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## Strengthening Corporate Governance: SEBI's Second Amendment to Listing Obligations and Disclosure Requirements

**Introduction**

On June 14, 2023 Securities and Exchange Board of India (**"SEBI"**) vide the SEBI's (Listing Obligations and Disclosure Requirements) (Second Amendment) Regulations, 2023 (**"Amendment"**) made amendments to SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (**"Regulation"**) with the primary objective of empowering shareholders and strengthen compliance. The Amendment introduced strengthened approvals and disclosure requirements for certain types of agreements that bind the listed entities, ensuring periodic approval for special rights granted to certain shareholders.

Some of the key amendments include introduction of new concept for non-permanency of directors on the board, requirement for appointment of a Key Managerial Personnel (**"KMP"**) within 3 months of vacancy, establishing a threshold of parameters for identifying materiality of events.

**Appointment of KMP**

SEBI has also inserted a new regulation 26A which mandates listed entities to fill vacancies in the office of the compliance officer and other key positions, such as Chief Financial Officer, Chief Executive Officer, Managing Director, and Whole-time Director, within 3 months from the date of the vacancy.

**Non-Permanency of Directors**

The shareholders of listed entities did not get an opportunity to evaluate the performance of directors appointed which allowed directors to serve on the board of listed entities as long as they desired. Recently, the issue of a few directors of listed entities enjoying permanency on the board which gave them an undue advantage, prejudicial to the interest of the public shareholders was highlighted in the media. This issue was highlighted when Diageo Plc sought to remove Vijay Mallya from the board following its acquisition of control over United Spirits Limited ("**USL"**). However, Mallya contested the decision, claiming his legal entitlement to remain on the board. Complicating matters further, USL'S Article of Association (**AOA**) granted Mallya the position of board chairman, a claim he maintained even as he evaded India's law enforcement authorities.


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Therefore, in order to deal with these issues Regulation 17 (1D) has been inserted to the Regulation, according to which, from April 01, 2024, directors of the listed companies will require shareholder approval in a general meeting at least once in every five years from the date of appointment/ reappointment. Additionally, in case there is a director on the board of a listed company (as on March 31, 2024) who has served on the board or five years or more without shareholders' approval, such person's continuation on the board shall be subject to shareholder approval in the first general meeting held thereafter. This ensures that shareholders of the listed company have the option to evaluate the performance of all the members of the current board.

However, these amendments do not extend to:

I. Whole time directors, managing directors, managers, independent directors or directors whose appointment or reappointment otherwise requires shareholders' approval under the Companies Act 2013 or the LODR.
II. Directors appointed pursuant to an order of a tribunal or court.
III. Nominee director of the Indian government on the board of a listed company, other than a public sector company.
IV. Nominee director of a financial sector regulator on the board of listed company.
V. Director nominated by a financial institution registered with or regulated by the Reserve Bank of India under a lending arrangement in its normal course of business.
VI. A director nominated by a SEBI registered debenture trustee Board under a subscription agreement for the debentures issued by the listed company.

**Materiality Criteria**

It was observed by SEBI that many entities were not disclosing events specified in Para B of Part A of Schedule III of the Regulations on the ground that they are not considered material by them as per their Materiality Policy framed in terms of the criteria prescribed in Regulation 30(4) of Regulations. Moreover, most entities follow a very generic materiality policy, simply reproducing therein merely the regulatory provisions under the Regulations, affording them a lot of discretion to decide whether or not to disclose an event specified under in Para B of Part A of Schedule III of the Regulations.

In order to deal with this issue, SEBI has introduced the threshold criteria for determining the materiality of an event/information. Accordingly, a listed entity is required to consider the following criteria for determining the materiality and the omission of an event or information, whose values or the expected impact in terms of value, exceeds the lower of the following thresholds:

I. 2% of turnover, as per the last audited consolidated financial statements
II. 2% 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.
III. 5% of the average of the absolute value of profit or loss after tax, as per the last three audited consolidated financial statements of the listed entity.

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Further, a new provision has been added which states that policy added for determination of materiality by the entities shall not dilute any requirement specified under the provisions of the Regulations. Also, such a policy for the determination of materiality shall assist the relevant employees of the listed entity in identifying any potential material event or information and reporting the same to the authorized KMP.

**Revised Disclosure Timeline of Material Events**

The Amendment significantly reduced the timeline for making disclosures of material events/information. Listed entities are required to make disclosures of material events/ information as soon as reasonably possible and no later than:

I. 30 minutes from the closure of the board meeting in which the decision pertaining to the event or information has been taken;

II. 12 hours from the occurrence of the event or information if it does not emanate from within the listed entity; and

III. Within 24 hours from the occurrence of the event or information if it does not originate from within the listed entity.

This amendment significantly reduces the timeline previously available to listed entities to make disclosures and paint events that were disclosable on a mandatory basis or subjective basis i.e., paragraph A and paragraph B Part A of Schedule III of the Regulations events, with the same broad brush. Listed entities will need to ensure that they have in place a mechanism for timely internal reporting, particularly for items that are triggered by an external action such as litigation, MAE events, etc. rather than voluntary actions such as execution of an agreement or board approval of a transaction.

**Disclosure Requirements for Agreements**

There have been instances where promoters have entered into binding agreements with third parties without disclosing facts to shareholders and listed entity which could potentially have an impact on the management or control of a listed entity, or such agreements could have placed certain restrictions on the listed entity. In order to avoid these circumstances, SEBI has inserted a new regulation 30A in the Regulations, which will require all shareholders, promoters, promoter group entities, directors, KMP and employees of a listed entity to inform about the agreement to the listed entity within 2 days of entering into such agreements.

**Additional Cyber Security Disclosures**

With the advancements in technology and the companies adopting such newer technologies, cyber security incidents or breaches and loss of data/documents have become a major concern. Such incidents may become a major concern and may impact the operations and performance of the listed entity. Disclosure of such incidents are important for investors to understand the associated risks and impact. In order to deal with this issue a new sub- regulation (ba) has been inserted in regulation 27 of the Regulations which mandates the disclosure of details regarding cyber security incidents or breaches or loss of data or documents in the quarterly compliance report.

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**Sale, Lease or Disposal of an Undertaking outside the Scheme of Arrangement**

Section 180(1) of the companies Act, 2013 imposes certain restrictions on the powers of the board which can only be exercised with consent of the shareholders by a special resolution. One of these restrictions include selling, leasing, disposing any such undertaking only after taking prior approval of shareholders through a special resolution.

Earlier such sale, disposal or lease happened either through a scheme of arrangement as prescribed in the Companies act and/ or the Regulations and the circulars issued by SEBI or outside the scheme of arrangement framework, generally referred to as business transfer agreement.

The Amendment introduced a new provision, Regulation 37A in the Regulations which imposes a stricter regime for the disposal of undertakings by listed entities, requiring approval from the majority of public shareholders who are not interested in the transaction. Additionally, listed entities must disclose the object, commercial rationale, and use of proceeds arising from the transaction. The approval regime does not apply in cases where the notice for seeking shareholders' approval has already been dispatched. The Amendment also exempts transfers of undertakings to wholly owned subsidiaries (**"WOS"**). However, if the WOS further transfers the undertaking or the listed company dilutes its shareholding in the WOS, the approval regime applies. The regulation also distinguishes approval requirements for material related party transactions from the disposal of undertakings. The Amendment clarifies that the provisions will apply when the WOS itself is a result of a transfer of an undertaking by the listed entity. Listed entities need to be cautious about compliance and seek necessary approvals in the specified scenarios.

**Conclusion**

The Amendment marks a significant step towards strengthening corporate governance in listed entities. This reflects SEBI's commitment to promoting investor confidence and creating a more effective regulatory framework in India's capital markets. These changes will enhance the overall functioning and integrity of listed entities, benefiting both stakeholders and the broader economy.

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# *Flight or Fight: Voluntary Corporate Insolvency Resolution Process by Go Airlines*

**Introduction**

The Indian aviation sector is riddled with financial and regulatory hassles. With only a handful of airlines operating profitably with many on the verge of collapse, the industry's viability is at stake. Notable examples of struggling airlines include Kingfisher and Jet Airways, both of which were declared insolvent and liquated. However, some airlines, like Jet Airways, still have the possibility of restructuring in order to operate as frills airline subject to the terms and conditions set forth by the Hon'ble National Company Law Tribunal (**"NCLT"**). The initiation of voluntary Corporate Insolvency Resolution Process (**"CIRP"**) by Go Airlines (India) Limited (**"Go Airlines"**) came as a bit of shock to the aviation sector and corporate sector in general in India. The Insolvency and Bankruptcy Code, 2016 (**"IBC"**) has proved to be a viable recourse for reaching a resolution plan that can potentially revive a business from the brink of extinction. In this article, we will delve into the process of voluntary insolvency process under Section 10 of the IBC with special emphasis on an order issued by the NCLT, Delhi dated May 10, 2023 (**"Order"**) in case of Go Airlines.

**CIRP and Go Airlines**

Section 10 of the IBC states that "*Where a corporate debtor has committed a default, a corporate applicant thereof may file an application for initiating corporate insolvency resolution process with the Adjudicating Authority*." From a clear reading of the above section, one can make out that the initial essentiality for filing an application under Section 10 of the IBC is when a corporate debtor has committed a default on repayment of a debt.

Go Airlines moved the application for voluntary CIRP under Section 10 of the IBC citing numerous reasons, primary being "*to preserve the assets of the Corporate Applicant and to keep the Company as a going concern in the larger public interest*". Go Airlines started defaulting on payments to vendors and aircraft lessors from 2022 onwards, leading to mounting dues of significant amounts. The defaults were attributed to financial distress caused by defective engines supplied by Pratt and Whitney (**"P&W"**), resulting in grounded airplanes. To address the issue, Go Airlines initiated arbitration proceedings against P&W, seeking the supply of serviceable engines. Despite winning the arbitration, P&W failed to comply with the orders, leading to enforcement actions in various jurisdictions. Go Airlines, on May 4, 2023 had committed default of Rs.11.03 Crores towards interest dues to the Financial Creditor pursuant to which it proceeded with an application for voluntary CIRP under IBC.

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**Opposition from Operation Creditors**

Any CIRP has an impact on all the stakeholder but the foremost and immediate impact is felt by the creditors and more so by the operational creditors. The CIRP application by the Go Airlines was no different. During the hearing for the admission of the application of CIRP by Go Airlines, the operational creditors of the airline opposed it vehemently and expressed their interest to file an application under Section 65 of the IBC, which states as under:

> "*65 (1) If, any person initiates the insolvency resolution process or liquidation proceedings fraudulently or with malicious intent for any purpose other than for the resolution of insolvency, or liquidation, as the case may be, the Adjudicating Authority may impose upon such person a penalty which shall not be less than one lakh rupees, but may extend to one crore rupees.*
>
> *(2) If, any person initiates voluntary liquidation proceedings with the intent to defraud any person, the Adjudicating Authority may impose upon such person a penalty which shall not be less than one lakh rupees but may extend to one crore rupees*."

Further, they contended that before adjudicating the above application, notice should be issued to the creditors giving them a fair chance to be heard. They contended that as per Section 424 of the Companies Act 2013, Hon'ble NCLT is to be guided by the principles of natural justice and therefore, is bound to afford an opportunity of being heard to the creditors.

**The Order**

The NCLT in the Order highlighted the following issues:

A. Whether there is any mandatory requirement of issuing notice to the creditors before admitting an Application filed under Section 10 of the IBC?
B. Whether the Financial Creditor is a necessary party in the current insolvency proceedings?
C. Whether the ingredients for a voluntary CIRP are fulfilled?
D. Whether an interim moratorium for the Corporate Applicant (Go Airlines) be granted?
E. Whether the petition has been filed for liquidation with a malicious intent?

In the Order, the Hon'ble NCLT noted that an application under Sections 7 and 9 of the IBC are in personam where notice to the respondent/corporate debtor is a matter of right. However, the same is not the case under Section 10 of IBC. The Hon'ble NCLT relied on the judgement of Hon'ble National Company Law Appellate Tribunal (**"NCLAT"**) dated December 01, 2017 passed in the matter of *Unigreen Global Private Limited vs. Punjab National Bank & Ors. in Company Appeal (AT) (Insolvency) No. 81 of 2017*, wherein the Hon'ble NCLAT discussed on what grounds, a creditor can object to an application under Section 10

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of the IBC. The relevant extract from the judgment which the Hon'ble NCLT relied on is reproduced below:

> *"21. In an application under Section 10, the 'financial creditor' or 'operational creditor', may dispute that there is no default or that debt is not due and is not payable in law or in fact. They may also oppose admission on the ground that the Corporate Applicant is not eligible to make application in view of ineligibility under Section 11 of the I & B Code. The Adjudicating Authority on hearing the parties and on perusal of record, if satisfied that there is a debt and default has occurred and the Corporate Applicant is not ineligible under Section 11, the Adjudicating Authority has no option but to admit the application, unless it is incomplete, in which case the Corporate Applicant is to be granted time to rectify the defects."*

The Hon'ble NCLT observed that the creditor has limited grounds to object to an application preferred under Section 10 of the IBC i.e., if the debt is not due and is not payable in law or in fact or corporate applicant is not eligible to make an application in view of its ineligibility under Section 11 of the IBC. The Hon'ble NCLT held that notices of the operational creditors in the instant case of Go Airlines do spell out that the default exist and is in thousands of crores.

The Hon'ble NCLT went on to examine Sections 7, 9, and 10 of the IBC and referred to Rules 4, 6, and 7 of the Application to Adjudicating Authority Rules, 2016 (**"Rules"**). The Hon'ble NCLT observed that rule 4 of the Rules prescribes that an application filed under Section 7 of the IBC by a financial creditor has to be served to the corporate debtor. Similarly, rule 6 of the Rules prescribes that an application filed by an operational creditor under Section 9 of the IBC has to be served to the corporate debtor. However, rule 7 of the Rules which deals with the filing of an application by a corporate applicant under Section 10 of the IBC, does not stipulate that the application is required to be served to the creditor(s).

Consequently, the Hon'ble NCLT held that there is no express provision in the law, which necessitates the issue of notice or service of a copy of the Section 10 application to the creditor(s).

With regards to Section 424 of the Companies Act, 2013 being the adjudicating authority is to be guided by the principals of natural justice, the Hon'ble NCLT relied on the judgment passed by the Hon'ble Supreme Court in the matter of *Kumar Nag Vs G.M (P.J) India Oil, Civil Appeal No. 4544 of 2005.* The Hon'ble NCLT held that "*there is no straight-jacket formula for applying the Principles of Natural Justice. The proceedings under Sections 7 & 9 of IBC 2016, where only 2 parties are involved, no 3rd party can interfere and notice of hearing is issued, cannot be compared with the proceedings under Section 10, where a Corporate Debtor is having multiple Creditors and each of the Creditors will plead for a hearing. This is so because the timelines, that are specified in the IBC 2016, have also to be adhered to.*"

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In so far as application under section 65 of the IBC by the creditors is concerned, the Hon'ble NCLT held that there was no malafide intention on part of Go Airlines to file for CIRP. The aircrafts of Go Airlines were grounded due to the defective engines supplied by P&W, against which it had an arbitral award in its favor. The Hon'ble NCLT further noted that *"Accordingly, we conclude that there is no bar in entertaining/considering/ adjudicating a Section 65 Application after the initiation of the CIR Process."*

The Hon'ble NCLT finally held that Go Airlines' application under Section 10 of the IBC was filed on bona fide grounds. Go Airlines had fulfilled all the necessary ingredients for admitting the matter before the Hon'ble tribunal to initiate voluntary CIRP. Furthermore, the Hon'ble NCLT granted interim mortarium under Section 14 of the IBC.

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Warm Regards,

**Dipali Sarvaiya Sheth**

Founder

D-226, Neelkanth Business Park,

Vidyavihar (West), Mumbai– 400086

Email: contact@eternitylegal.com Tel no.: +91 22 2515-9001

Website: www.eternitylegal.com

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