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Articles

SEBI approves shares with differential voting rights - A welcome move

By **L. Badri Narayanan and Pooja Vijayvargiya**

The Securities and Exchange Board of India ("SEBI") in its Board meeting dated 27th June, has approved a framework for issuance of shares with differential voting rights ("DVRs"), along with amendments to the relevant SEBI regulations to give effect to the framework.

This framework is in furtherance to the comments received on the consultation paper of the DVR Group formed by the Primary Market Advisory Committee of SEBI ("PMAC") and the recommendations of the PMAC.

DVR shares are a class of shares with fractional rights ("FRs") or superior voting rights ("SRs") than ordinary equity shares. Traditionally, shares with DVRs have not been an attractive source of raising capital in India. However, with the ever-growing number of tech related start-ups in India, it was the need of the hour to provide for shares with DVRs, which enable such companies to not dilute control while also raising capital.

While not all the recommendations made by PMAC were accepted by SEBI, the key proposals made in the board meeting are enlisted below:-

i. **Eligibility**:

A company having SR shares would be permitted to do an initial public offering (IPO) of only ordinary shares to be listed on the Main Board, subject to fulfillment of the necessary provisions of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 and the following conditions :-

a) The issuer company is a tech company (as per the definition in Innovators Growth Platform) i.e., intensive in the use of technology, information technology, intellectual property, data analytics, bio-technology or nano-technology to provide products, services or business platforms with substantial value addition.

b) The SR shareholder must only be promoters/ founders who hold an executive position in the company and whose collective net worth (excluding the investment of SR shareholders in the shares of the company) does not exceed Rs. 500 Crores.

c) SR shares have been held for a period of at least 6 months prior to the filing of the Red Herring Prospectus (RHP) and have voting rights in the ratio of minimum 2:1 to maximum 10:1, compared to ordinary shares.

ii. **Listing and Lock-in:**

SR shares shall also be listed on Stock Exchanges post public issue but they shall be under lock-in until their conversion to ordinary shares. Further, transfer of SR shares amongst promoters and any pledge or lien on them shall not be permitted.

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iii. **Right of SR shares:**

Accepting the PMAC proposal, the Board decided that SR shares shall be treated at par with ordinary shares in every respect, including dividends, except in the case of voting on resolutions. However, the total voting rights of SR shareholders (including ordinary shares), post listing, shall be capped at 74%.

iv. **Coat-tail provisions:**

Accepting most of PMAC's proposals, the Board decided that post IPO, SR shares will have only one vote in the following key management decisions:-

a. Appointment or removal of independent directors and/or auditor;

b. In case where promoter is willingly, transferring control to another entity;

c. Related Party Transactions involving SR shareholder;

d. Voluntary winding up of the company;

e. Changes in the company's Article of Association or Memorandum - except any changes affecting the SR instrument;

f. Initiation of a voluntary resolution plan under Insolvency and Bankruptcy Code;

g. Utilization of funds for purposes other than business;

h. Substantial value transaction based on materiality threshold as prescribed under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015;

i. Passing of special resolution in respect of delisting or buy-back of shares; and

j. Any other provisions notified by SEBI.

v. **Sunset-clauses:**

The following circumstances will lead to conversion of SR shares into equity shares:-

✓ Time-based conversion on the 5th anniversary of listing with only one extension upto 5 years through a resolution (where SR shareholder would not be permitted to vote).

✓ Event-based conversion on occurrence of certain specified events (such as demise, resignation of SR shareholders etc.)

Apart from the above, the Board prohibited issue of FR shares by existing listed companies, however, the same may be reviewed once enough experience is gained with SR shares.

It is worth noting that the above changes will come into effect once necessary amendments are made in the relevant legislations and regulations of SEBI. Nevertheless, with SEBI proposing the aforesaid amendments for tech start-ups, India seems to be following the norms prevailing in the international arena where tech companies like Facebook, Google etc. have introduced shares of different classes to raise capital. This effort of SEBI will certainly spurt the growth of start-ups in India and is a welcome move.

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Roles and responsibilities of Compliance Officers under SEBI regulations

By **Rohit Subramanian**

Business environment in India has undergone a sea-change in the past decade. Increased emphasis on values such as accountability, transparency, risk management has led to integration of compliance management with business processes. Executive board member(s) of companies are now incentivized and encouraged to multiply their efforts towards value protection and management and not just value creation. The paradigm shift in the expected role of managerial personnel(s) can be attributed to the shift in penal measures adopted by regulators from corporate liability to a personal liability regime. This article focuses specifically on the stand taken by Securities Exchange Board of India ("SEBI") with respect to role, responsibilities and liability of "compliance officers".

SEBI expects numerous compliances from listed entities and vide SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("LODR") establishes a framework for corporate governances applicable to every entity listed with stock exchange(s) in India. One of the primary requirements of the LODR is the appointment of a qualified company secretary in the capacity of a compliance officer, to ensure conformity with SEBI regulations in letter as well as spirit. So much so that, the said compliance officer along with the the chief executive officer is authorized to sign the quarterly compliance report on corporate governance, to be filed with the relevant stock exchange.

The Compliance officer is inter-alia responsible for carrying out numerous core functions including co-ordination with recognised stock exchange(s) and depositories vis-a-vis compliance with rules, regulations and other directives of SEBI; monitoring e-mails received by grievance redressal division of the listed entity; maintenance of appropriate procedures to ensure correctness, authenticity and comprehensiveness in information being filed with SEBI etc.

The SEBI (Prohibition of Insider Trading) Regulations, 2015 ("PIT Regulations") propagates a self-regulatory mechanism to enforce prohibitions on insider trading in listed entities and, thereby, piles on more responsibilities on the compliance officer.

As per the PIT Regulations, a compliance officer could be any senior officer who is designated so and is reporting to the board of directors. The compliance officer shall be responsible for compliance of policies, procedures, maintenance of records and monitoring adherence to the provisions of PIT Regulations for preservation of unpublished price sensitive information (**UPSI**). Every trading plan is required to be reviewed and approved by the compliance officer before it is notified to the stock exchanges on which the securities are listed.

Every company whose securities are listed on stock exchanges and every market intermediary registered with SEBI is mandatorily required to formulate a code of conduct to regulate, monitor and report trading by its employees. The onus of administering the code of conduct is on the compliance officer. The compliance officer shall also advise the board of directors on the designated person proposed to be covered by the said code of conduct.

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It is pertinent to note that, compliance officer performs requisite functions/responsibilities under the overall supervision of the board of directors or head of organization of the listed entity. Notwithstanding the above, the compliance officer has the obligation to perform his duties independent of the board of directors. The extent of power and liability of the compliance officer came into question in the infamous matter of *Satyam Computer Services Limited*[1], wherein SEBI was of the opinion, that the compliance officer being one of the key personnel, has an important role to play in the company for monitoring adherence to SEBI regulations, preservation of price sensitive information and implementation of code. Even if the relevant regulations specify that the compliance officer shall execute his responsibilities under the overall supervision of the Board, yet the provision confers key responsibilities on the compliance officer per se, which cannot be overlooked. SEBI, in its order, stated that the compliance officer cannot raise the defence that internal approvals were not available, because if such contention is accepted, it would render the concept of appointment of compliance officer meaningless.

Given the aforesaid background, the adjudicating officer found that the compliance officer failed in its responsibility to close the trading window and adhere to provisions of the code of conduct and applicable SEBI regulations and, therefore, imposed monetary penalty as per Section 15HB of the Securities and Exchange Board of India, 1992. SEBI referred to the Supreme Court judgement in *SEBI v. Shri Ram Mutual Fund*[2] wherein it was held that "*once the violation of statutory regulations is established, imposition of penalty becomes sine qua non of violation and the intention of parties committing such violation becomes totally irrelevant. Once the contravention is established, then the penalty is to follow.*" An appeal was preferred with the Securities Appellate Tribunal (SAT)[3], which did not result in a different outcome for the appellant. The SAT confirmed penalty of INR 5,00,000 on the compliance officer for violating applicable SEBI regulations.

More recently SEBI provided further insight on the authority of a compliance officer with respect to pre-clearance of security trade in an Interpretative Letter dated February 3, 2017 issued to Kirloskar Chillers Private Limited (KCPL). One of the queries raised by KCPL was whether compliance officer has discretionary power to accept or reject pre-clearances for any reason it deems fit, even if they are extraneous to the provisions of the PIT Regulations or the code of conduct.

SEBI, in its response, stated that Regulation 2(1)(c) read with Schedule B of the PIT Regulations casts certain obligations on the compliance officer, which includes making decisions with respect to a pre-clearance request after necessary assessment as per PIT Regulations and the code of conduct. Since the compliance officer acts under the overall supervision of the board of directors or the audit committee, the acts of the compliance officer can be referred to the board of directors or the audit committee, irrespective of whether such action is extraneous to the provisions of the PIT Regulations or the code of conduct. Therefore, SEBI is of the view that the board of director or the audit committee, as the case maybe, shall merely serve as a review mechanism to examine the decisions made by the compliance officer and does not dilute the compliance officer's obligations under the PIT regulations or the code of conduct.

[1] SEBI Adjudication Order No. PG/AO-115/2011 dated November 29, 2011

[2] (2006) 68SCL 216 (SC)

[3] Appeal No. 182 of 2012, Securities Appellate Tribunal, Mumbai dated 24.12.2013

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It is clear from the judgment and interpretation letter that SEBI holds the compliance officer responsible for general compliance of all SEBI regulations. Given that the board of directors are required to establish controls, especially to prevent disclosure of UPSI, ambiguity continues to exist with respect to attribution of liability and responsibility under PIT regulations.

The role of compliance officer in a listed company for the aforesaid reasons is abound with risks for a professional from a regulatory perspective. Therefore, it is extremely important for the professional to meticulously examine the applicable SEBI regulations while accepting the role of a compliance officer and negotiate on matters such as D&O liability insurance or indemnity protection prior to accepting such a position in a listed entity.

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A step towards strengthening institutional arbitration in India - New Delhi International Arbitration Centre Act, 2019

By **Akshita Alok**

With a view to promote institutional arbitration and to make India a destination for conducting international arbitration, a new bill was introduced and has been passed by both the Houses of the Indian Parliament and assented by the President of India – The New Delhi International Arbitration Centre Act, 2019.

The Act replaces the New Delhi International Arbitration Centre Ordinance, 2019 (“the Ordinance”) which was promulgated on 2nd March 2019.

The objective of the Act is to promote institutional arbitration in India and it is based on the recommendations of the High-Level Committee headed by Mr. Justice B.N. Srikrishna, former Judge, Supreme Court of India. The recommendations of the Committee, *inter alia*, suggested that the International Centre for Alternative Dispute Resolution at New Delhi (ICADR), established in the year 1995 to promote alternative dispute resolution mechanism, had not been able to achieve its objectives and should be taken over by the proposed New Delhi International Arbitration Centre (“the Centre”). It has also been proposed to declare the Centre an institution of national importance.

A shift in policy towards promoting ease of business in India, increasing pendency of cases in courts, lack of options for institutional arbitration in India and issues being faced by parties in ad-hoc arbitrations are a few of the reasons that led to this Act.

Key features of the Centre, as enshrined in the Act, are discussed below –

i. **Members and Chairperson** – The Centre shall be headed by a Chairperson appointed by the Central Government in consultation with the Chief Justice of India and such person should have been a judge of the

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Supreme Court or a High Court or an eminent person with special knowledge and expertise in arbitration, law or management. The 7-member body would consist of two eminent person having knowledge and expertise in international and domestic institutional arbitration appointed by the Central Government; one representative from a recognised body of commerce and industry chosen by the Central Government; Secretary, Department of Legal Affairs, Ministry of Law and Justice; a Financial Advisor nominated by the Department of Expenditure, Ministry of Finance and a Chief Financial Officer.

ii. **Transfer of Undertakings of ICADR** – The Act provides that, from a date specified by the Central Government by a notification, the right, title and interest of the ICADR in relation any undertaking which form part of or are relatable to ICADR, shall stand transferred to and vest in the Central Government, which shall in turn, direct by notification that the undertakings shall vest in the Centre.

iii. **Objects of the Centre** – The Centre will be established with the object of (i) bringing targeted reforms to develop itself as the flagship institution for conducting international and domestic arbitration; (ii) promoting research, study, training, teachings, seminars and conferences etc. in ADR; (iii) providing facilities for arbitration, mediation and conciliation proceedings; (iv) maintaining a panel of accredited arbitrators, conciliators and mediators; (v) ensuring credibility of the Centre through collaborations with other organisations; (vi) setting up facilities in India and abroad to promote the activities of the Centre; (vii) lay down parameters for conducting ADR mechanisms of the Centre and so on.

iv. **Functions of the Centre** – The Centre shall facilitate conducting of arbitral proceedings; provide cost effective and timely services for conduct of arbitral proceedings; promote studies and reforms in ADR and settlement of disputes; undertake teachings and provide certification therefor on procedures of ADR; impart training to those handling arbitration, conciliation and mediation; cooperate with other organisations and societies for promoting ADR and promote ADR as per Central Government's instructions.

v. **Conduct of Functions** – The Centre shall constitute committees for discharging its functions and meet at least four times a year which meetings shall be presided by the Chairperson. The decisions at the meetings shall be taken by majority. A Chief Executive Officer shall be appointed at the Centre who shall be responsible for day to day administration of the Centre. The Centre shall also have a Secretariat consisting of a Registrar, Counsel and other officers and employees.

vi. **Funds** - The Centre shall maintain a fund that shall be applied towards salaries and allowances of Members and expenses of the Centre.

vii. **Chamber of Arbitration** – A key feature of the Act is the establishment of a Chamber of Arbitration through which the Centre shall empanel arbitrators at the national and international level and maintain a permanent panel of arbitrators.

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viii. **Arbitration Academy** – The Centre may also establish an Arbitration Academy to train the arbitrators to bring them at par with international arbitration institutions; to conduct research in the area of ADR and to give suggestions for achieving the objects of the Centre under the Bill.

The provisions of the Act are largely based on the recommendations of the Report of the High-Level Committee set up to review the Institutionalisation of Arbitration Mechanism in India under the chairmanship of Justice B.N. Srikrishna (retired), released in June 2017.

While there is no denying the urgent need for a premier flagship arbitration institution in India, it is also true that the International Centre for Alternative Dispute Resolution at New Delhi (ICADR) was set up with similar noble intentions and objectives which are also the driving force behind the current New Delhi International Arbitration Centre Act, 2019. The onus lies on the Central Government to ensure that the objectives of the Act are brought to its intended fruition by establishing a Centre that makes India a desirable destination for international and domestic institutional arbitration.

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Notifications and Circulars

External Commercial Borrowing (ECB) Policy – RBI eases end-use restrictions: In order to further liberalize the External Commercial Borrowings (ECB) framework, the Reserve Bank of India has relaxed the end-use restrictions. Eligible borrowers would be able to raise ECBs with a minimum average maturity period of 10 years for working capital purposes and general corporate purposes. Borrowing by NBFCs, with said maturity period, for on lending has also been permitted. As per RBI Circular dated 30-7-2019, ECBs with a minimum average maturity period of 7 years can be availed for repayment of Rupee loans availed domestically for capital expenditure.

NBFCs can also raise ECBs with such maturity for on-lending for the same purpose. It may however be noted that for repayment of Rupee loans availed domestically for purposes other than capital expenditure and for on-lending by NBFCs for the same, the minimum average maturity period of the ECB is required to be 10 years. The Circular also states that the prescribed minimum average maturity provision for the said end-uses will have to be strictly complied with under all circumstances.

Standardizing reporting of violations related to code of conduct under SEBI (Prohibition of Insider Trading) Regulations, 2015: The Securities and Exchange Board of India, vide Circular dated 19th July, 2019 has standardised the reporting of violations under the Code of Conduct ('Code') formulated by listed companies, intermediaries and fiduciaries under SEBI (Prohibition of Insider Trading) Regulations, 2015.

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In terms of the Regulations, the Board of Directors of every listed company, intermediary and fiduciary, is required to formulate a Code for designated persons, and their immediate relatives, monitor the compliance and report to SEBI any violations of said Code.

SEBI has observed that in absence of standardized reporting formats, many references on violations of the Code are often incomplete or inadequate in terms of details of violations, designation, etc., which are crucial for taking any necessary action.

Therefore, SEBI, through the said Circular, has prescribed the format for reporting violations of the Code. The format *inter alia* prescribes inclusion of (a) relevant details of the entity, as to whether the entity is a listed company, intermediary or a fiduciary; (b) the relevant details of 'designated person', as to the designation, functional role, etc.; (c) the name of the scrip; (d) number of scrips traded; (e) value of the transaction; (f) details of violations under the Regulations; and (g) details of previous instances of violations.

Modification of format for compliance report on corporate governance to be submitted to stock exchange(s) by listed entities/companies: The Securities and Exchange Board of India, vide Circular dated 16th July, 2019, has modified the format for compliance report on corporate governance to be submitted to stock exchange(s) by listed companies. In accordance with Regulation 27(2) of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ('Listing Regulations'), every listed entity must submit a quarterly compliance report on corporate governance, in the format specified by SEBI from time to time, to recognised Stock Exchange(s) within fifteen days from the close of each quarter. SEBI had prescribed a format vide circular dated 24th September 2015.

Based on certain recommendations of the Committee on Corporate Governance, under the Chairmanship of Shri Uday Kotak ('Kotak Committee'), SEBI had made amendments to the Listing Regulations vide a notification dated 09th May, 2018. In the background of the amendments, the format of the said quarterly compliance report is now modified, to reflect the amendments, which shall be applicable to/ come into effect from the quarter ending on 30th September, 2019.

Consultative paper on policy proposals with respect to resignation of statutory auditors from listed entities: With a significant increase in the instances of abrupt resignations of Statutory Auditors from listed entities, generally citing 'pre-occupation' as the reason for such resignations, the Securities and Exchange Board of India ('SEBI'), vide Circular dated 18th July, 2019, has issued a consultative paper ("Paper") on strengthening the disclosure norms in the event of resignation of a Statutory Auditor. The Paper *inter alia* recommends that, upon such resignation, the views of the Audit Committee and the Board of Directors (of the listed entity/ unlisted material subsidiary, as applicable) be mandatorily submitted to the stock exchange(s), along with the disclosure of the resignation letter of the auditor, in the prescribed format. The prescribed format may include:

i. Detailed reasons for resignation;
ii. Declaration by the auditor that there are no other material reasons other than those provided within the letter (similar to the requirement in case of resignation of independent directors); and
iii. In case of any concerns, efforts made by the auditor prior to resignation to address the same (including approaching the Audit Committee);

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Further, it is recommended within the Paper to amend the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("*LODR Regulations*") to strengthen the role of the Audit Committee. The Paper is open for public comments till 08th August 2019.

Fees for delayed filing of e- Form DIR-3 KYC or DIR-3 KYC-WEB - Companies (Registration Offices and Fees) Fourth Amendment Rules, 2019: The Ministry of Corporate Affairs, vide its Notification dated 25th July, 2019, has introduced the Companies (Registration Offices and Fees) Fourth Amendment Rules, 2019, to insert details of the fees payable for the delayed filing of e-Form DIR-3 KYC or DIR-3 KYC-WEB, as permissible under Rule 12A of the Companies (Appointment and Qualification of Directors) Rules, 2014. Accordingly, a fee of INR 5000 (Rupees Five Thousand Only) has to be paid in each case, if the individual fails to file e-form DIR-3 KYC or DIR-3 KYC-WEB through web service for the immediate previous financial year, or there is a delay in filing of such e-forms, as the case may be.

Web-based filing of e-form DIR-3 KYC-WEB - Companies (Appointment and Qualification of Directors) Third Amendment Rules, 2019: The Ministry of Corporate Affairs, vide its Notification dated 25th July, 2019, has introduced Companies (Appointment and Qualification of Directors) Third Amendment Rules, 2019 to introduce a web-based filing of e-form DIR-3 KYC-WEB, which must be filed with the Central Government on or before 30th June of every immediate next financial year. In case an individual desires to also update his/her personal mobile number or e-mail address, as the case may be, he/she shall now update the same by submitting e-form DIR-3 KYC only. The fee for filing e-form DIR-3 KYC, or web-form DIR-3 KYC-WEB through the web service, shall be payable as provided in Companies (Registration Offices and Fees) Rules, 2014.

Nidhi (Amendment) Rules, 2019 notified: The Ministry of Corporate Affairs, vide notification dated 1st July, 2019 has introduced the Nidhi (Amendment) Rules, 2019 to revise and amend the Nidhi Rules, 2014. The amended Rules shall be effective from 15th August, 2019.

The Amended Rules define 'Nidhi' as a public company which has been incorporated as Nidhi, with the object of cultivating the habit of thrift and savings amongst its members, receiving deposits from, and lending to its members only, for their mutual benefit, and which complies with the rules made by the Central Government for regulation of such class of companies.

Every public company incorporated after the amended Rules must file a Form NDH-4 within sixty days from the date of expiry of one year from its incorporation, or up to such extended period granted by the Regional Director ('RD'), for declaring it as Nidhi. The RD, on receipt of an application in Form NDH-4, along with prescribed fee, on being satisfied that the company meets the requirements under the Rules pertaining to a 'Nidhi' company, shall notify the said company as a Nidhi company in the official Gazette. In case a company does not comply with the requirements of the Rules, it shall not be allowed to file Form No. SH-7 (Notice to Registrar of any alteration of share capital) and Form PAS-3 (Return of Allotment).

Further, every existing Nidhi as defined under clause (a) of rule 2 of the Rules shall file the Form NDH-4 for updating its status, along with fees as per Companies (Registration Offices and Fees) Rules, 2014, provided that no fees shall be charged only if the said Form is filed within six months of the commencement of the amended Rules.

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Additionally, pursuant to the amended Rules, in case of non-payment of the deposit or part thereof as per the terms and conditions of such deposit, the depositor may now approach the relevant bench of the National Company Law Tribunal having jurisdiction over the Nidhi company, instead of the Registrar of Companies.

Ratio Decidendi

Operation of Arbitration Sections 31(8) and 31A if fees of Tribunal is decided by agreement between parties to arbitration

Brief Facts:

The parties to the matter had entered into a contract in 2006, that contained a dispute resolution clause referring the parties to arbitration, to be presided over by a tribunal of three arbitrators. The said arbitration clause *inter alia* also fixed the fee of arbitrators, in accordance with the policy decision of National Highways Authority of India ('Respondent') dated 31st May, 2004, as substituted in 2017, vide a Circular ('Circular').

The matter of fee of the arbitrators came up before the Arbitral Tribunal ('Tribunal'). Gammon Engineers and Contractors Private Limited ('Appellant') had informed the Tribunal that there was no prior agreement between the parties regarding the fees of the Tribunal. The Respondent herein had requested that the fees be fixed in terms of the instructions issued by NHAI, vide their Circular.

Relying on the judgment of the High Court of Delhi in *National Highways Authority of India* v. *Gayatri Jhansi Roadways Limited*, (2017) SCC OnLine Del 10285, the Tribunal held that it was competent to fix the fees regardless of the agreement of the parties to the arbitration. The judgment of the Delhi High Court was based on the understanding that, after Arbitration and Conciliation (Amendment) Act, 2015 ("Amendment Act"), the phrase 'unless otherwise agreed by the parties' in the beginning of Section 31(8) of the Arbitration and Conciliation Act, 1996 ("Arbitration Act") was omitted.

Aggrieved by the decision of the Tribunal, the Respondent moved an application under Section 14 of the Arbitration Act before the High Court of Delhi, to terminate the mandate of the Tribunal. The Delhi High Court, disagreeing with its judgment in the *Gayathri Jhansi* case, based on the reasoning that the decision within the judgment was *per incuriam*, allowed the application under Section 14 of the Arbitration Act. This decision was challenged before Supreme Court

Issue for consideration:

Whether Sections 31(8) and 31A of the Arbitration Act will operate if the fees of the Tribunal is decided by agreement between the parties to the arbitration.

Held:

Section 31(8) of the Arbitration Act states that costs of the arbitration shall be fixed by the arbitral tribunal, in accordance with Section 31A of the said Act. The Supreme Court held that the arbitrators are entitled to charge their fees in accordance with the fee schedule fixed by the parties, and not in accordance with Fourth

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Schedule of the Amendment Act. However, the Supreme Court upheld the interpretation of the Delhi High Court, in the present case, that the change in language of Section 31(8) after the Amendment Act, read with Section 31A of the Arbitration Act, deals only with the costs generally and not with/ including the Tribunal's fees. [*Gammon Engineers and Contractors Private Limited* v. *National Highways Authority of India* - 2019 SCC ONLINE SC 906]

'Employee' under EPF Act – Test of control and supervision over workers

Brief Facts:

Respondent had engaged certain women workers to make garments from their home. The sewing machines used by the workers were owned by them, and not provided by the Respondent company. The Officer-in-Charge, Sub Regional Provident Fund Office ('Appellant') held that the workers so engaged for stitching garments were covered by the definition of 'employee' under Section 2(f) of the Employees' Provident Fund and Miscellaneous Provisions Act, 1952.

On appeal to the Bombay High Court, it was held by the Court that the Respondent had no direct or indirect control over the workers. It was further observed that the conversion of cloth into garment could have been done by any other person on behalf of the workers. Hence, it was held that the workers would not fall within the definition of 'employee' under the EPF Act and the Respondent is consequently not liable to make any contributions on behalf of said Workers to the Employees Provident Fund.

Aggrieved by the decision of Bombay High Court, the Appellant preferred an appeal before the Supreme Court.

Issue for consideration:

Whether the women workers i.e., the workers employed by the Respondent company are covered by the definition of 'employee' under Section 2(f) of the EPF Act.

Arguments:

The Appellant herein submitted that the workers employed by the Respondent shall fall within the definition of "Employee" under Section 2(f) of the EPF Act. The Appellant relied on the decision in *P. M. Patel & Sons* v. *Union of India*, (1986) 1 SCC 32, wherein it was held the definition of 'employee' under the EPF Act is wide and inclusive of persons employed in connection with the work of a factory, specifically home workers.

On the other hand, the Respondent contended that there existed no employee-employer relationship between the Respondent company and the workers, based on the following factual points:

i. The Respondent exercised no supervisory control over the workers;
ii. The sewing machines used by the workers were not provided by the Respondent, but were rather owned by the workers themselves;
iii. The workers worked from their homes and not at the production centres of the Respondent, neither were they bound to report to the same; and
iv. The work to be performed by them could have been done by their relatives, or any other person on their behalf;

Held:

The Apex Court observed that the definition of 'Employee' under Section 2(f) of the EPF Act is an inclusive definition and is widely worded to include any person engaged either directly or

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indirectly in connection with the work of any establishment. The mere fact the workers stitched the garments at home would make no difference to their employment status. It is an admitted position that workers were paid wages directly by the Respondent company, on a per piece basis, for every garment stitched by them and supplied to the Respondent.

The Court further relied upon its decision in *Silver Jubilee Tailoring House and Others* v. *Chief Inspector of Shops and Establishments*, (1974) 3 SCC 498, where it was held that if the employer had the right to reject the end product for not conforming to the instruction of said employer and the right to direct the worker to rework it, the element of control and supervision could be said to be present.

The Court reiterated the fact the EPF Act is a beneficial social legislation for the benefit of the workers and has to be construed accordingly.

In this present case, the Respondent had the absolute right to reject the garments in case of any defects. Thus, it was held that the control and supervision test was met. Accordingly, the workers were construed to be employees of the Respondent, not dependent on the place of stitching garments or the payment of wages by the Respondent on a per piece basis. [*Officer-in-Charge, Sub Regional Provident Fund Office and Another* v. *Godavari Garments Limited* - 2019 SCC OnLine SC 903]

IBC - Counterclaim against corporate debtor when need not be stayed

In a case involving a claim by plaintiff (corporate debtor) and counterclaim by the defendant for the same transaction, Delhi High Court has held that both claims ought to be adjudicated comprehensively by the same forum. Observing that adjudication of the plaint and counter claim were interlinked with each other, the Court held that the question as to whether the defendant is in fact entitled to any amounts, if determined by the NCLT, prior to the adjudication of the plaintiff's claim for recovery, would result in the possibility of conflicting views in respect of the same transaction.

Directing proceeding of trial of suit and counter claim before the High Court, the High Court observed that counterclaim not to be stayed under Section 14 of the Insolvency and Bankruptcy Code, even though strictly speaking a counterclaim against the corporate debtor was covered by the moratorium. The Court observed that NCLT/RP cannot be burdened with the task of entertaining the counterclaim which was uncertain, undetermined and unknown.

The plaintiff had filed a suit for recovery and had since gone into insolvency and a Resolution Professional had been appointed. The question before the Court was as to whether, the adjudication of the counter claim would be liable to be stayed in view of Section 14 of the Code. [*SSMP Industries Ltd.* v. *Perkan Food Processors Pvt. Ltd.* – Decision dated 18-7-2019 in CS (COMM) 470/2016 & CC(COMM) 73/2017, Delhi High Court]

Employee cannot claim wages for the period he was voluntarily absent

Brief facts:

In the present case, the Respondent was relieved from the Allahabad branch of the Appellant to join the Jaunpur branch of the Appellant. However, the Respondent did not join the Jaunpur branch on the assigned date and was unauthorizedly absent from work for four months. Disciplinary enquiry was conducted against the Respondent and an order for reduction of basic pay by two steps was passed in May 2009. However, the Respondent continued to be absent from work until 2012. Consequently, the Appellant passed an order in June 2012, terminating the services of the Respondent. The Respondent preferred a

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series of writ petitions before the High Court of Allahabad against the above-mentioned orders. The High Court of Allahabad quashed the above-mentioned orders citing procedural lapses in the conduct of disciplinary enquiry, without specially directing the Appellant to provide back wages to the Respondent from 2009-2012. Upon refusal of the Appellant to pay back wages from 2009-2012, the Respondent filed another writ petition before the High Court of Allahabad. The High Court of Allahabad directed the Appellant to pay salary for the period 2009-2012, along with 18% interest. The Appellant preferred the present appeal before the Supreme Court against this order of the Allahabad High Court.

Issues for consideration:

"Whether the respondent is entitled for back wages?" The counsel for the appellant submitted that the respondent is not entitled for the salary on the principle of 'No work No pay' as there was no termination of services by the appellant and the respondent was absent from his work on his own.

The counsel for the respondent submitted that he was not allowed to take charge of the work when he went back to join the work.

Observations:

The court observed that this is not the case where the respondent was dismissed from the service and consequent to dismissal, he could not work and when dismissal was set aside, he will be automatically entitled for back wages. In the present case, order of termination of his services was passed after his retirement and it did not prohibit the respondent from working.

The court mentioned *Airports Authority of India and Others v. Shambhu Nath Das alias S.N. Das*[4] in which it was held that there was no justification whatsoever to grant any back wages to the respondent on the general principle that nobody could be directed to claim wages for the period that he remained absent without leave or without justification.

Ratio:

The court held that the employee cannot claim wages for the period he was voluntarily absent and not by the order of the employer and hence in such case the principle of "No work No pay" would apply. [*Chief Regional Manager, United India Insurance Company Ltd*. v. *Siraj Uddin Khan* – Judgement dated 11-7-2019 in Civil Appeal No. 5390 of 2019, Supreme Court]

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News Nuggets

Arbitration of prior agreement cannot be invoked in dispute post compromise

Supreme Court has held that when the parties have settled their differences and compromised the matter, in a dispute subsequently arising between the parties, arbitration clause in the prior agreement cannot be invoked. The Apex Court in the case of *Zenith Drugs v. Nicholas Piramal India Ltd.* observed that the parties can be referred to arbitration in an application under Section 8 of Arbitration and Conciliation Act

[4] (2008) 11 SCC 498.

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only if the subject matter of the action relates to dispute which is subject matter of the arbitration agreement. It noted that that there was no arbitration clause relating to the dispute between parties.

Non-Banking Financial Institution is out of purview of IBC

NCLAT has held that a non-banking financial institution is out of the purview of Insolvency and Bankruptcy Code and thus application under Section 7 of IBC against a NBFC is not maintainable. Definitions of 'financial service' and 'financial service provider' under IBC, were relied upon. The Tribunal in the case of *HDFC Ltd v. RHC Holding* observed that respondent was a non-banking financial institution as evident from RBI certificate. It also held that definition of financial services under Section 3(16) is not limited to only 9 activities and that it is not necessary that financial service providers must accept deposits.

Jurisdiction of specific High Court when venue of arbitration specified in contract

Observing that parties agreed on Bhubaneshwar as venue of arbitration, Supreme Court has held that Madras High Court erred in assuming jurisdiction under Section 11(6) of Arbitration and Conciliation Act. It noted that if contract specifies a particular court, parties intend to exclude other courts. Relying on decision of the Court in *Swastik Gases (P) Ltd.,* Court in the case of *Brahamani River Pellets v. Kamachi Indus.* reiterated that absence of words like *only*, *exclusive, alone* in the agreement was not material.

No scheme of compromise under Section 391/394 of Companies Act 1956 for FD holders

NCLAT has held that to protect interest of FD holders –creditors for protection of which special provisions (Section 58A of Companies Act, 1956) are made, Scheme of Compromise by issuance of shares, is outside general purview of Section 391/394. Tribunal in the case of *Morepan Labs v. RD, MoC* observed that only a small portion of FD holders participated in the meeting and hence the compromise will run contrary to the protection provided under Section 58A. It also held that there was no question of deciding petition under the Companies Act, 2013 and SEBI has nothing to do with a scheme under Section 391/394.

High Court when cannot rule on arbitration award

Three-Judge Bench of the Supreme Court has set aside the High Court judgement which had set aside the partial arbitral award by entertaining a writ petition against an order of the District Judge passed under Section 20 of the Arbitration Act. The Court observed that as application made to district judge against a partial award was not tenable under Section 16(6), setting aside of award by the High Court was not correct. The Apex Court in the case of *Sterling Industries v. Jayprakash Associates* relied on Court's judgement in *SBP & Co. v. Patel Engineering*.

Despite overlap of issues, arbitration under 2 contracts to be independent

Delhi High Court has held that overlapping disputes between the parties, as the agreements were interconnected, cannot be

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the sole ground for the Court to direct the parties to go for a composite arbitration. The Court in the case of *Libra Automotives v. BMW India* refused to appoint common arbitrator. It observed that arbitration clauses contained in different agreements/deeds provided for different mechanism for constitution of arbitral tribunal. It also noted that in dealership agreement, respondent-2 was not party and in financing agreement, respondent-1 was not party.

Arbitration – No differential treatment to be given to government

Supreme Court has held that Government cannot be given exceptional treatment for its stay application in the proceedings under Section 34 of the Arbitration and Conciliation Act. Court held that Arbitration Act is self-contained and reference of CPC in Section 36 cannot take away the power conferred in the main statute. Court in the case of *Pam Developments v. State of WB* held that provisions of Order XXVII Rule 8A of CPC are archaic and even if applied, same would only exempt Govt. from furnishing security, but under Order XLI Rule 5 of CPC, Court can direct Govt. to furnish security of decretal amount.

Contractual provisions would prevail over Section 56 of Contract Act

Delhi High Court has held that Section 56 of the Indian Contract Act would have little application where parties expressly contemplate recourse to be adopted in the event which renders it impossible to perform the contract. The Court in the case of *NTPC Ltd v. Voith Hydro JV* observed that the Arbitral Tribunal rightly construed NTPC to have terminated the contract, which it undoubtedly could have in case of force majeure event rendering it impossible to perform the contract. The Court upheld the view that decision of National Ganga River Basin Auth. to scrap the project was force majeure.

Purchase of minority share – Section 236 of Companies Act when cannot be invoked

Setting aside the NCLT Order, NCLAT has held that notices issued by respondent under Section 236 of the Companies Act, cancelling shares of minority shareholder, are illegal and amounted to oppression. The Tribunal in the case of *S. Gapakumar Nair v. OBO Bettermann India* observed that Section 236(1) requires occurring of an event by amalgamation, share exchange, conversion of securities, which had not occurred in present case. It also held that valuation by a registered valuer is also required and that words 'for any other reasons' should be circumscribed by the preceding words.

Promoter of MSME corporate debtor not to compete with other Resolution Applicant

NCLAT has held that in exceptional circumstances, if corporate debtor is MSME, it is not necessary for its promoters to compete with other resolution applicants to regain control of corporate debtor. Tribunal held that for MSME promoters, it is not required to follow all procedures for accepting proposal under Section 12A of IBC. The Tribunal in the case of *Sarvana Global Holdings v. Bafna Pharmaceuticals* observed that legislature intended that the promoters of MSME should be allowed to pay back to the satisfaction of CoC and regain control of the corporate debtor.

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Consumer Protection Bill 2019 passed by Parliament

Consumer Protection Bill 2019 which seeks to replace Consumer Protection Act, 1986 has been passed by the lower house (Lok Sabha) of Indian Parliament on 30-7-2019 and by the upper house (Rajya Sabha) on 6-8-2019. As per the Bill, Central Consumer Protection Authority to promote, protect and enforce the rights of consumers will be set up. The Authority will regulate matters related to violation of consumer rights, unfair trade practices, and misleading advertisements.The Authority can also impose penalty up to Rs.10 lakh on a manufacturer or an endorser in respect of false or misleading advertisement.

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