>

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From Ambiguity to Certainty Issue and Reporting of Partly Paid Units by Investment Vehicles

The Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 (NDI Rules) were introduced to govern the inflow of equity and other non-debt capital instruments. However, these rules originally lacked clarity regarding the issuance of partly paid units to foreign investors by investment vehicles such as Alternative Investment Funds (AIFs).

Before March 14, 2024, there was no express provision under the NDI Rules allowing the issuance of partly paid units to non-residents. As a result, fund managers and legal practitioners operated within an area of regulatory uncertainty. Many investment vehicles cautiously avoided such issuances, while others proceeded based on legal interpretations, exposing themselves to the risk of non-compliance under FEMA. Moreover, the absence of a dedicated reporting mechanism within the RBI's FIRMS portal added another layer of uncertainty.

March 2024 Amendment:

Recognizing the pressing need for clarity, the Foreign Exchange Management (Non-Debt Instruments) (Second Amendment) Rules, 2024, were notified via notification S.O. 1361(E) on March 14, 2024. This amendment explicitly permitted investment vehicles to issue partly paid units to persons resident outside India, thus bringing long-awaited certainty to the sector. The change aligned India's capital markets more closely with global norms, especially in how staged investments can be structured over time.

Treatment of Prior Issuances: Compounding as a Remedy:

To address the issuances made prior to March 14, 2024, the RBI issued A.P. (DIR Series) Circular No. 7, dated May 21, 2024 directing such transactions to be regularized through compounding under FEMA.

This required investment vehicles to first report the details of the partly paid units on the FIRMS portal, followed by submitting an application for compounding. Additionally, Authorized Dealer (AD) Banks were instructed to support this process by providing conditional acknowledgments and ensuring proper documentation.

The reporting and timelines for reporting partly paid units in Form InVi still remained a question.

Reporting Obligations:

The RBI vide A.P. (DIR Series) Circular No. 06 dated May 23, 2025 provided for reporting of Partly paid Units in Form InVi within 30 days of the issuance date in terms of Regulation 4(10) of the Foreign Exchange Management (Mode of Payment and Reporting of Non-Debt Instruments) Regulations, 2019

One-Time Window for Delayed Reporting:

180-Day Window for Regularizing Delayed Reporting for Issuance Prior to Notification

Understanding that many investment vehicles could not report earlier due to lack of clarity to both to the applicants and Authorised Dealer banks, the RBI's May 2025 circular provided a one-time **180-day window (180 days shall be counted from the date of circular)** for delayed filings without any late submission fees.

However, for issuances on or after the date of the circular, the standard 30-day reporting deadline continues to apply, and delays will attract penalties as per FEMA regulations.

Compounding for any other contraventions:

It is important to note that this amnesty window is limited to delays in filing Form InVI and does not cover other forms of non-compliance or contraventions under FEMA (including issue of partly paid units prior to March 14, 2024). Entities must ensure that all other regulatory obligations are met independently and, where necessary, addressed through appropriate compounding or late filing fees.

❖ Timely Compliance and Institutional Best Practices:

With the updated regulatory and technical framework in place, timely reporting has become non-negotiable. Investment vehicles must implement internal compliance mechanisms to track and report issuances promptly. AD Banks now play a more active role in oversight, ensuring that submissions are in line with regulatory expectations.

This article is published in Taxguru. The link to the same is as follows: -

<https://taxguru.in/rbi/issue-reporting-partly-paid-units-investment-vehicles.html>

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Section 14 of IBC in no manner impact invocation of Bank Guarantee during pendency of the Moratorium

In the matter of Mitsubishi Heavy Industries Limited (Appellant) vs Punj Lloyd Limited (Respondent) and others at National Company law Appellate Tribunal (NCLAT) 9 August 2024

Facts of the Case:

- In 2015, a contract was entered between Indian Oil LNG Private Limited (IOLPL) and Mitsubishi Heavy Industries Limited (the appellant) on 15 September 2015. The appellant subcontracted parts of the work to Punj Lloyd Ltd. (Respondent No. 1/Corporate Debtor/CD)
- As per the contract's general conditions, the Corporate Debtor (CD) was required to provide an unconditional and irrevocable Bank Guarantee as security for proper and timely performance of the obligations. A Performance Bank Guarantee worth approximately Rs. 47.7 Crores was issued by State Bank of India in favor of the appellant.
- The agreed mechanical completion date under the contract with CD was 23 March 2018, but the appellant issued a Mechanical Completion Certificate with a completion date of 31 January 2019.
- On 8 March 2019, the Corporate Insolvency Resolution Process (CIRP) was initiated against CD before the National Company Law Tribunal (NCLT).
- On 30 October 2019, the appellant invoked the Performance Bank Guarantee due to fundamental breaches of the contract, including delays in achieving mechanical completion and failure to inspect and repair leakage in the LNG Tank during the defect liability period.
- On 13 November 2019, the Resolution Professional (RP) of CD filed an application before the NCLT, seeking directions under Section 14 of the Insolvency and Bankruptcy Code, 2016 (IBC) to restrain the appellant from encashing the Performance Bank Guarantee.
- *NCLT referred to the NCLAT judgment in C&C Construction Ltd. v. Power Grid Corporation of India Limited (26 July 2021), where it was held that the moratorium period under Section 14 of the IBC does not cover performance bank guarantees.*
- On 27 May 2022, NCLT directed the liquidation of the CD as a going concern.
- Despite this, the RP's application to restrain the appellant from encashing the Performance Bank Guarantee was allowed by an order dated 30 October 2023, against which this appeal has been filed.

Arguments of the Appellant

- The Performance Bank Guarantee (PBG) issued by State Bank of India in favor of the appellant was irrevocable and unconditional.
- The CD had agreed to complete the work by the mechanical completion date, but there was a 10-month delay. During the defect liability period, the appellant sent emails to CD to inspect leakage in the LNG tank, but these requests were refused, resulting in a breach of contract by CD.

- As a result, the appellant was forced to invoke the PBG on 30 October 2019.
- The RP filed an application on 13 November 2019, seeking to restrain the appellant from encashing the PBG. However, the application was not maintainable because:
 - NCLT lacked jurisdiction to determine the legality of the PBG invocation or adjudicate contractual disputes between the appellant and CD.
 - The PBG is an independent contract, and courts should not interfere with its invocation except in exceptional circumstances, which did not exist in this case.
- Since the bank guarantee was unconditional and irrevocable, the appellant was not required to prove losses at the time of invocation. The appellant had valid claims due to:
 - Delay in mechanical completion.
 - Failure to cure defects during the defect liability period
- The Defect Liability Period was 30 months from the mechanical completion date or 24 months from the issuance of the completion certificate. During this period, the CD was required to conduct searches, tests, or trials to determine the cause of any defect.
- The NCLT's order restraining the appellant from encashing the PBG was without jurisdiction.
- The PBG has been explicitly excluded from the moratorium under Section 14 of the IBC, following an amendment by Act 26/2018 effective 6 June 2018.
- As such, the moratorium under Section 14 of the IBC did not apply to the PBG, and the appellant was fully entitled to invoke the PBG even after the insolvency proceedings against CD which began on 8 March 2019.
- In similar cases within the same CIRP, NCLT rejected applications filed by the RP seeking to restrain the invocation of guarantees by IOCL and GAIL, but in this case, the NCLT allowed the RP's application, resulting in an inconsistent ruling.
- The NCLT was aware that the issue was pending before the NCLAT in the case of C&C Construction Ltd., which was decided on 26 July 2021, confirming that the moratorium period under Section 14 does not cover performance bank guarantees, meaning the RP's application should have been rejected

Arguments of the Respondent

- NCLT had ample jurisdiction to adjudicate the application filed by the RP regarding the bank guarantee.
- NCLT previously considered similar applications filed by the RP in cases involving IOCL, GAIL, and Triveni-Mersens and passed orders on the issues related to bank guarantees, indicating that the appellant cannot now claim that NCLT lacks jurisdiction .
- The orders passed by NCLT in the IOCL, GAIL, and PLL cases were not overturned by the NCLAT, and the Triveni-Mersens order applied directly to this case. In the Triveni-Mersens case, NCLT held that once a Mechanical Completion Certificate is issued, the bank guarantee should be discharged.
- Even if the bank guarantee was termed unconditional and irrevocable, this did not mean the appellant could invoke it arbitrarily or outside the scope of contractual provisions. Any claim during the Defect Liability Period should have been quantified and communicated to the Corporate Debtor (CD) with sufficient evidence, which the appellant failed to do.

- As per Clause 7.1.2, once a Mechanical Completion Certificate is issued, the contractor is no longer responsible for that part of the work, unless there is damage caused by the CD's ongoing activities.
- In this case, the Mechanical Completion Certificate was issued on 3 September 2018, so the CD could not be held responsible for the alleged leakage. The invocation of the bank guarantee could lead to asset stripping of the CD.
- The argument that the bank guarantee is not an asset of the CD should be rejected, as State Bank of India extended the bank guarantee based on the CD's collateral. If the bank guarantee was wrongfully invoked, the State Bank of India would claim the same from the CD as a creditor, causing the CD to suffer the ultimate loss.
- NCLT has jurisdiction to examine all aspects related to bank guarantee invocation, including factual aspects. Given the special equities in favor of the CD, the bank guarantee should not have been invoked, as doing so would cause irretrievable injury to the CD.

HELD:

- NCLAT referred the following cases:
 - *State Bank of India Vs. V. Ramakrishnan & Anr.*
 - *Himadri Chemical Industries Ltd. Vs. Coal Tar Refining Co.*
 - *Standard Chartered Bank Vs. Heavy Engineering Corporation Limited & Anr.*
- *It was noted that the issue regarding the invocation of performance bank guarantees during the moratorium period is well established in law. Also noted that the definition clarifies that "Security Interest" does not include PBG. Effective from June 6, 2018, Section 14(3) explicitly excludes security in a contract of guarantee from the provisions of Section 14(1) of the IBC. It is well settled that Section 14 does not affect the right of a beneficiary to invoke a bank guarantee during the moratorium. The disputes between the beneficiary and the party who requested the bank guarantee are immaterial and do not affect invocation. Invocation of a bank guarantee may only be restrained on the grounds of irretrievable injury and special equity.*
- NCLT did not allow the application filed by the Resolution Professional (RP) based on exceptions highlighted by the Supreme Court in *Standard Chartered Bank*. Instead, NCLT stated that the appellant failed to prove any fault on the part of the CD or quantify its claim
- NCLT allowed the application on the grounds that the appellant did not prove a default of contract by the CD.
- According to the Supreme Court in *Standard Chartered Bank*, disputes raised by the contractor regarding the invocation of an unconditional and irrevocable bank guarantee are not to be considered.
- The NCLT erred by allowing the application to restrain the appellant and other banks from invoking the bank guarantee, rendering its order unsustainable. The appeal was allowed, overturning the NCLT's decision.

This article is written by **Esha Tandon – Deputy Manager** -eshatandon@mmjc.in and **Arti Ahuja Partner** – artiahuja@mmjc.in



SEBI Circular Dated 26th June 2025

Sr. No.	Circular	Link
1.	SEBI Circular on Industry Standards on “Minimum information to be provided to the Audit Committee and Shareholders for approval of Related Party Transactions	https://www.sebi.gov.in/legal/circulars/jun-2025/industry-standards-on-minimum-information-to-be-provided-to-the-audit-committee-and-shareholders-for-approval-of-related-party-transactions-_94809.html

