

# Corporate Spring Cleaning

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## Managing the Business Impact of Lockdown



New Delhi

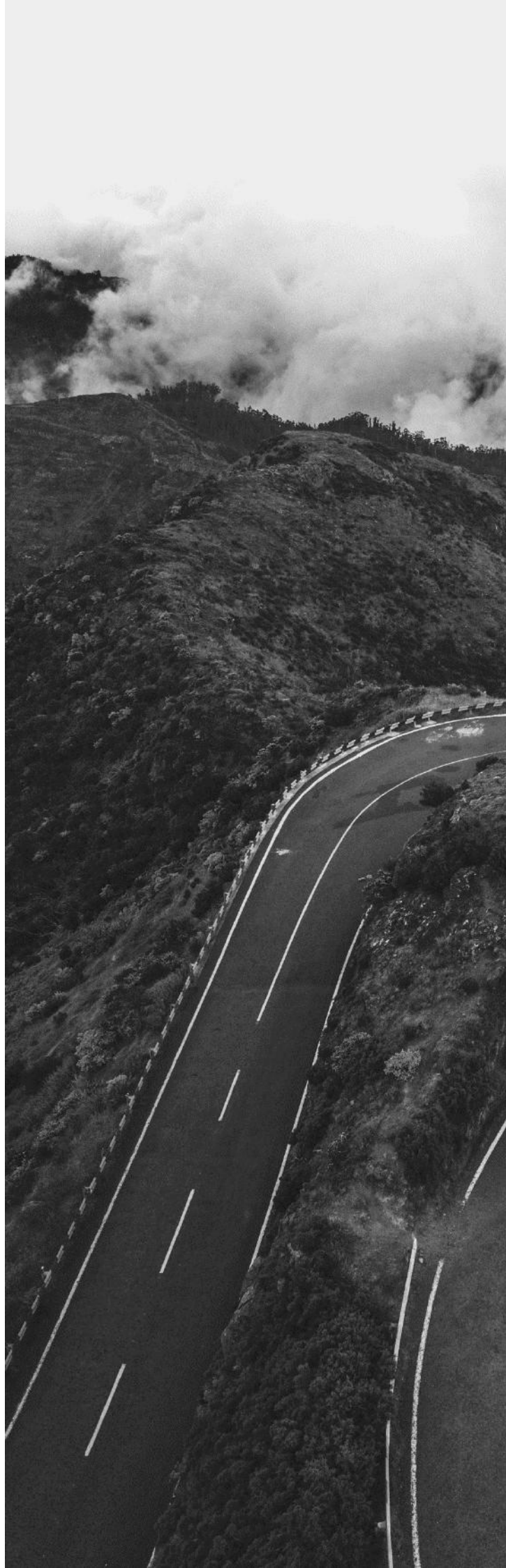
Mumbai

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# Corporate spring cleaning

**Black swan events change the trajectory of governments, economies and businesses – altering the course of history. With Covid-19, we are already seeing early signs of a shift in how consumers and businesses behave. Some of these changes are direct, short-term responses to the crisis. However, some of these shifts will continue, creating a long-term disruption that will shape businesses for decades to come.**

Given the restrictions on businesses and households by governments desperately trying to contain the ongoing Covid pandemic, the global economy is taking a battering not seen in decades. India imposed a three-week nationwide lockdown for its 1.3 billion people, the most far-reaching measure undertaken by any government to curb the spread of coronavirus pandemic. While these unprecedented measures are indeed required to ‘flatten the curve’ of infections, it’s taken an obvious toll on the economy. Pegging the cost of lockdown at USD 120 billion or 4% of the GDP, analysts have sharply cut their growth estimates and stressed on the need for economic relief from the government to support domestic industry.

Even as most of India Inc. is confined to their homes, it is pertinent to consider whether the present circumstances can be used for ‘**corporate spring-cleaning**’, that will help companies’ de-risk themselves in the times to come. While focusing on operational, financial and other aspects of day-to-day functioning, companies often relegate non-critical aspects to the back burner. This note is an attempt to draw attention to a series of activities that businesses should focus upon, in order to effectively utilize the increased availability of management bandwidth during the national lockdown.

## Corporate spring-cleaning list: Top 5 to-do’s

- **Reviewing the Standard Form Contracts (SFCs):** Most businesses have a range of SFCs that are used to enter into a series of contractual arrangements in the normal course of business. A sample survey conducted by HSA highlighted that almost 7 out of 10 companies fail to update their SFCs to reflect the latest position in law, which can potentially expose the organization to heightened risk. There have been series of developments spanning a range of statutes – Specific Relief Act, IBC, Arbitration Amendment Act, Companies Act, MSMED Act, to name a few – that can materially impact contractual rights, payment terms, representations, warranties, indemnities, termination, etc. Businesses can use this lull in operations to revise and update their SFCs as a risk-mitigation exercise, to ensure increased compliance with legal and regulatory requirements.
- **Analyzing the implications of non-performance under contracts:** With the disruption in supply and sourcing networks, businesses are actively considering provisions pertaining to Force Majeure clauses in their contracts or taking recourse to alternate provisions, such as Doctrine of Frustration as per the Indian Contract Act, 1872. Proactively understanding the specific requirements and consequences of such decisions can prove helpful once economic activity resumes.
- **Planning ahead for potential disputes:** With Courts taking up only urgent matters and the extension of period of limitation in all proceedings, businesses essentially have significantly more time available to plan and prepare for potential disputes that were being earlier contemplated. Utilizing this time to properly strategize with your legal advisor, dig deeper and prepare a robust case will yield clear downstream benefits.
- **Stressed asset investment opportunity:** Stressed asset investment in India has been steadily increasing over the last couple of years. As uncertainty looms over the economic situation, stressed asset investment opportunities are likely to expand further. Companies under the bankruptcy resolution process might witness potential buyers pulling out given the uncertainties regarding viability of businesses and attendant valuation, which will be a compelling proposition for businesses exploring inorganic growth. Utilizing this time to proactively understand the stressed asset investment space and attendant considerations will help in taking informed decisions down the line.
- **Enhancing corporate governance:** Businesses should focus on updating their internal compliance frameworks, including statutory and non-statutory compliances as well as internal policies, in order to ensure heightened corporate governance focus.



# Recent updates & relief measures



India has introduced a USD 23 billion financial stimulus package to battle coronavirus pandemic spreading its tentacles across the country. The country is now in midst of a 21-day national lockdown aimed at avoiding a colossal disaster.

The stimulus announced by finance minister covers some of the basics like ensuring essential services remain operational, migrant workers' welfare, functional public distribution system, etc.

## Reserve Bank of India

Reserve Bank of India (RBI) announced a slew of measures to mitigate the impact of coronavirus-related lockdown on businesses. The steps taken would push lending rates down, encourage banks to infuse money into productive sectors, infuse liquidity and address the financial stress in the system. RBI rolled out a notification dated March 27, 2020 which provides for a massive dose of monetary stimulus to be injected to overcome the current situation in economy and to help strengthen the extremely fragile financial markets.

### Liquidity measures

- Reduction in the Credit Reserve Ratio for banks by 100 basis point, thereby bringing the effective rate from 4% to 3% of the net demand and time liabilities.
- Revised limit of 3% of the statutory liquidity ratio for borrowing under the marginal standing facility.
- Infusion of liquidity of INR 2.74 lakh crores into the banking system through adjustments in capital conservation buffer.
- Infusion of additional liquidity of INR 1 lakh crores through auction of targeted long-term Repo, provided the liquidity availed by the banks under this scheme shall mandatorily be deployed in investment grade corporate bonds, commercial paper, and non-convertible debentures.

### Supervisory measures

- Lending institutions allowed to grant a moratorium of three months for repayments of term loans falling due between March 1, 2020 and May 31, 2020; lending institutions permitted to defer the recovery of interest during the Moratorium Period in respect of the working capital facility availed by borrowers in the form of either cash, credit and overdraft.
- While interest shall continue to accrue on both the term loan and the working capital facility during the Moratorium Period, the accrued interest on working capital facility shall be recoverable immediately on the elapse of Moratorium Period (the notification is silent on recovery of such interest in respect to term loans).
- The lending institutions have further been advised to revise the working capital limit available to borrowers under existing facility agreements by reassessing the margins and/or the working capital cycle, subject to bank satisfying itself that such rearrangements are necessitated due to economic fallout of Covid-19.

### Impact

- Even though the Covid-19 regulatory package announced by the RBI is advisory in nature, but it nevertheless clarifies the intent of RBI to ensure that the additional liquidity infused through adoption of unprecedented liquidity measures reaches its intended targets i.e. the borrower(s)
- The Apex Bank has directed the lending institutions to frame Board approved policies for providing the relief stated in the regulatory package
- Further, slashing of the repo rate will bring down the cost of the borrowing for the new loans and significantly reduce the cash outflow due to loans on floating interest, if the same is passed on to the borrowers by the lending institution.
- RBI has clarified that such rearrangements in the working capital facility or deferred repayments in respect of the term loan, shall not be treated as concession or change in terms and conditions of loan agreements due to financial difficulty of the borrower under paragraph 2 of the Annex to the Reserve Bank of India (Prudential Framework for Resolution of Stressed Assets) Directions, 2019 dated June 7, 2019 (Prudential Framework). Consequently, such a measure, by itself, shall not result in asset classification downgrade and will not qualify as a default for the purposes of supervisory reporting and reporting to Credit Information Companies by the lending institutions.

## Procedure

- Since the discretion to extend the relief under the Covid-19 regulatory packages vests with the concerned lending institutes, the process for making such application shall be notified by the concerned lending institute.
- In the absence of any such procedure being notified by the concerned lender, it is advisable that an application is made to the said lender requesting grant of relief under the package. In respect of revision of working capital limits, it is advisable that the representation includes the detailed reasoning for seeking such revision.

## Extension of realization period of export proceeds

- The time period for realisation and repatriation of export proceeds for exports made up to or on July 31, 2020, has been extended to 15 months (Increased from 9 months) from the date of export. This will enable the exporters to realise their receipts, especially from virus affected countries, within the extended period and also provide greater flexibility to the exporters to negotiate future export contracts with buyers abroad.

## Review of WMA limits of States/UTs

- The RBI had constituted an advisory committee to review the Ways and Means Advances (WMA) limits for state governments and Union Territories (UTs).
  - Pending submission of the final recommendations by the committee, it has been decided to increase WMA limit by 30% from the existing limit for all states/UTs to enable the state governments to tide over the situation arising from the outbreak of coronavirus.
  - The revised limits will come into force with effect from April 1, 2020 and will be valid till September 30, 2020.
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# Insolvency and Bankruptcy Code

On March 24, 2020, the Finance Ministry announced special relief packages for companies and inter alia raised the existing threshold of default of INR 1 lakh for triggering insolvency proceedings under the IBC to INR 1 crore. It was also announced that the Ministry would also consider suspending Sections 7, 9 and 10 of the IBC for six months if the lockdown situation continues beyond April 30, 2020.

## Measures taken by Registrar, National Company Law Tribunal (NCLT)

- All NCLT Benches will remain closed from March 23, 2020 till April 14, 2020. Matters to be listed between during this time will be suitably listed from April 15, 2020 onwards before respective NCLT benches.
- Regarding urgent matters, the Notice mentions that an Application should be filed (after verification by the respective counsel through Affidavit) by the respective counsel vide email to the Registrar NCLT after service of notice to the other side.
- The Acting President sitting singly at Chennai examined Applications and passed necessary orders on March 25, 2020 and March 27, 2020. Currently, urgent matters filed has been uploaded on NCLT's website and shown in NCLT Chennai Bench.

## Measures taken by Registrar, National Company Law Appellate Tribunal (NCLAT)

- Till April 01, 2020, only urgent matters shall be listed before the NCLAT, for which the Registrar of NCLAT would have to be contacted via telephone (9412159663).
- The matters listed for hearing between March 21, 2020 and April 01, 2020 shall stand adjourned and the next date of hearing will be informed later.
- The interim orders passed in the said matters will continue till the next hearing. The filing counters will also remain closed.

## Period of Limitation

- Vide order passed in *Suo Moto Writ Petition (Civil) No. 3/2020*, the Supreme Court exercised its powers under Article 142 read with Article 141 of the Constitution of India and ordered that the period of limitation in all proceedings irrespective of the limitation prescribed under the general law or special Laws whether condonable or not will stand extended w.e.f. March 15, 2020 till further orders.
- Consequent to the above, on March 24, 2020 the NCLT and NCLAT issued notices stating that the litigant public pertaining to the matters within the jurisdiction of the said authorities shall abide by the abovementioned order passed by the Supreme Court.

## IBBI and Insolvency Professionals

- The Insolvency and Bankruptcy Board of India (IBBI) issued a letter to Insolvency Professionals inter alia reminding them of their obligations towards the corporate debtors and their stakeholders in these difficult days.
- Further, the Insolvency Professionals were also advised to follow certain steps such as holding stakeholders' meetings through virtual platforms, allowing their staff to work from home, exercising social distancing etc.

# Ministry of Corporate Affairs

## Relaxations under the Companies Act, 2013

The Ministry of Corporate Affairs notified various relaxations on March 24, 2020:

### Extended till September 30, 2020

- No additional fees will be charged for any late filing (in the MCA21 Registry) during the moratorium from April 1, 2020 until September 30, 2020.
- Mandatory requirement of holding board meetings within the intervals provided in Section 173 of the Companies Act, 2013 extended by a period of 60 days, i.e. until September 30, 2020.

### Extended till June 30, 2020

- Requirement under Section 73(2)(c) of CA-13 to create the deposit repayment reserve of 20% of deposits maturing during the financial year 2020-21 before 30th April 2020 shall be allowed to be complied with till June 30, 2020.
- Requirement under Rule 18 of the Companies (Share Capital & Debentures) Rules, 2014 to invest or deposit at least 15% of amount of debentures maturing in specified methods of investments or deposits before April 30, 2020, may be complied with till June 30, 2020.

### Others

- Compliance of Companies (Auditor's Report) Order, 2020 shall be made applicable from FY 2020-21 instead of being applicable from FY 2019-20
- The independent directors are not mandated to hold a meeting with the management and other directors of the company
- Newly incorporated companies can file a declaration under Section 10A of the Companies Act, 2013 for Commencement of Business within 360 days of incorporation (instead of 180 days)
- Requirement for 'Indian' director to spend at least 182 days in India shall be suspended for FY 2019-20

## Implementation date for Stamp Duty Amendments deferred

Last year, the Indian Stamp Act, 1899 was amended and a centralized system of stamp duty with a unified rate for all financial securities transactions was introduced, which was to be implemented with effect from April 1, 2020. In light of Covid19 outbreak, the date of implementation has been shifted to July 1, 2020, in order to give further time to market participants to shift to the new requirements. As per the amendments and the new notification, stock exchanges will now collect stamp duty for trading in securities at a unified rate from July 1, 2020 and deposit the proceeds with the Centre, which will then divide it among states where the trade took place.

## Introduction of fresh start scheme for defaulting companies

The Ministry of Corporate Affairs on March 30, 2020 has introduced the Companies Fresh Start Scheme, 2020 (**Scheme**) allowing defaulting companies to make filings (in the nature of MGT-7, AOC-4, INC-22A, PAS-3, ADT-1, MGT-14 etc.) between April 1, 2020 and September 30, 2020, irrespective of the time of their default and without paying any additional fee. This would provide complying companies immunity from prosecution from specific provisions of the Companies Act, 2013 and reduce their financial burden. Prior to this Scheme being in effect, the MCA was taking actions for non-compliance of statutory compliances (for e.g. delay or non-filing of annual returns, annual statutory forms and documents, etc.). Inactive companies are also allowed to take benefits under this Scheme. In order to avoid confusion, specific exceptions have also been provided which would not be covered under the said Scheme. The tenure of the Scheme is from April 01, 2020 to September 30, 2020.

## Securities and Exchange Board of India

Securities and Exchange Board of India (**SEBI**) has relaxed various compliances for listed companies during the month of March 2020:

- The timeline for issuance and filing for issuers who have listed/propose to list their Non-Convertible Debentures (**NCDs**)/ Non-Convertible Redeemable Preference Shares (**NCRPS**)/ Commercial papers which had to be done by March 31, 2020, has now been extended to May 31, 2020.
- On March 23, 2020, SEBI has extended the due date for regulatory filings and compliances for REIT and InvIT for the financial year ending on March 31, 2020 by one month over and above the timelines prescribed by REITs, InvITs prescribed under SEBI (Infrastructure Investment Trusts) Regulations, 2014 and SEBI (Real estate Investment Trusts) Regulations, 2014 and circulars issued thereunder.
- SEBI has also relaxed compliance with disclosure requirements pertaining to Mutual Funds as per Regulation 59 of SEBI (Mutual Funds) Regulations, 1996 and circulars issued thereunder. Also the dates of implementation of risk management framework, policy for investment norms have been extended.
- Relaxation of various timelines under the SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 (**LODR**):
  - The requirement of audit committee and board of directors meeting for at least 4 times a year, with a maximum time gap of 120 days between any two meetings has been exempted
  - The yearly meeting of the nomination and remuneration committee, the Stakeholders Relationship committee and the Risk Management Committee has now been extended to June 30, 2020
  - Relaxation of the operation of the SEBI circular on Standard Operating Procedure on imposition of fines and other enforcement actions for non-compliances with provisions of the LODR dated January 22, 2020. It will now come to force with effect on or after June 30, 2020

Requirement under LODR	Original date	New date
<b>Regulation 7(3):</b> Compliance certificate on share transfer facility (filed half-yearly)	Apr 30, 2020	May 31, 2020
<b>Regulation 13(3):</b> Statement of Investor complaints (filed quarterly)	Apr 21, 2020	May 15, 2020
<b>Regulation 24A:</b> Secretarial Compliance report to (filed yearly)	May 30, 2020	Jun 30, 2020
<b>Regulation 27(2):</b> Corporate Governance report (filed quarterly)	Apr 15, 2020	May 15, 2020
<b>Regulation 31:</b> Shareholding Pattern (filed quarterly)	Apr 21, 2020	May 15, 2020
<b>Regulation 33:</b> Financial Results (filed quarterly/annual)	May 15, 2020	Jun 30, 2020
<b>Regulation 40(9):</b> Certificate from Practicing Company Secretary on timely issue of share certificates (filed half yearly)	April 30, 2020	May 31, 2020
<b>Regulation 44(5):</b> Holding of AGM by top 100 listed entities by market capitalization for FY 19-20 to be done on annual basis	Aug 31, 2020	Sep 30, 2020
<b>Regulation 47:</b> Publishing in the newspapers of information such as notice of the board meeting, financial results etc.	Within 48 hours of Board meeting	Exempted until May 15, 2020



## Labour & Employment

To give effect to the proclaimed nationwide lockdown in response to the Coronavirus Pandemic, the Ministry of Home Affairs, Government of India (**GoI**) released an order on March 24, 2020 (**Order**), in line with the responsibilities and powers granted to it by Section 6 of the Disaster Management Act, 2005 (**Act**), which will have an overriding effect over all other laws or orders issued across India on the subject, to the extent of their inconsistency.

The GoI Order and the measures to be taken thereunder as mentioned in the associated Guidelines (**Guidelines**) will affect employees in several labor-intensive industries and white-collar establishments. The pertinent labor and employment legal issues and its widespread impact are addressed below.

The Guidelines issued prescribe closure of all offices of/under the GoI or any State Government, commercial or private establishments, industrial establishments, hospitality services, transport services, educational institutions, places of worship and bar all kinds of gatherings, with certain exceptions. They fundamentally relate to the movement of people, and not of essential goods/commodities, and similarly list exceptions under each head mentioned above, pertaining to the kinds of establishments (providers of essential services & commodities) that may continue to operate during the period of the lockdown, all others being permitted only to work-from home.

- **Non-exempt employers:** The Act prescribes for piercing the corporate veil by holding every individual (and the company itself) in charge of/responsible for managing the affairs of the company (at the time of contravention) guilty for offences committed consensually or negligently. Persons held guilty are liable for punishment unless proven that the offence was committed without knowledge or preventive due diligence was exercised. This correspondingly applies to firms (and partners) and other associations of individuals and government departments. Employers engaged in the provisioning of non-essential services & commodities that are not-exempt under the guidelines must refrain from opening their offices or requiring employees to perform any duties other than working from home.
- **Non-exempt employees:** Non-compliance with the obligation to work from home during the period of the lockdown may result in punishment under Section 188 of the Indian Penal Code, 1860.
- **Essential services and commodities:** Employees working in the essential services and commodities establishments, both private establishments and government departments, would fall under the exempt category, subject to the Guidelines issued under the Order.
- **Private establishments:** Employers are obligated to assure that passes for enabling essential movements are obtained for each employee separately, from the Executive Magistrates, which can be facilitated online. Employers in essential services/commodities will have to ensure that the employees perform their employment obligations taking necessary measures against Covid-19, as prescribed by the GoI. Applicable labour and employment laws would continue to regulate employees during this period, including provisions for leave, termination and other contractual obligations inter alia.
- **Government departments:** The offices should operate with minimum number of employees, ensuring necessary precautions against COVID-19 including social distancing measures. An officer, on whom a duty has been imposed by the Order or any other order made under the Act, may not cease or refuse to perform it unless approved by their official superior or done with a lawful excuse.

### Employment regulatory insights

- The Employees' Provident Fund Scheme has been amended to allow withdrawal of non-refundable advance by EPF Members due to the pandemic. It permits withdrawal of amount not exceeding the basic wages and dearness allowance for three months or up to 75% of the amount standing to the credit of the members' EPF account, whichever is less.
- Employers will be required to pay contribution for 45, instead of 15 days for the months of February and March, towards Employees' State Insurance. The deadlines for the same have been extended by a month each.
- The Unified Annual Return (under 8 labour laws) for 2019 may now be filed up to April 30, 2020.
- The Ministry of Labour & Employment has issued an advisory for all private establishments against terminating or reducing the wages of their employees during the period of non-operationality due to COVID-19. Any Employee on leave should be deemed to be on duty in such cases. The enforceability of such advisory by way of letters to all Employers' Associations and the Ministry of Housing and Urban Affairs, however, remains in question.

# Taxation

## Direct taxes

- The due date for filing Income Tax Returns (ITR) for the Financial Year 2018-19 has been extended to the June 30, 2020.
- The due date for issuance of notices, filings, compliances, availing benefits under the following acts where the time limit is expiring between March 20, 2020 to June 29, 2020 have been extended to the June 30 2020: The Income Tax Act, 1961; The Wealth Tax Act, 1957; The Benami Transaction (Prohibition) Act, 1988; The Black Money Act; The Security Transaction Tax; and The Commodity Transaction Tax.
- Interest rates on delayed payments of advance tax have been reduced from 12% to 9%.
- No extension has been provided on deposit of TDS. However, interest rates payable on the delayed payment has been reduced from 18% to 9%. This reduction is temporary and the same will only be valid till June 30, 2020.
- Last date for Investment related deduction under Section 80, 54, 54B, 54EC etc extended to June 30, 2020.
- Deadline for linking Aadhar and PAN Card has been extended to June 30, 2020 from March 31, 2020.
- Investments/constructions/purchases for claiming roll over benefit/deduction in respect to capital gains under Section 54 to 54G of the Income Tax Act has been extended to June 30, 2020.
- The date for commencement of operation for the SEZ units for claiming deduction under deduction 10AA of the Income Tax Act has been extended to June 30, 2020 for the units which received necessary approval by March 31, 2020.
- The deadline for availing benefits under the Vivaad se Vishwas Scheme has been extended to June 30, 2020 *vide* an amendment to Section 3 of the Vivaad se Vishwas Scheme Act, 2020.

## Indirect taxes

### Goods and Services Tax

- An enabling Section 168A has been inserted in the CGST Act, 2017 empowering the Government to extend due dates for various compliances.
- The due date for filing the GSTR-3B for March, April and May have been extended till the June 30, 2020- Notification no. 15/2020 – Central Tax dated 23 March 2020 has already been issued in relation to the extension of due date for filing annual return for FY 2018-19.
- Deadline for availing the composition scheme, which enables taxpayers with less than an annual turnover of INR 1.5 crore to pay Goods and Services Tax at a fixed rate, has been extended to June 30, 2020.
- Sabka Vishwas Scheme i.e. the scheme which was introduced with an aim to resolve and conclude disputes pertaining to the erstwhile indirect tax regime which was earlier extended to March 31, 2020 has now been extended to June 30, 2020. No interest would be levied irrespective of amount involved pertaining to the said scheme.

### Customs and Service Tax Act

- The last date for filing appeal, refund application or any other documents under the Central Excise Act, 1944 and the rules made thereunder from March 20, 2020 to June 29, 2020 has been extended to June 30, 2020.
- The last date for filing of appeal etc. relating to Service Tax which is from March 20, 2020 to June 29, 2020 has been extended to June 30, 2020.
- For companies with an annual turnover of less than INR 5 Crores, no interest, late fee or penalty will be charged. However, for companies with a turnover higher than INR 5 Crore, interest at the rate of 9% would be charged from 15 days after the due date. The rate of interest is concessionary as the current rate of interest at 18%.

- Customs clearance would operate 24X7 till June 30, 2020. Further, the due date for issuing of notices, notifications, sanctions, claiming refund and any other document under the Customs Act and other allied laws has been extended to the June 30, 2020.

#### **Central Excise Act**

- The due date for filing the annual return for the financial year 2018-19 has been extended to June 30, 2020 from March 31, 2020.
- The last date for furnishing the Central Excise returns due in March, April and May has been extended to June 30, 2020.

#### **PM CARES Fund**

- A special fund called as Prime Minister's Citizen Assistance and Relief in Emergency Situations Fund (**PM CARES FUND**) has been set up for providing relief to the persons affected from the outbreak of the Covid-19.
  - Accordingly Section 10(23C)(i) and Section 80G(2)(a) of Income Tax Act have been amended to include the said fund.
  - The donation made to the PM Cares Fund shall be eligible for 100% deduction under Section 80G of the Income Tax Act, without any limit.
  - Donation made up to June 30, 2020 shall also be eligible for deduction from income of financial year 2019-20.
  - Any person including corporate paying concessional tax on income of financial year 2020-21 under new regime can make donation to PM Cares Fund upto June 30, 2020 and can claim deduction under Section 80G against income of financial year 2019-20 and shall also not lose his eligibility to pay tax in concessional taxation regime for income of financial year 2020-21.
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# Force Majeure & Covid-19

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The interplay that contracting world needs to know



In light of the economic slowdown and supply chain disruption brought about by the Covid-19 outbreak, the possibility of invoking Force Majeure to avoid liability from delayed, interrupted or otherwise failed performance of contracts is being widely debated.

This note brings out practical aspects pertaining to Force Majeure and analyzes whether Covid-19 can be categorized as a Force Majeure event.



## What is Force Majeure?

A creature of contractual innovation, Force Majeure refers to the principle that upon the occurrence of an event or circumstance that is not reasonably within the control of and would not have been avoided or overcome by a party, and which prevents or delays that party from performing some or all of its contractual obligations, that party will be relieved from liability which might otherwise arise as a result of that party's failure to perform those affected obligations.

The intention of a Force Majeure clause is to relieve the affected party from the consequences of something over which it has no control. Its provisions do not suspend the requirement for performance and typically require the affected party to continue to perform its obligations to the extent not prevented by the event of Force Majeure.

## Force Majeure and Indian Contract Act, 1872

Force Majeure is essentially a common law principle and there is no statutory definition of Force Majeure under the Indian laws. That said, the principle is embodied in Section 32 & 56 of Indian Contract Act, 1872 which provide that in case any act to be performed pursuant to a contract becomes impossible to perform, then such an act will become void. Judicial precedents have evolved the principle thoroughly over a period of time and the courts, relying on principles of sanctity of contracts, especially those which are commercial in nature, have tested such cases on the touchstone that whether the event giving rise to non-performance is specifically listed as a qualifying Force Majeure in the clause in such contracts or not.

In several landmark cases including in *Satyabrata Ghose v. Mugneeram Bangur & Co.*<sup>1</sup> and *Energy Watchdog v. CERC*<sup>2</sup>, the Supreme Court has applied the following tests to determine validity of Force Majeure events:

- Whether the event qualifies as Force Majeure under the contract?
- Whether the risk of non-performance was foreseeable and able to be mitigated?
- Whether performance is truly impossible?

## Covid-19 and Force Majeure

Availability of Force Majeure relief cannot be implied into a contract under Indian law. It must be expressly provided for under the provisions of the contract and the nature of protection afforded will depend on the precise language of the provision. Therefore, the answer to the question of whether Covid-19 can be categorized as a Force Majeure event is simple enough – Look in the contract!

Whether Covid-19 could be used to trigger the Force Majeure clause would depend on the specific language of the contract. A contracting party may be able to invoke rights of suspension or termination under this clause if Force Majeure clause provisions specify epidemics, pandemics, quarantines or government intervention/declaration as a result. In addition, presence of terminology such as 'extraordinary circumstances beyond control of contracting parties' or similar phrasing in the contract may also be tested to trigger the clause for outbreak of Covid-19.

In case the Force Majeure clause does not contemplate any of the above scenarios, one may explore whether 'government action/declaration' that has rendered the party unable to perform the contract can be used to expand the ambit of the existing Force Majeure provisions. However, the party should first ascertain whether non-performance is due to the outbreak of Covid-19 itself or the resulting government action for controlling infections such as limitations on transportation, self-quarantines, closures of premises, etc.

## Securing Force Majeure relief

The relief available upon invoking Force Majeure clause will depend upon the provisions laid down in the contract itself. These may include the following:

- Immediate termination of the contract upon the occurrence of the Force Majeure event
- Putting performance on hold until the Force Majeure event is resolved
- Elongation of the contract period
- Specific time period after which either party may terminate the agreement with written notice to the other (i.e. if non-performance caused by the event is prolonged or permanent)
- Allowing for certain obligations to be suspended

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<sup>1</sup> AIR 1954 SC 44

<sup>2</sup> (2017) 14 SCC 80

As a general principle, a party assumes the risk of its own subjective incapacity to perform its contractual duties unless the contract envisions otherwise. Accordingly, unless a particular event may clearly fall within the ambit and scope of Force Majeure Clause under the contract, the judicial forums may not accept the same as a triggering event to provide the desired contractual relief of non-performance (as seen in Energy Watchdog Case).

Whether a party can be excused from performance of its obligations claiming Covid-19 as a pandemic will also depend on the nature of the contract, a party's obligation therein and its duty to mitigate, which will usually entail all reasonable endeavors undertaken a party to perform its obligations.

Having said that, it is reasonable to state that any party contracting with the Government of India or its agencies/departments can seek relief under the Force Majeure clause in light of Government of India's circular issued in February 2020 stating that for Government contracts relating to procurement of goods and services, Covid-19 outbreak could be covered by a Force Majeure clause on the basis that it is a 'natural calamity', caveating that 'due procedure' should be followed by any Government department seeking to invoke it. Furthermore, the government invoked the Disaster Management Act on March 11, 2020 with retrospective effect from January 17, 2020. Additionally, MNRE on March 20, 2020 instructed all implementing agencies to treat delay on account of disruption of supply chain due to Covid-19 as Force Majeure and grant extension of time based on evidence/documentary proof by developer in support of their claims.

The following are key considerations for affording a party Force Majeure relief:

- **Burden of proof:** The affected party carries the burden of proving the validity of its claim through supporting evidence that an event of Force Majeure has indeed occurred.
- **Scope and interpretation:**
  - Contracts typically identify and list a series of events or circumstances that can legitimately be claimed by a party as an event of Force Majeure. Usually, such events can include an act of god or natural disasters, adverse weather conditions, fire, war or war-like situations, labour unrest, strikes, epidemics, pandemics, etc.
  - Force Majeure provision may exclude outright certain events such as changes in either party's market factors, a party's inability to finance its obligations under the agreement or the unavailability of funds to pay amounts when due, breakdown or failure of plant or equipment caused by normal wear and tear or by a failure to properly maintain such plant or equipment from constituting events of Force Majeure.
  - In the context of the ongoing pandemic, courts and tribunals would examine whether in each case, impact of Covid-19 pandemic prevented or delayed the party from performing its contractual obligation. In disputes arising out of complex contracts, they will also carry out a textual natural and ordinary interpretation of the Force Majeure provision in order to ascertain its objective meaning.
  - **Causation:** Depending on specific provisions, it is for affected party to demonstrate that an event of Force Majeure delayed performance of the contract or caused failure in performance of the contract notwithstanding the commercially reasonable efforts of the affected party to overcome or mitigate the effect of the said event.
- **Notification:** A Force Majeure provision commonly contains a time-bound notification requirement, which can operate as a contractual condition precedent to relief. Such provisions are generally enforceable, and so complying fully with all notice requirements will be important for parties seeking to invoke Force Majeure.

## Limitations on securing relief

The extent of Force Majeure relief will be affected by the following considerations:

- **Duty to mitigate:** In the unlikely event that an express duty to mitigate is absent, a duty to do so may be implied albeit on commercially reasonable terms, which can be ousted only by clear and unequivocal language. Provisions may specify the extent to which a party declaring Force Majeure must mitigate not only the event of Force Majeure but also its effect.
- **Certifications:**
  - Force Majeure certificates issued by governmental agencies may aid an affected party's efforts in securing relief, but they may not prove determinative.
  - 'The categorisation of the outbreak as a 'pandemic' by WHO may be of significant persuasive value in cases where Force Majeure provision contains appropriate language.
  - The Department of Expenditure, Ministry of Finance, Government of India on February 19, 2020 issued a cryptic office memorandum stating that the outbreak that has caused disruptions in the supply chain should be considered as a case of 'natural calamity' and Force Majeure provisions may be invoked 'wherever considered appropriate'. This memorandum may persuade pliant counterparties, but it is debatable whether such certificates have force of law.

## Contracts not having Force Majeure clause

While the above analysis deals with contracts having a defined Force Majeure clause, many contracts do not contain this provision. In such instances, it becomes important to consider whether the parties to such contracts continue to be bound by performance obligations or they have a recourse in cases such as the outbreak of Covid-19.

In absence of a specific Force Majeure clause, parties may seek the benefit embedded under Section 56 of the Indian Contract Act, 1872 by factually demonstrating before a court that the purpose and underlying principles of the contract have been eroded/frustrated and the performance under the contract has become impossible. The essential element for a claim of frustration is impossibility of performance of the contract and the party claiming frustration carries the burden of proof. In this context, it is important to remember that it settled law that abnormal rise in price, onerous conditions or change in circumstances do not lead to frustration of contract (*Alopi Parshad and Sons Ltd. v. Union of India*<sup>3</sup>) – it will have to be proved on facts that the frustrating event has led to the fundamental basis of the contract being dislodged.

For claiming frustration of contract for the outbreak of Covid-19, party would have to factually prove that the present lockdown and consequent disruption has made it impossible to perform the obligations under the contract. Having said that, the outcome would depend on the facts of each case.

### RERA and Force Majeure

It is noteworthy that Real Estate (Regulation and Development) Act, 2016 (**RERA Act**) specifically provides for extension of period for completion of the project and the registration, in addition to defining Force Majeure. RERA envisages two situations within which the registration granted to a project can be extended:

- In case of Force Majeure: Explanation to Section 6 of the RERA Act has defined Force Majeure to mean ‘a case of war, flood, drought, fire, cyclone, earthquake or any other calamity caused by nature affecting the regular development of the real estate project.’
- As per proviso to Section 6 of the RERA Act, extension up to a maximum period of 1 year can be granted under reasonable circumstances.

Whether the period of extension of a maximum of 1 year as stipulated in proviso is mandatory or directory came to be tested in *Neel kamal Realtors Suburban Pvt. Ltd. & anr. v. Union of India & ors.*<sup>3</sup>, wherein the Bombay High Court whilst upholding the constitutionality of the various provisions of the RERA Act and mandatory nature of Section 6, observed that a harmonious and balanced construction of the provisions relating to extension of time as encompassed in Section 6 of the Act shall suffice the purpose of dealing with a situation where a genuine promoter, after making good efforts, is unable to complete the project within the time stipulated at the time of initial declaration or under extended period. The Court referred to the scheme of RERA Act and interpreted the provisions of Sections 6, 7(3), 8 and 37 of the RERA Act to advance the proposition that the RERA Authority shall be entitled to take into consideration reasons and circumstances due to which the project could not be completed within the extended aggregate period of one year as prescribed under Section 6. Thus, it may be legally tenable to contest Covid-19 as a Force Majeure event.

It is pertinent to note that information has emerged from news items that Confederation of Real Estate Developers Association of India (**CREDAI**), the apex body of private Real Estate Developers, has asked the Government to declare Covid-19 as Force Majeure event under Section 6 of the RERA Act.

In the altered landscape of Force Majeure events or other extraordinary situations and events as encapsulated herein impacting the performance of a contract and leading to delays and defaults, it just may be the need of the hour to get to the drawing board and rework the agreements and arrangements, Force Majeure definitions and other necessary contractual provisions to build in safeguards for mitigating damages and addressing future ambiguities.

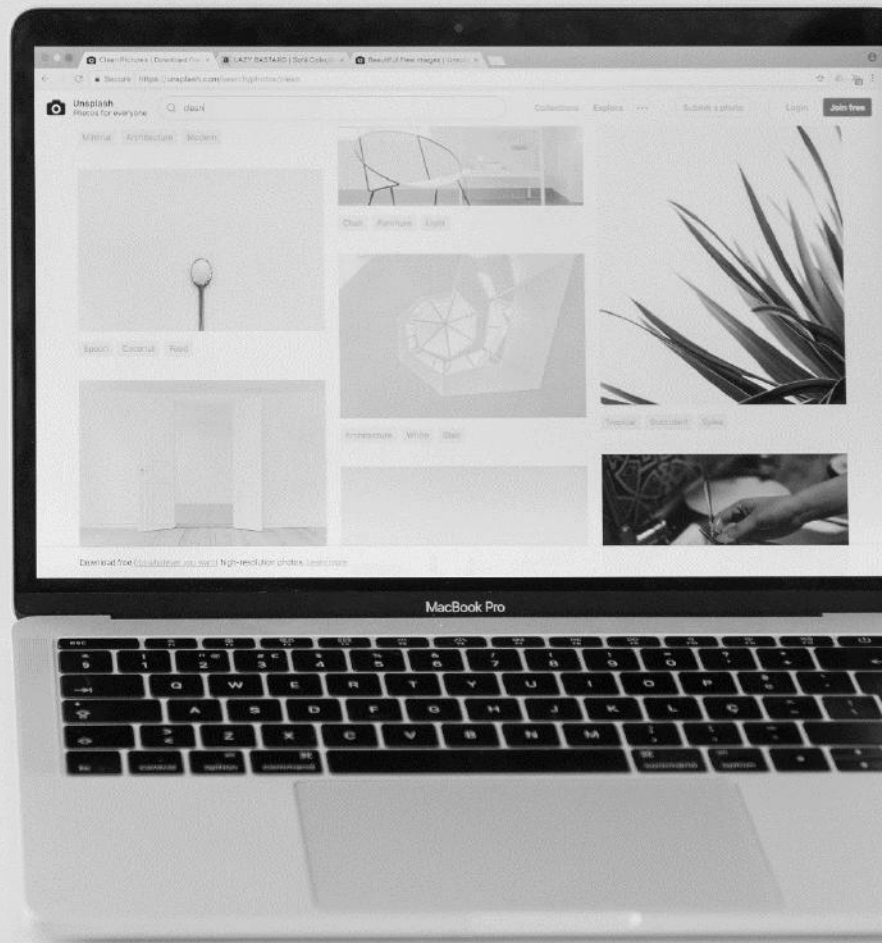
<sup>3</sup> AIR 1960 SC 588

# Key considerations for startups



On account of the Covid-19 pandemic, new investment deals will be few and far between as most VCs and early stage investors are focusing on their current portfolio companies and ensuring that their run-way requirements are being supported.

The impact is likely to be more severe in relation to growth (Series A and Series B) and late (Series C and above) stage deal-making. In these uncertain circumstances, startups must re-think how they do business with their partners, analyze specific considerations while executing/negotiating business deals, and their own business functioning.





## Business contracts

In relation to existing business contracts, we have highlighted some important considerations for startups to investigate/assess:

- **Material Adverse Effect:** Whether Covid-19 would be categorized as a 'material adverse effect', and what would be the implications under contract.
- **Suspension of performance/ mutuality clauses:** Whether Covid-19 provides an opportunity to suspend performance for a temporary period of time?
- **Event of Default and Force Majeure Clauses:** Nature of obligations that may become impossible to execute due to the ongoing Covid-19 restrictions and whether such non-compliance would result in an event of default or invocation of a force majeure?
- **Indemnity/damages risk:** Whether the counterparty may enforce contractual indemnities/damages, irrespective of the ongoing Covid-19 situation?
- **Business risks:** Whether the insolvency of any third-party supplier or supply chain vendor enables the startup to hire other third-party suppliers or supply-chain managers.
- **Renegotiation of terms:** Whether any existing contracts enable the startup to re-negotiate its existing terms?

## Co-Founders agreement

For mitigation of downside risks in times like these, a co-founder's agreement could be a useful tool to ensure business continuity in relationships between founders. A well-structured co-founder's agreement can help plan for, inter alia, founder exits in cases where businesses become tough to operate.

- **Board Composition and Administration:** What shall the role of the co-founders on the board and how will decisions be made at the board level, and which actions should be delegated to the authority of the larger shareholder body?
- **Deadlock Resolution:** How will the co-founders resolve disputes between themselves at the board level in case of deadlocks?
- **Appointment of the CEO:** Who shall be the CEO of the company and what should be the role of the CEO?
- **Exit:** Mechanism for enforcing exits and share transfers? What shall be the rights of a founder in case of only a partial exit?

## Insolvency risks

Startups may consider insolvency scenarios of its suppliers or vendors or retailers and may further draft provisions for:

- Finding alternative suppliers in case of an insolvency scenario for its suppliers and vendors
- Identify alternative methods to collect payments, if such suppliers and vendors are unable to repay
- Where applicable, retain title of the goods until monies have been repaid in full.

In the event the startup in question owes monies to other service providers, care must be taken to draft credit extension clauses in Force Majeure situations and provide for latitude in credit terms to account for such cases.

## Managing intellectual property (IP)

With respect to IP, early stage start-up must consider the following as a part of their larger IP strategy:

- Identify 'core IP' in relation to the products/services of the startup.
- Conducting research and development and developing new IP such as trademarks, copyrights and patents.
- Implement IP Assignment Agreements between the startup and its employees/ freelancers or independent contractors, wherein such employees/freelancers or independent contractors assign all work product or IP to the company.
- Register with appropriate authority and under applicable law all of the IP of the startup.
- Put in place an IP licensing policy and have standard IP licensing agreements drafted.

## Dealing with employee compensation and leaves

An employee who is in self-quarantine needs to be compensated and given leave (if leave has been extinguished) in case the self-quarantine is due to the employee travelling on business on behalf of the start-up. Alternatively, employees may use existing leaves for self-quarantine.

Employees infected with Covid-19 may seek special compensation in cases where they can establish that they contracted Covid-19 in the course of employment.

Employees who may have been exposed to the Covid-19 virus must be given work from home as they cannot be forced to take leaves from home.



**Certain sectors like F&B, travel, co-working and co-living, shared mobility, student housing, food delivery, home services, sports and recreation have altogether lost sheen overnight, so investment deals in those sectors are likely to witness a funding winter spell for an extended period till things settle.**

**Such companies must think of ways to pivot their existing business models and re-think/re-negotiate their business contracts, employee relationships to successfully weather the storm.**

# Enterprise risk

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## The Board's perspective



With the outbreak of the Covid-19, corporate India has stepped up to render assistance either by way of donations to relief funds or creating infrastructure to help the victims.

However, with all the focus and energy of India Inc. on the corporate social responsibility (and rightly so!), an overlooked vacuum is created which is calculation of the 'enterprise risk'.



The role of Board of Directors in Indian companies has been in the limelight for quite some time and has attracted increased public and governmental scrutiny. The Board's role in monitoring and managing enterprise risk becomes even more critical in the present scenario characterized by continuing global economic slowdown, contraction in domestic economic activity and retrenchment/lay-off fear amongst the workforce.

While risk management should ideally be tailored to the specific company, but, in general, an effective risk management system will include:

- Identification of the material risks that the company faces in a timely manner and processes for transmitting necessary information with respect to material risks to senior executives and, as appropriate, to the board or relevant committees
- Implementation of appropriate risk management strategies that are responsive to the company's risk profile, business strategies, specific material risk exposures and risk tolerance threshold, followed by integration of these strategies in business decision-making throughout the company

### Covid-19 and enterprise risk assessment

Anticipating future risk is a key element of risk mitigation and helps avoid such risks manifesting as crisis situations. While several companies with robust risk assessment protocols saw the Covid-19 red flags well in advance, many others were slow to respond. Corporate India has suddenly realized that the unthinkable can indeed happen and needs to be planned for ahead of time. One way of ensuring this is through adoption of best-in-class risk assessment and management protocols which should include ongoing efforts to assess and analyze the most likely areas of future risk for the company and creation of internal response and escalation structures.

In reviewing risk management, the Board or relevant committees should ask the company's executives to discuss the most likely sources of material future risks and how the company is addressing any significant potential vulnerability. Specific types of actions that the Board/appropriate committees may consider as part of their risk management oversight include the following:

- Establish a clear framework for building and maintaining an effective risk appetite framework and providing the Board with regular, periodic reports on the company's residual risk status
- Clear communication of the board's expectations as to each committee's and management's respective responsibilities for risk oversight and management of specific risks to ensure a shared understanding as to accountabilities and roles
- **Conduct a regular review of the following:**
  - Company's executive compensation structure to ensure it is appropriate in light of the company's articulated risk appetite and risk culture and to ensure it is creating proper incentives in light of the risks the company faces
  - Risk policies and procedures adopted by management, including procedures for reporting matters to the board and appropriate committees and providing updates, in order to assess whether they are appropriate and comprehensive
  - Management's implementation of its risk policies and procedures, to assess whether they are being followed and are effective
  - Steps taken by management to ensure adequate independence of the risk management function and the processes for resolution and escalation of differences that might arise between risk management and business functions
  - Internal systems of formal and informal communication across divisions and control functions to encourage the prompt and coherent flow of risk-related information within and across business units and, as needed, the prompt escalation of information to management (and to the board or board committees as appropriate)
  - Reports from management, independent auditors, internal auditors, legal counsel, regulators, stock analysts, and outside experts as considered appropriate regarding risks the company faces and the company's risk management function, and consider whether, based on individual director's experience, knowledge and expertise, the board or committee primarily tasked with carrying out the board's risk oversight function is sufficiently equipped to oversee all facets of the company's risk profile—including specialized areas such as cybersecurity—and determine whether subject-specific risk education is advisable for such directors.



▪ **Review the following aspects with management:**

- Company's risk appetite and risk tolerance, the ways in which risk is measured on an aggregate, company-wide basis, the setting of aggregate and individual risk limits (quantitative and qualitative, as appropriate), the policies and procedures in place to hedge against or mitigate risks, and the actions to be taken if risk limits are exceeded
- Categories of risk the company faces, including any risk concentrations and risk interrelationships, as well as the likelihood of occurrence, the potential impact of those risks, mitigating measures and action plans to be employed if a given risk materializes
- Assumptions and analysis underpinning the determination of the company's principal risks and whether adequate procedures are in place to ensure that new or materially changed risks are properly and promptly identified, understood and accounted for in the actions of the company
- Quality, type and format of risk-related information provided to directors
- Design of the company's risk management functions, as well as the qualifications and backgrounds of senior risk officers and the personnel policies applicable to risk management, to assess whether they are appropriate given the company's size and scope of operations
- Means by which the company's risk management strategy is communicated to all appropriate groups within the company so that it is properly integrated into the company's enterprise-wide business strategy

# HSA Emergency Assistance Team

In order to offer real time assistance to clients, for any exigency that might come during the lockdown, HSA has developed a cross-discipline team to render immediate support. For any such assistance please reach out to us at [helpline@hsalegal.com](mailto:helpline@hsalegal.com).

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