Centre for Studies in Banking & Finance, NLU Jodhpur

SCHOLASTICUS

Volume X, Issue II

ISSN: 0975-1157

SEPTEMBER 2023



Articles

- Insolvency Resolution of Real Estate Companies: The Way Forward
  Uday Khare & Saptarishi Chatterjee
- Derailing the IPO Market: SEBI's Proposed Confidential Filing Mechanism
  Parameswaran Chidamparam
- License Fee as Operational Debt: Analysis of NCLAT's Order in Jaipur Expocentre v. Metro Jet Airways
  Alpesh Sharma
- Examining the Enforceability of Settlement Agreements under the Insolvency and Bankruptcy Code, 2016
  Avital Jain

Editorial

- Fintech Unicorns in India: Analysing and Predicting the Future
  Bhavika Verma & Krishna Pal Singh Bhati

-National Law University, Jodhpur Publication -

Published by

The Registrar, National Law University, Jodhpur

ISSN: 0975-1157 | Centre for Studies in Banking and Finance,

National Law University, Jodhpur

While the advice and information in this journal are believed to be true and accurate on the date of its publication, neither the editors, publisher, owners nor the authors can accept any legal responsibility for any errors or omissions that may be made or for the results obtained from the use of such material.

Volume X, Issue II SEPTEMBER 2023

Patron

Prof. Dr. Poonam Saxena

Vice-Chancellor, National Law University, Jodhpur

Chief Editor

Dr. Anand Kumar Singh

Assistant Professor, National Law University, Jodhpur

Editorial Board

Senior Editorial Board

Vaishnavi Bansal

Editor-in-Chief

Bhavya Kansara &
Palak Dwivedi
Managing Editors

Senior Associate Editors

Aniketa Jain

Jatin Soni

Associate Editors

Krishna Pal Singh

Nidhi Antil

Vanshika Agrawal

Vidhi Kanodia

Copy Editors

Anshuman Srivastava

Bhavika Verma

Technical Editor

Divyam Juneja

TABLE OF CONTENTS

ARTICLES

Insolvency Resolution of Real Estate Companies: The Way Forward..... 5

Uday Khare & Saptarishi Chaterjee

Derailing the IPO Market: SEBI's Proposed Confidential Filing Mechanism 20

Parameswaran Chidamparam

License Fee as Operational Debt: Analysis of NCLAT's Order in Jaipur Expocentre v. Metro Jet Airways 36

Alpesh Sharma

Examining the Enforceability of Settlement Agreements under the Insolvency and Bankruptcy Code, 2016.....45

Aviral Jain

Fintech Unicorns in India: Analysing and Predicting the Future.....61

Bhavika Verma & Krishnapal Singh Bhati

SCHOLASTICUS

Uday Khare & Saptarishi Chatterjee, Insolvency Resolution of Real Estate Companies: The Way Forward, 10(2) SCHOLASTICUS 5 (2023).

INSOLVENCY RESOLUTION OF REAL ESTATE COMPANIES: THE WAY FORWARD

Uday Khare[⊥] *& Saptarishi Chatterjee*[Ø]

ABSTRACT

The demolition of Supertech's twin towers in NOIDA serves as an eye-opener and gives a food for thought concerning the position of homebuyers, who are major stakeholders, during the insolvency of real estate companies, as their hard earned money is invested in the projects of these companies. The aim of the paper is to dwell upon the various problems that may arise in resolving real estate insolvencies through IBC and to claw a way out of this in order to serve justice in true sense. In examining as to how the homebuyers are left remediless during the entire process, the author takes assistance of various precedents to uncover theoretical issues that can arise in including homebuyers in the definition of "financial creditors" and for that matter, "operational creditors". Later, the paper critically examines the practical feasibility and theoretical implications of 2018 amendment which included homebuyers in the category of financial creditors. In doing so, it evaluates the role of developmental authorities as approving authority while making any changes in resolution plan which at times, can become an impediment for the payment of dues of homebuyers. To conclude, the paper looks into various judgments where the courts ask these authorities to act in reasonable manner and in the interest of public. In suggesting a way out of this conundrum, the author put forth the formulation of the policy on the basis of which the developmental authorities should approve the resolution plan.

[⊥]Uday Khare is a Partner at Cyril Amarchand and Mangaldas, specialised in the field of Banking and Finance and may be contacted at uday[dot]khare[at]cyrilshroff[dot]com.

[Ø]Saptarishi Chatterjee is a Senior Associate at Cyril Amarchand and Mangaldas, and may be contacted atSaptarshi[dot]Chatterjee[at]cyrilshroff[dot]com.

I. INTRODUCTION

The demolition of Supertech‟s "Twin Towers" was one of the most watched live events in recent times. The physical spectacle of the demolition, while compelling, also leads to the not unreasonable question of what is the fairest re-allocation of the resources which were expended in constructing the towers in the first place.

The Supreme Court judgment of August 2021[1], which had ordered the demolition in the first place, had a straightforward solution – the money collected from the allottees of the Twin Towers by Supertech was to be returned to them. However, in March 2022, the National Company Law Tribunal ("**NCLT"**) had admitted Supertech Limited into the corporate insolvency resolution process under the Insolvency and Bankruptcy Code, 2016 ("**IBC"**). Supertech had been unable to repay its lenders, and its insolvency was clear. Consequently, any funds used to repay the allottees of the Twin Towers are now funds which cannot be used to progress construction in any other stalled projects.

Difficult questions such as these are par for the course in most real estate insolvencies. Supertech joins a growing list of developers in the New Okhla Industrial Development Authority ("**NOIDA"**), the Greater New Okhla Industrial Development Authority ("**GNOIDA"**), and the Yamuna Expressway Industrial Development Authority ("**YEIDA"**) regions to become insolvent – JaypeeInfratech, the Amrapalli Group, the 3C group, and Unitech are amongst others to become insolvent in the last few years.

As with sector and location specific insolvencies like this, there are much larger factors at play. It was recently reported in the Indian Express[2] that the expected

[1] *Supertech Ltd. v. Emerald Court Owner Resident Welfare Association*, 2018 SCC OnLine SC 3707

[2] Fahad Zuberi, *Supertech and the NOIDA problem*, September 2, 2022, available at https://indianexpress.com/article/opinion/columns/noida-supertech-demolition-8125397/.

growth in the suburban population in these areas led planning authorities to earmark large parts of the region as residential use. This combined with the construction of the Delhi-Noida Toll Road, and the Yamuna Expressway, created a mirage of rising real-estate demand in the region. Consequently, builders invested in more and more housing units, with projects delayed as funds were siphoned off to build more projects. But with the actual population reaching only half of what was envisaged, there were not enough buyers, and not enough funds to complete the planned projects. The region today is littered with stalled semi constructed buildings being constructed by developers like Supertech, Amrapali, JaypeeInfratech.

II. THE RESOLUTION PROBLEM

Real Estate insolvencies are more complex than most due to the various stakeholders involved. Allottees pay in advance, through a series of scheduled payments to be made against scheduled completion milestones. They are left without their completed apartments in cases when the project falters owing to a lack of funding, with the company left with no money to issue a refund. Banks and financial institutions that finance the projects are similarly faced with a borrower with no ability to repay. Arguably, the most important stakeholders, however, are the development authorities, NOIDA, GNOIDA and YEIDA established by the State Government under the Uttar Pradesh Area Development Act, 1976 ("**UPAD Act**"). Under the UPAD Act, these development authorities have a dual role as the owners and lessors of the land, who acquire and hold property for development in their area., as well as planning authorities who lay down, and regulate adherence to, land use norms and building regulations for all construction in their jurisdictions.

Typically, at the time when a developer company goes insolvent, the allottees are owed completion of their apartments (or refunds, should they opt to); banks and financial institutions are owed principal and interest on their loans; and the developmental authorities are owed outstanding premium charges, lease rents, and various penalties in accordance with their lease deeds.

Effective solutions to such real estate insolvencies have not yet been found, despite a variety of solutions having been explored. This paper specifically examines some of the difficulties faced in attempts to resolve real estate insolvencies through the IBC, and argues that it could be an effective resolution tool if the development authorities can adopt necessary policies towards such cases.

III. HOMEBUYERS AND THE IBC'S EVOLUTION

The IBC has undergone significant changes in its framework to accommodate the difficulties faced in real estate insolvencies. Initially, when the IBC was enacted, homebuyers attempted to invoke the provisions of the IBC against real estate companies, and the judiciary was called upon to determine their place within the IBC‟s creditor classification. In *Nikhil Mehta v. AMR Infrastructure*[3],the NCLT held that homebuyers did not fall within the definition of "financial creditors" as the debt in question was not disbursed against the consideration of time value of money[4], while in *Col Vinod Awasthy v. AMR Infrastructure*[5] (***"Col Vinod Awasthi"***) and *Pawan Dubey v. JBK Developers Private Limited*[6] *("**Pawan Dubey**")*, the NCLT concluded that operational `creditors were limited to

[3]2017 SCC Online NCLT 219.
[4] While the judgment was overturned on appeal, this was on the basis of the particular facts of that transaction, whereby one party had advanced monies against the consideration of an assured return, thereby giving it the character of financial debt. These facts, however, did not apply to most homebuyer contracts with builders.
[5] 2017 SCC Online NCLT 16278.
[6] 2017 SCC OnLine NCLT 520.

creditors providing goods, services, employment dues, and crown debts, and that homebuyers did not fall within any of these categories.

As a consequence, homebuyers were held to be neither financial nor operational creditors. Since the IBC then, contemplated no other class of creditor nor provided any protection to any other stakeholder, homebuyers were effectively not recognized under the IBC at all. Moreover, once a company is admitted into the corporate insolvency resolution process ("**CIRP**"), a legal moratorium or stay applies to all suits and proceedings against the corporate debtor, thus denying any potential litigant or claimant recourse outside of the CIRP.

In addition to civil suits, homebuyers have recourse to the Consumer Protection Act, 1986, and its successor legislation, the Consumer Protection Act, 2019 ("**CPA**"), under which they can seek remedies including compensation. In March 2016, the Real Estate (Regulation and Development) Act, 2016 ("**RERA**") was enacted with a view to better regulate real estate projects. RERA provides for regulation of real estate project developers, creation of escrows for monies collected from homebuyers, and establishment of a regulatory authority with power to impose penalties on developers and award refunds to homebuyers. As a consequence of these NCLT judgments, these remedies were not available to homebuyers and they were left with no recourse, within or outside the CIRP.

This was not just unfortunate for the homebuyers, but also resulted in an anomaly in the IBC‟s framework. By virtue of these judgments, purchasers of consumer goods or services were considered to be operational creditors under the IBC, but homebuyers who had advanced crores of rupees for their apartments were not.

This anomaly could possibly have been avoided. The IBC does not define the expressions "goods" or "services", and while interpreting these terms in the *Col Vinod Awasthi* and *Pawan Dubey* cases, the NCLT need have looked no further than the CPA itself, which also used the expressions "goods" and "services", and included "real estate services" within the ambit of services. This could have been a parallel to consider homebuyers as operational creditors, a result which would have placed them on par with prepaying customers of other goods and services and fit neatly into the IBC"s framework.

Ultimately, the IBC was amended on August 17, 2018 to confer upon homebuyers the status of financial creditors. The genesis for this change was the recommendation of the insolvency law committee ("**ILC**") in its report dated March 26, 2018[7]. The ILC, noting the existing confusion under the law, came to the conclusion that amounts owed to homebuyers were financial debts. The definition of "financial debt" includes, in Section 5(8)(f) of the IBC, a "forward sale or purchase agreement having the commercial effect of a borrowing", and the ILC "*deliberated that the amounts so raised are used as a means of financing the real estate project, and are thus in effect a tool for raising finance, and on failure of the project, money is repaid based on time value of money*"[8]. Therefore "*not all forward sales or purchases are financial transactions, but if they are structured as a tool or means for raising finance, there is no doubt that the amount raised may be classified as financial debt under Section 5(8)(f)*"[9].

Consequently, the IBC was amended to include an explanation in Section 5 (8) (f) as follows:

"*(f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing;*

[7]Report of The Insolvency Law Committee, March 2018, available at https://ibbi.gov.in/uploads/resources/ILRReport2603_03042018.pdf. [hereinafter "ILC Report"].
[8]*Ibid*, at para 1.5, p. 16.
[9]ILC Report, *supra* note 19, at para 1.6, p. 17.

Explanation. -For the purposes of this sub-clause, - (i) any amount raised from an allottee under a real estate project shall be deemed to be an amount having the commercial effect of a borrowing; and (ii) the expressions, "allottee" and "real estate project" shall have the meanings respectively assigned to them in clauses (d) and (zn) of section 2 of the Real Estate (Regulation and Development) Act, 2016 (16 of 2016)"

When the constitutionality of the amendment was challenged by a group of real estate developers, the Supreme Court in *Pioneer Urban Land and Infrastructure Limited v. Union of India*[10] attempted to clarify the position using a different line of reasoning. Upholding the amendment, the court ruled that "t*he expression "borrow" is wide enough to include an advance given by the homebuyers to a real estate developer for "temporary use", i.e., for use in the construction project so long as it is intended by the agreement to give "something equivalent" to money back to the homebuyers. The "something equivalent" in these matters is obviously the flat/apartment.*"

While the Supreme Court"s reasoning was clearer than that of the ILC, it appears to have blurred the envisaged distinction between financial and operational creditors. If delivery of the product paid for equates to repayment of the advance by giving "something equivalent" to money to the payor, and thus assumes the nature of financial debt, every contract for supply of goods and services would then fall within its ambit.

It is therefore difficult to appreciate the stated logic justifying the inclusion of homebuyers as financial creditors, or at the very least, their inclusion but not the inclusion of other classes of operational creditors. The policy and political considerations, on the other hand, are easier to understand. As Warren notes "*The rationale for protecting parties without formal legal rights may simply be political in nature; such protection encompasses a wider range of voters than the particular creditors who would profit from the immediate enforcement of their rights. Moreover, some of the parties*

[10](2019) 8 SCC 416, para. 77.

without formal legal rights have well-organized political clout….Notwithstanding whatever cynicism is appropriate about congressional motives, it remains the case that the protection of parties without legal rights also reflects a more profound economic reality: the parties with formal legal rights never completely internalize the full costs of a business failure."[11]

The ILC too makes its considerations clear, stating that[12] "*the amount of money given by homebuyers as advances for their purchase is usually very high, and frequent delays in delivery of possession may thus, have a huge impact. For example, in Chitra Sharma v. Union of India[13], the amount of debts owed to homebuyers, which was paid by them as advances, was claimed to be INR fifteen thousand crore, more than what was due to the banks. Despite this, the banks are in a more favorable position under the Code since they are financial creditors. Moreover, the general practice is that these contracts are structured unilaterally by construction companies with little or no say of the homebuyers. A denial of the right of a class of creditors based on technicalities within a contract that such creditor may not have had the power to negotiate, may not be aligned with the spirit of the Code.*"

While the inclusion of homebuyers as financial creditors has led to certain inefficiencies in the resolution process[14], the legislative clarity has yielded various resolution plans which have been approved by the committee of creditors, i.e., homebuyers as well as banks, of various real estate companies. However, these have largely not progressed further due to the stance of the concerned development authorities, which is examined in more detail below.

---

[11] Elizabeth Warren, *Bankruptcy Policymaking in an Imperfect World*, Michigan Law Review, Vol. 92, p. 336 at 356.
[12] ILC Report, *supra* note 19, at paragraph 1.7, p. 17.
[13] W.P. (C) 744 of 2017.
[14] The IBC has had to be amended twice after the initial amendment to Section 5 (8) (f) to address difficulties caused by the inclusion of homebuyers as financial creditors. Firstly, to introduce a mechanism for calculation of homebuyer votes, which became necessary since very few homebuyers actually voted as part of the process, thus leading to the thresholds for approving resolution plans and other actions in the insolvency resolution process not being met. Secondly, to introduce a minimum number of homebuyers required to initiate the CIR process, so that an individual homebuyer cannot unilaterally cause the insolvency of a real estate company, which may affect thousands of other homebuyers.

IV. ROLE OF THE DEVELOPMENT AUTHORITIES

When National Building Construction Corporation‟s ("**NBCC**") resolution plan was approved by the committee of creditors of Jaypee Infratech, it was challenged on several grounds by various stakeholders. One of the challenges was by the Yamuna Expressway Industrial Development Authority ("**YEIDA**"), on the grounds that the resolution plan attempted to, *inter alia*, alter the concession structure by which Jaypee Infratech Limited ("**JIL"**) had been granted the land in the first place.

The concession agreement granted JIL the lease of land to construct and operate the Yamuna Expressway, as well as large portions of land parcels for development. NBCC‟s resolution plan attempted to bifurcate the concession for the expressway into a separate company, the land for development into a separate company, and retain only the land on which the incomplete apartments were located in JIL. The plan also sought to make different stakeholders, such as allottees and lenders responsible to pay increased compensation for farmers which was being demanded by YEIDA. YEIDA having been classified as an operational creditor was not a member of the committee of creditors of JIL, and these provisions in the plan were objected to by YEIDA on the grounds that such changes could not be made without the approval of YEIDA.

The Supreme Court agreed and held that "*any tinkering with the contract in question, that is, the Concession Agreement, could not have been carried out without the approval and consent of the authority concerned, that is YEIDA*." .The Supreme Court‟s judgment in JIL was consistent with its other judgments in *Municipal Corporation of Greater Mumbai v. Abhilash Lal*[15] and *Gujarat Urja Vikas Nigam Limited v. Amit Gupta*[16], wherein the approval rights of statutory authorities were similarly upheld. There

[15](2019) SCC OnLine SC 1479.
[16]Civil Appeal No. 9241 of 2019

is very little debate that can arise concerning the soundness of this judicial stance – the IBC does not prescribe that a resolution plan can override contracts with third parties without their consent, and in fact requires a successful resolution applicant to obtain all governmental approvals it needs to implement a resolution plan within a period of 12 months from the approval by the NCLT[17].

YEIDA was not the only development authority to play an active part in objecting to resolution plans. NOIDA also challenged its classification as an operational creditor and consequent exclusion from the committee of creditors in several resolutions under the IBC, each of which could not progress while NOIDA‟s challenge on its creditor status was adjudicated. Ultimately, the Supreme Court in the case of *New Okhla Industrial Development Authority v. Anand Sonbhadra*[18] held in its order on May 17, 2022 that NOIDA was correctly classified as an operational creditor under the IBC. Unlike allottees, the legislature has thus, far not taken the step of amending the IBC to include the developmental authorities as financial creditors.

After several years of litigation, there is today legal clarity on the place of development authorities within the IBC resolution process. While they are not financial creditors and are thus not eligible to be a part of the committee of creditors and vote on resolution plans, their approval is required to any changes a resolution plan seeks to make to the underlying contract between the corporate debtor and the development authority.

Such clarity on the matter, however, has done little to aid resolution. Typically, at the point when a real estate company has become insolvent, it has already defaulted on its dues to the development authority and has failed to adhere to the required timelines for completion of construction. Under the terms of the underlying lease deed, these typically result in massive financial penalties

[17]§31(4), The Insolvency and Bankruptcy Code, 2016.C
[18]Civil Appeal No. 2222 of 2021.

payable to the development authority, and thus any potential resolution applicant seeking to resolve the company steps into a company with huge amounts payable to the development authorities, in addition to the funds required to complete construction, and payments to be made to banks and financial institutions. Additionally, waivers are required from the development authorities, for example to extend the construction completion timelines, changes to the approved building plan, any corporate restructuring to aid resolution etc.

Any resolution plan therefore has very little chance of succeeding without the necessary approvals from the development authorities. Development authorities, in turn, have very little incentive to, and generally do not, grant approvals unless their dues are fully cleared. Given that the penalties comprising these dues are extremely high, any resolution plan becomes prohibitively expensive. Although as operational creditors, dues of the development authorities until commencement of the insolvency can be extinguished or minimized under a resolution plan, doing so would likely cause the development authorities to reject any necessary approvals or waivers, and cause the resolution to fail. Thus, despite being operational creditors under the framework of the IBC, development authorities have essentially acquired the status of super creditors without whose explicit approval the resolution cannot succeed.

For example, the government appointed Board of Unitech Limited expressed its frustration with the stance taken by NOIDA in its proposed resolution framework filed with the Supreme Court:

"*...Noida has claimed inexplicable and unjustifiable amounts from the Unitech Group, and further caused unreasonable hindrances and delays in completion of the projects by withholding the due approvals without any concrete grounds. In any case, issues between Noida and*

developer should not affect the interests of homebuyers. Noida has only been concerned with revenue rather than the development of project and delivery to homebuyers, leave alone the sustainability of any Developer. Even today when the Hon'ble Supreme Court has had to intervene to safeguard the interests of Homebuyers, Noida has not been concerned with sustaining and completing the developments and Homebuyers of Unitech Group in general but is concerned with its recovery. This is manifested in its proposal which if accepted would effectively denude Unitech Group of substantial assets and sources of funds and thereby jeopardise interest of Homebuyers."

Similarly, the Supreme Court in *Bikram Chatterji v. Union of India* its orders dated June 10, 2020 and July 10, 2022, stated that the interest on the outstanding premium and other dues of the authorities as per the prevailing policies are too high, and directed that such interest be calculated at SBI MCLR rates.

Insolvency theorists posit the "hold out" problem in insolvency frameworks, where bargaining may be hindered because the parties have an incentive to hold out in order to extract the maximum value from each other[19]. In part, this is a problem which the IBC seeks to sidestep by excluding operational creditors from the bargaining table completely. However, given the status of development authorities, they are a necessary bargaining party, and as their stance in various resolution proceedings has already demonstrated, their holding out has already hindered resolution in many cases.

V. THE JUDICIAL "NUDGE"

Having laid down the principle that development authority approval is required for any changes to their underlying contracts and refrained from intervening by directing the development authorities to accept resolution plans, courts have instead sought to nudge the development authorities to cooperate with the

[19]Anthony J. Casey, *Chapter 11's Renegotiation Framework and the purpose of Corporate Bankruptcy*, 120 Columbia Law Review 1709 (2020) at 1737.

resolution process. For example, the Supreme Court in the matter of *Jaypee Kensington Boulevard Apartments Welfare Association v. NBCC*[20], while rejecting NBCC‟s resolution plan, had stated the following: "*Before concluding on this point for determination where we have accepted the major parts of the objections of YEIDA, we may, in fairness to all the parties concerned, reiterate that despite stating its objections, YEIDA has consistently maintained before the NCLT as also before this Court that it does not stand to oppose the resolution plan only for the sake of opposition; rather it would like the plan to succeed but, it has a public duty to ensure that the framework under CA is preserved and else, it would be ready to do everything within its power to ensure that the plan is a success. Thus, it would not be out of place to add a sanguine hope that being the owner of the land in question and public authority, YEIDA, who had envisaged and promoted the entire project, would, in future dealing with the matter, act with caution and circumspection, while earnestly reflecting upon the practical impact of its propositions/decisions on various stakeholders, including the homebuyers.*"

Similarly, in *Bhupinder Singh v. Unitech Ltd*[21]the Hon‟ble Supreme Court stated "*it would serve the ends of justice if the Sub-Committee nominated by the Board of Management of Unitech Limited and the Concerned officials of NOIDA and Greater NOIDA at a senior level engage in discussions so as to provide a way forward which, while protecting the interests of these statutory authorities would also protect the interests of the ultimate flat purchasers. We expect that both NOIDA and Greater NOIDA shall find a pragmatic solution to an issue which has been raised, including their demands*", and again in its order dated May 5, 2022, stated that: "*Allowing the lands to remain unused and undeveloped will not sub-serve the interest of the statutory authorities and will result in a situation where the home buyers will not be able to secure their flats. Once the construction commences, it is anticipated by the Board of Management that realizations will also take place from which the dues can be paid over in a staggered manner. Cooperation in this regard from the statutory*

[20]Civil Appeal No. 3395 of 2020; order dated March 24, 2021 [Pr. 108].
[21] Civil Appeal No.10856/2016; order dated 25.08.2021 [Pr.6-7].

authorities would facilitate the completion of the projects and protect the interest of the home buyers, while at the same time facilitating the realization of the dues of the statutory authorities. The payments of the dues of the statutory authorities is also dependent on the construction taking place and it is from the realizations from the projects that the dues can be paid."

Despite the courts seeking to prompt the development authorities to act in a pragmatic manner to aid resolution, the authorities have not yet been forthcoming in this regard. The ball is now in their court, and the future success of real estate resolution depends on how practical the authorities are in accepting haircuts like other creditors to enable resolution plans to succeed.

VI. NEED FOR A POLICY

In insolvency resolution of real estate companies, misalignment of incentives can be identified between the three main classes of creditors: homebuyers, development authorities and secured creditors. Homebuyers are likely to prioritize speedy delivery of their constructed apartments while the authorities and secured creditors to prioritize maximization of recovery. Any potential resolution applicant therefore needs to decide how to efficiently allocate its resources between construction and payment to authorities and secured creditors. While the homebuyers and secured creditors are members of the committee of creditors and therefore able to negotiate with the resolution applicants and each other, the position of the development authorities, as essentially a super creditor outside the committee of creditors, is fundamental to how feasible resolutions may be going forward.

It should be noted that for the development authorities, stalled construction projects have long presented difficulties. As planning authorities, the ultimate responsibility for difficulties faced by homebuyers falls upon them, and attempts have been made in the past to tackle these difficulties. For instance,

the Government of Uttar Pradesh issued a project settlement policy[22]providing for settlement of different classes of projects such as rescheduling packages for dues to Development Authorities for plots with construction, and in 2018, a High-Level Committee was constituted by the Government of Uttar Pradesh which prepared a report [23]("**HLC Report**") with various suggestions on how different classes of stalled projects could be progressed. However, these solutions sought to be introduced by the Government of UP and development authorities faced the following challenges:

(i) Only the defaulting developer had a legal and contractual relationship with each class of affected stakeholder, and therefore each stakeholder, including the development authorities, are constrained to deal with the defaulting developer.

(ii) Each stakeholder, particularly allottees, seeks independent directions from various courts and tribunals, thus making it impossible to find a holistic solution, and increasing the time taken due to various stays and directions granted by such courts and tribunals.

The IBC therefore presents a unique opportunity for developmental authorities to solve a multi-stakeholder problem by bringing the company under one common resolution process, supervised by the NCLT/NCLAT/Supreme Court, under which each stakeholder can accept suitable compromises and progress the construction of stalled projects.

The development authorities therefore would do well to formulate an appropriate policy to consider and approve resolution plans under the IBC and thus seek to resolve a long-standing problem.

[22]Government Order *[5085/77-4-16-142N/08]*, dated December 15, 2016.
[23]Report of High-Level Committee constituted by the Government of Uttar Pradesh *vide* Order No. 1337-77-4-18-1422N/08 dated 18th June 2018.

SCHOLASTICUS

Parameswaran Chidamparam, DERAILING THE IPO MARKET: SEBI"S PROPOSED CONFIDENTIAL FILING MECHANISM, 10(2) SCHOLASTICUS 20 (2023).

DERAILING THE IPO MARKET: SEBI'S PROPOSED CONFIDENTIAL FILING MECHANISM

Abstract

The Securities and Exchange Board of India has taken a number of steps in the recent past to encourage companies to raise capital from the public. The success of SEBI's regulatory measures is reflected by the unprecedented rise in the number of IPOs in the last two financial years with some of the biggest offerings occurring in 2021. Despite the success in the primary market, companies have raised concerns regarding their competitors having access to sensitive business information when their draft offer documents are filed. To address this issue, SEBI, in its Consultation Paper dated May 11, 2022, proposed a confidential pre-filing mechanism which shields an issuer's draft offer documents from the eyes of the public. In this article, the author shall examine the concept of a confidential pre-filing mechanism, discuss its advantages and disadvantages and evaluate the effect of its introduction in the United States of America. The author argues that SEBI, when framing India's confidential pre-filing mechanism, will have to be mindful of the aftermath of a similar mechanism's introduction in the United States. Ultimately, the author argues that SEBI should not implement a confidential pre-filing mechanism and should offer more disclosure benefits instead. If SEBI were to implement the mechanism, the author is of the opinion that it should impose strict timelines for companies that opt to go public through the proposed confidential pre-filing mechanism or increase the time for which a confidentially filed draft red herring prospectus is available to the public, for the benefit of retail investors.

I. INTRODUCTION

The Securities and Exchange Board of India ("**SEBI**"), on May 11, 2022, released a consultation paper titled „*Pre-filing of Offer Document in case of Initial Public Offerings* ***("IPO").***"[1] Through this paper, SEBI invited public comments on the idea of having an alternative "regulatory review" mechanism which permits pre-filing offer documents with SEBI and the relevant stock exchanges on which the prospective issuer chooses to list its securities.

This article examines the concept of a confidential pre-filing mechanism and discusses the possible issues that could arise if such a mechanism is brought into the Indian securities market. It unfolds in four parts. Part I discusses the concept of a confidential pre-filing mechanism and how it could address the practical limitations of the present filing procedure under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 ("**ICDR**"). Part II contemplates the theoretical implications of bringing in a pre-filing mechanism by relying on India‟s legal framework, foreign laws, and by deducing it from various events in the primary market. Although the success or failure of a regulatory mechanism in the securities market is generally assessed after its implementation through empirical studies, the implementation of an alternative review mechanism in India would be more thorough if SEBI were to draw upon the experiences of foreign jurisdictions. Part III surveys empirical studies conducted in the United States to show that the effect that a similar regulatory change had on the American IPO market was a reduction in the number of IPOs, which is a possible consequence that SEBI ought to keep in mind before

[1]Securities and Exchange Board of India, *Consultation Paper on Pre-filing of Offer Document in case of Initial Public Offerings (IPO)*, available at: https://www.sebi.gov.in/reports-and-statistics/reports/may-2022/consultation-paper-on-pre-filing-of-offer-document-in-case-of-initial-public-offerings_58875.html [hereinafter „**Consultation Paper on Pre-filing of Offer Documents**‟].

bringing in an alternate filing mechanism of its own. Part IV concludes by contemplating a possible alternative to a confidential pre-filing mechanism and offering suggestions on how it can be implemented if SEBI were to go through with such a filing mechanism.

II. THE PRESENT REGULATORY REGIME AND DELAYS IN OBTAINING APPROVALS FOR DRAFT OFFER DOCUMENTS

Presently, the procedure to file offer documents in India is governed by ICDR.[2] Regulation 25 of ICDR states that the issuer would have to file three copies of the draft red herring prospectus ("**DRHP**") with the SEBI.[3] The issuer would also have to file the DRHP with the stock exchanges that the specified securities are proposed to be listed on.[4] The DRHP should be made available to the public for a minimum of 21 days,[5] and SEBI would have to specify changes to the DRHP within a 30 days" timeframe.[6]

Unfortunately this process has faced consistent delays with several DRHPs taking months to obtain SEBI"s approval.[7] The Consultation Paper states that the average time to obtain approvals for DRHPs is between thirty and seventy days.[8] While companies such as Paytm, Zomato and Star Health had their DRHPs approved in a window of two to three months, this has not always

[2] *See*, Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018, Gazette of India Part III, Section IV (Sept. 18, 2018).
[3] *Id.*, at Reg. 25(1).
[4] *Id.*, at Reg. 25(3).
[5] *Id.*, at Reg.26.
[6] *Id.*, at Reg. 25(4).
[7] SamieModak, *Sebi mulls launch of confidential IPO filings to address privacy concerns*, BUSINESS STANDARD (May 12, 2022), available at: https://www.business-standard.com/article/markets/sebi-mulls-launch-of-confidential-ipo-filings-to-address-privacy-concerns-122051101324_1.html.
[8] Consultation Paper on Pre-filing of Offer Documents, *supra* note 1, at ¶ 2.1.

been the case in the recent past.[9] The Nykaa and PolicyBazaar DRHPs, for example, were approved six months after they were filed.[10]

Such massive delays in obtaining approvals result in two consequences for prospective issuers. *First*, sensitive information is disclosed in DRHPs. Such disclosures result in the competitors of an issuer gaining access to issuer‟s consolidated financial statements, business strategies and other sensitive information for prolonged periods, thereby increasing the possibility of obstructive strategies by an issuer‟s competitors.[11] *Second*, feedback obtained from "potential institutional investors" on the pricing of shares becomes redundant due to the dynamic nature of the securities market.[12] To tackle these issues, SEBI has proposed an alternative to the existing filing procedure: allowing issuers to confidentially file DRHPs with SEBI and the stock exchanges on which the specified securities will be listed.[13]

III. THE POSITIVE AND NEGATIVE IMPLICATIONS OF BRINGING IN A CONFIDENTIAL PRE-FILING MECHANISM

Introducing a confidential pre-filing mechanism will definitely change the perspective of companies that intend to raise capital from the public. It could have several positive and negative implications and its own advantages and disadvantages. This section relies on academic literature, the already existing regulatory regime and recent events happening in India, and the manner in

[9] *Supra* note 7.
[10] *Supra* note 7.
[11] Consultation Paper on Pre-filing of Offer Documents, *supra* note 1, at ¶ 2.2; *see also* Gallagher, *infra* note 38, at 316 where the author argues that increased obligations of a public company give its competitors access to information that would not have been available had it been private.
[12] Consultation Paper on Pre-filing of Offer Documents, *supra* note 1, at ¶ 2.3.
[13] *Id.*, at ¶ 3.2.1.

which confidential pre-filing mechanisms work in other countries to explore the pros and cons of the possible implementation of a similar mechanism in India.

A. Confidentiality, flexibility and reduced risks – the benefits of a pre-filing mechanism

SEBI brought in the proposal for an alternate mechanism to tackle the issues of delayed regulatory approvals and ease of access to sensitive business information. Apart from these two advantages of an alternate mechanism to tackle the delayed regulatory approvals, companies are also less likely to be subjected to litigation and will have greater flexibility with their IPOs.

(i) Flexibility with IPO timelines

On a *prima facie* examination of SEBI"s Consultation Paper, it seems as though it intends to replicate §106 of the Jumpstart Our Business Startups Act. ¶3.2.5 of the Consultation Paper states, "*Pursuant to receipt of SEBI observations, an issuer, if it* ***so desires based on market conditions and its own financial requirements****, may decide to pursue undertaking IPO*."[14] The language used by SEBI in this paragraph indicates that the alternate mechanism will allow issuers to strategize the time of their IPOs so that they reap the benefits of greater investments when they are in a financially stable position. Such a move should encourage more companies to adopt the confidential mechanism if it is implemented.[15]

(ii) Reduced risk of litigation

One of the biggest issues that prospective issuers face under the current regime is that their DRHP, which contains sensitive information regarding the companies" projects, financials etc. are easily available to the public. The ease of access to such information becomes a huge concern because the company"s competitors, ex-employees and ex-founders sometimes pursue litigation against

[14] *Id.*, at ¶ 3.2.5.

[15] This does not necessarily mean that the move will encourage more companies to go public. For a detailed discussion of how this could affect the number of IPOs, *see infra* Section III.

the issuer just before the issuer‟s company is about to go ahead with its IPO, which adversely affects the price of its shares, thereby causing greater hesitation among prospective investors.

In 2012, former SEBI Chairman, U.K. Sinha stated that the majority of the complaints against companies that were close to their IPOs were from the company‟s competitors.[16] This trend persisted even in 2021 as both Paytm and Oyo were subject to lawsuits before they went public.[17] Paytm faced a suit from one of its former directors after its DRHP was filed, where the allegation was that he invested an amount when the company was in its initial stages but did not receive shares.[18] Similarly, Zostel wrote a letter to SEBI requesting for the Oyo IPO to be stayed on grounds of Oravel‟s (Oyo‟s parent company) capital structure not being final.[19]

A similar trend was observed in the United States as well. Facebook, Zynga and GroupOn were sued in the year they went public, but not the year prior to that.[20] Of course, one could argue that the confidential filing mechanism does not eliminate disclosure completely; rather, it merely delays disclosure, which means that the competitors of a company can still obstruct the IPO process at a later stage.[21] While this may be true, the fact that the initial filing can be made confidentially means that the offer documents are available to the competitors of a company for a smaller time window, thereby reducing the possibility of

[16] *Supra* note 7.
[17] *Id.*
[18] Reuters, *Ex-director seeks to stall $2 billion Paytm IPO, company calls it harassment*, THE HINDU (Aug. 13, 2021), available at:https://www.thehindu.com/business/ex-director-seeks-to-stall-2-bln-paytm-ipo-company-calls-it-harassment/article35890749.ece.
[19] PTI, *Oyo IPO: Zostel writes to Sebi, seeks rejection of draft offer papers*, ECONOMIC TIMES (Oct. 12, 2021), available at:https://economictimes.indiatimes.com/markets/ipos/fpos/oyo-ipo-zostel-writes-to-sebi-seeks-rejection-of-draft-offer-papers/articleshow/86969868.cms?from=mdr.
[20] B. Esmer, N. BugraOzel&Suhas A. Sridharan, *Does Reducing Disclosure Mean Fewer Pre-IPO Lawsuits?* (June 12, 2020), available at:https://clsbluesky.law.columbia.edu/2020/06/12/does-reducing-disclosure-mean-fewer-pre-ipo-lawsuits/.
[21] *Id.*

frivolous litigation.[22] Hence, the proposed mechanism should significantly reduce pre-IPO litigation if it does not eliminate it.

B. Disadvantages of the proposed mechanism

The confidential pre-filing mechanism comes with very few disadvantages when looked at from the perspective of an issuer. Two such disadvantages are: the delayed opportunity cost and, increased compliance costs. For investors, the major disadvantage is that information regarding the issuer would be available publicly for a shorter period of time, thereby giving them less time to gauge the future prospects of the company. The disadvantage of the proposed mechanism from the perspective of the stock market and the Indian economy are discussed *infra* in Section III, by drawing upon the experience of the United States of America.

(i) Gauging the company's future prospects – hurting retail individual investors

The fundamental problem with a confidential filing mechanism is that it goes against the very purpose of a prospectus. A prospectus is a public document which gives potential subscribers to the shares of a company an accurate idea of its business ventures.[23] A DRHP, provides information regarding the issuer"s business strategies, management, capital structure, promoters and promoter group, group companies, financial statements, government approvals etc.[24]

With the confidential filing mechanism, investors will not have the benefit of perusing information in the DRHP before the final version of the offer document is filed. Since the offer document will be available to the public only for the mandatory 21-day period required under Regulation 26 of the ICDR, retail individual investors could be adversely affected. This is particularly concerning because of the unprecedented levels of retail investor participation

[22] *Id.*
[23] Companies Act, 2013, §26, No. 18, Acts of Parliament, 2013 (India); Companies (Prospectus and Allotment of Securities) Rules, 2014, Rules 3, 4 and 5.
[24] ICDR, *supra* note 2, Schedule VI, 224-284.

in the Indian stock market.[25] Data indicates that retail investor participation in NSE companies rose to 7.42% in 2022 which was 0.09% higher than the previous year.[26] After consistent participation in IPOs in the previous year, retail investor participation in IPOs may see a decline in the coming months because of the weak performances of start-ups like Zomato, Nykaa and Paytm.[27] With retail investors already losing confidence in the IPO market, bringing in a confidential filing mechanism which reduces the time for which they can access the DRHP could aggravate their concerns since they do not have the resources of a qualified institutional investor to make investment decisions. In summary, a confidential filing mechanism may benefit more experienced investors who have resources at their disposal, but it adversely affects retail investors and investors who are just starting out.

(ii) The "delayed" opportunity cost of a confidential filing

Perhaps one of the major disadvantages of the concept of a confidential pre-filing mechanism is the lack of alternate opportunities presenting themselves. When a company files its draft offer documents publicly, it opens up opportunities for itself. Schedule VI of the ICDR Regulations specify several disclosures that an issuer would have to make in the offer document. Certain disclosures such as the capital structure of the company, the cost of new projects that the issuer plans to undertake, and the issuer‟s business overview

[25]PTI, *Surging retail investors, soaring subscriptions spice up IPO offerings*, BUSINESS STANDARD (Aug. 18, 2021), available at:https://www.business-standard.com/article/markets/surging-retail-investors-soaring-subscriptions-spice-up-ipo-offerings-121081801437_1.html.

[26]Outlook Money Team, *Retail Investors' Holdings In NSE Companies Reach All-Time High Of Rs. 19 Lakh Crore*, OUTLOOK (May 04, 2022), available at: https://www.outlookindia.com/business/retail-investors-holdings-in-nse-companies-reach-all-time-high-of-rs-19-lakh-crore-news-194841.

[27] IANS, *New-age cash guzzler cos dented retail investors' confidence in IPO Market: Religare Broking*, TIMES OF INDIA (May 29, 2022), available at: http://timesofindia.indiatimes.com/articleshow/91866865.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst.

could attract alternate sources of growth such as acquisitions.[28] If an issuer adopts to shield such information from the public by filing its offer documents confidentially, it loses out on the publicity associated with a public filing and therefore misses out on possible alternatives to raising capital from the public. Although such opportunities will present themselves at a later stage, companies will lose out on these opportunities until their offer documents are made public thereby delaying the possible growth of the company.

(iii) Increased compliance costs under SEBI's proposed mechanism

SEBI"s Consultation Paper on Pre-filing of Offer Documents states that the company will have to file an updated DRHP ("**UDRHP**") after the confidentially filed DRHP is approved by SEBI.[29] Experts have raised concerns regarding such a proposal because it could mean that issuers will have to file three offer documents, namely, the pre-IPO documents, the UDRHP and then the finalised RHP which accommodates SEBI"s proposed changes.[30] Filing these many documents could significantly increase the expenses associated with going public and also increase the time required to complete the IPO approval process.[31]

Companies may resort to the increasingly popular method of special purpose acquisition companies ("**SPACs**") to raise capital since the compliance costs associated with this method is much lower than a traditional IPO.[32] Additionally, raising capital through SPACs also reduces the time it takes for companies to raise funds. Although India does not have a comprehensive

[28] *Id.*; *see also* Gallagher, *infra* note 38, 322.
[29] Consultation Paper on Pre-Filing of Offer Documents, *supra* note 1, at ¶ 3.2.5.
[30] Nick J. Adam, *The Pros And Cons Of Pre-Filing IPO Documents*, TECHILIVE(May 12, 2022), available at: https://techilive.in/the-pros-and-cons-of-pre-filing-ipo-documents/.
[31] *Id.*
[32] Rishi Raj, *SPACs: An Alternative to IPO for Private Companies* (Feb. 06, 2022), available at: https://www.ccl.nluo.ac.in/post/spacs-an-alternative-to-ipo-for-private-companies.

framework for SPACs yet, SEBI and the Company Law Committee Report seem to be advocating for its recognition in India sooner rather than later.[33]

IV. LEARNING FROM THE AMERICAN EXPERIENCE – THE AFTERMATH OF IMPLEMENTING A CONFIDENTIAL FILING MECHANISM

The United States of America experienced a significant drop in the number of public offerings in the 2000s.[34] To reinvigorate its capital markets and encourage companies to go public, changes to existing filing mechanisms were made through the Jumpstart Our Business Startups Act in 2012 ("**JOBS Act**") which was aimed at encouraging emerging growth companies ("**EGCs**") to raise capital from the public.[35] The JOBS Act was the starting point for the confidential filing mechanism, since it was the first statute to bring in such an option.[36] The filing mechanisms under the JOBS Act were made applicable to all prospective issuers in 2017,[37] with the SEC expecting such a move to increase the number of IPOs.[38] Since the proposed framework SEBI seeks to implement is quite similar to the mechanism under the JOBS Act, studying the effect that the framework had on the market becomes extremely important.

---

[33]Palak Shah, *SEBI readies framework for SPAC listing in India*, HINDU BUSINESSLINE (May 19, 2022), available at: https://www.thehindubusinessline.com/markets/sebi-readies-framework-for-spac-listing-in-india/article65430748.ece.

[34]Louis Lee, *The Decline of the IPO*, STANFORD BUSINESS (April 12, 2018), available at:https://www.gsb.stanford.edu/insights/decline-ipo.

[35] Jumpstart Our Business Startups Act, Public Law 112-106, Apr. 05, 2012, An EGC is a company with an annual revenue of less than $1.07 billion.

[36] Sergei Klebnikov, *Here's Why More Companies Are Filing Confidential IPO Paperwork*, FORBES (Aug. 25, 2020), available at:https://www.forbes.com/sites/sergeiklebnikov/2020/08/25/heres-why-more-companies-are-filing-confidential-ipo-paperwork/?sh=445ccfc16e68.

[37]Andrew Brady et al., SEC permits all issuers to submit confidential draft registration statements, 18 JOURNAL OF INVESTMENT COMPLIANCE 16 (2017).

[38] Patrick J. Gallagher, *Going Public Secretly: The SEC's Unavailing Effort to Increase Initial Public Offerings Through Confidential Registration*, 2019 COLUM. BUS. L. REV. 305 (2019).

C. The confidential filing mechanism under the JOBS Act and its effect on IPOs

Since the JOBS Act provided a confidential filing mechanism, it was widely expected that more EGCs would choose to go public.[39] Academic literature, however, does not seem to have a concrete answer on whether the JOBS Act fulfilled the objective of reversing the declining number of IPOs.[40] While initial studies indicate that the JOBS Act significantly increased the average number of IPOs by 25% annually,[41] more recent empirical studies seem to express more doubts on the success of the JOBS Act.[42] Professor Gallagher examines four empirical studies that were carried out after the confidential filing mechanism came into effect. He refers to one particular study that found that the proportion of EGCs going public reduced by 2.9% after the confidential filing mechanism came in.[43] Such a trend is surprising because of the various benefits offered to EGCs under the JOBS Act, and, it also goes against the intention with which the Act was brought in.[44]

In fact, the 2017 IPO Report by the Harvard Law School Forum on Corporate Governance confirms that the JOBS Act seems to have an effect opposite to what was intended.[45] It states that the JOBS Act has incentivized EGCs to remain private for a longer time and engage in strategizing the timing of their

---

[39] JOBS Act, *supra* note 35 at §106.

[40] *See* Gallagher, *supra* note 38, where the author discusses several empirical studies with mixed results; *see also* E.P.M Vermeulen, *High-Tech Companies and the Decision to Go Public: Are Backdoor Listings Still an Alternative to Front-Door Initial Public Offerings*, 4 PENN. ST. J.L. & INT"L AFF. 442-443 (2015) where the author concludes that the JOBS Act has been a success with its confidential filing mechanism causing more EGCs to go public and adopt such a mechanism.

[41] *See generally*, M. Dambra, L.C. Field & M.T. Gustafson, *The JOBS Act and IPO volume: Evidence that disclosure costs affect the IPO decision*, 116 J. FIN. ECON. 121 (2015).

[42] Gallagher, *supra* note 32, 327-330.

[43] *See id.* at 328; *see also*, Carlos Berdejó, *Going Public After the JOBS Act*, 76 OHIO ST. L.J. 36-37 (2015).

[44] JOBS Act, *supra* note 35, Preamble.

[45] L.D. Marderosian et al., *2017 IPO Report*, HARVARD L. SCHOOL FORUM ON CORPORATE GOVERNANCE (May 25, 2017), available at: https://corpgov.law.harvard.edu/2017/05/25/2017-ipo-report/.

public offerings.[46] Such an immense amount of flexibility would necessarily have an effect on the market as a whole, and simply increases the number of "qualified IPO candidates" and not the number of IPOs.[47] Professor Gallagher concludes that the implications of the JOBS Act on the number of IPOs by EGCs cannot be determined on the basis of existing studies as none of them offer a conclusive answer.[48]

Hence, the best course of action for SEBI should be to err on the side of caution. By implementing a confidential filing mechanism in India, SEBI could open a Pandora"s box for the Indian securities market, similar to what had occurred in the United States. Such a move should be made with extreme caution especially because of the unprecedented rise in the number of IPOs since the beginning of the pandemic.[49] Past experience shows that such unprecedented highs in the stock market are often followed by a crisis.[50] In the current circumstances, where concerns regarding the sudden quiet phase in the IPO market due to the global financial situation are being raised,[51] it may not be prudent for SEBI to bring in a pre-filing mechanism that could encourage companies to remain private and strategize their IPO timelines. Although such a result need not necessarily occur, it is a possibility that SEBI ought to keep in mind before bringing in the proposed pre-filing mechanism.

---

[46]*Id.*
[47]*Id.*
[48]*Supra* note 38, 330.
[49] K.R. Srivats, „*2021 best IPO year in India in the last 20 years': EY*, HINDU BUSINESSLINE (Dec. 23, 2021), available at:https://www.thehindubusinessline.com/markets/stock-markets/2021-best-ipo-year-in-india-in-the-last-20-years-ey/article38023373.ece.
[50]Prarthana Balasubramanian, *Surge in Initial Public Offerings ("IPO"): Smooth Sailing or a Forthcoming Sink?*, 10 SCHOLASTICUS 82-83 (2022).
[51]ShwwetaPunj, *Is the Indian start-up boom over?*, INDIATODAY(July 13, 2022), https://www.indiatoday.in/india-today-insight/story/is-the-indian-start-up-boom-over-1975173-2022-07-13; *see also* Niti Karan, *Why we are in a season of IPO drought*, LIVEMINT(July 15, 2022), https://www.livemint.com/market/ipo/jittery-mkt-leads-to-longest-dry-spell-for-ipo-launch-in-a-year-11657819092487.html. Such concerns however, could be misplaced, since there have been 4 companies that have filed DRHPs since the start of July, 2022.

D. Extending the confidential filing mechanism to all companies in America – A Similar Story?

In June 2017, the Securities and Exchange Commission **("SEC")** through a Press Release stated that the confidential filing mechanism applicable to EGCs would extend to all companies in the United States.[52] The purpose behind such an extension was to reverse the declining number of IPOs in the United States over the last decade.[53] Unfortunately, an empirical study conducted by Professor Gallagher indicates that the fate of the SEC"s measures to encourage IPOs met the same fate as the JOBS Act.[54] The study found that there was not much of a difference between the number of IPOs pre and post the SEC"s decision to bring in a confidential filing mechanism for all companies in the United States.[55]

Professor Gallagher, however, mentions two limitations of the study. *First*, the data used for the study was collected a year after the SEC"s regulatory change came into effect. Since IPO timelines are usually lengthy, a study conducted immediately after a regulatory measure is brought in may not be an accurate representation of what the true effect of the regulatory change is. *Second*, the main advantage of the SEC"s confidential filing mechanism is that companies have greater freedom in timing their IPOs. Joseph Kaufman argues that the confidential filing mechanism allows companies to choose to go public when the market is on the rise or in a better position.[56]

There are other limitations also that one should make note of as well, such as like number of non-EGCs in the United States is only about 10% of the total

---

[52]SEC, Press Release, *SEC's Division of Corporation Finance Expands Popular JOBS Act Benefit to All Companies* (June 29, 2017), https://www.sec.gov/news/press-release/2017-121.
[53]Reuters Staff, *Update 2-SEC to allow all companies to file secretly for IPOs*, THOMSON REUTERS (June 30, 2017), https://www.reuters.com/article/usa-sec-ipo/update-2-sec-to-allow-all-companies-to-file-secretly-for-ipos-idUSL3N1JR1JA where Chairman Jay Clayton stated that the objective of the move was to "reverse the steep decline in IPOs."
[54]*Supra* note 38, 335-340.
[55]*Id.*
[56] Lawrence A. Hamermesh & Peter I. Tsoflias, *An Introduction to the Federalist Society's Panelist Discussion Titled Deregulating the Markets: The JOBS Act*, 38 DEL. J. CORP. L. 466 (2013).

number of companies.[57] Hence, there are only a limited number of non-EGCs that could go public after the regulatory change, and therefore, statistics may not be the best indicator of how the SEC‟s change has affected the primary market.[58]

Irrespective of whether the SEC‟s change resulted in the American IPO Market retaining *status quo*, the results of Professor Gallagher‟s empirical study, along with the other studies discussed in Section III.A., lead us to the conclusion that following the United States‟ lead on a confidential pre-filing mechanism could be detrimental to the Indian IPO Market.

V. SUGGESTIONS AND CONCLUSION

One of the worst possible consequences that could result from the implementation of a confidential pre-filing mechanism would be a reduction in IPO numbers as it could create an even bigger wealth gap between the common man and experienced investors who can tap into the activities of private companies.[59]

Drawing from the experience the United States had with the JOBS Act and subsequently, the SEC‟s regulatory change in 2017, avoiding a confidential filing mechanism may be the most plausible way to ensure that IPO numbers in India continue to grow. As an alternative, SEBI could consider offering increased disclosure benefits by shielding information that could be used by the competitors of a company from the eyes of the public. These details could be

[57] *Id.* at 475; *see also* Gallagher, *supra* note 38, noting that the number of non-EGCs could be the reason that the year-on-year percentage of non-EGCs going public remains the same. If there are fewer non-EGCs, then it becomes more difficult for a greater number of them to go public. Hence, empirical studies on the effect of the SEC‟s change may not serve a purpose at all.
[58] *Id.*
[59] *Supra* note 38.

disclosed once the company decides to go through with its IPO. Information that benefits investors such as internal risk factors, the objects of the issue can be retained in the DRHP to inspire confidence in investors. However, information such as the capital structure of the company, promoter contribution, the business strategies of the issuer including collaborations, products and services can be disclosed at a later stage, since they can be perused by prospective investors even in the 21-day period that the offer document is available to the public.

If SEBI were to go through with implementing a confidential pre-filing mechanism, it would be best if it does not follow the model adopted in the United States. Offering an endless amount of flexibility to companies on their IPO timelines could result in more companies choosing to remain private while being "qualified" to go public.[60] Instead, SEBI could impose a timeline within which the offer documents have to be made public, failing which the company would have to repeat the entire confidential filing process. An idea that is quite similar was put forward by NASSCOM in their response to SEBI"s call for public comments.[61] The query that was posed was whether SEBI would notify the company to file the final RHP.[62] NASSCOM suggested that SEBI specify a time within which it would note changes to the DRHP and notify the issuer to file the RHP.[63]

Another option that SEBI could explore to address the needs of retail investors while also appeasing companies would be to increase the mandatory 21-day period under Regulation 26 of the ICDR to give retail investors more time to peruse the offer documents of the issuer. Since the confidential mechanism

[60]*Id.*
[61]Garima Prakash, *Response to SEBI's Consultation Paper on Pre-Filing Offer Document in Case of IPO* (June 27, 2022), available at: https://community.nasscom.in/communities/policy-advocacy/response-sebis-consultation-paper-pre-filing-offer-document-case-ipo.
[62]*Id.*
[63]*Id.*

would require the DRHP to be made public for 21 days in any case,[64] the regulatory framework could have an increased time period for companies that choose to file confidentially.[65]

If SEBI does not tread carefully while implementing the proposed mechanism, the number of IPOs in India could decline just like they did in the United States. While the proposed mechanism and the Consultation Paper indicate that SEBI is actively responding to concerns raised by issuers, it may not be practical for SEBI to ensure the growth of the primary market while simultaneously responding to these concerns. SEBI‟s approach may have to shift from its current model of improvising the IPO processdue to concerns raised by companies to a model where it incentivizes the idea of going public.

[64] Consultation Paper on Pre-filing of Offer Documents, *supra* note 1 at ¶ 3.2.5.

[65] For example, a company that files through the confidential mechanism would have to make the draft offer documents public for a period of at least 30-60 days, depending on what the optimum number is for retail individual investors to benefit, while simultaneously ensuring that the issuer‟s competitors are not given enough time to strategize litigation.

SCHOLASTICUS

Alpesh Sharma, LICENSE FEE AS OPERATIONAL DEBT: ANALYSIS OF NCLAT"S ORDER IN *JAIPUR EXPOCENTRE V. METRO JET AIRWAYS*, 10(2) SCHOLASTICUS 36 (2023).

LICENSE FEE AS OPERATIONAL DEBT: ANALYSIS OF NCLAT'S ORDER IN JAIPUR EXPOCENTRE V. METRO JET AIRWAYS

Abstract

In Jaipur Expocentre Private Limited v. Metro Jet Airways Training Private Limited, the National Company Law Appellate Tribunal held that the unpaid license fee constitutes as operational debt. The Appellate Tribunal also overruled its own judgements in the cases of M. Ravindranath Reddy v. Mr. G. Kishan & Others and Promila Taneja v. Surendri Designe Private Limited. The Appellate Tribunal considered the definition of services under Central Goods and Services Act, 2017 to be relevant to be imported for the purpose of operational debt. The author, in this article, tries to analyse the aforementioned judgement particularly in considering whether the granting of premises would fall under services or not.

I. INTRODUCTION

Recently, a five-judge bench of the Hon‟ble National Company Law Tribunal ("**NCLAT**") in ***Jaipur Expocentre Private Limited v. Metro Jet Airways Training Private Limited***[1] (hereinafter referred as the "**judgement**") held that a claim for payment of license fee for use and occupation of immovable premises for commercial purposes is an operational debt within the meaning of Section 5(21) of the Insolvency and Bankruptcy Code, 2016 ("**IBC**" or "**Code**").[2]

In determining the two questions of law, namely, (i) whether the judgement passed in ***M. Ravindranath Reddy v. Mr. G. Kishan& Others***[3]by the Hon‟ble NCLAT lays down the correct law and (ii) whether the claim of the licensor in case of non-payment the license fee constitutes an operational debt, the Hon‟ble NCLAT has overruled its own judgement passed in *M. Ravindranath Reddy* and the subsequent judgement in the case of ***PromilaTaneja v. Surendri Designe Private Limited.***[4]

In this case note, I have tried to analyse the implications of the order of the Hon‟ble NCLAT in *Jaipur Expocentre v. Metro Jet Airways.*

II. BACKGROUND

Jaipur Expocentre Private Limited ("**Appellant**" or "**Operational Creditor**") entered into a License Agreement with Metro Jet Airways Training Private Limited ("**Respondent**" or "**Corporate Debtor**") to grant a

[1]*Jaipur Expocentre Private Limited v. Metro Jet Airways Training Private Limited*, 2022 SCC OnLine NCLAT 263.
[2]Insolvency and Bankruptcy Code, 2016, No. 31, Acts of Parliament, 2016 (India).
[3]*M. Ravindranath Reddy v. Mr. G. Kishans*, 2020 SCC OnLine NCLAT 84.
[4]*Promila Taneja v. SurendriDesigne Private Limited*, 2020 SCC OnLine NCLAT 1105.

license of an immovable property to the Respondent, the Licensee, for the purposes of running an educational establishment. Upon multiple defaults of the Respondent in paying the monthly license fee, the Appellant sent a demand notice under Section 8 of the IBC. After receiving no reply, the Appellant filed a Section 9 application before the Hon' ble National Company Law Tribunal, Jaipur ("**NCLT**"). The Hon' ble NCLT *vide* its order dated March 4, 2020 rejected the application, holding that the claim arising out of grant of license to use an immovable property does not fall in the category of goods or services, thus, the amount claimed in Section 9 application is not an unpaid operational debt.

Aggrieved by the said order, the Appellant filed an appeal before the Hon"ble NCLAT. The two- member bench vide its order dated March 7, 2022 referred the questions of law to a larger bench. The three-member bench heard the parties and vide its order dated March 9, 2022 directed the questions of law to be placed before a larger bench. Hence, the present appeal was placed before the five-member bench.

III. LICENSE FEE AS OPERATIONAL DEBT

The "operational debt" is defined under Section 5(21) of the IBC as claims in respect of the provision of goods or services. Therefore, the major question which was dealt by the Hon"ble NCLAT was whether leasing out can be included under the expression of "services". Under Section 3(37), words and expressions not defined under the IBC but defined under other mentioned Acts can be imported. For this purpose, the Hon"ble NCLAT also relied upon the judgement of **Keshavlal Khemchand and Sons Private Limited and Others v. Union of India and Others**[5] and **Anup Sushil Dubey v. National Agriculture Co-operative Marketing Federation of India Limited and**

[5] *KeshavlalKhemchand and Sons Private Limited v. Union of India*, (2015) 4 SCC 770.

Another[6]to rule that when a statute does not contain a definition of a particular expression employed in it, it is the duty of the court to expound the meaning of an undefined expression in accordance with the law of well-established principles of statutory interpretation.

In the case of *Promila Taneja*, the Hon‟ble NCLAT held that since the Consumer Protection Act, 2019 ("**CPA**") and Central Goods and Services Tax Act, 2017 ("**CGST Act**") are not mentioned in Section 3(37), the definition of "services" under those acts cannot be adopted. However, in the present case, the Hon‟ble NCLAT adopted the definition of "services" under Section 2(102) of the CGST Act[7] because of two reasons: (i) the License Agreement contemplates payment of GST for the services under the License Agreement on which GST is payable, and (ii) the IBC does not contain the definition of "services" expression employed in it, it becomes the duty of the courts to expound the meaning of the undefined expressions in accordance with the well-established rules of statutory interpretation. In this regard, the Hon' ble NCLAT held that even if an expression is not defined in the statute, the meaning of expression in general parlance has to be considered for finding out the meaning and purpose of expression.

The Hon‟ble NCLAT considered definition of "services" under CGST Act relevant in the present case because the License Agreement did contemplate services and therefore, the Licensee was held liable to pay GST over and above the License Fee. The Hon‟ble NCLAT further relied on the Bankruptcy Law Reforms Committee‟s report dated November 2015, especially para 5.2.1 for

[6]*Anup Sushil Dubey v. National Agriculture Co-operative Marketing Federation of India Limited*, (2020) SCC OnLine NCLAT 674.
[7]Central Goods and Services Tax Act, No. 12, Acts of Parliament, 2017 (India).

including rental property for commercial activities as services.[8] The extract of the para is produced below:

> *"5.2.1. Who can trigger IRP?*
>
> *Here, the Code differentiates between financial creditors and operational creditors. Financial creditors are those whose relationship with the entity is a pure financial contract, such as a loan or a debt security. Operational creditors are those whose liability from the entity comes from a transaction on operations. Thus, the wholesale vendor of spare parts whose spark plugs are kept in inventory by the car mechanic and who gets paid only after the spark plugs are sold is an operational creditor. Similarly, the lessor that the entity rents out space from is an operational creditor to whom the entity owes monthly rent on a three-year lease. The Code also provides for cases where a creditor has both a solely financial transaction as well as an operational transaction with the entity. In such a case, the creditor can be considered a financial creditor to the extent of the financial debt and an operational creditor to the extent of the operational debt." (Emphasis supplied)*

In order to understand the definition of the term "operational", the Hon"ble NCLAT referred the definition of "operating cost" and "operating profit or loss" as defined in P Ramantha Aiyar"s Advanced Law Lexicon (6th Edition Volume 3). "Operating cost" is defined as, "An expense incurred in the conduct of the principal activities of the enterprise". Operating cost or loss is defined as, "Profit or loss arising out of the principal business of a company, before extraordinary items (such as investments) are taken into accounting". Accordingly, the Hon'ble NCLAT held that the Respondent or the Corporate Debtor has taken a licensed premises for running an educational institution. Therefore, all

[8]The report of the Bankruptcy Law Reforms Committee- Volume I: Rationale and Design, Bankruptcy law Reforms Committee (November 2015).

cost incurred by the Corporate Debtor and which remained unpaid shall become an operational debt on the part of the Operational Creditor.

It is pertinent to note that the Hon‟ble NCLAT in the present judgement distinguished between the dues in the nature of rent of immovable property and granting the premises for a particular kind of use for a commercial activity. Hence, the debt pertaining to unpaid license fees is very well covered under the meaning of "operational debt" under Section 5(21) of the IBC.

The "operational debt" is defined under Section 5(21) of the IBC as claims in respect of the provision of goods or services. The Hon‟ble Supreme Court of India in the case of **M/s. Consolidated Construction Consortium Limited v. M/s. Hitro Energy Solutions Private Limited**[9] has held that the definition of "operational debt" contained in Section 5(21) of the IBC means a claim in respect of the provision of goods or services. Hence, the operative requirement is that the claim must bear some nexus with the provision of goods or services, without specifying who is to be the supplier or the receiver. The judgment further goes on to state that the aforesaid interpretation is also in consonance with the observations in the Bankruptcy Law Reforms Committee Report (November 2015), which specifically states that operational debt is in relation to operational requirements of an entity. Accordingly, the Hon‟ble Supreme Court opined that the phrase „in respect of‟ contained in Section 5(21) of the IBC has to be interpreted in a broad and purposive manner in order to include, within the ambit of operational creditor, all those who provide or receive operational services/ goods from the corporate debtor.

[9] *M/s. Consolidated Construction Consortium Limited v. M/s. Hitro Energy Solutions Private Limited*, (2022) 7 SCC 164.

IV. M. RAVINDRANATH REDDY AND PROMILA TANEJA DOES NOT LAY DOWN THE CORRECT LAW

The Hon'ble NCLAT vide the judgement overruled its own judgements in the case of M. Ravindranath Reddy and Promila Taneja ruling that the said judgements does not lay down the correct law. The Hon'ble NCLAT in the case of M. Ravindranath Reddy relied on the term "essential goods or services" which is defined under Regulation 32 of the Insolvency Resolution Process for Corporate Persons Regulation, 2016.[10] The Hon'ble NCLAT observed there has to be a nexus between the direct input to the output produced by the corporate debtor to be considered as an operational debt.

The Hon'ble NCLAT in the present case held that this observation is a much wider observation which is not supported by the scheme of the IBC. The Hon'ble NCLAT held that the reliance on the term "essential goods or service" under Section 14(2) is invalid as it gives a stricter meaning while the expression of "services" under the definition of "operational debt" is wider than that. Moreover, the judgement in the case of M. Ravindranath Reddy does not consider the extent and expanse of the expression "service" used in Section 5(21) of the Code.

The Hon'ble NCLAT in the case of Promila Taneja held that the definition of "service" under CPA and CGST Act, 2017 is not covered under section 3(37) of the IBC. Therefore, they cannot be imported while interpreting the expression "services" under Section 5(21) of the IBC. However, in the present case the Hon'ble NCLAT held that the Services Agreement itself contemplates payment of GST for the services under the Agreement, on which GST is payable, the definition of "service" under CGST Act, 2017 cannot be said to be irrelevant. Moreover, relying on the case of ***Keshavlal Khemchand***

[10]Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016, Regulation 32 (India).

and Sons Private Limited and Others v. Union of India and Others[11] even if an expression is not defined in the statute, the meaning of expression in general parlance has to be considered for finding out the meaning and purpose of expression. This in turn means that Section 3(37) is not restrictive in nature. The meaning of terms not defined under the IBC but defined in other Acts, can be imported from Acts other than those mentioned in Section 3(37) on case to case basis.

However, the appeal filed against the judgement in the case of Promila Taneja is still pending before the Hon"ble Supreme Court of India. Therefore, final position of law is yet to be decided by the Apex Court which will settle the issue entirely.

V. CONCLUSION

The five-member bench of the Hon' ble NCLAT *vide* the judgement endeavors to settle highly debated issue by considering license fee as operational debt under Section 5(21) of the IBC. Moreover, the Ministry of Finance *vide* the Notification No. 05/2022-Central Tax (Rate) dated July 13, 2022 included renting of immovable property to a GST registered person or business as service who are required to pay 18% GST on the rent.[12] However, the aforementioned judgement is slightly contrary to the said notification as it also includes renting of residential property within the ambit of services. However, the judgement in the present case considers "services" as granting the premises for a particular kind of use for a commercial activity. Therefore, this complete reliance on the definition of "services" as per the CGST Act, 2017

[11] *KeshavlalKhemchand and Sons Private Limited v. Union of India*, (2015)4 SCC 770.
[12] Ministry of finance (Department of Revenue), Notification No. 05/2022, Central Tax (Rate) (Jul. 13, 2022).

because the License Agreement contemplated for the payment of GST is not a plausible reasoning in light of the said notification. While the final appeal against the judgement in the case of Promila Taneja is yet to be decided by the Supreme Court of India, the judgement of the five-member bench in the present case still stands as the current position of law.

SCHOLASTICUS

Aviral Jain, *Examining the Enforceability of Settlement Agreements under the Insolvency and Bankruptcy code, 2016,* 10 (2) SCHOLASTICUS 45 (2023).

EXAMINING THE ENFORCEABILITY OF SETTLEMENT AGREEMENTS UNDER THE INSOLVENCY AND BANKRUPTCY CODE, 2016[1]

Abstract

*A recent judgment by the NCLT Bench of Delhi in the case of **Ahluwalia Contracts (India) Limited v. Logix Infratech Private Limited** reintroduced to the world the dilemma of breach of settlement agreements and its applicability under the Insolvency and Bankruptcy Code, 2016.The benches across the country have been holding conflicting opinions regarding the admissibility of breach of settlement agreements as a base for initiating the Corporate Insolvency Resolution Process ("**CIRP**"), but there is no definite answer which the law provides. The aim of this research paper is to dive deep into the discussion of the eligibility of settlement agreements and provide conclusive evidence to support the different viewpoints surrounding this topic.*

*.Aviral Jain is a second-year law student at Jindal Global Law School, O.P. Jindal Global University, Sonepat and he may be contacted at aviralnatishay0721[at]gmail[dot]com.

I. INTRODUCTION

The Insolvency and Bankruptcy Code, which came into effect in 2016, guides the insolvency and bankruptcy proceedings of the corporate firms, partnerships and individuals. This code creates a consolidated structure to govern and direct the organization which fails to pay back their creditors.

The subject matter of this code covers various aspects pertaining to companies which become insolvent and fail to pay back their creditors, yet there are few exceptions where it fails to provide with a solution to the conflict arising out in these cases and one of those includes the settlement agreements formed between the creditor and the corporate debtor to settle any claims which the corporate debtor owns.

Recently this scenario surfaced and brought back the debate relating to this issue in a judgement delivered by the New Delhi bench of the National Company Law Tribunal ("**NCLT"**) in ***Ahluwalia Contracts (India) Limited v. Logix Infratech Private Limited***[2]. The NCLT analysed that the default under settlement agreements between the parties does not constitute an „operational debt" for the purposes of Insolvency and Bankruptcy Code, 2016 (IBC) which commences the Corporate Insolvency Resolution Process ("**CIRP**") which is used to determine if the company is in the position to pay back its loans and liabilities or not

This judgment, one of many, offers the judiciary"s point of view on the right of the creditors in regards to initiation of CIRP right after the breach of settlement agreements by the operational debtor.

This paper focuses on providing an insight on the validity of the settlement agreements between the creditors and the debtors and its enforceability under the IBC, 2016.

[2]Ahluwalia Contract (India) Limited v. M/s Logix Infratech Private Limited, CP No. (IB) 882/ND/2022.

II. INSOLVENCY AND BANKRUPTCY CODE, 2016[3]

In layman‟s terms, insolvency and bankruptcy are used interchangeably, yet there is a major difference between them. Insolvency, on one hand, refers to the state of being insolvent or a state where you fail to pay the creditors their money back. On the other hand, bankruptcy refers to the state of being bankrupt which could be described as a legal proceeding involving a person or a business that is unable to pay their dues and debts.[4]

The Insolvency and Bankruptcy Code, 2016, formally introduced by the Parliament of India in 2016 by the act No. 31 of 2016, provided with a proper framework relating to the matters of insolvency and also with the guidelines and procedure to be followed in the case of bankruptcy.

The highlight of the Code is the institutional framework it envisions. The regulatory body (Insolvency and Bankruptcy Board of India), insolvency experts, information services, and adjudicative authorities (NCLT and National Company Law Appellate Tribunal-NCLAT) make up this system. These organisations and structures support corporate governance while facilitating a formal, time-bound settlement of insolvency. A two-step method for corporate debtor bankruptcy resolution is one of the Code‟s main elements. One process introduced by the code is – Insolvency Resolution Process under sections 6-32 of the code, in which the creditors play a vital role in evaluating and ultimately determining whether the debtor‟s business can be continued and what are the choices for its revival.

[3]Insolvency and Bankruptcy Code, 2016, No. 31, Acts of Parliament, 2016 (India).
[4]Alicia Tuovila Bankruptcy Explained: Types and How it works, Investopedia, available at:https://www.investopedia.com/terms/b/bankruptcy.asp.

According to the code‟s Statement of Objects and Reasons [“**the Code”**][5], the Legislature believed the pre-existing structure for insolvency and bankruptcy was insufficient and ineffective and caused unnecessary delays in resolution. The Code was proposed with the aim of harmonizing and amending the laws pertaining to the reorganisation and insolvency resolution of corporate persons, partnership firms, and individuals in a timely manner in order to maximise the value of such persons‟ assets, to promote entrepreneurship, availability of credit, and balance the interests of all stakeholders, including alteration in the priority of payment of Government dues.

The new rule promises a better and less painful process for reorganising or restructuring a company‟s debt. It also promises to accelerate the liquidation of a failing company and effectively recover creditors‟ investments. The much-needed and much expected creditor-driven bankruptcy and insolvency resolution process has been put in place, owing to IBC. The adoption of the new code represents a historical shift in the economy of the nation, its effect will be seen in years to come and will depend on the infrastructural support and capacity of the implementing authorities and newly formed protocols.

III. SETTLEMENT AGREEMENTS

A settlement agreement is a legal contract that is formed between two parties which legally binds them into performing the activity as directed by the agreement. After negotiations but prior to a final judgement, parties can come to a mutual agreement to an outcome for the case and enter a legally binding contract, known as settlement agreement[6]. This type of agreement is necessary in order to settle any discrepancy between the parties where both of them agree to some common purpose or a negotiation, which directs the functioning of

[5]Short Note on Insolvency and Bankruptcy Code, 2016,IBC Laws, July 30, 2019, available at: https://ibclaw.in/short-note-on-insolvency-and-bankruptcy-code-2016/**.**

[6]Arpan Banerjee, Settlement Agreements, JUS MUNDI),available at:https://jusmundi.com/en/document/publication/en-settlement-agreement.

both the parties in accordance to the agreement to which they both agreed upon.

The purpose of the settlement agreement is to serve as an alternative to settling a dispute instead of taking the matter to the court. With this type of agreement, one party must complete an action or pay a certain amount in exchange for the other party‟s promise to stop legal proceedings. Some situations wherein this agreement could be employed include-

A. **Property claims**
B. **Employment disputes**
C. **Default in repayment**
D. **Marital issues, etc.**

With any settlement agreement, initially there is a need to have negotiations in order to agree on certain provisions. In some corporate settlements, one party may only agree to settle if no wrongdoing or liability must be admitted. Some settlement agreements may also have conditions, such as how long a party has to fulfil his or her contractual obligations.

The courts have the authority to enforce settlement agreements between the parties in the case. A settlement agreement once signed by the relevant parties is a legally binding contract if all the terms are deemed valid. The court may adopt the agreement and incorporate it into a judgment or decree; however, the court cannot add substantive terms to the agreement. The court must accept the terms on which the parties have settled their dispute. The court‟s obligation is to construe and enforce contracts as made, not to make them for the parties[7].

[7]NeelabhNiket, Scrutinizing the Status of Settlement Agreements under the IBC, INDIACORPLAW, available at: https://indiacorplaw.in/2022/06/scrutinizing-the-enforceability-of-settlement-agreements-under-the-ibc.htm.

IV. CORPORATE INSOLVENCY RESOLUTION PROCESS (CIRP)

Any organization is declared insolvent if they are unable to pay back their dues to its creditors and that the cash flow depicts lack of cash. There are two tests to determine for corporate insolvency:

1) **The Cash Flow Test** - It is the determination of the current and future situations of the organization by determining if either they will be able to pay their debts orwill fall short in the payment by analysing the cash flow of the organization[8].
2) **The Balance Sheet Test** – It determines the ability of the organization to clear its debts by a careful analyzation of the balance sheet of the organization. If the assets of the company fall short of the liabilities reflected on the financial statements, then they will most probably fall short in paying back their dues[9].

CIRP plays a crucial role in determining the future of the organization. It is a recovery mechanism process for creditors, which can be initiated by the creditors or the debtors themselves in order to analyse if the organization which has defaulted is capable of paying back its loans and liabilities and that the creditors are paid back by the organization. This framework is placed with greater importance as it determines if the company is capable enough or it requires restructuring or liquidation.

The Insolvency and Bankruptcy Code, 2016 is the act which covers and lays down the ground rules for the Corporate Insolvency Resolution Process. This act provides with the framework starting from the necessities to be fulfilled for a company to be considered for this process to the application process of this process.

[8]Handbook on Corporate Insolvency Resolution Process under The Insolvency and Bankruptcy Code, 2016: ICAI. (2021), Consultease,available at:, https://www.consultease.com/icai/handbook-corporate-insolvency-resolution-process-insolvency-bankruptcy-code-2016icai/#.Y3ZDRXZBw2w.
[9]*Id.*

However, this code also directs a differentiation between the types of creditors and guides as to which creditor has the access to substantiate this process through which specific procedure.

1) **Financial Creditor**: A financial creditor, under section 5 (8) of the code[10], is defined as a creditor who owes the corporate debtor a sum of money as a debt which is to be received from the debtor along with the interest. Banks and other financial institutions are considered as examples of the same.
2) **Operational Creditor**: An Operational Creditor, as per section 5(20) of the code[11], is defined as a creditor who owes the corporate debtor any operational debt which includes the claim in respect of the goods and services, in respect to employment or in respect to any debt payable to the Government. Vendors and suppliers, employees and government are considered as examples of the same.

These creditors have the autonomy to file for the CIRP against its debtors in order to claim the sum the corporate debtor has defaulted but not so in the case where there is presence of any kind of settlement agreements over that sum.

V. OPERATIONAL CREDITOR

In the case of default, any operational creditor may file for CIRP under the section 9 of the code[12], which guides that after the expiry of the notice of unpaid operational debtor, a copy of an invoice demanding payment of the unpaid amount, is to be filed under section 8 of the code, under the Adjudicating Authority. The section defines every pathway of filing and the necessary guidelines for the same.

[10]Insolvency and Bankruptcy Code, 2016, § 5(8), No. 31, Acts of Parliament,2016(India).
[11]*Id* at § 5 (20).
[12]*Id* at § 9.).

The code specifies that, while filing for CIRP, a proof of default is necessary.[13] The documents pertaining to default includes a copy of the invoice demanding payment or demand notice delivered by an operational creditor, affidavit stating no dispute of the debt has been raised by a corporate debtor and a copy of certificate from financial institution, record with information utility or any proof, confirming that there is no payment of unpaid debt.

The code provides the parameters to be followed in most of the scenarios, but is silent on the eligibility of settlement agreements in filling for the CIRP by the creditors. As it has been established that the need for filing of the corporate insolvency resolution process arises in the situation where there is a breach of the settlement agreement by the corporate debtor for returning the sum of money borrowed from the creditor.

This scenario was clearly established in the Ahluwalia case, as the operational creditor was refused the right to sue the debtor for insolvency and hence file for CIRP when the debtor failed to pay the agreed amount to the creditor.

A. Ahluwalia Contracts (India) Limited v. M/s Logix Infratech Private Limited[14]:

The case followed that Ahluwalia Contracts, being an operational creditor, brought suit before the NCLT Delhi Bench for filling for the Corporate Insolvency Resolution Process because the corporate debtor, Logix Infratech, failed to pay the sum money of Rs. 11,00,00,000/- in six instalments along with 7 flat/inventories. However, the corporate debtors failed to pay the six instalments, as mentioned in the settlement agreements, even after repeated reminders from the creditors to which they responded providing reasons such as fall of housing market as well as other unprecedented circumstances like environmental restrictions and Covid-19 due to which they faced heavy losses and were falling short of the money they agreed to return. The judgement noted

[13] *Supra*note 3.
[14] *Supra* note 2.

that the default in the payment of settlement agreements does not come under the definition of Operational Debt and hence does not hold any ground for initiation of the insolvency resolution process.

Now, this judgment set the message clear that the breach of settlement agreements and default by the debtor is no valid reason for filing of the resolution and that various precedents supporting this case reflect on the validity of settlement agreements and the role it plays in the eyes of judiciary.

B. M/s Delhi Control Devices (P) Limited v. M/s Fedders Electric and Engineering Ltd.[15]:

This matter brought up before NCLT Allahabad notes that the corporate debtor failed to pay the second instalment of the money borrowed from the operational creditor as the settlement agreement directed, which led to the action being brought up against the debtor, as creditor filed for the CIRP of the debtor as he failed to pay the money. In this case, the bench made a judgment in favour of corporate debtor and rejected the application of the operational creditor, as they noted that a demand notice was issued before the settlement agreement was formed, which meant that the demand notice was already withdrawn and that a demand notice is necessary for filing the application for initiating the procedure of CIRP. Also, the judgement that breach of settlement agreement cannot be treated as an operational debt resulted in the same.

This case provides with the perfect precedence for the analysis of the Ahluwalia case, as it is noteworthy that the judgement of this case mentions that the failure of or breach of settlement agreement between the parties can‟t be used as a ground for CIRP against Corporate Debtor as its remedy may lie somewhere else and not necessarily before the Adjudicating Authority.

[15]M/*s Delhi Control Devices (P) Limited v. M/s Fedders Electric and Engineering Ltd*., CP No. (IB) 343/ALD/2018.

C. Brand Realty Services Limited v. Sir John Bakeries Indian (P) Limited[16]:

In this case, a settlement agreement existed between the parties seeking investment and consultancy services, but the corporate debtor failed to pay the dues of the creditor as per the agreement. Consequently, the NCLT then referring to several precedent including that of *Delhi Control Devices (P) Ltd v. Fedders Electric and Engineering Limited*, held that the debt due in terms of a settlement agreement cannot be considered as an operational debt in terms of section 5(21) of IBC and hence unpaid instalments under the settlement agreements do not suffice to trigger resolution process against a corporate debtor.

This case, strengthens the fact that National Company Law Tribunals are of the viewpoint that the settlement agreements are not considered a strong proof, as per the Insolvency and Bankruptcy Code, 2016, to start the process of CIRP against a corporate debtor, as they fail to pay the instalment(s) as per the recorded settlement agreements which exists between the operational creditor and the corporate debtor.

VI. FINANCIAL CREDITOR

In case of default, a financial creditor may file for CIRP under section 7 of the code read with rule 6, which guides that in case of default which includes any financial debt, the financial creditor can file for application of Corporate Insolvency Resolution Process. It provides guidance to the financial creditors with the process and guidelines which needs to be followed in filing for the same under the Adjudicating Authority.

As per the guidelines[17], while filling for CIRP under the IBC, 2016, the applicant needs to show the proof that there has been a default in paying back

[16] *Brand Realty Services Limited v. Sir John Bakeries Indian (P) Limited*, (IB) 1677(ND)/2019.

the financial debt with information utility or other record or evidences of default as specified and the name of the proposed interim resolution professional. To invoke CIRP, it is necessary that default is specified under the definition of financial debt as per the section 5 (8) of the code[18].

However, following the same scenario as in the case of Operational Creditor, the code fails to provide any definite response to the question of settlement agreements and its application in the process of CIRP. The code remains silent on what and how should the authority act on the case when the default is on the payment of the instalment as per the settlement agreement by the corporate debtor.

The financial creditors face a lot of unfavorable and heavy losses just because the adjudicating authorities issue orders which denies the claims to commence CIRP based on a settlement agreement. This scenario can be evidently seen in various cases such as-

A. Amrit Kumar Agrawal v. Tempo Appliances Pvt. Ltd.[19]:

In this case the NCLT, Delhi Bench denied the claims of the appellant to file for corporate insolvency resolution process, as they found that the default in payment according to the settlement agreements does not come under the definition of financial debt, according to the section 5(8) of the code which defines the same. They analysed that mere obligation to pay does not bring the liability within the ambit of „financial debt" which is the main necessity of filings for CIRP by financial creditors to recover their pending amount from the corporate debtor.

[17]*supra* note 3.
[18]*supra* note 10.
[19]*Amrit Kumar Agrawal v. Tempo Appliances Pvt Ltd*, Company Appeal (AT) (Insolvency) No. 1005 of 2020.

In the same way the authorities dismissed the claims in the case of ***NidhiRekan v. Samyak Projects Pvt Ltd***[20], which witnessed the ruling that the appellant being a speculative investor cannot file for the CIRP as he is not a financial creditor and that the money owed to them does not come under the definition of a financial debt, thus dismissing the claims.

B. Mphasis Limited v. Strategic Outsourcing Service Pvt Ltd[21]:

The appellant filed for the Corporate Insolvency Resolution Process under the IBC, as the corporate debtor failed to pay the advance payment of Rs. 4 crores, as per the settlement agreement before the NCLT Bengaluru Bench. The bench rejected the petition on regard that the CIRP cannot be invoked for recovery of outstanding payment but in case of insolvency. They used *Mobilox Innovations Private Limited v. Kirusa Software Private Limited*[22] as a precedent to highlight the fact that IBC is not intended to be a substitute to a recovery forum. A part of this judgment was substantiated by the fact that advance payment does not come under the definition of financial debt, as per the code.

This ruling by the NCLT solidifies the claims that even though a settlement agreement exists between the parties, what is actually necessary is establishing the fact that corporate debtor defaulted in pay the financial debt, which repeatedly have been identified as different from default in paying the instalments as per the settlement agreement. The different views of different NCLT benches regarding the interpretation of the definition of financial debt with respect to settlement agreements is an indication of the complexity of the code and the various ways in which it can be interpreted.

[20] *Nidhi Rekhan v. Samyak Projects Pvt Ltd*, Company Appeal (AT) (Ins) No. 1035 of 2020.
[21] *Mphasis Limited v. Strategic Outsourcing Services Pvt Ltd*, C.P. (IB) No. 233/BB/2018.
[22] *Mobilox Innovations Private Limited v. Kirusa Software Private Limited*, Civil Appeal No. 9405 of 2017.

C. Arenja Enterprises (P) Ltd. v. Edward Keventer (Successors) (P) Ltd.[23]:

In this case, the issue arose whether the terms of consent decree tantamount to a financial debt. The NCLAT opined that, as per section 5(8)(f) of the IBC, the appellant could claim a financial debt only when the amount raised from it as an allottee is used for a real estate project. Based on the facts and the findings, it was held that the appellant could neither be termed as an allottee nor has any amount been raised from the appellant that could constitute to have effect of a borrowing thus dismissing the claim of invoking CIRP against the corporate debtor.

This case has reflected that the position of law is that a debt based on a consent decree would not be treated as a financial debt, even under the context of real estate projects.

This has been clearly established before that the NCLT Benches are of the view that the breach in settlement agreements is not really considered as an acceptable form of proof for starting CIRP against a corporate debtor by an operational creditor, andthese judgments extend the same result in the case of financial creditor invoking the CIRP as well. This point of view by the judiciary is something which is hampering the financial creditors hopes of recovering the sum due to the corporate debtor through the Insolvency and Bankruptcy Code, 2016.

[23] *Arenja Enterprises (P) Ltd. v. Edward Keventer (Successors) (P) Ltd*., Common Appeal (AT) (Insolvency) No.528 of 2020.

VII. THE CONFLICTING POINT OF VIEW

One thing which is noteworthy is that NCLT does not always hold their point of view of dismissing the appeals for initiating the procedure of CIRP by operational and financial creditors against the corporate debtor. The bench sometimes finds that the breach in the settlement agreement can be a basis to file for insolvency resolution procedure in order to recover the sum owed to the corporate debtor.

This contention can be seen in the following cases-

A. M/s SEW & Prasad – Joint Venture v. M/s Gati Infrastructure Private Limited[24]:

The case was filled by the appellant for initiating the process of Corporate Insolvency Resolution Process before the Hyderabad Bench of NCLT, against the debtor for multiple defaults in repayment of instalments under section 9 of the code. The bench ordered in favour of the petitioner as the bench was of the view that the petition for CIRP deserved to be admitted and the law as required to be complied with regard to the provision of the Insolvency and Bankruptcy Code shall follow.

In this case, we saw the adjudicating authority admitting the case under the section 9 of the IBC on the basis of the default in payment of instalments as directed by the existing settlement agreements between both the parties – operational creditor and corporate debtor.

B. Mahesh Kumar Panwar v. Neelam Singh[25]:

The case was filed by the appellant against the corporate debtor as the debtor defaulted in repayment of the debt. In this case, the bench was of the opinion that the appellant was a financial creditor as the debt against him was coined the term financial debt, completely fulfilling the requirements of being one, as

[24] *M/s SEW & Prasad – Joint Venture v. M/s Gati Infrastructure Private Limited*, CP (IB) No. 227/9/HDB/2017.
[25] *Mahesh Kumar Panwar v. Neelam Singh*, 2018 SCC OnLine NCLAT 596.

directed by the IBC. The dishonoured cheques disclosed that the corporate debtor had committed default in payment of debt to the financial creditor and thus the application was accepted.

This trend shows the conflicting nature of the NCLT Benches who at times dismiss the appeals for invoking the Corporate Insolvency Resolution Process as per the IBC, 2016, meanwhile, admits some of the claims and allows for the same. This inconsistency in the procedure and multiple ways of interpreting the laws makes the process cumbersome and inconsistent.

The defence to this inconsistency can be that majorly it depends upon the facts and findings of the case which differs from each other, which fails the precedential value of benchmark cases. A few benches may find that the settlement agreements between the parties and the default caused under those agreements is covered under the scope of Insolvency and Bankruptcy Code, meanwhile at times the findings of the bench might be the exact opposite which supports the conflicting nature of the results of the appeals of cases under the breach of settlement agreements.

VIII. CONCLUSION

Even after more than 6 years of implementation of the Insolvency and Bankruptcy Code, 2016, it is still unclear as to various aspects of this code and its implementation. Among many exceptions, the settlement agreements continue to play the bigger part of puzzling the adjudicating authorities upon the implementation of the code and making the decisions under the purview of those laws.

It wouldn‟t be wrong to state that the scope of settlement agreements is yet to be defined under the Insolvency and Bankruptcy Code, 2016. The Corporate

Insolvency Resolution Process or CIRP, as mentioned, is the process which holds immense importance for any corporate debtor as it is something which will have a direct effect on the future of his organization. However, the position with respect to a settlement agreement constituting a financial or an operational debt is still divergent and conflicting, when it comes to it being necessary for initiation of the CIRP.

Considering the above judgements, one thing has been made crystal clear that in order to decide whether the settlement agreement or any other similar arrangement is admissible for the purpose of initiating insolvency proceedings, the adjudicating authority must consider the history and the nature of the debt owing to the creditors. As a general rule, agreements that are supported by a commercial loan or a right to payment that results from the provision of products and services under the terms of the agreement are permitted to serve as the foundation for the start of a CIRP. The Supreme Court's clear explanation on the subject would undoubtedly put an end to the controversy and make things easier.

SCHOLASTICUS

Bhavika Verma& Krishna Pal Singh Bhati, *Fintech Unicorns in India: Analysing and Predicting the Future*10(2) SCHOLASTICUS 61 (2023).

FINTECH UNICORNS IN INDIA: ANALYSING AND PREDICTING THE FUTURE

Bhavika Verma[⊥]& Krishna Pal Singh Bhati[ø]

Abstract

FinTech's have grown into a multi-billion-dollar industry. Due to the pandemic hampering the conventional methods of transactions have been substituted by digital transactions which has led to this extraordinary upsurge in recent times. The import of the word Fintech can be quite simply explained as Financial Technology consisting, it comprises an array of goods services and technology that is transforming the Indian landscape, In the article the authors first introduce the concept comprehensively , its evolution in the global landscape, tracing its origins in the west and its eventual percolation all over the world including Asia and particularly India, the authors shall try and analyze various regulations which govern FinTech's in India and what are the lacunas in the existing framework, highlighting how financial inclusion and empowerment, infrastructural support and tax reliefs by the govt. can go a long way in sustaining the growth of these Fintech Unicorns. The role of various regulators including NCPI, RBI and other statutes has been critically analyzed. Lastly a thorough analysis on the future of Fintech is made looking into the lacunas in the present framework, while also assuming a positive and cheerful position, identifying key areas with the greatest potential and suggesting changes which will create an inducive environment for Fintech Unicorns in the country.

[⊥]BhavikaVerma is a third-year undergraduate law student at National Law University, Jodhpur; and may be contacted at bhavika[dot]verma[at]nlujodhpur[dot]ac[dot]in.

[ø]Krishna Pal Singh Bhati is a third-year undergraduate law student at National Law University, Jodhpur; and may be contacted at krishanpalsingh[dot]bhati[at]nlujodhpur[dot]ac[dot]in.

I. INTRODUCTION

During the 2008 financial crisis, the financial system suffered huge loss and events that dramatically modified the banking industry and gave rise to previously unheard-term i.e. financial institutions known as *fintech*. The term "FinTech" is short for "financial technology" and could apply to any kind of technology that is used to drive a financial transaction or service, offered by any entity.[1] However, in business and regulatory jargon, FinTech has come to mean the technology used by financial service providers that disrupt the traditional way of providing such services. Thus, businesses such as PayTM, PhonePe, RazorPay, MobiKwik, PayU are all classified as fintech businesses.[2]

Furthermore, banks and other financial institutions have always been on the cutting edge of using technology for business purposes. This is partly driven by the desire to reduce costs while also providing better customer service. Automatic Teller Machines ("**ATMs**") became popular, as did telephone banking, which allows customers to conduct a variety of financial transactions over the phone that do not involve cash or financial instruments (such as checks) without having to visit a bank branch or ATM. Internet banking emerged as internet usage increased. ICICI introduced internet banking to India in 1998.[3] As simple mobile phones gave way to smartphones, mobile banking gained traction. Telephone banking and internet banking must be distinguished from mobile banking. Customers use mobile banking to conduct financial transactions remotely, using a smartphone and an application developed by the relevant bank.

---

[1]Aaron C. F. Salerno, *Regulating the Fintech Revolution: How Regulators Can Adapt to Twenty-First Century Financial Technology*, vol. 75, N.Y.U. ANN. Surv. AM. L.,pp. 365-391 (2020).

[2]Dr. Neeta Tripathi &Iqra Tabassum, *Growth of Fintech Unicorns in India: Recent Trends,*vol.22(B1),GLOBAL JOURNAL OF MANAGEMENT AND BUSINESS RESEARCH: B ECONOMICS AND COMMERCE,pp.19-31 (2022).

[3]ICICI Bank.com, *About us: History, India*, available at: https://www.icicibank.com/about-us/history (last visited Jan. 19, 2023).

In December 2007, the Payment and Settlement Systems Act, 2007 ("**P&SS Act**"),[4] was enacted to provide for the regulation and supervision of payment systems in India. The Reserve Bank of India is designated as the authority for such purposes by the P&SS Act. A "Payment System" is defined as a system that allows payment to be made between a payer and a beneficiary, involving clearing, payment, or settlement services, or all of them, but excluding a stock exchange.[5] Section 4 of the P&SS Act [6] states that in order to start or operate a payment system, an authorisation issued by the RBI is required. Payment systems include systems that enable the use of credit or debit cards, smart cards, and prepaid payment instruments.

Huge technological developments have created the possibility to provide services that were not even imaginable until a few years ago from digital wallets for payment (e.g., PayPal),[7] to cryptocurrencies (e.g., Bitcoin),[8] to investment advice through automated algorithms (e.g., "Robo advice") and many more.[9]

This article tries to analyse fintech unicorns in India. The article is divided into four parts. Firstly, the evolution of fintech in India, Secondly, the rise of fintech in finance, thirdly, the regulatory framework with regard to fintech unicorns in India, fourthly, what impact did Covid 19 has on fintech market and India"s current position with regard to fintech unicorns and lastly, the authors have tried to analyse future of these financial institutions.

[4]The Payment and Settlement Systems Act, 2007, § 4, No. 51, Acts of Parliament,2007 (India).).
[5]Reserave Bank of India , Frequently Asked Questions (Updated as on November 22, 2022), available at:https://m.rbi.org.in/scripts/FAQView.aspx?Id=73#:~:text=Section%202(1)%20(i,states%20that%20its%20provisions%20will.
[6]*supra* note 4.
[7]Robert Woroch, Gero Strobel et al.,, *Four Shades of Customer: How Value Flows in Fintech Ecosystems,* INTERNATIONAL CONFERENCE ON INFORMATION SYSTEMS,(2022)..
[8]*Id.*
[9]*Id.*

II. EVOLUTION OF FINTECH IN INDIA

The advent of online banking, ATMs, credit cards, EMI choices, the internet, and many other things has resulted in a revolution of major change. There have been reports of investments in the nation‟s fintech sector totalling about $8 billion.[10] India has the third-largest fintech ecosystem in the world with an adoption rate of 87% compared to the global average of 64% for fintech.[11] In the last five years, more than 1400 companies have been associated in fintech.[12]

The fintech industry has developed as a result of how quickly India's urban areas are adopting digital lifestyles. Fintech companies are expanding, placing India at the top of the fintech industry due to its growth and ability to adapt to new technology.

Studies have also been showing how India is the future of fintech by some statistics and the example of a significant Indian fintech start up - Paytm: The value of Fintech transactions is expected to increase from US$ 66 billion in 2019 to US$ 138 billion in 2023.[13] A start-up company with a value of over $1 billion is known as a unicorn, and there are reportedly more than 17 fintech companies in India.[14]

For instance, Paytm is a trailblazer in India's fintech sector. It is a worldwide financial corporation that offers banking, e-commerce, and digital payment technologies. The company's overall revenue as of 2021 was 3,187.6 crores INR (420 million US dollars).[15] It is the most widely utilised platform in India and is used for a wide range of financial transactions, including online payments,

---

[10]Douglas W. Arner, Janos Barberis et el.,, *The Evolution of FinTech: A New Post-Crisis Paradigm*, vol. 47, GEO. J. INT'l L,.pp. 1271-1316 (2016)..
[11]*id.*
[12]*Supra* note 1.
[13]Fintech Today, *India Becomes the World's Third Largest Fintech Centre as Investments Doubled*, PAYTM BUSINESS BLOG (2021), available at: https://business.paytm.com/blog/india-becomes-the-worlds-third-largest-fintech-centre-ft/).
[14]Vanya Gautam, *17 Indian Companies that have Turned Unicorns in 2022,* INDIATIMES, Jun 13, 2022, available at: https://www.indiatimes.com/worth/news/indian-companies-that-became-unicorns-this-year-572038.html.
[15]*Supra* note 13.

bookings, loans, and credit cards. Since its founding in 2010, it has grown from a $2 billion firm to a successful one that generates income.[16]

Because of the rapid growth of technology, regulators are finding it difficult to keep up with the most recent technical advancements in order to adjust the fintech rules effectively. In order to establish policies that improve service without jeopardising security, regulators and policymakers must be aware of the most recent advances in fintech. As fintech expands, potential hazards including fraud, breaches, and cybersecurity concerns are on the rise. New payment mechanisms and models may jeopardise market security and integrity. Customers who are uninformed of the risks or who are unwilling to accept them may be sold new products and services. The hazards of fraud and hacking for Distributed Ledger Technology ("**DLT**"), blockchain, and crowdfunding is increasing.

These services are highly regulated globally due to the hazards associated with the finance industries. The growth of the fintech sector in India has been promoted admirably by the Indian regulators, and this momentum will be required for even more radical and prompt regulatory actions in the future. For Indian authorities, it may be difficult to strike a balance between the expansion of the complex regulatory framework and the management of the rapidly expanding Indian fintech industry. They might work to put in place some of the recognised worldwide regulatory rules in order to get around this. For instance, Financial Conduct Authority ("**FCA**") created "Project Innovate" in the UK as an initiative to help companies work with British financial regulators to create innovative goods for the market.[17]

---

[16]*Id*.

[17]RohitGajbhiye, *Evolution of fintech in India and Investors' Attitude*, TIMES OF INDIA BLOG, August 13, 2022, available at:https://timesofindia.indiatimes.com/blogs/voices/evolution-of-fintech-in-india-and-investors-attitude/.

A. What Makes a Top Fintech Unicorn?

A privately held start-up company valued at more than $1 billion is referred to as a "unicorn". The phrase "unicorn" is frequently used in venture capital firms. Aileen Lee, a venture capitalist, was the first to use the term.

Razorpay's valuation of $7.5 billion places it at the top of the list of fintech unicorns in India.[18] Following the payments gateway unicorn is CRED, which recently raised $140 million, bringing its valuation to $6.4 billion.[19]PhonePe, Pine Labs, and Paytm round out the list of five fintech unicorns worth over $5 billion.[20]

Frequently, India's unicorns have been criticised for being unprofitable and lacking a path to profitability. In terms of profitability, only one-third of India's 21 fintech unicorns are in the black. The bootstrapped fintech unicorn Zerodha became India's most profitable fintech unicorn in FY21, reporting a profit of INR 1,122.30 Cr. Bill desk, MobiKwik, Oxyzo, Chargebee, Razorpay, and groww are the additional profitable unicorns.[21]

B. Rise of Fintech in Finance

FinTech‟s have exploded all over the world since the global financial crisis of 2007–2009.[22] There are numerous causes for this, including:

---

[18]HarichandanArakali, *India's maturing Fintech Ecosystem: Five Companies to Watch in 2023,*FORBES INDIA, Jan. 04, 2023, available at:, https://www.forbesindia.com/article/take-one-big-story-of-the-day/indias-maturing-fintech-ecosystem-five-companies-to-watch..

[19]BL Bengaluru Bureau, *Cred is Raising $140 M in Series F Funding Round*, THE HINDU BUSINESS LINE, Jun. 09, 2022, available at: , https://www.thehindubusinessline.com/companies/cred-is-raising-140-m-in-series-f-funding-round/article65511528.ece.

[20]Mishra, Digbijay. *Razorpay's Valuation Rises to $7.5 Billion After $375-Million Funding*, THE ECONOMIC TIMES, Dec. 20,2021, available at: economictimes.indiatimes.com/tech/funding/razorpays-valuation-rises-to-7-5-billion-after-375-million-funding/articleshow/88377247.cms.

[21]Hemant Kashyap, *The List Of Fintech Unicorns In India*, INC42 MEDIA, June 12 2022, available at: inc42.com/features/fintech-unicorns-in-india.

[22] Philippe Gelis& Timothy Woods, *The Rise of Fintech in Finance,* KANTOX, available at: https://cdn2.hubspot.net/hub/310641/file-1445626583-pdf/Rise_of_Fintech_in_Finance/Fintech_DEF.pdf.

i. **Resentment for the established banking system and the major players** - The popular perception remains that banks are exploiters of the poor and instruments to make the rich richer.

ii. **Loss of Confidence**- A general loss of confidence in banks following the crisis has developed. Following the crisis, banks ceased granting loans; businesses had to deal with denials of bank loans or credit lines, and individuals were denied home and personal loans.

iii. **The Internet Incentive**- Similar to how the music and newspaper industries were radically changed by the internet, our relationship with money is undergoing a drastic change as well. Fintechs have benefited from this and developed financial services based on the evolution of internet. Nowadays, people do financial transactions on their cellphones or tablets.[23] So, today, Fintechs use the internet to offer quicker and more affordable services.

iv. **The Banker's Dilemma**- Because it was more profitable for them to do so, banks resisted change for a long time. Since there has been little to no competition in the financial services market for such a stretch, they have been able to charge large commissions and frequently obfuscated or hidden fees, including inflated rate of foreign exchange spreads or cost of letter of credit. The question then remains why would they be encouraged to change and evolve when doing so will only result in lower profits, there is no incentive. Fintechs are aware of this and provide an efficient alternative, they do so, in addition to providing lower rates and open pricing.

v. **No priority investing**- The global banking system nearly fell apart during the Financial Crisis. Since 2008, a slew of new regulations that

[23] *Id.*.

banks must abide by have absorbed their attention.[24] It was not considered important to prioritise investing in new technologies or adjusting to the shifting financial situation. Because of this, banks are currently catching up to fintech in terms of technology. Fintech companies are raising the bar. One cause for this is the ongoing closure of high street branches by banks throughout Europe. Generations X and Y in particular are just not doing their banking in person any longer, and banks have so far been unable to engage customers online while fintechs have done so because this is where they excel.

III. FINTECH REGULATIONS IN INDIA

In India, the fintech industry's regulatory environment is extremely disjointed. Fintech services and products are not specifically subject to any laws or regulations in India. It is challenging to shape the regulatory environment when there is no clear set of regulations for fintech services, yet authorities recognised that India's fintech industry needed to be governed.

A. Payment and Settlements Systems Act, 2007

The primary piece of legislation controlling payments regulation in India is the Payment and Settlement Systems Act of 2007.[25] Without prior RBI approval, this statute forbids the establishment and operation of any "payment system" in India. Payment methods include money transfers, PPIs, smart card operations, credit and debit card operations.

A major lacuna in this statute remains, given that prepaid instruments do not cover credit card operations, and the lack of a regulatory system under the PSS Act, 2007, it is a very gray area especially for fintech companies. Since no such provision exists, it is assumed that credit card issuance is limited to only banks

[24] *Id*.
[25] *Supra* note 4.

and certain NBFCs. So a separate regulatory mechanism is the need of the hour. [26]

Only recently, the RBI had imposed a hefty fine of 5.93 Lakhs on a ObopayMoblie technology, a fintech firm, since the firm was not in compliance with the RBI rules. Section 30 of the PSS Act which confers on the RBI the power to impose fines on firms if they act in contravention to section 26 of the act, which means that is a firm wilfully withholds or lies about information which it was liable to furnish to the RBI, a penalty is imposed, this may either be 5 lakh rupees or two times the amount comprised in such a contravention, whichever is more.

B. UPI Procedural Guidelines[27] by the National Payments Corporation of India ("NPCI")

These guidelines govern the UPI payments in India, there are no specific sections and the guidelines are issued in form of circulars. This framework mandates that banks produce money transfer services over UPI systems, In the process of doing so, banks are free to hire technological companies to complete the task. The banks may work with technology suppliers to manage mobile applications for UPI payments, but only under the eligibility requirements and prudential standards outlined by the NPCI.

In order to further improve the regulatory mechanism, the Watal Committee‟s recommendation to categorise NPCI as a Critical Payment Infrastructure

[26]Anita Baid, *Overview of regulatory framework of payment and settlement systems in India,* VINOD KOTHARI CONSULTANTS, available at:https://vinodkothari.com/2017/04/overview-of-regulatory-framework-of-payment-and-settlement-systems-in-india-by-anita-baid/..

[27]National Payment Corporation of India, NPCI/UPI/OC No.4/2016-17 (Notified on August 12, 2016), available at: Circular04-Compliance-with-the-NPCI-Circulars-and-Procedural-Guidlines-of-UPI.pdf.

Company ("**CPCI**") should be followed. This will lead to more transparency as a well-established comprehensive mechanism exits for CPICs. [28]

Moreover, the NPCI which is a provider for payment network is also, in effect the sole regulator of the entire ecosystem, instead of publishing guidelines intermittently, perhaps a robust authority especially dedicated for Fintechs, under the umbrella and aegis of the RBI with a separate code for itself is desirable, given the rapid growth of Fintechs.

The above recommendation seems relevant, given the backdrop of the Bank of Maharashtra Fraud case in 2017, where a hefty 25 crores were fraudulently siphoned off through UPI, what is surprising is that although the account was without any funds, the said transaction was honoured by the system, this seriously highlights the need for a more effective technology to be put in place which is able to detect such fraudulent activities in the bud, the use of high end AI seems to be the solution, so a concerted effort to bring in fold the AI experts and engineers and a partnership with such firms to improve and evolve the technology in place must be prioritised.

C. RBI regulations and RBI Act, 1934

Earlier RBI had only a „fintech division" operating inside the DPSS, however a distinct „fintech Department" has been put in place only recently in January 2022. This department has been specially constituted for innovation and regulation in the Fintech industry. Since the department is at a very nascent stage it is too early to critique its activities.

All NBFCs are governed by the Reserve Bank of India Act of 1934[29]. Any firm offering fintech services in India must register with the RBI, as per its requirements. No NBFC may start or operate a non-banking financial

[28] *Supra* note 20.
[29] The Reserve Bank of India, 1934, No. 2, Act of Parliament, 1934 (India).

institution without first obtaining a certificate of registration from RBI, according to section **45-IA** of the RBI Act[30].

A major challenge is the lenders occupying the digital space, who are outside the regulation of the RBI and are incognito, offer ready and swift loans at an exorbitantly high interest rates. In view of the increasing fraud, RBI has made efforts to protect consumer information. Via a circular dated June 2020, every lending fintech firm is mandated to reveal the lender‟s information.

Apart from this, there exist separate guidelines for Payment Banks under which the payment banks do conduct banking business, but on a lower scale. Both loans and credit cards cannot be issued by it. Banks activities are also restricted by specific licensing conditions, especially when it comes to demand deposits acceptance and settlements.

D. Government Incentives

The role of the government is most definitely the main factor determining fintech's success or failure in a highly fragmented regulatory financial sector. The Indian government and institutions like SEBI and the RBI are actively pushing the Indian economy's goal to grow into a robust ecosystem and go cashless through funding and promotional initiatives.

The following strategy has been adopted to help penetration of the digitally enabled financial systems:

i. Financial empowerment and inclusion

The Indian government's StartUp India plan includes a USD 1.5 billion fund fo r start-ups. Aadhar has been expanded for pension, provident fund, and the Jan

[30] *id.*

Dhan Yojana, bringing over 200 million formerly unbanked people into the banking system. [31]

Recently, a comprehensive repository has been put in place called the central Know Your Customer ("**KYC**"), which comes as a massive relief to small companies who earlier had to undergo various KYCs for different institutions.[32] Government has also made strides in reducing the burden of compliance to incentivize the development of fintech companies, Whilst monitoring a whole mass of database related to compliance by fintech‟s a regulatory Compliance Portal was set up on January 2021, as an effect, 25,000+ requirements for compliance have been removed. [33]

„Regulatory Sandbox‟ has also been formed recently with a view to incentivize innovation and encourage efficiency. This sandbox enables field tests to be conducted in order to tab information on the benefits of these innovations, the security risks attached, how to contain such risks etc. It is a regulatory regime which is largely evidence based and therefore highly accurate and trustworthy.

ii. Relief from tax and surcharge

On this front, a few noteworthy initiatives include Tax credits for businesses who process more than 50% of their transactions online, rebates of 80% on startup companies' patent expenses, a three-year period of income tax exemption for new businesses, longer-term investments in unlisted companies are exempt from capital gains tax (from 36 months needed earlier).[34] Moreover, the Ministry of Finance has recommended eliminating the surcharge for using a credit card or online to pay for government services.

iii. Infrastructure support

---

[31]NehaPunater&Vidhya Shankar, *Fintech in India,* KPMG (2016), available at: https://assets.kpmg/content/dam/kpmg/pdf/2016/06/FinTech-new.pdf.
[32]*Key initiatives taken by the government for Fintech Ecosystem in India,*TAX GURU, Dec 15, 2021, available at:https://taxguru.in/corporate-law/key-initiatives-taken-government-fintech-ecosystem-india.html.
[33]*Id.*
[34]*Id.*

The initiatives such as *Smart Cities* and *Digital India* were started to encourage the growth of the nation's digital infrastructure and draw in international investment. The government is planning to open a special portal to make it easier for startups to register.[35] In addition there is newfound need for support for IP Facilitation, the government will assist start-ups with the costs of facilitators for their patent, trademark, and other design work.

The RBI has played a significant role in fostering the growth of the fintech industry in India and advocating a cautious approach to addressing worries about enforcement of the law and consumer protection. In India, payments, loans, security/biometrics, and wealth management are the primary fintech enabling sectors. These have been the RBI‟s primary areas of focus, and significant strategies for encouraging participation in fintech have been revealed.[36]

Instances of this would include advent of the "Unified Payment Interface" by the NPCI, which could radically change digital payments and bring India nearer to its ultimate goal of a "Less-cash" society. Only recently the govt authorised the formation of 10 small financial institutions and the authorization of 11 companies for the formation of payment banks, both of which can significantly advance the purpose of financial inclusion.

Although the strides made by government and the RBI for developing infrastructure for the highly dynamic fintech industry, incentivization for new startup companies is praiseworthy, the authors feel that with the emergence of new businesses in the Fintech industry, such haphazard and fragmented laws are insufficient, that too being an understatement. These are also not capable to cater to customer and user protection. The industry, it goes without saying,

[35] *Id.*
[36] *Id*.

requires greater reforms in order to create efficient and productive business structures which values privacy, data protection and also encourages new business models to emerge with ease. However, it is not appropriate to say that no concerted effort has been made in this regard, India‟s first holistic and comprehensive framework of data protection is already in place. This data privacy regime, and the RBI‟s growing focus on the Fintech sector has in some ways ushered in a „Compliance Centric Approach‟ to privacy. The authors feel a user centric approach is the need of the hour, which requires fintech corporations to inculcate privacy in their systems, integrity would go a long way in ensuring consumer reliance and would most likely attract a whole new consumer base.

IV. FINTECH INDUSTRY: INDIA'S TRACK RECORD

The robust fintech ecosystem in India, where numerous stakeholders are helpful in terms of giving finances as well as developing technology and entrepreneurial capabilities, is the main factor driving the country's steady ascent up the fintech growth ladder. One of the best aspects of the fintech industry in the country is its robust talent pool of a low-cost, simple-to-hire tech workforce. Absence of reliable consumer information and poor digital infrastructure are two barriers to mainstream adoption in India. Governmental incentives, regulatory requirements, and a strong business climate will be the most effective accelerators in making the fintech market come up to speed and enabling it to effectively address these hurdles.

The market‟s expansion is being fuelled by increased market participant cooperation in order to pool and share lessons learned and entrepreneurial experiences. Building a cohesive fintech environment that comprises of complete penetration of digital infrastructure, neutral start-up incubator support and lucrative incentives ranks as the most pressing issue. The next step is to establish an **independent trade group** focusing on fintech that can coordinate and establish a formal sector for aspiring entrepreneurs.

The development of fintechs in India is a precursor to changes in the payments, loans, and personal-finance sectors that have attracted a lot of investor attention. The whole value chain of traditional financial institutions is now empowered by fintech to improve client connections and introduce fresh products to the market. There are many start-ups operating in a variety of industries and job activities, primarily in the lending and payment sectors.

- **Financial Inclusion: India's Track record?**

The development of an ecosystem that gives individuals the chance to use financial instruments in their daily lives and allows banks to effectively utilise the proliferation of fintech operating in these inaccessible areas is expected to be a major driver of financial inclusion in India.

India currently has a low level of financial inclusion, with 145 million households lacking access to banking services. Numerous ways for displacing cash, giving credit information for screening, enabling lending online, and enabling the purchase of financial items through digital methods have emerged in India as a result of the internet and smartphones' rapidly increasing prevalence.

Going forward, RBI's recent grant of payment bank licences is probably going to help with commercialising this digital trend and elevating technology to the position of the primary services. The potential for fintech in the domain of government-to-person cash transfers is considerable. According to the RBI, the Direct Benefit Transfer ("**DBT**") shall ensure greater financial service penetration and assist in achieving financial inclusion targets.[37] Banking services will be made available to every household through the Government of India's financial inclusion mission by taking actions such as use of a bank account with

[37] *supra* note 21.

a line of credit, the Aadhar card, which serves as each Indian's individual identification, an ATM debit card with Rupay support.[38]

Moreover, Fintech companies now have the chance to assist banks in pursuing this possibility because banks have struggled to reach a sizable portion of the population with financial services despite strenuous efforts.

V. THE FUTURE OF FINTECH IN INDIA

According to our understanding, Fintech has already sparked a revolution, and Fintech entrepreneurs have begun disrupting the financial services market in various ways. In light of this, it becomes necessary to identify the factors that will drive the next wave of innovation.

- ***Blockchains*** - Traditionally, transactions required the validation of a third party. Then blockchains appeared, eliminating the need for third-party reconciliation and providing cryptographic security. Bitcoins, which utilise blockchain technology, have already gained widespread popularity. However, it is anticipated that blockchains will go well beyond bitcoins, payment transactions, and the banking business, into many other industries such as media, telecom, travel, and hospitality, among others.[39]

- ***Alternative lending*** - The traditional banking industry determined that lending to small business owners was unprofitable. Fintech companies capitalised on this opportunity by embracing peer-to-peer ("**P2P"**) financing and constructing web platforms to connect lenders and borrowers at reduced interest rates. This tendency will continue, and further alternative loan options, such as crowdfunding, will develop.

[38]*id.*
[39]Dr. C. Vijai., *Fintech in India – Opportunities and Challenge*s, vol. 8(1), SAARJ JOURNAL ON BANKING & INSURANCE RESEARCH, pp. 42-54 (2019)..

- ***Robo advising***- In the past, intermediaries were crucial in bridging the gap between the stock market and investors. This frequently resulted in untraceable and ineffective transactions. Robo advising will increase the value added for savvy investors and make the stock market more accessible, transparent, and traceable.[40]

- ***Digital payments***- Fintech start-ups have accelerated and streamlined the payment process. With improved and faster payment options, mobile wallets will continue to displace traditional wallets in many regions. And yes, ATMs will also become obsolete.[41]

- ***Insurance industry***- At the moment, there are several online marketplaces where customers may compare their insurance coverage and make informed choices. Through automation powered by data, fintech will advance the technological transformation in the insurance value chain, lowering operating costs while expanding the range of products on the market.

VI. CONCLUSION

India has emerged as one of the world's leaders in Fintech innovation. Financial technology is transforming the lives of Indian individuals and may be a game changer in the development of a digital economy. Fintech companies will undoubtedly find numerous opportunities to capitalise in the "Digital India" age. The Government of India has launched the "Jan Dhan Yojana" scheme, which aims to open a bank account for every citizen. The digitization of banks

[40]Accenture, *The Rise of Robo-Advice Changing the Concept of Wealth Management*, available: https://www.accenture.com/_acnmedia/PDF-2/Accenture-Wealth-Management-Rise-of-Robo-Advice.pdf.

[41]Accenture, *Fintech and the Evolving Landscape: Landing Points for the Industry*, available: http://www.fintechinnovationlablondon.co.uk/pdf/Fintech_Evolving_Landscape_2016.pdf.

will make fintech technology the long-term future of India's banking and financial sectors.

With the development of new payment mechanisms and interfaces such as Immediate Payments Service ("**IMPS**"), Unified Payments Interface ("**UPI**"), Bharat Interface for Money ("**BHIM**"), and others, India's payments infrastructure has witnessed significant advances. The government's "Make in India" and "Digital India" initiatives also played an important impact in increasing Fintech adoption. Furthermore, government moves such as demonetization and GST adoption have generated a significant growth opportunity for fintech ventures across the country. Although demonetization caused a lot of chaos and frenzy, especially among the common people, it was ultimately the catalyst for a shift away from a paper-based, cash-based economy toward digital, electronic, technology-driven platforms, which boosted the country‟s already-existing FinTech revolution. And it's only natural to believe that the Covid-19 pandemic has accelerated this digitalization across multiple categories, with contactless and cashless payments advocated to encourage social distance.

With the proper regulatory mechanism and government incentive, India can achieve great heights in terms of fintech revolution. The historically cash-based Indian economy has responded well to the fintech opportunity, which has been principally sparked by the growth of e-commerce and Smartphone adoption. In addition to focusing on and encouraging the fintech industry, the Indian government promotes new ideas and developments within the fintech sector.