Centre for Aerospace & Defence Laws (CADL)
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Course Material

M.A. (AVIATION LAW AND AIR TRANSPORT MANAGEMENT)

2.3.10. Aviation Corporate Laws

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COURSE OUTLINE

The times when only government used to exercise monopoly on the civil aviation sector are long gone and in its place there has been a splurge of entry of private entities and investors in the domestic and international aviation market. Aviation sector in India has been transformed from an over regulated and under managed sector to a more open, liberal and investment friendly sector since 2004. In order to regulate the business of aviation in India, the varied range of corporate laws that are applicable to regular business enterprises are also applicable to aviation business. Corporate Laws provide the business enterprises with a legal form that possesses these five core attributes. By making this form widely available and user-friendly, corporate law enables entrepreneurs to transact easily through the medium of the corporate entity, and thus lowers the costs of conducting business.

The dominance of private corporations including the aviation corporate enterprises over our economy and society is such that they have come to colonize our thinking. Aviation Corporate Law deals with the formation and operations of corporations and is related to commercial and contract law. A corporation is a legal entity created under the laws of the state it's incorporated within. State laws, which vary from state to state, regulate the creation, organization and dissolution of their corporations. A corporation creates a legal or "artificial person" or entity that has standing to sue and be sued, enter into contracts, and perform other duties necessary to maintain a business, separate from its stockholders.

The objective of this paper is to train the corporate law professionals in the legal formation of corporations and to construct joint ventures, licensing arrangements, mergers, acquisitions, and the countless other transactions entered into by corporations. Other areas of practice include business formations, securities law, venture capital financing, business agreements, internal forms, and business tax consultations.

It is of paramount importance for the course participants to familiarize themselves with the fundamental law of business before starting an aviation business as it will help you operate your business without the hindrances of ignorance. Hence the first module of the paper deals with the fundamentals of company law. Any discussion on the corporate law is incomplete without deliberating upon the mother of corporate laws in India i.e. the Indian Companies Act 2013. It lays down the fundamental legal provisions on start, conduct and regulation of business.

Given the growing trend of mergers and acquisitions in the field of aviation sector, the second module is entirely dedicated towards an elaborate discussion on the issue of mergers and acquisitions. The initial chapters of the second module dwell upon the significance, rationale, procedures and varied forms of mergers and acquisitions. The module thereafter digs deeper in to the cases of mergers and acquisitions in the aviation sector and the contemporary issues that have arisen in the last few years.

Another significant aspect of the civil aviation business is related to the competition law and competition norms. Hence the third module contains a detailed discussion on the competition law of India. The second part of this module consists of a detailed discussion on the emerging issues which have arisen due to application of competition law to Indian civil aviation sector.

Over recent years the global aviation sector has witnessed the rapid growth of air travel in emerging markets, the continuing growth of low cost carriers across the globe, and regulatory changes to global emissions trading schemes to name but a few developments. Increased FDI inflows, surging tourist inflow, increased cargo movement, sustained business growth and supporting government policies are the major drivers for the growth of aviation sector in India and have opened up new doors of intersection between the business and aviation norms. Domestic airlines have been allowed to fly overseas, forge partnerships with foreign carriers while foreign carriers in turn have been interlining with domestic airlines to access secondary destinations. The fourth module on business opportunities in aviation sector focuses on such new contemporary issues that have arisen due to application of business laws on civil aviation. The module thus discusses these contemporary issues.

The final module of the paper briefly throws light on other corporate laws which carry the potential to affect business venture in aviation sector.

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MODULE I

FUNDAMENTALS OF COMPANY LAW

INTRODUCTION- JURISPRUDENCE OF COMPANY LAW

Company Law in India, is the cherished child of the English parents. Our various Companies Acts have been modelled on the English Acts. Following the enactment of the Joint Stock Companies Act, 1844 in England, the first Companies Act was passed in India in 1850. It provided for the registration of the companies and transferability of shares. The Amending Act of 1857 conferred the right of registration with or without limited liability. Subsequently this right was granted to banking and insurance companies by an Act of 1860 following the similar principle in Britain. The Companies Act of 1856 repealed all the previous Acts. This Act covered aspects of incorporation, regulation and winding up of companies and other associations. This Act was recast in 1882, embodying the amendments which were made in the Company Law in England upto that time. In 1913 a consolidating Act was passed, and major amendments were made to the consolidated Act in 1936. In the meantime England passed a comprehensive Companies Act in 1948. In 1951, the Indian Government promulgated the Indian Companies (Amendment) Ordinance under which the Central Government and the Court assumed extensive powers to intervene directly in the affairs of the company and to take necessary action in the interest of the company. The ordinance was replaced by an Amending Act of 1951.

HISTORY AND DEVELOPMENT OF THE CONCEPT OF COMPANY LAW IN INDIA

1. Companies Act, 1956 (Bhaba Committee Recommendations)

The Act came into force on 1st April, 1956 and it was enacted with a view to consolidate earlier laws relating to companies and other associations. This act was based largely on Bhaba Committee recommendations. The Companies Act, 1956 consisted of 658 sections and 15 schedules. This Act provided the legal framework for corporate entities in India and was a mammoth legislation. As the corporate sector grew in numbers and size of operations, the need for streamlining this Act was felt and as many as 24 amendments had taken place since then.

The Companies Act, 1956 had undergone changes by amendments in 1960, 1962, 1963, 1964, 1965, 1966, 1967, 1969, 1971, 1977, 1985, 1988, 1996, 1999, 2000, 2002 and 2006. The provisions of Companies (Second Amendment) Act, 2002 were not enforced except that of definitions and the constitution of NCLT (National Company Law Tribunal). The Companies Act, 1956 was also amended pursuant to the enactment of the Depositories Act, 1996. Unsuccessful attempts were made in 1993 and 1997 to replace the present Act with a new law. Companies (Amendment) Bill, 2003 containing important provisions relating to Corporate Governance and aimed at achieving competitive advantage was also introduced.

Full and fair disclosure of various matters in prospectus; detailed information of the financial affairs of company to be disclosed in its account; provision for intervention and investigation by the Government into the affairs of a company; restrictions on the powers of managerial personnel; enforcement of proper performance of their duties by company management; and protection of minority shareholders were some of the main features of the Companies Act, 1956.

The Companies Act, 1956 was enacted with the object to amend and consolidate the law relating to companies. This Act provided the legal framework for corporate entities in India and was a mammoth legislation. As the corporate sector grew in numbers and size of operations, the need for streamlining this Act was felt and as many as 24 amendments had taken place since then.

SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992

The Securities and Exchange Board of India (SEBI) was officially appointed as the authority for regulating the financial markets in India on 12th April 1988. It was initially established as a non-statutory body, i.e. it had no control over anything but later in 1992, it was declared an autonomous body with statutory powers. SEBI plays an important role in regulating the securities market of India. Thereby it is important to know the purpose and objective of SEBI. SEBI acts as a watchdog for all the capital market participants and its main purpose is to provide such an environment for the financial market enthusiasts that facilitate efficient and smooth working of the securities market. To make this happen, it ensures that the three main participants of the financial market are taken care of, i.e. issuers of securities, investor, and financial intermediaries.

DEPOSITORIES ACT, 1996

The Depositories Act initially came into force as an ordinance viz. The Depositories Ordinance, 1995 promulgated on 7th January 1996. It was designed to provide a legal framework for establishment of depositories to record ownership details in book entry form. The Act also made consequential amendments in the Companies Act, 1956; the Securities and Exchange Board of India Act, 1992; the Indian Stamp Act, 1899; the Income tax Act, 1961; and the Benami Transactions (Prohibition) Act, 1988.

The Depositories Act, 1996 was enacted with the objective of ensuring free transferability of securities with speed, accuracy, and security, by making securities of public companies freely transferable subject to certain exceptions by restricting company's right to use discretion in effecting the transfer securities and dispensing with the transfer deed and other procedural requirements under the Companies Act. The Depositories Act, 1996 is an Act to provide for regulation of depositories in securities and for matters connected therewith or incidental thereto.

CONCEPT PAPER ON COMPANY LAW, 2004 & J.J. IRANI REPORT

A concept paper on Company Law drawn up in the legislative format was open for public on the electronic media so that all interested parties may not only express their opinions on the concepts involved but may also suggest formulations on various aspects of

Company Law. Therefore, the proposals and suggestions in the concept paper were put to merited evaluation by an independent expert committee. A Committee was constituted on 2nd December, 2004 under the Chairmanship of Dr. J J Irani, the then Director, Tata Sons. Dr. J J Irani Expert Committee on Company Law had submitted its report charting out the road map for a flexible, dynamic and user-friendly new company law. The Committee had taken a pragmatic approach keeping in view the ground realities, and had sought to address the concerns of all the stakeholders to enable adoption of internationally accepted best practices. The Expert Committee had recommended that private and small companies need to be given flexibilities and freedom of operations and compliance at a low cost. Companies with higher public interest should be subject to a stricter regime of Corporate Governance.

COMPANIES ACT, 2013

The Companies Bill, 2012 finally became the Companies Act, 2013. It received the assent of the President on August 29, 2013 and was notified in the Gazette of India on 30.08.2013. Companies Act, 2013 has undergone amendments four times so far. Companies (Amendment) Act, 2015 and Companies (Amendment) Act, 2017 aimed at enhancing efficiency and promoting ease of doing business. The Act was also amended by The Insolvency and Bankruptcy Code, 2016 and Finance Act, 2017. The Insolvency and Bankruptcy Code, 2016 led to omission of various sections i.e. section 253 to section 269, section 289, section 304 to section 323 and section 325. The Finance Act, 2017 amended section 182 with regard to prohibitions and restrictions regarding political contributions. So far Ministry has come out with several circulars, notifications, Orders and various amendment rules to facilitate better and smooth implementation of the Act.

The Companies Act 2013 introduced new concepts supporting enhanced disclosure, accountability, better board governance, better facilitation of business and so on. It includes associate company, one Person Company, small company, dormant company, independent director, women director, resident director, special court, secretarial standards, secretarial audit, class action, registered valuers, rotation of auditors, vigil mechanism, corporate social responsibility, E-voting etc.

MEANING AND DEFINITION OF A COMPANY

The word ‘company’ is derived from the Latin word (Com means with or together; panis means bread), and it originally referred to an association of persons who took their meals together. In the leisurely past, merchants took advantage of festive gatherings, to discuss business matters. Nowadays, the company form of organization has assumed great importance. In popular parlance, a company denotes an association of likeminded persons formed for the purpose of carrying on some business or undertaking.

A Company is called a body corporate because the persons composing it are made into one body by incorporating it according to the law and clothing it with legal personality. The word ‘corporation’ is derived from the Latin term ‘corpus’ which means ‘body’. Accordingly, ‘corporation’ is a legal person created by a process other than natural birth.

It is, for this reason, sometimes called artificial legal person. As a legal person, a corporate is capable of enjoying many rights and incurring many liabilities of a natural person.

An incorporated company owes its existence either to a Special Act of Parliament or to company law. Public corporations like Life Insurance Corporation of India, SBI etc., have been brought into existence through special Acts of Parliament, whereas companies like Tata Steel Ltd., Reliance Industries Limited have been formed under the Company law i.e. Companies Act, 1956 which is replaced by the Companies Act, 2013. In the legal sense, a company is an association of both natural and artificial persons and is incorporated under the existing law of a country.

In terms of the Companies Act, 2013 (Act No. 18 of 2013) a "company" means a company incorporated under this Act or under any previous company law [Section 2(20)].

Lord Justice Lindley has defined a company as "an association of many persons who contribute money or money's worth to a common stock and employ it in some trade or business and who share the profit and loss arising therefrom. The common stock so contributed is denoted in money and is the capital of the company. The persons who contributed in it or form it, or to whom it belongs, are members. The proportion of capital to which each member is entitled is his "share". The shares are always transferable although the right to transfer them may be restricted."

WHETHER COMPANY HAS NATIONALITY AND RESIDENCE?

Though it is established through judicial decisions that a company cannot be a citizen, yet it has nationality, domicile and residence. In '*Gasque v. Inland Revenue Commissioners, (1940) 2 K.B. 88*', Macnaghten. J. held that a limited company is capable of having a domicile and its domicile is the place of its registration and that domicile clings to it throughout its existence. He observed in this case: "It was suggested that a body corporate has no domicile. It is quite true that a body corporate cannot have a domicile in the same sense as an individual. But by analogy with a natural person the attributes of residence, domicile and nationality can be given to a body corporate."

In '*Tulika v. Parry and Co., (1903) I.L.R. 27 Mad. 315*', Kelly C.B. observed: "A joint stock company resides where its place of incorporation is, where the meetings of the whole company or those who represent it are held and where its governing body meets in bodily presence for the purposes of the company and exercises the powers conferred upon it by statute and by the Articles of Association."

NATURE AND CHARACTERISTICS OF A COMPANY

Since a corporate body (i.e. a company) is the creation of law, it is not a human being, it is an artificial juridical person (i.e. created by law) and it is clothed with many rights, obligations, powers and duties prescribed by law. The most striking characteristics of a company are discussed below:

(i) Corporate personality

A company incorporated under the Act is vested with a corporate personality so it bears its own name, acts under name, has a seal of its own and its assets are separate and distinct from those of its members. It is a different 'person' from the members who compose it. Therefore it is capable of owning property, incurring debts, borrowing money, having a bank account, employing people, entering into contracts and suing or being sued in the same manner as an individual. Its members are its owners however they can be its creditors simultaneously. A shareholder cannot be held liable for the acts of the company even if he holds virtually the entire share capital.

The shareholders are not the agents of the company and so they cannot bind it by their acts. The company does not hold its property as an agent or trustee for its members and they cannot sue to enforce its rights, nor can they be sued in respect of its liabilities. Thus, 'incorporation' is the act of forming a legal corporation as a juristic person. A juristic person is in law also conferred with rights and obligations and is dealt in accordance with law. In other words, the entity acts like a natural person but only through a designated person, whose acts are processed within the ambit of law [Shiromani Gurdwara Prabandhak Committee v. Shri Sam Nath Dass AIR 2000 SCW 139].

<u>The case of Salomon v. Salomon and Co. Ltd., (1897) A.C. 22</u>

The above case has clearly established the principle that once a company has been validly constituted under the Companies Act, it becomes a legal person distinct from its members and for this purpose it is immaterial whether any member holds a large or small proportion of the shares, and whether he holds those shares as beneficially or as a mere trustee.

In the case, Salomon had, for some years, carried on a prosperous business as a leather merchant and boot manufacturer. He formed a limited company consisting of himself, his wife, his daughter and his four sons as the shareholders, all of whom subscribed to 1 share each so that the actual cash paid as capital was £7. Salomon sold his business (which was perfectly solvent at that time), to the Company formed by him for the sum of £38,782. Salomon was the managing director and two of his sons were other directors.

The company soon ran into difficulties and went into liquidation. The petitioners further pleaded that Salomon, as a principal beneficiary, was ultimately responsible for the debts incurred by his agent or trustee on his behalf.

Their Lordships of the House of Lords observed: "…the company is a different person altogether from the subscribers of the memorandum; and though it may be that after incorporation the business is precisely the same as before, the same persons are managers, and the same hands receive the profits, the company is not, in law, their agent or trustee. The statute enacts nothing as to the extent or degree of interest, which may, be held by each of the seven or as to the proportion of interest, or influence possessed by one or majority of the shareholders over others. There is nothing in the Act requiring that the subscribers to the memorandum should be independent or unconnected, or that they or any of them should take a substantial interest in the undertakings, or that they should have a mind or will of their own, or that there should be anything like a balance of power in the constitution of company."

Lee v Lee's Air Farming Ltd

In this case, Mr. Lee's accountant formed a company (Lee's Air Farming Ltd), and Mr. Lee was the principal shareholder also the governing director of this company. The company contracted with farmers to perform aerial topdressing. Mr. Lee worked for the company as a pilot and received a wage for that work. In a work accident, Mr. Lee died then his wife claimed on a workers compensation insurance policy that the company's solicitor had taken out naming Mr. Lee as an employee. The insurer denied liability on the ground that Mr. Lee could not be a servant because he was a director of the company. The Judicial Committee of the Privy Council upheld the claims made by Mrs. Lee and firmly rejected the insurer's argument. Lord Morris quoted Lord Halsbury LC's judgment in Salomon's case, that company 'was a real thing' and noted that:

"… Always assuming that the respondent company was not a sham, then the capacity of the respondent company to make a contract could not be impugned merely because the deceased was an agent of the respondent company in its negotiation [of Mr Lee's contract of service]."

Supreme Court of India in the case of Bacha F Guzdar, Bombay v. Commissioner of Income Tax, Bombay held that 'A Company is a distinct legal entity, corporate body, separate from its members. It is a juristic person entirely distinct from its shareholders. Any liability of the *company **is*** liable to be recovered *from* it or its assets. It is not liable to be recovered *from its Directors* unless such a liability is cast on them by any provision of law or they have, by any act of theirs, made themselves personally liable for the amount.'

(ii) Company as an artificial person

A Company is an artificial person created by law. It is not a human being but it acts through human beings. It is considered as a legal person which can enter into contracts, possess properties in its own name, sue and can be sued by others etc. It is called an artificial person since it is invisible, intangible, existing only in the contemplation of law. It is capable of enjoying rights and being subject to duties.

Union Bank of India v. Khader International Construction and Other [(2001) 42 CLA 296 SC]

In this case, the question which arose before the Court was whether a company is entitled to sue as an indigent (poor) person under Order 33, Rule 1 of the Civil Procedure Code, 1908. The aforesaid Order permits persons to file suits under the Code as pauper/indigent persons if they are unable to bear the cost of litigation. The appellant in this case had objected to the contention of the company which had sought permission to sue as an indigent person. The point of contention was that, the appellant being a public limited company, it was not a 'person' within the purview of Order 33, Rule 1 of the Code and the 'person' referred to only a natural person and not to other juristic persons. The Supreme Court held that the word 'person' mentioned in Order 33, Rule 1 of the Civil Procedure Code, 1908, included any company as association or body of individuals, whether incorporated or not. The Court observed that the word 'person' had to be given its meaning in the context in which it was used and being a benevolent provision, it was to be given an extended meaning. Thus a company may also file a suit as an indigent person.

(iii) Company is not a citizen

The company, though a legal person, is not a citizen under the Citizenship Act, 1955 or the Constitution of India. In State Trading Corporation of India Ltd. v. C.T.O., A.I.R. 1963 S.C. 1811, the Supreme Court held that the State Trading Corporation though a legal person, was not a citizen and can act only through natural persons. Nevertheless, it is to be noted that certain fundamental rights enshrined in the Constitution for protection of "person", e.g., right to equality (Article 14) etc. are also available to company. Section 2(f) of Citizenship Act, 1955 expressly excludes a company or association or body of individuals from citizenship.

<u>In R.C. Cooper v. Union of India, AIR 1970 SC 564</u>

In this case, the Supreme Court held that where the legislative measures directly touch the company of which the petitioner is a shareholder, he can petition on behalf of the company, if by the impugned action, his rights are also infringed. In that case, the court entertained the petition under Article 32 of the Constitution at the instance of a director as shareholder of a company and granted relief. It is, therefore, to be noted that an individual's right is not lost by reason of the fact that he is a shareholder of the company.

<u>Bennet Coleman Co. v. Union of India, AIR 1973 SC 106</u>

In this case, the Supreme Court stated that: "It is now clear that the Fundamental Rights of shareholders as citizens are not lost when they associate to form a company. When their Fundamental Rights as shareholders are impaired by State action, their rights as shareholders are protected. The reason is that the shareholders' rights are equally and necessarily affected if the rights of the company are affected.

(iv) Limited Liability

"The privilege of limited liability for business debts is one of the principal advantages of doing business under the corporate form of organisation." The company, being a separate person, is the owner of its assets and bound by its liabilities. The liability of a member as shareholder, extends to the contribution to the capital of the company up to the nominal value of the shares held and not paid by him. Members, even as a whole, are neither the owners of the company's undertakings, nor liable for its debts. In other words, a shareholder is liable to pay the balance, if any, due on the shares held by him, when called upon to pay and nothing more, even if the liabilities of the company far exceed its assets. This means that the liability of a member is limited. For example, if A holds shares of the total nominal value of 1,000 and has already paid Rs.500/- (or 50% of the value) as part payment at the time of allotment, he cannot be called upon to pay more than Rs. 500/-, the amount remaining unpaid on his shares. If he holds fully-paid shares, he has no further liability to pay even if the company is declared insolvent. In the case of a company limited by guarantee, the liability of members is limited to a specified amount of the guarantee mentioned in the memorandum.

Buckley, J. in Re. London and Globe Finance Corporation, (1903) 1 Ch.D. 728 at 731, has observed: ‘The statutes relating to limited liability have probably done more than any legislation of the last fifty years to further the commercial prosperity of the country. They have, to the advantage of the investor as well as of the public, allowed and encouraged aggregation of small sums into large capitals which have been employed in undertakings of “great public utility largely increasing the wealth of the country”.

(v) Perpetual Succession

An incorporated company never dies, except when it is wound up as per law. A company, being a separate legal person is unaffected by death or departure of any member and it remains the same entity, despite total change in the membership. Perpetual succession, means that the membership of a company may keep changing from time to time, but that shall not affect its continuity.

The membership of an incorporated company may change either because one shareholder has sold/transferred his shares to another or his shares devolve on his legal representatives on his death or he ceases to be a member under some other provisions of the Companies Act. Thus, perpetual succession denotes the ability of a company to maintain its existence by the succession of new individuals who step into the shoes of those who cease to be members of the company. Professor L.C.B. Gower rightly mentions, “Members may come and go, but the company can go on forever. During the war all the members of one private company, while in general meeting, were killed by a bomb, but the company survived — not even a hydrogen bomb could have destroyed it”.

(vii) Separate Property

A company being a legal person and entirely distinct from its members, is capable of owning, enjoying and disposing of property in its own name. The company is the real person in which all its property is vested, and by which it is controlled, managed and disposed off. Their Lordships of the Madras High Court in R.F. Perumal v. H. John Deavin, A.I.R. 1960 Mad. 43 held that “no member can claim himself to be the owner of the company’s property during its existence or in its winding-up”. A member does not even have an insurable interest in the property of the company.

Mrs. Bacha F. Guzdar v. The Commissioner of Income Tax, Bombay, A.I.R. 1955 S.C. 74

The Supreme Court in this case held that, though the income of a tea company is entitled to be exempted from Income-tax up to 60% being partly agricultural, the same income when received by a shareholder in the form of dividend cannot be regarded as agricultural income for the assessment of income-tax. It was also observed by the Supreme Court that a shareholder does not, as is erroneously believed by some people, become the part owner of the company or its property; he is only given certain rights by law, e.g., to receive notice of or to attend or vote at the meetings of the shareholders. The court refused to identify the shareholders with the company and reiterated the distinct personality of the company.

(viii) Transferability of Shares

The capital of a company is divided into parts, called shares. The shares are said to be movable property and, subject to certain conditions, freely transferable, so that no shareholder is permanently or necessarily wedded to a company. When the joint stock companies were established, the object was that their shares should be capable of being easily transferred. Section 44 of the Companies Act, 2013 enunciates the principle by providing that the shares held by the members are movable property and can be transferred from one person to another in the manner provided by the articles. If the articles do not provide anything for the transfer of shares and the Regulations contained in Table "F" in Schedule I to the Companies Act, 2013, are also expressly excluded, the transfer of shares will be governed by the general law relating to transfer of movable property.

(ix) Capacity to Sue and Be Sued

A company being a body corporate, can sue and be sued in its own name. To sue, means to institute legal proceedings against (a person) or to bring a suit in a court of law. All legal proceedings against the company are to be instituted in its name. Similarly, the company may bring an action against anyone in its own name. A company's right to sue arises when some loss is caused to the company, i.e. to the property or the personality of the company. Hence, the company is entitled to sue for damages in libel or slander as the case may be [Floating Services Ltd. v. MV San Fransceco Dipaloa (2004) 52 SCL 762 (Guj)]. A company, as a person distinct from its members, may even sue one of its own members.

A company has a right to seek damages where a defamatory material published about it, affects its business. Where video cassettes were prepared by the workmen of a company showing, their struggle against the company's management, it was held to be not actionable unless shown that the contents of the cassette would be defamatory. The court did not restrain the exhibition of the cassette. [TVS Employees Federation v. TVS and Sons Ltd., (1996) 87 Com Cases 37]. The company is not liable for contempt committed by its officer. [Lalit Surajmal Kanodia v. Office Tiger Database Systems India (P) Ltd., (2006) 129 Com Cases 192 Mad].

(x) Contractual Rights

A company, being a legal entity different from its members, can enter into contracts for the conduct of the business in its own name. A shareholder cannot enforce a contract made by his company; he is neither a party to the contract, nor be entitled to the benefit derived from of it, as a company is not a trustee for its shareholders. Likewise, a shareholder cannot be sued on contracts made by his company. The distinction between a company and its members is not confined to the rules of privity but permeates the whole law of contract. Thus, if a director fails to disclose a breach of his duties towards his company, and in consequence a shareholder is induced to enter into a contract with the director on behalf of the company which he would not have entered into had there been disclosure, the shareholder cannot rescind the contract. Similarly, a member of a company cannot sue in respect of torts committed against the company, nor can he be sued for torts committed by the company. Therefore, the company as a legal person can take action to enforce its legal rights or be sued for breach of its legal duties. Its rights and duties are distinct from those of its constituent members.

(xi) Limitation of Action

A company cannot go beyond the power stated in its Memorandum of Association. The Memorandum of Association of the company regulates the powers and fixes the objects of the company and provides the edifice upon which the entire structure of the company rests. The actions and objects of the company are limited within the scope of its Memorandum of Association. In order to enable it to carry out its actions without such restrictions and limitations in most cases, sufficient powers are granted in the Memorandum of Association. But once the powers have been laid down, it cannot go beyond such powers unless the Memorandum of Association, itself altered prior to doing so.

(xii) Separate Management

As already noted, the members may derive profits without being burdened with the management of the company. They do not have effective and intimate control over its working and they elect their representatives as Directors on the Board of Directors of the company to conduct corporate functions through managerial personnel employed by them. In other words, the company is administered and managed by its managerial personnel.

(xiii) Voluntary Association for Profit

A company is a voluntary association for profit. It is formed for the accomplishment of some stated goals and whatsoever profit is gained is divided among its shareholders or saved for the future expansion of the company. Only a Section 8 company can be formed with no profit motive.

(xiv) Termination of Existence

A company, being an artificial juridical person, does not die a natural death. It is created by law, carries on its affairs according to law throughout its life and ultimately is effaced by law. Generally, the existence of a company is terminated by means of winding up. However, to avoid winding up, sometimes companies adopt strategies like reorganisation, reconstruction and amalgamation.

To sum up, "a company is a voluntary association for profit with capital divisible into transferable shares with limited liability, having a distinct corporate entity and a common seal with perpetual succession".

Company v. Other Associations

Though there are a number of similarities between a limited company and other forms of associations, there is much dissimilarity. In both the cases individuals are the subjects, and trading is generally the object. In the following paragraphs a limited company is distinguished from a partnership firm, a Hindu Joint Family business, a club and a registered society.

Though there are a number of similarities between a limited company and other forms of associations, there are a great number of dissimilarities as well. In both the cases individuals are the subjects, and trading is generally the object. In the following paragraphs, a limited company is distinguished from a partnership firm, a Hindu Joint Family business and a registered society

Company v. Partnerships

(a) A company can be created only by certain prescribed methods - most commonly by registration under the Companies Act. A partnership is created by the express or implied agreement of the parties, and requires no formalities, though it is common to have a written agreement.
(b) A company incurs greater expenses at formation, throughout its life and on dissolution, though these need not be excessive.
(c) A company is an artificial legal person distinct from its members. Although in Scotland a partnership has a separate legal personality by virtue of s.4 (2) of the Partnership Act 1890, this is much more limited than the personality conferred on companies.
(d) A company can have as little as one member and there is no upper limit on membership. A partnership must have at least two members and has an upper limit of 20 (with some exceptions).
(e) Shares in a company are normally transferable (must be so in a public company). A partner cannot transfer his share of the partnership without the consent of all the other partners.
(f) Members of a company are not entitled to take part in the management of the company unless they are also directors of it. Every partner is entitled to take part

in the management of the partnership business unless the partnership agreement provides otherwise.

(g) A member of a company who is not also a director is not regarded as an agent of the company, and cannot bind the company by his actions. A partner in a firm is an agent of the firm, which will be bound by his acts.

(h) The liability of a member of a company for the debts and obligations of the company may be limited. A partner in an ordinary partnership can be made liable without limit for the debts and obligations of the firm.

(i) The powers and duties of a company, and those who run it, are closely regulated by the Companies Acts and by its own constitution as contained in the Memorandum and Articles of Association. Partners have more freedom to alter the nature of their business by agreement and without formality, and to make their own arrangements as to the manner in which the firm will be run.

(j) A company must comply with formalities regarding the keeping of registers and the auditing of accounts which do not apply to partnerships.

(k) The affairs of a company are subject to more publicity than those of a partnership - e.g. companies must file accounts which are available for public inspection.

(l) A company can create a security over its assets called a floating charge, which permits it to raise funds without impeding its ability to deal with its assets. A partnership cannot create a floating charge.

(m) If a company owes a debt to any of its shareholders they can claim payment from its assets ratably with its other creditors. A partner who is owed money by the partnership cannot claim payment in competition with other creditors.

(n) A partnership (unless entered into for a fixed period) can be dissolved by any partner, and is automatically dissolved by the death or bankruptcy of a partner, unless the agreement provides otherwise. A company cannot normally be wound up on the will of a single member, and the death, bankruptcy or insanity of a member will not result in its being wound up.

Company and Joint Hindu Family Business

a. A company consists of heterogeneous members, whereas a Hindu Undivided Family Business consists of homogenous members since it consists of members of the joint family itself.
b. In a Hindu Joint Family business the Karta (manager) has the sole authority to contract debts for the purpose of the business, other coparceners cannot do so. There is no such system in a company.
c. A person becomes a member of Joint Hindu Family business by virtue of birth. There is no provision to that effect in the company.
d. No registration is compulsory for carrying on business for gain by a Hindu Joint Family even if the number of members exceeds twenty [*Shyamlal Roy v. Madhusudan Roy*, AIR 1959 Cal. 380 (385)]. Registration of a company is compulsory

Company and Corporation

Generally speaking, an association of persons incorporated according to the relevant law and clothed with legal personality separate from the persons constituting it is known as a corporation. The word 'corporation' or words 'body corporate' is/are both used in the Companies Act, 1956. Definition of the same which is reproduced below is contained in Clause (7) of Section 2 of the Act:

"Body corporate" or "corporation" includes a company incorporated outside India but does not include—

(a) a corporation sole;

(b) a co-operative society registered under any law relating to co-operative societies; and

(c) any other body corporate not being a company which the Central Government may, by notification in the Official Gazette, specify in this behalf."

The expression "corporation" or "body corporate" is wider than the word 'company'. A corporation sole is a single individual constituted as a corporation in respect of some office held by him or function performed by him. The Crown or a Bishop under the English law are examples of this type of corporation. It may be noted that though a corporation sole is excluded from the definition for the purposes of the Companies Act, it continues to be a legal person capable of holding property and becoming a member of a company.

A society registered under the Societies Registration Act has been held by the Supreme Court in *Board of Trustees v. State of Delhi*, A.I.R. 1962 S.C. 458, not to come within the term 'body corporate' under the Companies Act, though it is a legal person capable of holding property and becoming a member of a company.

Advantages of Incorporation

As compared to other types of business associations, an incorporated company has the following advantages:

- Corporate Personality: Unlike a partnership firm, which has no existence apart from its members, a company is a distinct legal or juristic person independent of its members. Under the law, an incorporated company is a distinct entity, even the one-man company as discussed above in Salomon & Co. Ltd., case is different from its shareholders. Section 34(2) of the Companies Act, 1956 provides that from the date of incorporation, the subscribers to the memorandum and other members shall be a body corporate by the name contained in the Memorandum, capable of exercising all the functions of an incorporated company and having perpetual succession and a common seal.
- Limited Liability: The Companies Act provides that in the event of the company being wound-up, the members shall have liability to contribute to the assets of the company in accordance with the Act [Section 34(2)]. In the case of companies limited by shares, no member is bound to contribute anything more than the nominal value of the shares held by him which remains unpaid.

The privilege of limiting the liability is one of the principal advantages of doing business under the corporate form of organization.

- Perpetual Succession: As stated in Section 34(2) of the Companies Act, an incorporated company has perpetual succession. Notwithstanding any change in its members, the company will be the same entity with the same privileges and immunities, estate and possessions. The death or insolvency of individual members does not in any way, affect the corporate entity, its existence or continuity. The company shall continue to exist indefinitely till it is wound-up in accordance with the provisions of the Companies Act.
- Transferable Shares: Section 82 of the Companies Act provides "The shares or other interest of any member in a company shall be movable property, transferable in the manner provided by the articles of the company". This encourages investment of funds in the shares, so that the members may encash them at any time. Thus, it provides liquidity to the investors as shares could be sold in the open market and in stock exchange. It also provides stability to the company.
- Separate Property: A company as a legal entity is capable of owning its funds and other assets. "The property of the company is not the property of the shareholders, it is property of the company" [*Gramophone & Typewriter Co. v. Stanley, (1906) 2* K.B. 856 at p. 869]. "The company is the real person in which all the property is vested, and by which it is controlled, managed and disposed of". In the eyes of law, even a member holding majority of shares or a managing director of a company is held liable for criminal misappropriation of the funds or property of the company, if he unauthorizedly takes it away and uses it for his personal purposes.
- Capacity to Sue: As a juristic legal person, a company can sue in its name and be sued by others. The managing director and other directors are not liable to be sued for dues against a company.
- Flexibility and Autonomy: The company has an autonomy and independence to form its own policies and implement them, subject to the general principles of law, equity and good conscience and in accordance with the provisions contained in the Companies Act, Memorandum and Articles of Association.

The company form of management of business disassociates the "ownership" from the "control" of business, and helps promote professional management and efficiency. The directors and managers can carry on the business activities with freedom, authority and accountability in accordance with the Company Law. Precisely this is the reason why the Government has generally adopted the company form of management for its various undertakings in preference to management through the departmental undertakings.

Disadvantages of Incorporation

There are, however, certain disadvantages and inconveniences in Incorporation. Some of these disadvantages are:

- Formalities and expenses: Incorporation of a company is coupled with complex, cumbersome and detailed legal formalities and procedures, involving considerable amount of time and money. Such elaborate procedures have been laid down to deter persons who are not serious about doing business, as a company enjoys various facilities from the community. Even after the company is incorporated, its affairs and working must be conducted strictly in accordance with legal provisions. Thus various returns and documents are required to be filed with the Registrar of Companies, some periodically and some on the happening of an event. Certain books and registers are compulsorily required to be maintained by a company. Approval and sanction of the Company Law Board, the Government, the Court, the Registrar of Companies or other appropriate authority, as the case may be, is necessarily required to be obtained for certain corporate activities. Certain corporate activities such as corporate meetings, accounts, audit, borrowings, lending, investment, issue of capital, dividends etc. are necessarily required to be conducted and carried out strictly in accordance with the provisions of the Act and within the prescribed time. Any breach of the legal provisions is followed by severe penal consequences. Other forms of business organizations are comparatively free from these legal complexities and procedural formalities.
- Corporate disclosures: Notwithstanding the elaborate legal framework designed to ensure maximum disclosure of corporate information, the members of a company are having comparatively restricted accessibility to its internal management and day-to-day administration of corporate working.
- Separation of control from ownership: Members of a company are not having as effective and intimate control over its working as one can have in other forms of business organisation, say, a partnership firm. This is particularly so in big companies in which the number of members is too large to exercise any effective control over its day-to-day affairs. No member of a company can act in his individual capacity for and on behalf of the company. The members of a company are neither the owners nor the agents of the company. Thus, the position of ownership of members is more passive in nature. The members may not have an active and complete control over the company's working as the partners may have over the firm's affairs.
- Greater social responsibility: Having regard to the enormous powers wielded by the companies and the impact they have on the society, the companies are called upon to show greater social responsibility in their working and, for that purpose, are subject to greater control and regulation than that by which other forms of business organisation are governed and regulated.
- Greater tax burden in certain cases: In certain circumstances, the tax burden on a company is more than that on other forms of business organisation. A

company is liable to tax without any minimum taxable limit as is prescribed in the cases of registered partnership firms and others. Also it has to pay income-tax on the whole of its income at a flat rate whereas others are taxed on graduated scale or slab system. These tax implications may have crucial bearing on a decision regarding the selection of any form of business organisation and the time when the existing form of business organisation should be changed to a new one. Thus, tax implications may direct the adoption of the partnership form of business organisation as expedient at the initial stage to be converted into a company later on, when the tax implications may be more favorable because of the size of the organisation and its scale of operations.

- Detailed winding-up procedure: The Act provides elaborate and detailed procedure for winding-up of companies which is more expensive and time consuming than that which is applicable to other forms of business organisation.

Principle of Lifting the Corporate Veil

Law has clothed a corporation with a distinct personality, yet in reality it is an association of persons who are in fact, in a way, the beneficial owners of the property of the body corporate. A company, being an artificial person, cannot act on its own, it can act only through natural persons. Indeed, the theory of corporate entity is still the basic principle on which the whole law of corporations is based. But as the separate personality of the company is a statutory privilege, it must be used for legitimate business purposes only. Where a fraudulent and dishonest use is made of the legal entity, the individuals concerned will not be allowed to take shelter behind the corporate personality. The Court will break through the corporate shell and apply the principle of what is known as "lifting of or piercing through the corporate veil". The Court will look behind the corporate entity and take action as though no entity separate from the members existed and make the members or the controlling persons liable for debts and obligations of the company.

The corporate veil is lifted when in defence proceedings, such as for the evasion of tax, an entity relies on its corporate personality as a shield to cover its wrong doings. [BSN (UK) Ltd. v. Janardan Mohandas Rajan Pillai [1996] 86 Comp. Cas. 371 (Bom).]

In the following cases the Courts have lifted the corporate veil:

1. Where the corporate veil has been used for commission of fraud or improper conduct, Courts have lifted the veil and looked at the realities of the situation. In Gilford Motor Co. v. Horne, (1933) 1 Ch. 935, a former employee of a company made a covenant not to solicit its customers. He formed a company which undertook solicitation. The company was restrained by the Court.

2. Where the corporation is really an agency or trust for some one else and the corporate facade is used to cover up that agency or trust. In re R.G. Films Ltd., (1953) 1 All E.R. 615, an American company produced a film in India technically in the name of a British Company, 90% of whose capital was held by the President of the American Company which financed the production of the film. Board of Trade refused to register the film as a British film on the ground that English company acted merely as the nominee of the American corporation.

3. Where the doctrine conflicts with public policy, Courts have lifted the corporate veil for protecting the public policy. In Connors Bros. v. Connors (1940) 4 All E.R. 179, the principle was applied against the managing director who made use of his position contrary to public policy. In this case, the House of Lords determined the character of the company as "enemy" company, since the persons who were de facto in control of its affairs, were residents of Germany, which was at war with England at that time. The alien company was not allowed to proceed with the action, as that would have meant giving money to the enemy, which was considered as monstrous and against "public policy".

4. For determining the true character or status of the company. In Daimler Co. Ltd. v. Continental Tyre and Rubber Co., (1916) 2 A.C. 307, the Court looked behind the facade of the company and its place of registration in order to determine the true character of the company, i.e., whether it was an "enemy" company.

5. Where the veil has been used for evasion of taxes and duties, the Court upheld the piercing of the veil to look at the real transaction. (Commissioner of Income Tax v. Meenakshi Mills Ltd., A.I.R. (1967) S.C. 819).

6. Where it was found that the sole purpose for which the company was formed was to evade taxes the Court will ignore the concept of separate entity, and make the individuals liable to pay the taxes which they would have paid but for the formation of the company. In the case of Sir Dinshaw Manakjee Petit, AIR 1927 Bombay 371, the assesse was a wealthy man enjoying large dividend and interest income. He formed four private companies and agreed with each to hold a block of investment as an agent for it. Income received was credited in the accounts of the company but the company handed back the amount to him as a pretended loan. This way he divided his income in four parts in a bid to reduce his tax liability. The Court disregarded the corporate entity on the grounds that the company was formed by the assessee purely and simply as a means of avoiding tax and the company was nothing more than the assessee himself.

7. Where the purpose of company formation was to avoid welfare legislation. Where it was found that the sole purpose for the formation of the new company was to use it as a device to reduce the amount to be paid by way of bonus to workmen, the Supreme Court upheld the piercing of the veil to look at the real transaction (The

Workmen Employed in Associated Rubber Industries Limited, Bhavnagar and another, A.I.R. 1986 SC 1).

Exceptions to the principle of limited liability

- Members are severally liable in certain cases- if at any time the number of members of a company is reduced, in the case of a public company, below seven, in the case of a private company, below two, and the company carries on business for more than six months while the number of members is so reduced, every person who is a member of the company during the time that it so carries on business after those six months and is cognisant of the fact that it is carrying on business with less than seven members or two members, as the case may be, shall be severally liable for the payment of the whole debts of the company contracted during that time, and may be severally sued therefor.[Section 3A]
- When the company is incorporated as an Unlimited Company under Section 3(2)(c) of the Act Where a company has been incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants, direct that liability of the members of such company shall be unlimited. [Section 7(7)(b)]
- Further under section 339(1), where in the course of winding up it appears that any business of the company has been carried on with an intent to defraud creditors of the company or any other persons or for any fraudulent purpose, the Tribunal may declare the persons who were knowingly parties to the carrying on of the business in the manner aforesaid as personally liable, without limitation of liability, for all or any of the debts/liabilities of the company.[Section 339]
- Under Section 35(3), where it is proved that a prospectus has been issued with intent to defraud the applicants for the securities of a company or any other person or for any fraudulent purpose, every person who was a director at the time of issue of the prospectus or has been named as a director in the prospectus or every person who has authorised the issue of prospectus or every promoter or a person referred to as an expert in the prospectus shall be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by any person who subscribed to the securities on the basis of such prospectus.
- As per section 75(1), where a company fails to repay the deposit or part thereof or any interest thereon referred to in section 74 within the time specified or such further time as may be allowed by the Tribunal and it is proved that the deposits had been accepted with intent to defraud the depositors or for any fraudulent purpose, every officer of the company who was responsible for the acceptance of such deposit shall, without prejudice to other liabilities, also be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by the depositors.

TYPES OF COMPANIES

Companies may be classified on the basis of their incorporation, number of members, size, basis of control and motive. On the basis of incorporation of the companies, it may be classified into Charter Companies, Statutory Companies and Registered Companies. On the basis of liability, it may be Companies limited by shares/guarantee and unlimited liability companies. Further, on the basis of number of members, they may be classified into One Person Company, private company and public company. On the basis of size, they may be divided into small companies and other companies. On the basis of control, they may be classified into holding company, subsidiary company and associate company.

The Companies Act, 2013 provides for the kinds of companies that can be promoted and registered under the Act. The three basic types of companies which may be registered under the Act are:

(a) Private Companies;

(b) Public Companies; and

(c) One Person Company (to be formed as Private Limited Company)

CLASSIFICATION OF COMPANIES

The Companies Act, 1956 broadly classifies the companies into private and public companies and provides for regulatory environment on the basis of such classification. However, with the growth of the economy and increase in the complexity of business operation, the forms of corporate organizations keep on changing. Classification of Companies can therefore take many shapes and a multiple classification of companies can be made.

On the basis of size:

a. Small Companies: The concept of Small Company has also been introduced in the Companies Act, 2013. According to (Section 2(85) of the Companies Act, 2013, 'Small company' means a company, other than a public company, -

(i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than five crore rupees; or

(ii) turnover of which as per its last profit and loss account does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than twenty crore rupees:

Provided that nothing in this section shall apply to—

1. a holding company or a subsidiary company;
2. a company registered under section 8; or
3. a company or body corporate governed by any special Act;

b. Other companies

On the basis of number of members:

a. One Person Company: The concept of a 'one-person company' or OPC, has been introduced in the Act, and the intent is apparently to permit entrepreneurship of a single individual to obtain the benefit of a corporate form of organization. According to Section 2(62) of the Companies Act, 2013 ―One Person Company‖ means a company which has only one person as a member. It is a one shareholder corporate entity, where legal and financial liability is limited to the company only.
b. Private companies: As per Section 2(68) of the Companies Act, 2013, "private company" means a company having a minimum paid-up share capital as may be prescribed, and which by its articles,– (i) restricts the right to transfer its shares; (ii) except in case of One Person Company, limits the number of its members to two hundred: Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member: Provided further that – (A) persons who are in the employment of the company; and (B) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased, shall not be included in the number of members; and (iii) prohibits any invitation to the public to subscribe for any securities of the company;
c. Public companies: By virtue of Section 2(71), a public company means a company which: (a) is not a private company; and (b) has a minimum paid-up share capital, as may be prescribed Provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles.

On the basis of control:

a. Holding companies & Subsidiary companies: As per section 2(46) of the Companies Act, 2013 46) the "holding company", in relation to one or more other companies, means a company of which such companies are subsidiary companies and the expression "company" includes any body corporate. As per section 2(87) of the Companies Act, 2013 "subsidiary company" or "subsidiary", in relation to any other company (that is to say the holding company), means a company in which the holding company – (i) controls the composition of the Board of Directors; or (ii) exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies: Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.

b. Associate Company: As per section 2(6) of the Companies Act, 2013 the "associate company", in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.

   Explanation. - For the purpose of this clause, –

   (a) The expression "significant influence" means control of at least twenty per cent. of total voting power, or control of or participation in business decisions under an agreement;
   (b) The expression "joint venture" means a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement;

On the basis of liability

a. Limited
   i. By Shares: A company that has the liability of its members limited by the liability clause in the memorandum to the amount, if any, unpaid on the shares respectively held by them is termed as a company limited by shares. Section 2(22) of the Companies Act, 2013 provides that "company limited by shares" means a company having the liability of its members limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them. For example, a shareholder who has paid Rs. 75 on a share of face value Rupees 100 can be called upon to pay the balance of Rupees.25 only'. Companies limited by shares are by far the most common and it may be either public or private.
   ii. By Guarantee: Section 2(21) of the Companies Act, 2013 provides that a company that has the liability of its members limited to such amount as the members may respectively undertake, by the memorandum, to contribute to the assets of the company in the event of its being wound-up, is known as a company limited by guarantee. The members of a guarantee company are, in effect, placed in the position of guarantors of the company's debts up to the agreed amount. the members is liable to the company and to any other person.
   b. Unlimited: : In this type of company, the liability of members of the company is unlimited, Section 2(92) of the Companies Act, 2013 provides that unlimited company means a company not having any limit on the liability of its members, Such companies may or may not have share capital. They may be either a public company or a private company. . The members is liable to the company and to any other person.

On the basis of manner of access to capital

c. Listed companies: "listed company" means a company which has any of its securities listed on any recognized stock exchange;
d. Un-listed companies

On the basis of nature of business

e. Companies with charitable objects etc. (Section 8 of the Companies Act 2013)
f. Dormant Company (Section 455 of the Companies Act 2013)
g. Companies incorporated outside India (Chapter XXII of the Companies Act 2013)
h. Government Companies (Chapter XXIII of the Companies Act 2013)
i. Nidhi Companies (Chapter XXVI of the Companies Act 2013)

MEMORANDUM OF ASSOCIATION

The Memorandum of Association is a document which sets out the constitution of a company and is therefore the foundation on which the structure of the company is built. It defines the scope of the company's activities and its relations with the outside world. The first step in the formation of a company is to prepare a document called the memorandum of association. In fact, memorandum is one of the most essential pre-requisites for incorporating any form of company under the Companies Act, 2013 (hereinafter referred to as 'Act'). This is evidenced in Section 3 of the Act, which provides the mode of incorporation of a company and states that a company may be formed for any lawful purpose by seven or more persons, where the company to be formed is a public company; two or more persons, where the company to be formed is a private company; or one person, where the company to be formed is a One Person Company by subscribing their names or his name to a memorandum and complying with the requirements of this Act in respect of its registration. To subscribe means to append one's signature or mark a document as an approval or attestation of its contents.

According to Section 2(56) of the Act "memorandum" means the memorandum of association of a company as originally framed and altered, from time to time, in pursuance of any previous company law or this Act. Section 4 of the Act specifies in clear terms the contents of this important document which is the charter of the company. The memorandum of association of a company contains the objects of the company which it shall pursue. It not only shows the objects of formation of the company but also determines the scope of its operations beyond which its actions cannot go. "THE MEMORANDUM OF ASSOCIATION", as observed by Palmer, "is a document of great importance in relation to the proposed company".

ARTICLES OF ASSOCIATION

According to Section 2(5) of the Companies Act, 2013, 'articles' means the articles of association of a company as originally framed or as altered from time to time or applied in pursuance of any previous company law or of this Act. It also includes the regulations contained in Table A in Schedule I of the Act, in so far as they apply to the company.

In terms of section 5(1), the articles of a company shall contain the regulations for management of the company. The articles of association of a company are its bye-laws or rules and regulations that govern the management of its internal affairs and the conduct of its business. The articles play a very important role in the affairs of a company. It deals with the rights of the members of the company inter se. They are subordinate to and are controlled by the memorandum of association. The general functions of the articles have been aptly summed up by Lord Cairns, L.C. in '*Ashbury Railway Carriage and Iron Co. Ltd. v. Riche, (1875) L.R. 7 H.L. 653*' as follows: "The articles play a part that is subsidiary to the memorandum of association. They accept the memorandum of association as the charter of incorporation of the company, and so accepting it, the articles proceed to define the duties, rights and powers of the governing body as between themselves and the company at large, and the mode and form in which business of the company is to be carried on, and the mode and form in which changes in the internal regulations of the company may from time to time be made... The memorandum, is as it were. the area beyond which the action of the company cannot go; inside that area shareholders may make such regulations for the governance of the company as they think fit".

The memorandum lays down the scope and powers of the company, and the articles govern the ways in which the objects of the company are to be carried out and can be framed and altered by the members. The Articles of Association of a company are not 'law' and do not have the force of law. In '*Kinetic Engineering Ltd. v. Sadhana Gadia, (1992) 74 Com Cases 82 : (1992) 1 Comp LJ 62 (CLB)*' the Hon'ble CLB held that if any provision of the articles or the memorandum is contrary to any provisions of any law, it will be invalid in toto.

Clauses in MOA

1) Name Clause 2) Situation Clause
3) Objective Clause 4) Liability Clause
5) Capital Clause 6) Subscription Clause
7) Nomination Clause (Applicable in case of One person Company)

DOCTRINE OF ULTRA VIRES

An act which is ultra vires is void, and does not bind the company. Neither the company nor the contracting party can sue on it. The company cannot make it valid, even if every member assents to it. In the case of a company whatever is not stated in the memorandum as the objects or powers is prohibited by the doctrine of ultra vires*. The general rule is that an act which is ultra vires the company is incapable of ratification. An act which is intra vires the company but outside the authority of the directors may be ratified by the company in proper form[1]. The objective of this doctrine is to protect shareholders and the creditors of the company. If the act is ultra vires (beyond the powers of) the directors only, the shareholders can ratify it. If it is

[1] Rajendra Nath Dutta v. Shilendra Nath Mukherjee, (1982) 52 Com Cases 293 (Cal.)

ultra vires the articles of association, the company can alter its articles in the proper way and thereby such acts can be duly ratified.

CONSTRUCTIVE NOTICE OF MEMORANDUM AND ARTICLES

The memorandum and articles, when registered, become public documents and can be inspected by anyone on payment of nominal fee. Therefore, every person who contemplates entering into a contract with a company has the means of ascertaining and is consequently presumed to know, not only the exact powers of the company but also the extent to which these powers have been delegated to the directors, and of any limitations placed upon the exercise of these powers. In other words, every person dealing with the company is deemed to have a "constructive notice" of the contents of its memorandum and articles. In fact, he is regarded not only as having read those documents but also as having understood them according to their proper meaning [Griffith v. Paget, (1877) Ch. D. 517]. Consequently, if a person enters into a contract which is beyond the powers of the company, as defined in the memorandum, or outside the limits set on the authority of the directors, he cannot, as a general rule, acquire any rights under the contract against the company.[2]

DOCTRINE OF INDOOR MANAGEMENT

While the doctrine of 'constructive notice" seeks to protect the company against the outsiders, the principal of indoor management operates to protect the outsiders against the company. According to this doctrine, as laid down in '*Royal British Bank v. Turquand, (1856) 119 E.R. 886*', persons dealing with a company having satisfied themselves that the proposed transaction is not in its nature inconsistent with the memorandum and articles, are not bound to inquire the regularity of any internal proceedings. In other words, while persons contracting with a company are presumed to know the provisions of the contents of the memorandum and articles, they are entitled to assume that the provisions of the articles have been observed by the officers of the company. It is not a part of the duty of an outsider to see that the company carries out its own internal regulations.

<u>FORMATION AND INCORPORATION OF COMPANIES</u>

Section 3(1) states that a company may be formed for any lawful purpose by—

a) seven or more persons, where the company to be formed is to be a public company;
b) two or more persons, where the company to be formed is to be a private company; or
c) one person, where the company to be formed is to be One Person Company that is to say, a private company by subscribing their names or his name to a memorandum and complying with the requirements of this Act in respect of registration.

[2] Mohony v. East Holyfrod Mining Co., (1875)

A company formed under Section 3(1) may be either—

(a) a company limited by shares; or
(b) a company limited by guarantee; or
(c) an unlimited company.

Procedure for Incorporation of Company

A. SPICEe+

As part of Government of India's EODB initiatives, MCA has come up with new Form SPICE+ replacing the existing SPICe form. Spice+ would offer 10 services by 3 Central Government Ministries & Departments, thereby saving as many procedures, time and cost for starting a Business in India and would be applicable for all new company incorporations w.e.f 23rd February 2020. SPICe form or Form INC-32 helps incorporate a company with a single application for reservation of name, incorporation of a new company and/or application for allotment of DIN.

Some features of Spice+ Form (integrated Web Form)

- SPICe+ would be an integrated Web Form.
- SPICe+ would have two parts viz.: Part A-for Name reservation for new companies and Part B offering a bouquet of services viz. (i) Incorporation (ii) DIN allotment (iii) Mandatory issue of PAN (iv) Mandatory issue of TAN (v) Mandatory issue of EPFO registration (vi) Mandatory issue of ESIC registration (vii) Mandatory issue of Profession Tax registration(Maharashtra) (viii) Mandatory Opening of Bank Account for the Company and (ix) Allotment of GSTIN (if so applied for)
- Users may either choose to submit Part-A for reserving a name first and thereafter submit Part B for incorporation & other services or file Part A and B together at one go for incorporating a new company and availing the bouquet of services as above.

B. Run Form

Reserve Unique Name (RUN) is a web service used for reserving a name for a new company or for changing its existing name. The web service helps you verify whether the name you've chosen for your company is unique. Before the RUN web-form was introduced, all applications concerning company names were to be made in the Form INC-1. The names were to be accompanied with a minimum of 2 Director Identification Number and 1 Digital Signature. Today with the introduction of the RUN web-form, a company name can be reserved easily without the requirement of a digital signature. The purpose of RUN e-form is that any applicant seeking reservation of a proposed company or seeking to change an existing company should apply for reservation through the RUN service. This application will then be processed by the Central Registration Centre (CRC). The proposed name applied should not be undesirable as per the relevant provisions of the Act and the rules mentioned in it.

PROSPECTUS AND ALLOTMENT OF SECURITIES (SECTIONS 23 TO 42)

Prospectus and Allotment of Securities

PROSPECTUS – Sec 26

Sec. 2(70) of the Companies Act, 2013: prospectus means any document described or issued as a prospectus and includes a red herring prospectus referred to in Sec. 32 or shelf prospectus referred to in Sec. 31 or any notice, circular, advertisement or other document inviting offers from the public for the subscription of any securities of body corporate.

Matters to be stated in prospectus

According to Sec. 26 (1), every prospectus issued by or on behalf of a public Co. either with reference to its formation or subsequently, or by or on behalf of any person who is or has been engaged or interested in the formation of a public Co., shall be dated and signed.

The matter contained in the prospectus can be classified under three headings:

General information: the prospectus shall contained the following information, namely

- **Names and addresses**
- **Dates of the opening and closing** Details about underwriting of the issue;
- **Consent of the directors, auditors**, bankers to the issue, expert‘s opinion, if any, and of such other persons, as may be prescribed;
- **Capital structure** of the Co. in the prescribed manner;
- **Main objects of public offer**, terms of the present issue and such other particulars as may be prescribed;
- **Main objects and present business** of the Co. and its location, schedule of implementation of the project;
- **Minimum subscription**, amount payable by way of **premium**, issue of shares otherwise than on cash;

B. Financial information: Prospectus sets out the following reports for the purposes of the financial information, namely:

Reports by the auditors of the Co. with respect to its profits and losses and assets and liabilities and such other matters as may be prescribed;

Reports relating to profits and losses for each of the five financial years immediately preceding the financial year of the issue of prospectus including such reports of its subsidiaries and in such manner as may be prescribed:

C. **Statutory Information:** prospectus shall make a **declaration** about the **compliance of the provisions of this Act** and a statement to the effect that nothing in the prospectus is contrary to the provisions of this Act, the Securities Contracts (Regulation) Act, 1956 (42 of 1956) and the SEBI, 1992 (15 of 1992) and the rules and regulations made thereunder

Other Legal Provisions Relating to Prospectus

- **Compliance of requirements of this Section before registration :** The ROC shall **not register** a prospectus unless the requirements of this Sec. with respect to its registration are complied with and the prospectus is accompanied by the consent in writing of all the persons named in the prospectus.
- **Period for the issue of prospectus :** No prospectus shall be valid if it is issued **more than ninety days after the date on which a copy thereof is delivered to the ROC**
- Prospectus to be registered with the ROC within ninety days before issue and this fact should be stated in the prospectus. The ROC shall not register a prospectus unless the requirements of this Sec. with respect to its registration are complied with and the prospectus is accompanied by the consent in writing of all the persons named in.
- Expert's opinion could only be included if supported by his **consent** for such inclusion and that consent is **not withdrawn before delivering** the prospectus to ROC for registration.
- As per Sec. 2(38) — expert includes an **engineer, a valuer, a Chartered Accountant, a Co. Secretary, a Cost Accountant** and any other person who has the power or authority to issue a certificate in pursuance of any law for the time being in force;
- **Punishment in case of contravention :** If a prospectus is issued in contravention of the provisions of this Sec., the Co. shall be punishable with fine which shall not be less than **fifty thousand rupees but which may extend to three lakh rupees** and every person who is knowingly a party to the issue of such prospectus shall be punishable with imprisonment for a term which may extend to **three years** or with fine which shall not be less than **fifty thousand** rupees but which may extend to **three lakh rupees**, or with both.

Public offer of securities to be in dematerialized form

Sec. 29(1) states that every Co. making public offer; and Such other class or classes of public companies as may be prescribed under the Rule 9 of the *Companies (Prospectus and Allotment of Securities) Rules, 2014*, shall issue the securities only in dematerialised form by complying with the provisions of the Depositories Act, 1996 and the regulations made thereunder.

- Any Co., other than a Co. mentioned in sub-Sec. (1), may convert its securities into dematerialised form or issue its securities in physical form in accordance with the provisions of this Act or in dematerialised form in accordance with the provisions of the Depositories Act, 1996 and the regulations made thereunder.

- Securities could be held in physical or dematerialised form. However public offer of securities has to be mandatorily in demat form in accordance with the Depositories Act, 1996. Demat ensures fool proof control over issue, sale, purchase, pledge, extinguishment of securities lending transparency and credibility to the entire process and securities markets.

SHELF PROSPECTUS, RED HERRING PROSPECTUS AND ABRIDGED PROSPECTUS

Sec. 31 and Sec. 32 deals with important provision related to Shelf Prospectus and Red-herring Prospectus respectively. These twin provisions play a significant role in facilitating commercial and logistical consideration involved in the funds raising cycle. Imagine a situation where the issuer Co. issues debentures **frequently** and has to file a **prospectus every time** it issues a new series of debenture. In this case, concept of shelf prospectus comes into play. Literally, it means prospectus with a **given shelf life**. **Any number of issues** could be made during the **tenure of the shelf** prospectus. The only caveat is to supplement the shelf prospectus by an "**information memorandum**" containing **key updates** or changes. Likewise, developments in financial markets allow innovative methods of raising funds making the most of favourable market conditions. Timing the issue and **Book building** of issue are facilitated by the concept of **red herring prospectus** whereby the **price per security and number of securities** are **left open** to be decided post closure of the issue.

Shelf prospectus –The expression "shelf prospectus" means a prospectus in respect of which the securities or class of securities included therein are issued for subscription in **one or more issues over a certain period without the issue of a further prospectus**

- **Filing of shelf prospectus with the ROC :** According to Sec. 31, any class or classes of companies, as the SEBI may provide by regulations in this behalf, may file a shelf prospectus with the ROC at the stage-
    - of the **first offer** of securities included therein which shall indicate a **period not exceeding one year as the period of validity** of such prospectus which shall commence **from the date of opening of the first offer** of securities under that prospectus, and

- in respect of a **second or subsequent offer** of such securities issued during the period of validity of that prospectus, no further prospectus is required.

- **Filing of information memorandum with the shelf prospectus:** A Company filing a shelf prospectus shall be required to file an information memorandum containing all material facts relating to **new charges created, changes in the financial position of the Company**. as have occurred between the first offer of securities or the previous offer of securities and the succeeding offer of securities and such other changes as may be prescribed, with the ROC within the prescribed time, **prior to the issue** of a second or subsequent offer of securities under the shelf prospectus:

- Provided that where a Co. or any other person has **received applications for the allotment of securities along with advance payments** of subscription before the making of any such change, the Co. or other person shall **intimate the changes** to such applicants and if they express a desire to withdraw their application, the Co. or other person shall **refund** all the monies received as subscription **within fifteen** days thereof.

- **Memorandum together with the shelf prospectus shall be deemed to be a prospectus:** Where an information memorandum is filed, every time an offer of securities is made under sub-Sec. (2), such memorandum together with the shelf prospectus shall be deemed to be a prospectus.

Red herring prospectus— The expression "red herring prospectus" means a prospectus which does not include complete particulars of the quantum or price of the securities included therein. Sec. 32 deals with the issue of red herring prospectus by a Co.. Accordingly law states that-

- **Issue a red herring prospectus prior to the issue of a prospectus:** A Co. proposing to make an offer of securities may issue a red herring prospectus prior to the issue of a prospectus.
- Only the details such as amount of capital required and Price band / range will be specified. The issue price will be determined after the receipt of applications from the subscribers
- **Filing with the ROC :** A Co. proposing to issue a red herring prospectus shall file it with the ROC at least three days prior to the opening of the subscription list and the offer.
- **Same obligation:** A red herring prospectus shall carry the same obligations as are applicable to a prospectus and any variation between the red herring prospectus and a prospectus shall be highlighted as variations in the prospectus.
- After filing of final Prospectus, the subscribers to be given an opportunity to withdraw the application

Abridged prospectus means a memorandum containing such salient features of a prospectus as may be specified by the SEBI by making regulations in this behalf.

Document containing offer of securities for sale to be deemed prospectus Sec. 25 of the Act states the law related to the document by which the offer for sale to the public is made shall, for all purposes, be deemed to be a prospectus issued by the Co..

Securities offered for sale to the public : For the purposes of this Act, it shall, unless the contrary is proved, be evidence that an allotment of, or an agreement to allot, securities was made with a view to the securities being offered for sale to the public if it is shown—

- that an offer of the securities or of any of them for sale to the public was made within six months after the allotment or agreement to allot; or
- That at the date when the offer was made, the whole consideration to be received by the Co. in respect of the securities had not been received by it.

Offer of sale of shares by certain members of Co.

Sec.s 28 of the Act deals with the Offer for sale of securities by certain members of Co.. Where certain members of a Co. propose, in consultation with the Board to offer, in accordance with the provisions of any law for the time being in force, whole or part of their holding of shares to the public, they may do so in accordance with such procedure as may be prescribed.

Variation in terms of contract or objects in prospectus – Sec 27

Sec. 27 deals with Variation in terms of contract or objects in prospectus. Once funds are raised through a given prospectus, the principles of "doctrine of ultra vires" (*mutatis mutandis*) comes into play i.e., the Co. has to use the funds strictly in accordance with the prospectus. Deviations are required to be pre - approved by the investors and recall option to be given to dissenting investors. Deviation regarding use of issue proceeds for buying, trading or otherwise dealing in equity shares of any other listed Co. is not permitted.

Securities to be dealt With in Stock Exchanges: - Sec 40

In accordance to Sec. 40(1) every Co. making public offer shall, before making such offer, make an application to one or more recognised stock exchange or exchanges and obtain permission for the securities to be dealt with in such stock exchange or exchanges.

Mis-Statements in Prospectus

In common parlance, misstatement is the act of stating something that is false or not accurate. It could either be by commission or by omission or by both.

Misstatement of prospectus is a serious offence which attracts **Sec. 34** and / or **Sec. 35.** Liabilities can be classified under two headings:

Criminal liability for mis-statements in prospectus (Sec. 34)

- Where a prospectus, issued, circulated or distributed under this Chapter, includes any statement which is untrue or misleading in form or context in which it is included or where any inclusion or omission of any matter is likely to mislead, every person who authorises the issue of such prospectus shall be liable under Sec. 447:

- Provided that nothing in this Sec. shall apply to a person if he proves that such statement or omission was immaterial or that he had reasonable grounds to believe, and did up to the time of issue of the prospectus believe, that the statement was true or the inclusion or omission was necessary.

Civil liability for mis-statements in prospectus (Sec. 35)

- **Liabilities of persons :** According to **Sec. 35(1),** where a person has subscribed for securities of a Co. acting on any statement included, or the inclusion or omission of any matter, in the prospectus which is misleading and has sustained any loss or damage as a consequence thereof, the Co. and every person who—

    - is a director of the Co. at the time of the issue of the prospectus;
    - has authorised himself to be named and is named in the prospectus as a director of the Co., or has agreed to become such director, either immediately or after an interval of time;
    - is a promoter of the Co.;
    - has authorised the issue of the prospectus; and
    - is an expert referred to in sub-Sec. (5) of Sec. 26,

-shall, without prejudice to any punishment to which any person may be liable under Sec. 36, be liable to pay compensation to every person who has sustained such loss or damage.

Exceptions : No person shall be liable if he proves—

- withdrew his consent to become director before issue of prospectus
- Prospectus issued without his knowledge

ACTION BY AFFECTED PERSONS [SEC. 37]

A suit may be filed or any other action may be taken under Sec. 34 or Sec. 35 or Sec. 36 by any person, group of persons or any association of persons affected by any misleading statement or the inclusion or omission of any matter in the prospectus.

Class Actions – Gift of Companies Act, 2013

- Class action suit is for a group of people filing a suit against a defendant who has caused common harm to the entire group or class. This is not like a common litigation method where one defendant files a case against another defendant while both the parties are available in court. In the case of class action suit, the class or the group of people filing the case need not be present in the court and can be represented by one petitioner.

- The benefit of these type of suits is that if several people have been injured by one defendant, each one of the injured people need not file a case separately but all of the people can file one single case together against the defendant.

- The need for these types of suits was first felt in the context of securities market during the time of Satyam Scam, where a large group of people were cheated regarding their hard earned money invested in Stock Market. During that time, it was felt that it was not at all viable regarding cost effectiveness for a small stakeholder to file a case independently against the defendant. Millions of cheated investors during that time formed a large group and filed the case against the Co., but since there was no available legal remedy or law which can actually support this type of litigation of a group filing charges, it became tough for those investors to take a recourse or gain advantage in the Indian Judicial System by this method.

- Class action suits in India were so far filed under the guise of public interest litigations. Courts were free to dismiss these. These shareholders ran pillar to post right from the National Consumer Disputes Redressal Commission up to the extent of Supreme Court and had their claims rejected.

ALLOTMENT OF SECURITIES BY CO. – Sec 39

"Allotment" means the appropriation out of previously un-appropriated capital of a Co., of a certain number of shares to a person. Till such allotment, the shares do not exist as such. It is on allotment that the shares come into existence.

- According to Section 39 the company shall not allot the share capital unless the company receives the minimum subscription as specified in the prospectus. The company shall file the return of allotment with ROC.

- The Application amount shall not be less than 5% of the nominal value.

- If minimum subscription is not received within 30 days then the company shall refund the application money.

PRIVATE PLACEMENT - OFFER OR INVITATION FOR SUBSCRIPTION OF SECURITIES ON PRIVATE PLACEMENT [SEC. 42]

"Private placement" means any offer of securities or invitation to subscribe securities to a **select group of persons by a Co.** (other than by way of public offer) through issue of a private placement offer letter and which satisfies below conditions.

- A private placement is a way of raising capital that involves the sale of securities to a relatively small number of select investors
- A private placement is different from a public issue in which securities are made available for sale on the open market to any type of investor.
- Any offer or invitation **not in compliance** with the provisions of this Section shall be **treated as a public offer** and all provisions of this Act, and the Securities Contracts (Regulation) Act, 1956 (42 of 1956) and the SEBI, 1992 (15 of 1992) shall be required to be complied with if a Co. makes an offer or accepts monies in contravention of this Sec., the Co., its promoters and directors shall be liable for a penalty which may extend to the **amount involved in the offer or invitation or two crore rupees, whichever is higher**, and the Co. shall also **refund all monies** to subscribers within a period of **thirty days** of the order imposing the penalty.

Share Capital and Debentures

Shares and debentures are financial instruments for raising funds for the Co.. Under the Companies Act, 2013, these are jointly referred to as **"Securities"**. Generally, shares depict **ownership** interest in a Co. with entrepreneurial **risks and rewards** whereas debentures depict **lender's** interest in the Co. with limited risks and returns. Both these financial instruments are presented on the **liabilities side of the issuer Co.** and on the assets side of the investor or lender respectively

SHARE CAPITAL - TYPES [SEC. 43]:

According to Sec. 43, broadly, there are two kinds of share capital of a Co. limited by shares:

- Equity share capital
- Preference share capital.

- The Act defines **preference share capital** as instruments which have **preferential right** to **dividend** payment (absolute/fixed or ad-valorem/%) and preferential **repayment** during winding up of the Co.. These shareholders could also participate in equity pool post the preferential entitlements.
- Shares which are **not preference** shares are termed as **equity shares**.
- Equity shares are further classified as plain vanilla (same voting rights) or Differential equity shares (with differences w.r.t. dividend or voting rights or otherwise)

BASIC REQUIREMENTS [SEC. 45 AND SEC. 46]

Physical entitlement to a particular portion of share capital is *prima facie* evidenced by way of a share certificate which has to be

- Distinctively numbered; &
- Name of Share holder
- To be issued under common seal of the Co. or signed by two directors or by a director and the Co. Secretary, wherever the Co. has appointed a Co. Secretary.

(a) In case required, duplicate could be issued if it is proved to have been **lost** or destroyed; or has been defaced, **mutilated** or torn and is surrendered to the company. post necessary compliances and investigations.

- The aforesaid requirements are not there in case of **dematerialised** shares or shares held in **electronic form** with **any depository**. In that case records of the depository will be treated as *prima facie* evidence of the right involved.
- Where a share is held in depository form, the record of the **depository** is the prima facie evidence of the interest of the **beneficial owner.**

  Demat— Now-a-days most of the listed shares are held in **electronic format**. Even banks and financial institutions now insist for demat of securities for **charge creation** to facility corroboration with central registry for loans and mortgages. Physical securities are mostly limited to private limited companies and closely held companies.

  - At present there are **two depositories** in India: **NSDL and CDSL** with various depository participants (DPs) linked to them. Dematerialised securities are held by investors in their respective accounts with the DP. The DP keeps a track of transfer, transmission, charge creation etc. There are necessary enabling legal enactments to facilitate all these procedures.

RIGHTS AND VARIATION OF RIGHTS [SEC. 47 AND SEC. 48]:

- **Voting right of member holding equity share capital :** Every member of a Co. limited by shares who is holding equity share capital, shall have a **right to vote** on every resolution placed before the Co.; and his voting right on a **poll shall be in proportion to his share in the paid-up equity** share capital of the Co..
- **Voting right of member holding preference share capital :** Every member of a Co. limited by shares who is holding any preference share capital shall, in respect of such capital, have —
  - a right to vote only on resolutions placed before the Co. which **directly affect the rights attached** to his preference shares, and
  - any resolution for the **winding up** of the Co., or
  - for the **repayment or reduction of its equity or preference share capital**

and his voting right on a poll shall be in proportion to his share in the paid-up preference share capital of the Co..

- **Proportion of voting rights :** The proportion of the voting rights of equity shareholders to the voting rights of the preference shareholders shall be in the same **proportion as the paid-up capital in respect of the equity shares bears to the paid-up capital in respect of the preference shares**
    - Where the **dividend** in respect of a class of preference shares has **not been paid for a period of two years or more**, there such class of preference shareholders shall have a **right to vote on all the resolutions** placed before the Co..

VARIATIONS OF SHAREHOLDERS' RIGHTS [SEC. 48]

Where share capital of a Co. is divided into different classes of shares, it may sometimes be necessary for it to amend the rights attached to one or more classes of shares. The Companies Act states the following laws on the variations of shareholders' right :

The shareholders rights may be varied by passing the special resolution. But the shareholders who do not give consent for the resolution and having not less than 10% of the share capital may file a petition to set a side the resolution passed by the company at the general meeting.

SECURITIES ISSUED AT PREMIUM - SEC 52

Meaning: Issue of shares at a price ***higher than its Par value*** (Face Value) is called, Issue at Premium and the differential amount as premium.

- There could be several reason for issue at premium or discount like:
    - To capture the play of market forces between the issuer and investor at the time of issue;
    - To give effect to **fair value of underlying business** or rights linked to the securities;
    - To minimise payment of stamp duty / ROC fee during incorporation of the Co. which is based on the authorised capital of the Co.
- Neither provision in the AOA is required nor Co's act 2013 does not prescribe any or restrictions regarding issue of shares at premium. I.e. no restriction on amount of Premium.
- Where Co. issue shares at premium, the premium amount has to be transferred to separate account called ***Securities premium account***.
- Issue of shares for **cash or for consideration other than cash**, Premium should be transferred to Securities Premium & it should be utilized as per the act.

Utilization of Securities Premium – SP can be utilized only for the bellow mentioned purposes

1. Issuing unissued shares of the Co. ***as fully paid bonus shares*** to members.
2. Writing off ***Preliminary expenses*** of Co.
3. For ***Buy back*** of shares purchase of its own shares U/s 68 of Co's act 2013

4. Providing for ***Premium payable on redemption*** of any redeemable Preference Shares/debentures.
5. Writing of expenses, commission or discount allowed on issue of shares or debentures

ISSUE OF SHARES AT DISCOUNT - SEC 53

Meaning: Issuing shares at a price ***below its Nominal value*** is called issue at Discount. As per Section 53 issue of shares at discount is prohibited. Exception to this rule is issue of sweat equity shares.

PREFERENCE SHARES - ISSUE AND REDEMPTION [SEC. 55]:

No Company limited by shares shall issue any preference shares which are **irredeemable**;

- **Period for redeem of preference shares:** if authorised by its AOA, Co. can issue preference shares which are liable to be redeemed within a **period not exceeding twenty years** from the date of their issue subject to such conditions as prescribed under Rule 9 of the *Companies (Share Capital and Debentures) Rules, 2014*.
- **Exceptions :** A Co. may issue preference shares for a period exceeding twenty years (bot not exceeding thirty years) for **infrastructure projects** (specified in schedule VI), subject to the **redemption of 10 % of shares beginning 21st year** at the option of such preferential shareholders;
- **Shares to be redeemed out of the profits only:**
- **Redeemed shares to be fully paid:** no such shares shall be redeemed unless fully paid;
- **Proposed shares to be redeemed shall be transferred to the CRR account:**

FURTHER ISSUE OF SHARE CAPITAL – RIGHTS ISSUE; PREFERENTIAL ALLOTMENT [SEC. 62]

- A rights issue involves **pre-emptive subscription rights to buy additional securities** in a Co. offered to the Co.'s **existing security holders**.
- It is a **non-dilutive** prorata way to raise capital. **A public Co.** may issue securities through a rights issue or a bonus issue in accordance with the provisions of this Act and in case of a listed Co. or a Co. which intends to get its securities listed also with the provisions of the SEBI Act, 1992 and the rules and regulations made thereunder as per **Sec. 23(1)(c)** of the Companies Act, 2013.
- A **private Co.** may issue securities by way of rights issue or bonus issue in accordance with the provisions of this Act as per the **Sec. 23(2)(a)**.
- As per the Sec. 62 of the Companies Act, 2013-(1) where at any time, a Co. having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered—

(a) to persons who, at the date of the offer, **are holders of equity shares** of the Co. in **proportion, to the paid-up share capital** on those shares by sending a letter of offer subject to the following conditions, namely:—

(i) **the offer shall be made by notice** specifying the **number of shares** offered and limiting a time **not being less than fifteen days and not exceeding thirty days** from the date of the offer within which the offer, if not accepted, shall be deemed to have been **declined**

(b) to employees under a scheme of employees' stock option: subject to **special resolution** passed by Co. and subject to the conditions as may be prescribed; or

(c) to any persons, if it is authorised by a special resolution, whether or not those persons include the persons referred to in clause (a) or clause (b), **either for cash or for a consideration other than cash**, if the price of such shares is determined by the valuation report of a registered valuer subject to such conditions as prescribed under the Rule 13 of the *Companies (Share capital and Debentures) Rules, 2014*.

ISSUE OF BONUS SHARES – SEC 63

- Bonus shares can be issued only ***to existing shareholders*** as fully paid shares at **free** of cost to them by **capitalizing the reserves**.
- AOA authorization regarding issue of bonus shares, if no provision AOA should be altered.
- BOD recommending issue of bonus shares and it is authorized by shareholders in GM by passing OR.
- it has not defaulted in payment of interest or principal in respect of fixed deposits payment of statutory dues of the employees or debt securities issued by it
- Bonus shares issued only ***in respect of fully paid up*** shares and not partly paid up shares.
- ***Bonus shares also should be fully paid up.***
- Bonus shares can be issued out of following sources:

  a) Free Reserve ***b. Share premium received and***

  c) P/L account of credit balance and Capital redemption reserve (CRR)
- Ensure that Bonus shares not issued ***in lieu of declared divided***
- no default in payment of statutory dues and repayment of deposits, loans etc.

REDUCTION OF SHARE CAPITAL [SEC. 66]

Company having huge Accumulated **business losses, assets of reduced or doubtful value, having Fictitious assets** or having investments with no realizable value or having paid up capital in excess of wants of the Co. could lead to the need of reducing share capital.

(1) Reduction of share capital by special resolution: Subject to **confirmation by the**

Tribunal on an application by the Co., a Co. limited by shares or limited by guarantee and having a share capital may, **by a special resolution**, reduce the share capital in any manner —

(a) **extinguish or reduce the liability** on any of its shares in respect of the share capital not paid-up; or

(b) either with or without extinguishing or reducing liability on any of its shares,—

- cancel any paid-up share capital which is **lost or is unrepresented** by available assets; or
- pay off any paid-up share capital which is in excess of the wants of the Co., alter its MOA by reducing the amount of its share capital and of its shares accordingly:

- **No reduction shall be made:** Sec. further Provides that no such reduction shall be made if the Co. is in **arrears in the repayment of any deposits accepted** by it, either before or after the commencement of this Act, or the interest payable thereon.
- **Issue of Notice from the Tribunal:** The Tribunal shall give notice of every application made to it under sub-Sec. (1) to the **CG, Registrar and to the SEBI**, in the case of listed companies, and the creditors of the Co. and shall take into consideration the representations, if any made within a period of **three months** from the date of receipt of the notice
- Provided that where no representation has been received from the CG, Registrar, the SEBI or the creditors within said period, it shall be presumed that they have no objection to the reduction.
- **Order of tribunal:** The Tribunal may, if it is satisfied that the debt or claim of every creditor of the Co. has been discharged or determined or has been secured or his consent is obtained, make an order confirming the reduction of share capital on such terms and conditions as it deems fit:

BUY BACK OF SHARES - SEC 68

Meaning: Buy back means Co. purchasing its own shares. re-acquisition by a Co. of its own securities. It is a way of returning money to its investors

- **Objective/purpose:** Reducing the Dilution of Control
- **Sources:** Free reserves, Securities premium & Proceeds of fresh issue out of different kind of
    - shares or other specified securities.
- **Resolution:** AOA authorization required for buy back, if no provision, AOA should be altered by passing SR.

    a. ***BR in BM*** for buyback not ***exceeding 10% of Aggregate of Paid up Capital & Free Reserves.***

    b. ***Special Resolution*** of Members if buy back ***exceeds 10% but not exceeding 25% of Paid up Capital and Free Reserves (PUC & FR)***

- Buyback in any FY shall **not exceed 25%** of PUC & FR
- Debt equity ratio should not exceed ***2 : 1*** after Buy back.
- notice of the meeting at which special resolution is proposed to be passed shall be accompanied by an **explanatory statement** stating, a full and complete disclosure of all the material facts, the necessity for the buy-back, the class of shares or securities intended to be purchased under the buy back, the amount to be invested under the buy-back;
- The buy-back under Sub-Sec. (1) may be—

  (a) from the **existing share holders** or security holders on a proportionate basis; or

  (b) from the **open market**; or

  (c) by purchasing the securities issued to employees of the Co. pursuant to a scheme of stock option or sweat equity
- Offer of buyback should be open for a period of ***15 days & not exceeding 30 days***
- Buyback of shares can be done only in respect of ***fully paid shares***
- Whole process of Buyback shall complete within ***1 year*** from resolution date.
- Co. has to file ***Declaration of solvency*** with ROC / Stock exchange in case of listed co. stating that it will not be rendered insolvent within a period of one year of the date of declaration adopted by the Board, and signed by at least two directors of the Co., one of whom shall be the managing director
- Co. shall extinguish or ***Physically destroy shares certificates within 7 days***
- Co. shall not issue same kind of securities within ***next 6 months*** except by way of bonus shares, convertible debentures, Sweat equity shares and Employee stock option.
- Co. has to maintain proper register containing Security bought back, consideration paid, condition of buyback and list of eligible persons etc, has to specify in the notice sent to members.
- Return of Buyback should file with ROC and Stock exchange SEBI within 30 days from end of buyback.
- If buy back is from **Securities premium and Free reserves**, Nominal value of shares bought should transfer to CRR (Capital redemption Reserve) can be utilized for issue of bonus shares.
- Buy back is not permitted if Co. defaulted in payment of declared dividend, repayment of deposits and filing Annual returns with ROC. – **SEC 69**

DEBENTURES [SEC. 71]:

As per Sec. 2(30), debenture includes debenture stock, bonds or any other instrument of a Co. **evidencing a debt**, whether constituting a charge on the assets of the Co. or not but not includes instruments specified in III-D of RBI Act 1934 and any other instruments specified by CG win consultation with RBI.

(1) **Issue of debentures with an option to convert:** A Co. may issue debentures with an option to convert such debentures into shares, either **wholly or partly at the time of redemption** Provided that such issue should be approved by a special resolution in general meeting.

(2) No Co. shall issue any debentures carrying any **voting rights**.

(3) **Issue of secured debentures:** Secured debentures may be issued by a Co. subject to such terms and conditions as may be prescribed in Rule 18 of the *Companies (Share Capital and Debentures) Rules, 2014.*

SHAREHOLDERS

A company acts through two bodies of people – its shareholders and its board of directors. A shareholder, commonly referred to as a stockholder, is any individual, company, or institution that owns at least one share of a company's stock. Since shareholders are a company's owners, they receive the rewards of the company's successes in the form of increased stock valuation. For example someone who owns stock in Apple is a shareholder of Apple.

A person or corporation can become a shareholder of a company in three ways:

- By subscribing to the memorandum of the company during incorporation
- By investing in return for new shares in the company
- By obtaining shares from an existing shareholder by purchase, by gift or by will.

Ownership of the corporation entitles the shareholder to particular rights and privileges. However, the rights of a shareholder may be subject to the extent of ownership such that the individual who owns the majority of shares can exercise greater powers than the minority. Shareholders likewise have responsibilities that arise from their ownership of the corporation.

MEETINGS

Meetings of the Board are significant in the light of running of the company more efficiently and effectively. Companies Act, 2013, mandates a company to hold minimal number of meetings of the Board for its proper functioning. Board meetings are crucial for a company's development as these formal meetings are held to devise policies, drive the management, strategize and evaluate the expectations of the stakeholders.

A company is required to hold meetings of the members to take approval of certain business items, as prescribed in the Act. The meeting to be held annually for seeking approval to certain 'ordinary business' is called Annual General Meeting. A meeting to be held to transact any business other than ordinary business is called extraordinary general meeting. In certain cases, a company may have to hold a meeting of the members of a particular class of members. Therefore, the kinds of member meetings are a. Annual General Meeting b. Extra-ordinary general meeting c. Class meetings

ANNUAL GENERAL MEETING SEC. 96

Who Need to Conduct? : Every Company shall conduct Annual General Meeting.

When? Every Annual General Meeting shall be called during business hours, that is, between 9 a.m. and 6 p.m. on any day that is not a National Holiday and

Where? Shall be held either at the registered office of the Company or at some other place as the Central Government may approve in this behalf

Other Conditions:

- The Gap between Two AGMs shall not exceed 15 Months
- In every calendar year there shall be one AGM

EXTRA-ORDINARY GENERAL MEETING (SEC.100)

There are so many matters relating to the business of a company, which requires approval or consent of members in general meeting. It is always not possible for consideration of such matters to wait until the next annual general meeting. The articles of association of the company of the company make provisions for convening general meeting other than the annual general meeting. All general meetings other than annual general meeting are called extra-ordinary general meetings (EGM). According to SS-2 items of business other than ordinary business may be considered at an EGM or by means of a postal ballot, if thought fit by the Board. This means that all the transactions dealt upon in an EGM shall be special business. Following are the key provisions, regarding calling and holding of an extraordinary general meeting:

a) By the Board Suo motu [Section 100 (1)]
b) By Board on requisition of members [Section 100 (2)]
c) By requisitionists [Section 100(4)]
d) By Tribunal [Section 98

DIRECTORS

A corporation is an artificial person which is intangible and invisible. For making any decision and to have knowledge and intention, a living person has a mind and hands by which he carries out his actions. But a corporate body being an artificial person has none of these. So it needs to act through a living person. The company's business is entrusted in the hands of directors. As per **Section 2(34)** of Companies Act 2013 Director means a director appointed to the Board of a Company.

Position of Directors

The position held by the directors in any corporate enterprise is a tough subject to explain as held in the case of Ram Chand & Sons Sugar Mills Pvt. Ltd.v. Kanhayalal Bhargava. The position of a director has been cited by Bowen LJ in the case of Imperial Hydropathic Hotel Co Blackpool v. Hampson as a versatile position in a corporate body. Directors are sometimes described as trustees, sometimes as agents and sometimes as managing partners. These expressions are from indicating point by which directors are viewed in particular circumstances.

Are directors servant of the company?

The directors are the professional men of the company who are hired to direct the affairs of the company. They are the officers of a company and not a servant. In the case of Moriarty v. Regent's Garage Co, it was held that a director is not a servant of the company, but a controller of the affairs of a company.

Directors as agents

In the landmark case of Ferguson v. Wilson, it was clearly recognised that the directors are the agents of a company in the eyes of law. The company being an artificial person can act only through the directors. Regarding this, the relation between the directors and the company is merely like the ordinary relation of principal and agent.

The relation between the directors and the company is similar to the general principle of agency. When a director signs on behalf of the company, it is a company that is held liable and not the director. Also, like agents, they have to declare any personal interest if they have in a transaction of the company.

One of the important points to be noted is that they are not agents of its individual members. They are the agents of the institution.

In the case of Indian Overseas Bank v. RM Marketing, it has been held that the directors of a company could not be made liable merely because he is a director if he has not given any personal guarantee for a loan taken by the company,

Directors as Trustees

In a strict sense, the directors are not the trustees, but they are always considered and treated as trustees of money and properties which comes to their hand or which is under their control. As observed by the Madras High Court in the case of Ramaswamy Iyer v. Brahamayya & Co., regarding their power of applying funds of the company and for the misuse of power, the directors are liable as trustees and after their death, the cause of action survives against their legal representative.

Another reason due to which the directors are described as trustees is because of their nature of the office. Directors are appointed to manage the affairs of the company for the benefit of shareholders. But, the director of a company is not exactly a trustee, as a trustee of will or marriage settlement. He is a paid officer of a company.

As per the principles laid down in the case of Percival v. Wright, directors are not the trustees of the shareholders. They are trustees of the company. The same principle was repeated again in the case of Peskin v. Anderson that the directors are not trustees for shareholders and hold no fiduciary duty to them.

Directors as organs of Corporate body

In the case of Bath v. Standard Land Co. Ltd., Neville **J.** stated that the board of directors are the brain of the company and a company does act only through them.

A corporation has no mind or body and its action needs to be done by a person and not merely as an agent or trustee but by someone for whom the company is liable as his action is the action of the company itself. If we consider a company as a human body, the directors are the mind and the will of the company and they control the actions of the company

Appointment of Directors

The appointment of Directors of a company is strictly regulated by the Company's Act, 2013.

Company to have Board of Directors

Every company is required to have a Board of directors and it should be consisting of individuals as directors and not an artificial person. Section 149 lays down the minimum number of directors required in a company as follows:

1. Public Company– At least 3 directors
2. Private company- At least 2 directors
3. One person company– Minimum 1 director

There can be a maximum of 15 directors. A company may appoint more than 15 directors after passing a special resolution.

The Central Government may prescribe a class or classes of a company have a minimum one women director. Every company is also required to have a minimum of one director who has stayed in India in the previous year for a period of 182 days or more.

Independent Directors

The provisions of Independent Directors has been laid down under section 149(4) of the Companies Act, 2013**.** This section lays down that at least one-third of the total number of directors should be independent directors in every listed company The Central Government may prescribe the minimum number of independent directors in public companies.

Who is an independent director?

Sub-section (6) of section 149, defines that an independent director stands for a director other than a managing director, whole-time director or a nominee director:

1. Who is a person with integrity and has relevant expertise and experience.
2. Who has not been a promoter of the company, its subsidiary or holding company either in past or present.

3. Who himself or his relative has no pecuniary relationship with the company, its holding or subsidiary company, directors or promoters.
4. Who himself or his relative, do not hold the position in key managerial personnel, or not an employee of the company.

The independent director has to declare his independence at the first meeting of the Board and subsequently every year at the first meeting of the Board in the financial year.

An independent director holds office for a term of five years on the Board. He is also eligible for being reappointed after passing a special resolution, but no independent director is to hold the office for more than two consecutive terms.

Election of Independent Directors

The independent directors are to be selected from a data bank which contains certain information such as name, address and qualifications of persons who are eligible and willing to act as an independent director. The data bank is maintained by anybody, institute or association with expertise in the creation and maintenance of data bank and notified by the Central Government. A company has to pick up a person with due diligence, as stated in section 150.

The appointment has to be approved by the company in general meeting, and the manner and procedure for selection of independent directors who fulfil the qualification stated under section 149 may be prescribed by the Central Government.

Appointment of directors through election by small shareholders

A listed company is required to have one director who should be elected by small shareholders as per section 151 of the Companies Act, 2013. Small shareholders in this context are referred to shareholders holding shares of the value of maximum Rs. 20,000.

First Directors

The subscribers of the memorandum appoint the first directors of a company. They are generally listed in the articles of the company. If the first director is not appointed, then all the individuals, who are subscribers become directors. The first director holds the office only up to the date of the first annual general meeting, and the subsequent director is appointed as per the provisions laid down under section 152.

Appointment at the general meeting

Section 152 lays down the provision that directors should be appointed by the company in the General Meetings. The person so appointed is assigned with a director identification number. He also has to make sure in the meeting that he is not disqualified from becoming a director.

The individual appointed has also to file his consent to act as a director within 30 days with the registrar.

Annual rotation

The retirement of the directors by annual rotation can be prescribed by the company in the Articles. If not so, only one-third of the directors can be given a permanent appointment. The tenure of the rest of them must be determined by rotation.

At an annual general meeting, one-third of such directors will go out, and the directors who were appointed first and has been in the office for the longest period will retire in the first place. When two or more directors have been in the office for an equal period of time, their retirement will be determined by mutual agreement, or by a lot.

Reappointment [section 152]

The vacancies created should be filled up at the same general meeting. The general meeting may also adjourn the reappointment for a week. When the meeting resembles and no fresh appointment is made neither there is any resolution for the appointment, then the retiring directors are considered to be reappointed.

The exception to this practice is that the retired directors will not be considered to be reappointed when:

1. The appointment of that director was put to the vote but lost.
2. If the director who is retiring has addressed to the company and its board in writing that he is unwilling to continue.
3. If he is disqualified.
4. When an ordinary or special resolution is required for his appointment.
5. When a motion for appointment of two or more directors by a single resolution is void due to being passed without unanimous consent under section 162.

Fresh Appointment

When it is proposed that a new director should be appointed in the place of retiring director, then the procedure laid down under section 160 of the Companies Act, 2013 is followed:

1. A written notice for his appointment as a director should be left at the office of the company at least 14 days prior to the date of the meeting along with a deposit of Rs.1,00,000.
2. That amount should be refunded to the person if he is elected as a director, or
3. He gets more than 25% of the total valid votes cast.

Appointment by nomination

The appointment of Directors can also be made with respect to the Company's articles and not only through the general meetings. When an agreement between the shareholders has been included in the articles that entitles every shareholder with more than 10% share to be appointed as a director, then they can be nominated as director.

Also, subject to the articles of the company, the Board can appoint any nominated person by an institution in pursuance of law, as a director.

Appointment by voting on an individual basis

The appointment of a director is made by voting at the general meeting as laid down under section 162 of the Companies Act, 2013. The candidates have to vote individually and the wishes of the shareholders regarding each proposed director are required.

As held in the case of Raghunath Swarup Mathur v. Raghuraj Bahadur Mathur, when two or more directors are appointed on the basis of single resolution and voting then it is considered to be void in the eyes of law.

Appointment by proportional representation

As per section 163 of the Companies Act, 2013, the article of a company can enable the appointment of directors through the system of voting by proportional representation. This system of voting is used to make effective minority votes. This system of proportional representation can be followed by a single transferable vote or by the system of cumulative voting or other means.

Appointment of Directors by Board

Generally, the appointment of the directors is done in the annual general meeting of the shareholders but there are two instances when the Board can also appoint a new director:

1. If the article empowers the Board to appoint additional directors along with prescribing the maximum number.
2. Section 161 of the Act also authorises the directors to fill casual vacancies.

Appointment by Tribunal

Under section 242(j) of the Companies act 2013, the Company Law Tribunal has the power to appoint directors.

<u>Disqualifications</u>

The minimum eligibility requirement for the appointment of directors has been laid down under section 164 of the Companies Act, 2013**.** The disqualification for a person to be appointed as a director are:

1. Unsoundness of mind.
2. If he is an undischarged insolvent.
3. When is applied to be declared as insolvent and such application is pending.
4. When he is sentenced for imprisonment for an offence involving moral turpitude for a period of a minimum of 6 months.

5. If the Tribunal or court has passed an order disqualifying him for being appointed as a director.
6. If he has not paid his calls in respect to any shares of the company.
7. When he is convicted of an offence which deals with related party transaction.
8. When he has not complied with the requirements of Director Identification Number.

Removal of directors

The removal of directors takes place by:

1. Shareholders
2. Company Law Tribunal
3. Resignation

Removal by Shareholders

Section 169 of the Companies Act 2013 provides that a director can be removed from his office before the expiration of his term of office by an ordinary resolution. This section does not apply when:

1. The director is appointed by the tribunal in pursuance of section 242.
2. The company has adopted the system of electing two-thirds of his directors by the method of proportional representation.

To remove a director, special notice is required, and such notice should contain the intention to remove the director and the notice should be served at least 14 days prior to such meeting.

As soon as the company receives such notice, the copy of such notice is furnished to the director concerned. Then the concerned director has the right to make a presentation against the resolution in the general meeting. If a director makes a representation, then its copy needs to be circulated among the members.

Removal of Directors by Company Law Tribunal

The removal of directors by the Company Law Tribunal can be done under section 242(2)(h). When an application is made to the tribunal for relief from oppression or mismanagement, then it may terminate any agreement of the company which has been made with a director. When the appointment of a director is terminated then he cannot serve the managerial position of any company for five years without leave of the Tribunal.

Resignation

Earlier, there was no provision for the resignation that by what procedure a director can resign. The resignation was recognised under the provisions laid down under section 318 of the Companies Act, 1956. Under this section, it was held that when a director resigns his office, he is not entitled to compensation.

If the articles mention the provisions for resignation then it will be followed. In the case of Mother Care (India) Pvt. Ltd. v. Ramaswamy P Aiyar**,** the court held that the resignation of a director is effective even if he is the only director in the office.

Now, after the Act of 2013, section 168 lays down the provisions that:

1. The director can resign from his office by giving written notice to the company.
2. On receiving the notice, the board has to take notice of it.
3. The registrar needs to be informed by the company within the prescribed time period.
4. The fact of resignation needs to be placed by the company in the director's report in the immediately following general meeting.
5. The director has to send his copy of the resignation to the registrar along with the detailed reasons within 30 days of the resignation.

Even after resignation, the director is held responsible for any wrong associated with him and which happened during his tenure.

Powers of Directors

General Powers vested under section 179

Section 149 of the Companies Act, 2013 empowers the directors with the general power vested in the Board. The Board of directors is entitled to exercise all the powers and do all required actions which a company is authorised to exercise but such action is subject to certain restrictions.

The powers of directors are co-extensive with the powers of the company itself. The director once appointed, they have almost total power over the operations of the company.

There are two limitations on the exercise of the power of directors which are as follows.

1. The board of directors are not competent to do the acts which the shareholders are required to do in general meetings.

2. The powers of directors are to be exercised in accordance with the memorandum and articles.

The individual directors have powers only as prescribed by memorandum and articles.

The intervention of shareholders in exceptional cases

In following exceptional situations the general meeting is competent to act in matters delegated to the Board:

1. When directors have acted *mala fide*.
2. When directors have due to some valid reason become incompetent to act.
3. The shareholders can intervene when directors are unwilling to act or there is a situation of deadlock.
4. The general meetings of shareholders have residuary powers of a company.

Powers of Board of Directors without prior approval of shareholders

The Companies Act 2013 also lays the manner in which the powers of the company is to be exercised. There certain powers which can be exercised only when its resolution has been passed at the Board's meetings. Those powers such as the power:

1. To make calls.
2. To borrow money.
3. To issue funds of the company.
4. To grant loans or give guarantees.
5. To approve financial statements.
6. To diversify the business of the company.
7. To apply for amalgamation, merger or reconstruction.
8. To take over a company or to acquire a controlling interest in another company.

The shareholders in a general meeting may impose restrictions on the exercise of these powers.

Powers to be exercised with general meeting approval

Section 180 of the Companies Act 2013 states certain powers which can be exercised by the Board only when it is approved in the general meeting:

1. To sale, lease or otherwise dispose of the whole or any part of the company's undertakings.
2. To invest otherwise in trust securities.
3. To borrow money for the purpose of the company
4. To give time or refrain the director from repayment of any debt.

When the director has breached the restrictions imposed under the sections, the title of lessee or purchaser is affected unless he has acted in good faith along with due care and diligence. This section does not apply to the companies whose ordinary business involves the selling of property or to put a property on lease.

Power to constitute an Audit committee

The board of directors are empowered under section 177 to constitute an audit committee. It needs to be constituted of at least three directors, including independent directors. In the committee, the independent directors need to be in the majority. The chairperson and members of the audit committee should be persons with the ability to read and understand the financial statements.

The audit committee is required to act in accordance with the terms of reference specified by the Board in writing.

Power to constitute Nomination and Remuneration Committees and Stakeholders Relationship Committee

The Board of directors can constitute the Nomination and Remuneration Committee and Stakeholders Relationship Committee under section 178. The Nomination and Remuneration Committee should be consisting of three or more non-executive directors out of which one half are required to be independent directors.

The Board can also constitute the Stakeholders Relationship Committee, where the board of directors consist of more than one thousand shareholders, debenture holders or any other security holders. The grievances of the shareholders are required to be considered and resolved by this committee.

Power to make a contribution to charitable or other funds

The Board of directors of the company is empowered under section 181 to contribute to the bona fide charitable and other funds. When the aggregate amount of contribution, in any case, exceeds the 5% of the average net profit of the company for the immediately preceding financial years, then the prior permission of the company in a general meeting is required.

Power to make a political contribution

Under section 182 of the Companies Act 2013**,** the companies can make a political contribution. The company making a political contribution should be other than a government company or a company which has been in existence for less than three years.

Also, the amount of contribution should not exceed 7.5% of the company's net profit in the three immediately preceding financial years. The contribution needs to be sanctioned by a resolution passed by the Board of Directors.

Power to contribute to National Defence Fund

The Board of Directors is empowered to make contributions to the National Defence Fund or any other fund approved by the Central Government for the purpose of National defence under Section 183 of the Companies Act 2013. The amount of contribution can be the amount as may be thought fit. This total amount of contribution made should be disclosed in the profit and loss account during the financial year which it relates to.

CORPORATE SOCIAL RESPONSIBILITY- THE CONCEPT

CSR is a container concept which encompasses many different ecological, social and economic issues. There is a significant change in the social-political-economic environment in twentieth century from nineteenth century. In this century, the corporations are concerned about their social image and assume a variety of social responsibilities in that pursuit unlike their nineteenth century counterpart who were only concerned with limited goal profit maximization. Reason for this development is attributed to a decline in public confidence in corporate operations and sometimes the frustration generated by the large corporate failures and its influence on the everyday life of a common man. There are various definitions about CSR and it is really difficult to stick to one definition. CSR has to be defined in the context of its use and each time a working definition has to be evolved. Moreover, companies chose to adopt one or more CSR initiatives depending on several factors, such as the nature of their business; the diversity and dispersion of their supply chain; how they sell to customers, and sometimes it is just the interest area of a CEO.

By the term 'Corporate Social Responsibility' (CSR), what is generally understood is that business has an obligation to society that extends beyond its narrow obligation to its owners or shareholders. CSR is meeting the ethical, legal, commercial and public expectations of society from a business while the business carry outs its activity in the society. It can be said as giving back what business takes from the society. It is a corporate becoming a good 'corporate citizen' discharging its social and legal duties efficiently.

CSR – WHETHER VOLUNTARY, STRATEGIC OR COMPULSORY?

In the past decade, CSR has become "normal" business practice for most firms operating internationally. This applies even to national firms. There are varying views about CSR practices. Some feel it to be a voluntary initiative, some view it as strategic investment, and for few it is compulsory to make a brand image. An example of voluntary CSR activity would be Satyam Foundation which has started its famous Emergency Management and Research Institute (EMRI). The first view of being voluntary runs through all the views, as CSR is not legally binding on any company. It is on the respective firm to think about it or not to think.

Companies like Arcelor Mittal believe it to be a strategic investment and differentiate it from charitable contributions and even they don't feel that this is something they are pressured into doing. As an example to strategic investment, LN Mittal, cites Kazakhstan where the company has a steel plant and has renewed the tramways, power plants, hotels, stadiums, and developed social activities such as children's camps, and due to this the company believes it's a win-win situation for everyone concerned. But always it's not strategic; rather it is influenced by managers' personal preferences and by firm characteristics, making the CSR investment socially less optimal.

However, this is not the view of everyone. Nobel laureate, Mohammad Yunus has a different opinion about CSR. He says CSR is something which started with the idea to help other people; but today, CSR has only become money to gain better public relations. It is not limited to this proposition; history shows that CSR has been utilized by corporations as a tool of 'greenwashing'.

Speaking about the American Market, Clinard & Yeager (1980) have argued that it would be a mistake to assume that all socially useful contributions by the corporations to workers, consumers, and the environment have always been purely voluntary. Pressures have come from workers (unions) for improved working conditions, including safety guarantees, health insurance and high wages. Thus, even corporations are sometimes pressured into these kinds of activities.

CREATIVE CAPITALISM – SUSTAINABLE CSR

Bill Gates popularized the term 'creative capitalism' to more effectively spread the benefits of capitalism so as to bring improvements in quality of life of those who are left out. It is about "an attempt to stretch the reach of the market forces so that more companies can benefit from doing work that makes more people better of". The mantra of creative capitalism is "the genius of capitalism lies in its ability to make self-interest serve the wider interest." Kris Gopalakrishnan, says "creative capitalism, in many ways, is an evolution of CSR. To put it figuratively, CSR aims to provide fish to feed the hungry; Creative Capitalism aims to teach the needy how to fish, thereby securing their future. It's about making capitalism – the essential philosophy of profit-generation, more socially responsible, equitable and sustainable". Thus, creative capitalism is a CSR which is ingrained in the philosophy of the organizations and a corporate does not have to separately ear-mark a chunk of its capital towards CSR objectives, rather it should be ingrained in all its exercises. 'Creative capitalism' for Airlines Industry has a long way to go.

CSR IN A NEGATIVE TONE

Milton Friedman criticized CSR as subversion from free enterprise system. The direct costs of CSR are the loss of consumer surplus resulting from firms producing less output at higher cost and hence at higher prices. In addition, shareholders receive reduced financial returns. In a comprehensively researched paper sponsored by Oracle in 2005, the statement by David Gerald, founder of Securities Investors' Association, dramatically revealed that "the frittering away of precious shareholders' wealth by international corporations, boards should be given no mandate to give to charities. If they want to do that… then they should put it to a shareholder vote." The Economist report showed in reality only 2% of investors globally said they'll invest in companies undertaking CSR. It is interesting to note that big fraudulent companies like Enron, WorldCom, Tyco (even Satyam) topped the CSR contribution list too (greenwashing).

Going through the foregoing paragraphs it appears that the term 'CSR' is not easy to apply, interpret and follow. Aptly remarked by Martin Wolf:

> *The notion of corporate social responsibility is intensely confused. In particular, it mixes up three quite distinct ideas: intelligent operation of a business; charity; and bearing of costly burdens for the benefit of society at large. The first is essential; the second is optional; and the third is impossible, unless those obligations are imposed on competitors.*

CSR GOING GLOBAL

Global CSR practices are based on ethical values and respect for employees, communities and the environment. There is no internationally accepted approach to CSR, and there is no one right way for firms to incorporate CSR into their global business practices. Companies initiate global CSR initiatives in response to both home country demands (from employees, consumers, and investors) and to adverse conditions in the developing world.

UN Global Compact: The global compact is a voluntary initiative between the United Nations and business, which encourages CSR in the areas of human rights, core labour standards and the environment through its ten universally accepted principles. Speaking on the scheme, UN Secretary General, Ban Ki-moon states “we need business to give practical meaning and reach to the values and principles that connect cultures and peoples everywhere.”

CSR AUDIT

Auditing of CSR practices undertaken by the companies is a tedious and challenging task in view of the voluntary nature and varied area of CSR practices. NGOs have an important role to play in this process. A Tata Energy Research Institute-ORG Marg survey on CSR rated information technology and telecommunications industries as the best. Mehta (2003) in a survey of CSR practices among 30 companies found that the top two areas of intervention were education and health, 80 percent of the companies contributed in the first area and 66 percent in the second. There are processes like Global Reporting Initiative (GRI), AccountAbility 1000 (AA1000), Social Accountability 8000 (SA8000), International Standards Organization (ISO), International Audit Practices Committee (IAPC), International Standards on Auditing (ISAs), and Coalition of Environmentally Responsible Economies (CERES).

CORPORATE SOCIAL RESPONSIBILITY IN THE AVIATION INDUSTRY

CSR in Aviation Industry is an important topic from the point of view of educators, industry players and the society in which these operate. Aviation industry is one of the important links in the whole tourism industry and has several effects on the society in the form of generation of employment, effects on environment and communities. Various Airlines players follow CSR practices in one form or the other nationally and internationally. These practices range from community service to providing ‘free miles’ to the passengers to initiating researches for protection of the environment. There is always as surge to find out whether the airline industry is acting ethically and in a socially responsible manner and also to find out whether they are acting only in their self-interest.

Organizations in Aviation Sector – Their Concern towards CSR:

International Air Transport Association – IATA represents some 230 Airlines comprising of 93% of scheduled international air traffic. As far as CSR in aviation sector is concerned, IATA aims at zero emission future and has come up with a four-pillar strategy for achieving carbon neutral growth in the medium term. The four pillar strategy of IATA includes: (1) Investment in new technology and alternative fuels (2) flying aircraft effectively (3) building and operating efficient infrastructure and (4) supporting positive economic measures such as tax credits. Environment is one of the top priorities of IATA, to limit the climate change impact, emissions and noise.

International Civil Aviation Organization – ICAO was formed by Convention on International Civil Aviation which was signed by 52 States. Key objectives of ICAO include flight safety information exchange, aviation security, safety oversight audit and environmental protection. ICAO has endorsed the four-pillar strategy of IATA, as well as the target to improve fuel efficiency by a further 25% by 2020 compared to 2005. ICAO recognizes CSR provided by UN Global Compact. ICAO's current environmental activities are largely undertaken through the Committee on Aviation Environmental Protection (CAEP), which was established by the Council in 1983, superseding the Committee on Aircraft Noise (CAN) and the Committee on Aircraft Engine Emissions (CAEE).

Association of Corporate Travel Executives: CSR has been a part of ACTE's education curriculum since 2004. At all major ACTE conferences, CSR sessions are included ranging from green and environmental issues to social and human rights issues. There is a CSR committee and ACTE reaches out to business, industry, trade associations, communities, universities, and state and local governments to engage them on CSR issues related to the business travel industry. By partnering on educational events, research and advocacy, ACTE is able to leverage a global network of organizations to provide additional value to its members and its partners' members like British Airways, The Carbon Neutral Company, The Climate Trust, Concur, Lufthansa, and Philips.

Airports Authority of India – The AAI was formed on 1st April 1995 by merging the International Airports Authority of India and the National Airports Authority with a view to accelerate the integrated development, expansion and modernization of the operational, terminal and cargo facilities at the airports in the country conforming to international standards. There is no specific policy by AAI on CSR to be followed by aviation players in India.

Director General Civil Aviation – DGCA is an attached office of the Ministry of Civil Aviation in India. It is the regulatory body in the field of Civil Aviation primarily dealing with safety issues. It is responsible for regulation of air transport services to/from/within India and for enforcement of civil air regulations, air safety and airworthiness standards. It also co-ordinates all regulatory functions with ICAO. DGCA does not specifically deal with CSR initiatives.

Thus, one can see that apart from the environmental concern, CSR activities are not taken very seriously by these organizations. There is a need for seminars/discussions on this point by these associations and their members so as to form an opinion in favour of CSR.

Airlines Industry in India

Air travel has become an integral way of life in a highly globalised world. Aviation Industry in India is one of the fastest growing aviation industries in the world. Revolutionized by liberalization, the aviation sector in India has been marked by fast-paced changes in the past few years. By 2010, it is expected that India's fleet strength will stand at 500-550, and the domestic market size will cross 60 million and international traffic 20 million. According to the Ministry of Civil Aviation, the airline business in India is growing at 27 per cent a year. Between May 2007 and May 2008, airlines carried 25.5 million domestic and 22.4 million international passengers. Air passenger traffic in India had grown by a staggering 40 per cent in fiscal 2007 and 27 per cent in 2008 .

With the liberalization of the Indian aviation sector, aviation industry in India has undergone a rapid transformation. From being primarily a government-owned industry, the Indian aviation industry is now dominated by privately owned full service airlines and low-cost carriers. Private airlines account for around 75% share of the domestic aviation market. Earlier air travel was a privilege only a few could afford, but today comparatively air travel has become much cheaper and can be afforded by a large number of people.

Analysis of CSR Initiatives by Indian Aviation players

Airlines industry in India has seen a lot of twists and turns. Hike in fuel prices were of major concern. Lifting of restriction on foreign investment in this sector has revolutionalized the airlines industry. The following are the initiatives taken by the key important players in the Indian Airlines Industry.

Jet Airways (Jet Lite): This is an airline that has pioneered concepts like ThroughCheck-in, City Check-in, Web and Kiosk check-in, SMS check-in, automated tickets at travel agency locations, e-ticketing, JetMobile and the unique five-tier frequent flier programme JetPrivilege in India. Jet Airways commenced its operations in May 1993. Jet Airways, in 1998 launched its Yellow Rose campaign. Jet Airways is involved in community service by activities like Blood Donation, relief efforts for earthquake, tsunami, Magic-Box Contribution, Ecofriendly Napkin Cords, and Flights of Fantasy Programme. Recently, Jet Airways was in news for sacking 1,900 probationary and temporary workers to overcome the slowdown that hit the aviation sector as a result of which it was suffering daily losses of Rs 10 crore immediately a day after the alliance with Kingfisher. However, followed by the protests from various sectors, the decision was changed and the employees were reinstated.

Kingfisher (Kingfisher Red – formerly Deccan): It is one of the prominent Airlines in India managed and maintained by the famous conglomerate UB Group, which has majority business of manufacturing spirit and alcohol. UB Group as a conglomerate claims to be a silent crusader in the field of community service and has over the years been endeavoring to emerge as a socially responsible corporate citizen. CSR activities by UB Group includes a super specialty hospital - Mallya Hospital (Vijay Mallya) at Bangalore where subsidized health care is given to the under privileged class of society by providing a general ward which is reserved for them. In the field of education, the Group has assisted in the setting up of the Mallya Aditi International School. A certain number of seats are reserved for the economically backward strata of society whose education is subsidized by the UB Group.

Air India (Indian Airlines): To develop responsible and active citizen and promote a clean environment, Air India has taken up an innovative venture of encouraging students and teachers alike in nation-building exercise as part of the airline's pan- India corporate social responsibility initiative. RANK (Race for Awareness and Knowledge) and BOLT (Broad Outlook Learner Teacher) are the two awards that the Air India has instituted in a tie-up with a private television channel, designed to promote creative thinking and leadership among the students and teachers in areas of societal development. In the year 2006, Air India received The Galileo Express Travel World Awards Special Category (CSR) for its CSR initiatives in the areas of environmental conservation, social welfare, education and community development amongst others.

Go Airlines: Go Airlines (India) Pvt Ltd is the aviation foray of the Wadia Group. The airline operates its services under the brand GoAir. GoAir launched its operations in November 2005. Wadia Group uses the word ‘philanthropy’ for its CSR activities. Philanthropy by Wadia group includes construction of five gardens in Mumbai between 1908 to 1956. Further there are hospitals in Mumbai and college in Pune. Sir Ness Wadia Foundation, a charitable trust set up in 1969 has worked for rehabilitation of Latur earthquake victims, and scholarship for disabled in draught relief.

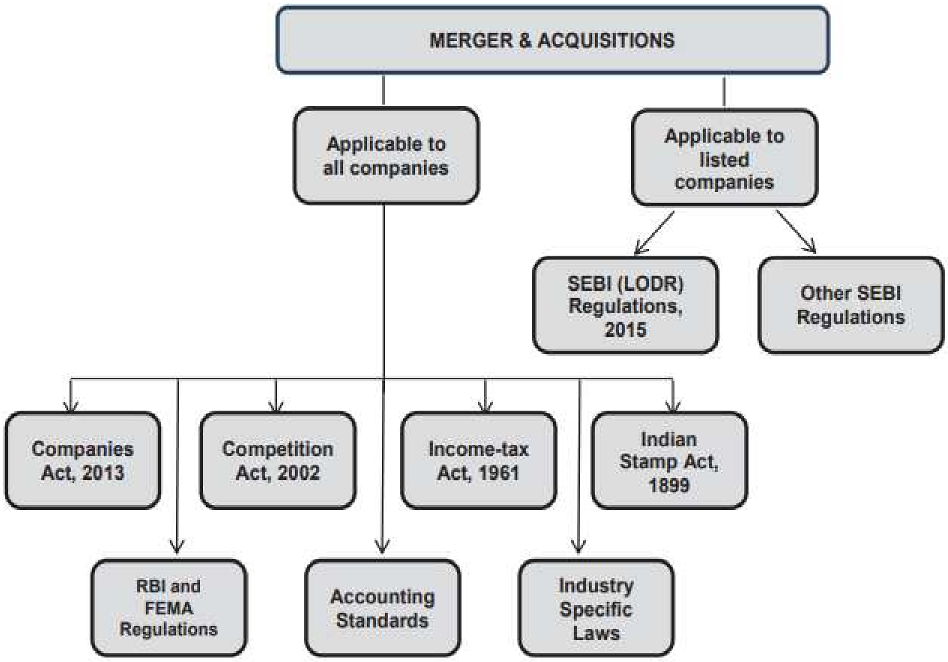
Indigo: InterGlobe Enterprises is a diversified international corporation with business interests in varied areas of tours and travels. One of its initiatives is the low-cost domestic airline services in India. There were no links available as to the company’s CSR activities.

SpiceJet: This is again a low-cost airline service provider which started its operation in 2005. though the company has a vision for total customer satisfaction and stakeholder’s value, it does not address the issue of CSR directly.

MODULE II

CORPORATE RESTRUCTURING & JOINT VENTURES IN AVIATION

LEGAL FRAMEWORK FOR MERGERS AND ACQUISITIONS



Corporate Restructuring is an expression that connotes a restructuring process undertaken by business enterprise. It is the process of redesigning one or more aspects of a company. Hence, Corporate Restructuring is a comprehensive process by which a company can consolidate its business operations and strengthen its position for achieving its short-term and long-term corporate objectives. A business may grow over time as the utility of its products and services is recognized, but it is a long drawn process. It may also grow through an inorganic process, symbolized by an instantaneous expansion in work force, customers, infrastructure resources and thereby an overall increase in the revenues and profits of the entity.

Corporate restructuring play a major role in enabling enterprises to achieve economies of scale, global competitiveness, right size, reduction of operational costs and administrative costs.

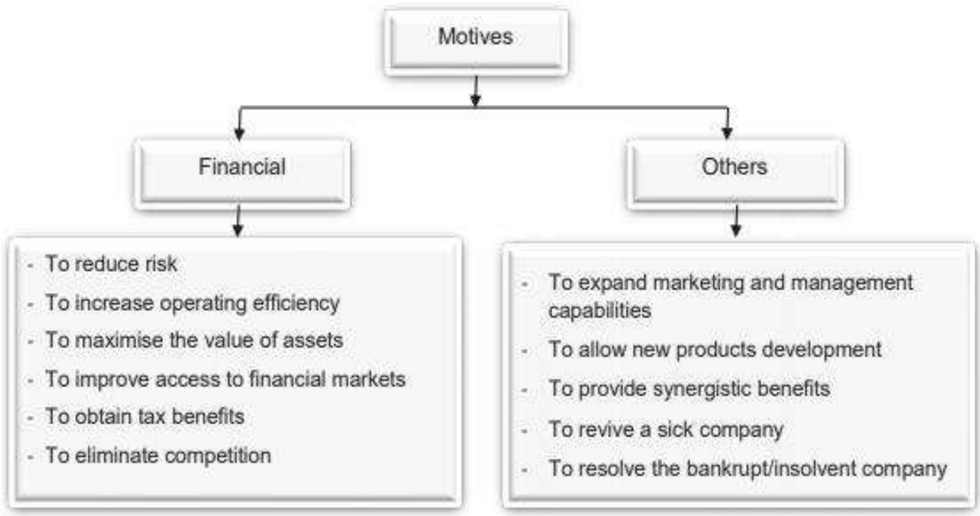
NEED AND SCOPE

Corporate Restructuring is concerned with arranging the business activities of the Corporate as a whole so as to achieve certain pre-determined objectives at corporate level. Objectives may include the following:

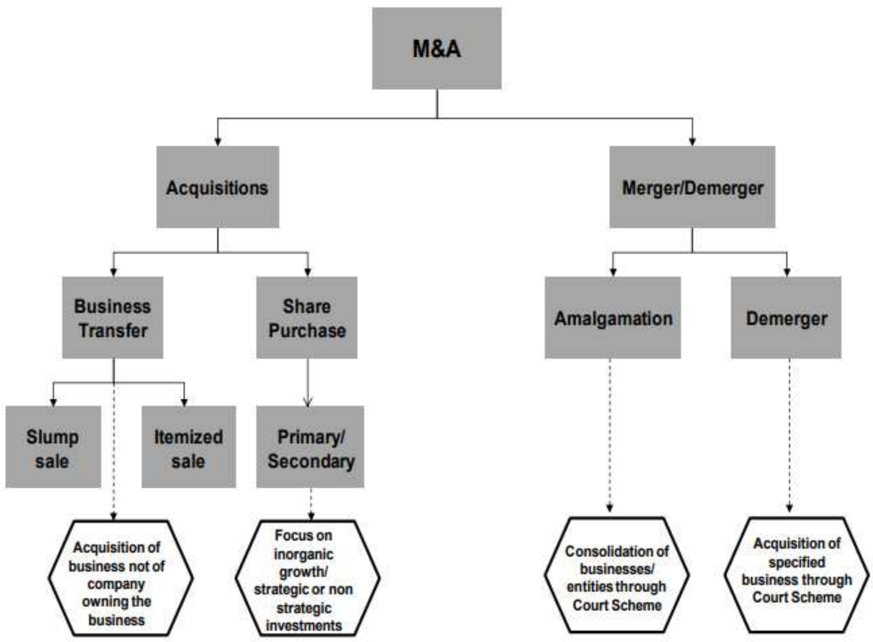
- To enhance shareholders value
- Orderly redirection of the firms activities
- Deploying surplus cash from one business to finance profitable growth in another
- Exploiting inter-dependence among present or prospective businesses

- Risk reduction
- Development of core-competencies
- To obtain tax advantages by merging a loss-making company with a profit-making company
- To have access to better technology
- To become globally competitive
- To increase the market share

MOTIVES BEHIND CORPORATE RESTRUCTURING



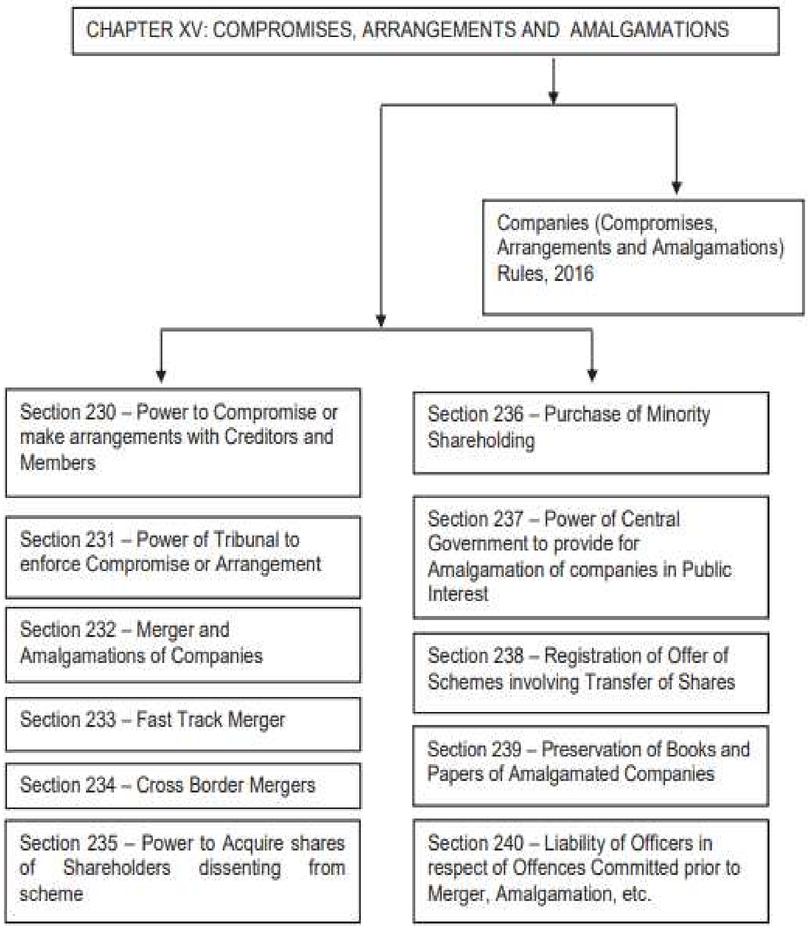
VARIOUS MODES OF CORPORATE RESTRUCTURING



LEGAL FRAMEWORK OF CORPORATE RESTRUCTURING

Corporate Restructuring in India is governed by the following Acts, Rules, etc.:

- Chapter XV of The Companies Act, 2013 (the Act)
- Buy Back of shares/purchase of own securities
- Reduction of share capital
- Companies (Compromises, Arrangements, and Amalgamations) Rules, 2016
- Income Tax Act, 1961
- Accounting Standards
- Foreign Exchange Management Act, 1999 : The Foreign Exchange Management Act, 1999 (FEMA) is an Act of the Parliament of India "to consolidate and amend the law relating to foreign exchange with the basics of facilitating external trade and payments and for increasing the orderly development & maintenance of foreign exchange market in India".
- Competition Act, 2002: The law of M&A and Competition Law are intrinsically bound with each other as any combination including merger and acquisition has to undergo the regulatory stratagem as enumerated under the Competition Act, 2002.
- Intellectual Property Rights
- Indian Stamp Act, 1899
- Insolvency and Bankruptcy Code, 2016



Regardless of their category or structure, all mergers and acquisitions have one common goal: they are all meant to create synergy that makes the value of the combined companies greater than the sum of the two parts. The success of a merger or acquisition depends on whether this synergy is achieved. Synergy takes the form of revenue enhancement and cost savings. By merging, the companies hope to benefit from the following:

Becoming bigger: Many companies use M&A to grow in size and leapfrog their rivals. While it can take years or decades to double the size of a company through organic growth, this can be achieved much more rapidly through mergers or acquisitions.

Pre-empted competition: This is a very powerful motivation for mergers and acquisitions, and is the primary reason why M&A activity occurs in distinct cycles.

Domination: Companies also engage in M&A to dominate their sector. However, since a combination of two behemoths would result in a potential monopoly, such a transaction would have to face regulatory authorities.

Tax benefits: Companies also use M&A for tax purposes, although this may be an implicit rather than an explicit motive.

Economies of scale: Mergers also translate into improved economies of scale which refers to reduced costs per unit that arise from increased total output of a product.

Acquiring new technology: To stay competitive, companies need to stay on top of technological developments and their business applications. By buying a smaller company with unique technologies, a large company can maintain or develop a competitive edge.

Improved market reach and industry visibility: Companies buy other companies to reach new markets and grow revenues and earnings. A merger may expand two companies' marketing and distribution, giving them new sales opportunities. A merger can also improve a company's standing in the investment community: bigger firms often have an easier time raising capital than smaller ones.

MERGERS

The term merger and amalgamation has not been defined under the Act. M&A is often known to be a single terminology. However, there is a thin difference between the two. 'Merger' is the fusion of two or more companies, whereby the identity of one or more is lost resulting in a single company whereas 'Amalgamation' signifies the blending of two or more undertaking into one undertaking, blending enterprises loses their identity forming themselves into a separate legal identity. There may be amalgamation by the transfer of two or more undertakings to a new or existing company. 'Transferor Company' means the company which is merging also known as amalgamating company in case of amalgamation and 'transferee company' is the company which is formed after merger or amalgamation also known as amalgamated company in case of amalgamation.

A merger is a legal consolidation of two entities into one entity which can be merged together either by way of amalgamation or absorption or by formation of a new company. The Board of Directors of two companies approve the combination and seek shareholders' approval. After the merger, the acquired company ceases to exist and becomes part of the acquiring company. Some recent examples are acquisition of eBay India by Flipkart, Vodafone-Idea merger and Axis Bank's acquisition of free charge, State Bank of India merger with all its subsidiary banks etc.

Types of Mergers

(A) Horizontal Merger

Horizontal Merger is a merger between companies selling similar products in the same market and in direct competition and share the same product lines and markets. It decreases competition in the market. The main objectives of horizontal merger are to benefit from economies of scale, reduce competition, achieving monopoly status and control of the market.

(B) Vertical Merger

Vertical Merger is a merger between companies in the same industry, but at different stages of production process. In another words, it occurs between companies where one buys or sells something from or to the other.

(C) Conglomerate Merger

Conglomerate merger is a merger between two companies that have no common business areas. It refers to the combination of two firms operating in industries unrelated to each other. The business of the target company is entirely different from the acquiring company. The main objective of a conglomerate merger is to achieve big 10 PP-CRILW size e.g., a watch manufacturer acquiring a cement manufacturer, a steel manufacturer acquiring a software company, etc.

(D) Congeneric Merger

Congeneric merger is a merger between two or more businesses which are related to each other in terms of customer groups, functions or technology e.g., combination of a computer system manufacturer with a UPS manufacturer.

ACQUISITION

Acquisition occurs when one entity takes ownership of another entity's stock, equity interests or assets. It is the purchase by one company of controlling interest in the share capital of another existing company. Even after the takeover, although there is a change in the management of both the firms, companies retain their separate legal identity. The companies remain independent and separate; there is only a change in control of the companies. When an acquisition is 'forced' or 'unwilling', it is called a takeover.

From a commercial and economic point of view, mergers and acquisitions generally result in the consolidation of assets and liabilities under one entity, and the distinction between a "merger" and an "acquisition" is less clear. A transaction legally structured as an acquisition may have the effect of placing one party's business under the indirect ownership of the other party's shareholders, while a transaction legally structured as a merger may give each party's shareholders partial ownership and control of the combined enterprise. Contemporary corporate restructurings are usually referred to as merger and acquisition (M&A) transactions rather than simply a merger or acquisition. The practical differences between the two terms are slowly being eroded by the new definition of M&A deals. In other words, the real difference lies in how the purchase is communicated to and received by the target company's board of directors, employees and shareholders.

Mergers and Acquisitions –

Primary Factors to be considered Merger or amalgamation is undertaken for acquiring cash resources, eliminating competition, saving on taxes or influencing the economies of large-scale operations. Therefore, there are host of factors, which require consideration before initiating a merger or amalgamation exercise. A detailed list of the primary factors requiring consideration before initiating a merger or amalgamation from the economic, commercial and legal perspective is explained as follows:

(i) Identification of Parties Will one or more businesses be transferred to an existing firm or a newly formed entity? Consider drafting heads of terms, do you require a confidentiality agreement? Do you require an exclusivity agreement? Review financial liability of the parties - undertake appropriate searches.

(ii) Due Diligence Carry out legal, commercial, tax and financial due diligence on the parties entering into the transaction. This will help in identifying risk areas along with any necessary consent you will need to obtain.

(iii) (Any third-party consents required? Ascertain if any third-party consents would be required such as from banks, business contracts, partner / shareholder consents. These should emerge from due diligence. Consider also regulatory consents / licences that may be required.

(iv) Taxation It will be necessary to ascertain the most suitable tax structure for the transaction and, in particular, the way in which the consideration should be structured, at an early stage, therefore consider consulting tax advisors.

(v) Risk Sharing of risk – What kind of indemnities / warranties be considered? Should there be a cap on such indemnities and warranties?

(vi) Will the transaction impact on existing loan/finance arrangements? Check loan documents and constitution documents to see whether any proposed borrowing would be a breach of any existing funding. What will happen in relation to third party funding of the Seller business? Confirm that there are no restrictions on the disposal of the target business or any of its assets. How will the merged business be funded?

(vii) Existing Charges / Modifications over the assets to be acquired Are there any mortgages, charges or debentures over any of the business assets? If yes, obtain copies and consider how they are to be discharged. If there are floating charges, obtain certificates of non-crystallisation / release. Obtain a Search Report from a Practicing Company Secretary.

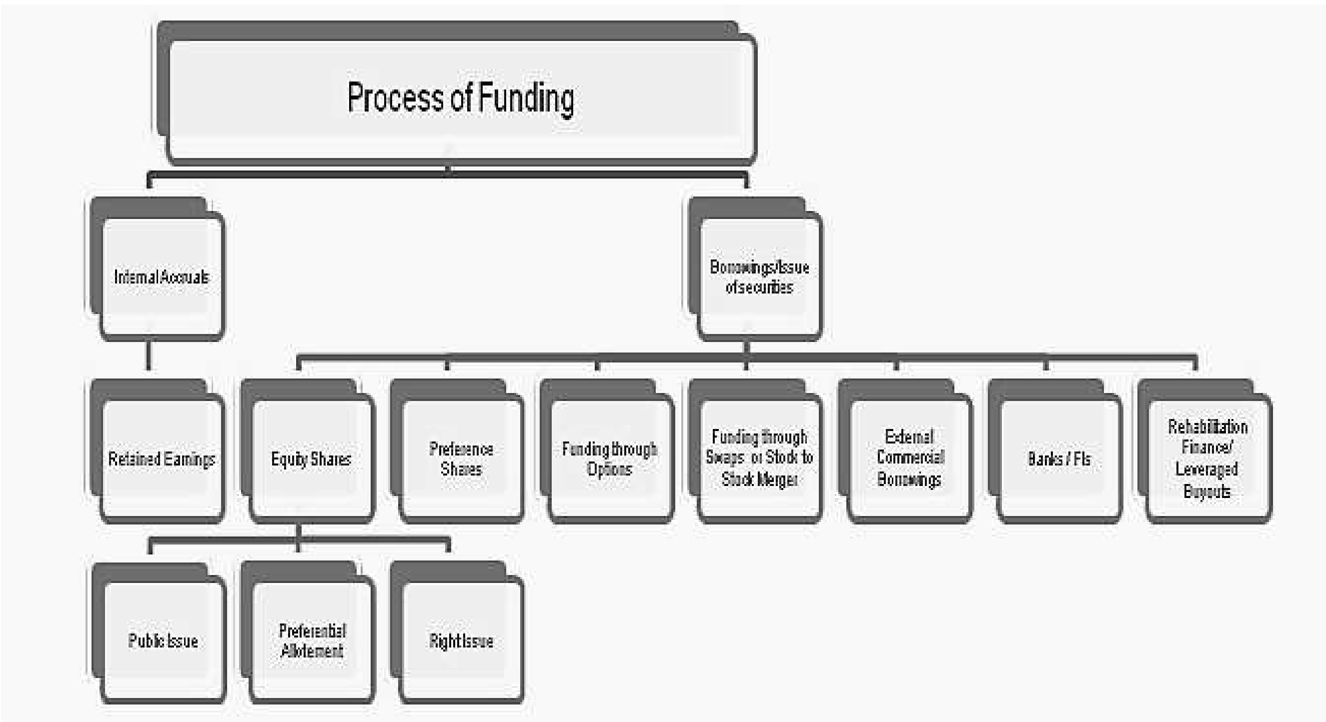
(viii) Guarantees and indemnities (bank or other) Has the Seller given or received any guarantees or indemnities in relation to the business? If yes, then obtain copies (including details of arrangements) and consider in particular, how to ensure the business continues to have the benefit of relevant guarantees.

(ix) Licences Will the Buyer have all other licences which it needs to operate the business?

(x) Supply contracts Will supply contracts be transferred or need to be terminated? How will this be done?

(xi) What IP is used in the business? Obtain a full list of trademarks, service marks, patents, designs, domain names, copyright and other registered and unregistered intellectual property used in the business. Carry out trade mark and patent searches as may be appropriate through an IPR Attorney.

PROCESS OF FUNDING:



AMALGAMATION

Amalgamation is defined as the combination of one or more companies into a new entity. It includes:

(i) Two or more companies join to form a new company.

(ii) Absorption or blending of one by the other.

Amalgamation is a legal process by which two or more companies are joined together to form a new entity or one or more companies are to be absorbed or blended with another as a consequence the amalgamating company loses its existence and its shareholders become the shareholders of new company or amalgamated company. In other words, property, assets, liabilities of one or more companies is taken over by another or are absorbed by and transferred to an existing company or a new company. Therefore, the essence of amalgamation is to make an arrangement thereby uniting the undertakings of two or more companies so that they become vested in, or under the control of one company which may or may not be the original of the two or more of such uniting companies.

The word "amalgamation" is not defined under the Companies Act 2013 whereas section 2(1B) of Income Tax Act, 1961 defines Amalgamation as: "amalgamation", in relation to companies, means the merger of one or more companies with another company or the merger of two or more companies to form one company (the company or companies which so merge being referred to as the amalgamating company or companies and the company with which they merge or which is formed as a result of the merger, as the amalgamated company) in such a manner that – (i) all the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation; (ii) all the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation; (iii) shareholders holding not less than three-fourths in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee for, the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of the amalgamation, otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first-mentioned company. Amalgamation includes absorption. The Institute of Chartered Accountants of India has issued Accounting Standard (AS) 14 on Accounting for Amalgamations.

Reasons for Amalgamation:

(a) To acquire cash resources

(b) To eliminate competition

(c) Tax savings/advantages

(d) Economies of large scale operations

(e) To Increase shareholders value

(f) To reduce the degree of risk by diversification

(g) Managerial effectiveness

(h) To achieve growth and financial gain

(i) Revival of weak or sick or insolvent/bankrupt company

(j) Survival

(k) Sustaining growth

CONSOLIDATION

A consolidation creates a new company. Stockholders of both companies approve the consolidation, and subsequent to the approval, receive common equity shares in the new firm. Example: In 1998 Citicorp and Traveller's Insurance Group announced a consolidation, which resulted in Citigroup.

TENDER OFFER

One company offers to purchase the outstanding stock of the other firm at a specific price. The acquiring company communicates the offer directly to the other company's shareholders. Example: Johnson & Johnson made a tender offer in 2008 to acquire Omrix Biopharmaceuticals for $438 million.

ACQUISITION OF ASSETS

In a purchase of assets, one company acquires the assets of another company. The company whose assets are being acquired, obtain approval from its shareholders. The purchase of assets is typical during bankruptcy proceedings, where other companies bid for various assets of the bankrupt company, which is liquidated upon the final transfer of assets to the acquiring firm(s).

MANAGEMENT BUYOUT

A management buyout (MBO) is a transaction where a company's management team purchases the assets and operations of the business they manage. MBO is appealing to professional managers because of the greater potential rewards from being owners of the business rather than employees. According to global consultancy giant Grant Thornton, the overall deal activity -- including both mergers and acquisitions and PE (private equity) -- was about $59 billion in the January-November period of 2017, a 9 per cent rise from the previous year 2016.

PURCHASE OF COMPANY AS RESOLUTION APPLICANT UNDER IBC LAW

The basic objective behind the Insolvency and Bankruptcy Code 2016 is to revive the insolvent company by approving the effective resolution plan and maximization of assets of the corporate debtor. As per the Code, the company under insolvency can be purchased by the resolution applicant by participating in the bid process by submitting the most effective resolution plan. This way the insolvent company can be revived by some other company/group/individuals., Example: Tata Steel has taken over the bankrupt Bhushan Steel for ₹35,200 crore.

JOINT VENTURE

A joint venture (JV) is a business or contractual arrangement between two or more parties which agree to pool resources for the purpose of accomplishing a specific task may be a new project or any other business activity. In a joint venture (JV), each of the participants is responsible for profits, losses and costs associated with it. Company enters into a joint venture when it lacks required knowledge, human capital, technology or access to a specific market that is necessary to be successful in pursuing the project on its own.

For example, A Ltd. may own technology, manufacturing and production facilities that B Ltd. needs to create and ultimately distribute a new product. A joint venture between the two companies gives B Ltd. access to the equipment without purchasing or leasing it, while A Ltd. is able to participate in production of a product without incurring costs to develop. Each company benefits when the joint venture is successful, and neither is left to complete the project alone.

Types of Joint Ventures

(a) Equity-based joint ventures is a type of joint venture in which two or more parties set-up a separate legal company to act as the vehicle for carrying out the project. This new company would usually be located in the same country as one of the two partner companies, with the purpose of mutually establishing an activity with its own objectives: marketing and distribution, research, manufacturing, etc. It benefits foreign and/or local private interests, or members of the general public through capital.

(**b) Non-equity joint ventures** also known as cooperative agreements, seek technical service arrangements, franchise, brand use agreements, management contracts, rental agreements, or onetime contracts, e.g., for construction projects, non-equity arrangements in which some companies are in need of technical services or technological expertise than capital. It may be modernizing operations or starting new production operations.

STRATEGIC ALLIANCE

Nike, the world's largest producer of athletic foot-wear, does not produce a single shoe. Boeing, the giant aircraft company, makes little more than cockpits and wing bits. These organizations, like a number of other businesses nowadays, have created strategic alliances with their suppliers to do much of their actual production for them. A strategic alliance is an arrangement between two companies that have decided to share resources to undertake a specific, mutually beneficial project. It is an excellent vehicle for two companies to work together profitably. It can help companies develop and exploit the unique strengths. Organizations get an opportunity to widen customer base or utilize the surplus capacity.

TAKE OVER

Where an acquirer takes over the control of the 'target company', it is termed as takeover. When an acquirer acquires 'substantial quantity of shares or voting rights' of the target company, it results into substantial acquisition of shares. Takeovers and acquisitions are common occurrences in the business world. In some cases, the terms takeover and acquisition are used interchangeably, but each has a slightly different connotation. A takeover is a special form of acquisition that occurs when a company takes control of another company without the acquired firm's agreement. Takeovers that occur without permission are commonly called hostile takeovers.

Acquisitions, also referred to as friendly takeovers, occur when the acquiring company has the permission of the target company's Board of directors to purchase and takeover the company. Acquisition refers to the process of acquiring a company at a price called the acquisition price or acquisition premium. The price is paid in terms of cash or acquiring company's shares or both. As the motive is to takeover of other business, the acquiring company offers to buy the shares at a very high premium, that is, the gaining difference between the offer price and the market price of the share. This entices the shareholders and they sell their stake to earn quick money. This way the acquiring company gets the majority stake and takes over the ownership control of the target company.

KINDS OF TAKEOVER

Takeovers may be broadly classified into three kinds:

(i) Friendly Takeover: Friendly takeover is with the consent of taken over company. In friendly takeover, there is an agreement between the management of two companies through negotiations and the takeover bid may be with the consent of majority or all shareholders of the target company. This kind of takeover is done through negotiations between two groups. Therefore, it is also called negotiated takeover.

(ii) Hostile Takeover: When an acquirer company does not offer the target company the proposal to acquire its undertaking but silently and unilaterally pursues efforts to gain control against the wishes of existing management.

(iii) Bailout Takeover: Takeover of a financially sick company by a profit earning company to bail out the former is known as bailout takeover. There are several advantages for a profit making company to takeover a sick company. The price would be very attractive as creditors, mostly banks and financial institutions having a charge on the industrial assets, would like to recover to the extent possible.

LEGAL ASPECTS OF TAKEOVER

The legislations/regulations that mainly govern takeover are as under: 1. Companies Act, 2013 2. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (The Regulations) 3. SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 As far as Companies Act, 2013 is concerned, the provisions of Section 186 apply to the acquisition of shares through a company. Section 235 and 236 of the Companies Act, 2013 lays down legal requirements for purpose of takeover of an unlisted company through transfer of undertaking to another company. SEBI (SAST) Regulations, 2011 lays down the procedure to be followed by an acquirer for acquiring majority shares or controlling interest in another company.

As per Regulation 31A(5) of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, if any public shareholder seeks to re-classify itself as a promoter, such a public shareholder shall be required to make an open offer in accordance with the provisions of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

TAKEOVER OF UNLISTED COMPANIES

Section 236 of the Companies Act contains a compulsory acquisition mode for the transferee company to acquire the shares of minority shareholders of Transferor Company. Where the scheme has been approved by the holders of not less than nine tenth (90%) in value of the shares of the transferor company whose transfer is involved, the transferee company, may, give notice to any dissenting shareholders that transferee company desires to acquire their shares. The scheme shall be binding on all the shareholders of the transferor company (including dissenting shareholders), unless the Tribunal orders otherwise (i.e. that the scheme shall not be binding on all shareholders). Accordingly, the transferee company shall be entitled and bound to acquire these shares on the terms on which it acquires under the scheme (the binding provision). The advantage of going through the route contained in Section 235 of the Companies Act is the facility for acquisition of minority stake. The transferee company shall give notice to the minority dissenting shareholders and express its desire to acquire their shares within a period of 4 months after making an offer as envisaged under Section 235 of the Act.

When a Company intends to takeover another Company through acquisition of 90% or more in value of the shares of that Company, the procedure laid down under Section 235 of the Act could be beneficially utilized. When one Company has been able to acquire more than 90% control in another Company, the shareholders holding the remaining control in the other Company are reduced to a minority. They do not even command a 10% stake so as to make any meaningful utilization of the power. Such minority cannot even call an extraordinary general meeting under Section 100 of the Act nor can they constitute a valid strength on the grounds of their proportion of issued capital for making an application to the Tribunal under Section 241 of the Act alleging acts of oppression and/or mismanagement. Hence the statute itself provides them a meaningful exit route.

The following are the important ingredients of the Section 235 route:

- The Company, which intends to acquire control over another Company by acquiring share, held by shareholders of that another Company is known under Section 235 of the Act as the "Transferee Company".
- The Company whose shares are proposed to be acquired is called the "Transferor Company".
- The "Transferee Company" and "Transferor Company" join together at the Board level and come out with a scheme or contract.
- Every offer or every circular containing the terms of the scheme shall be duly approved by the Board of Directors of the companies and every recommendation to the members of the transferor Company by its directors to accept such offer. It shall be accompanied by such information as provided under the said Act. The circular shall be sent to the dissenting shareholders in Form No: CAA 14 to the last known address of the dissenting shareholder.
- Every offer shall contain a statement by or on behalf of the Transferee Company, disclosing the steps it has taken to ensure that necessary cash will be available. This condition shall apply if the terms of acquisition as per the scheme or the contract provide for payment of cash in lieu of the shares of the Transferor Company which are proposed to be acquired.

VARIOUS MODES TO BE CONSIDERED FOR TAKEOVER

The acquiring company is always interested in the financial aspects, human aspects, assets and liabilities of the target company. The following due diligence checks may help in carrying out the process:

Financial Aspects:

- Read the auditor's report and qualifying remarks, if any and director's responsibility statement. Whether the company is profit making, dividend paying company
- Calculate financial ratios and compare it with the previous year(s) figures of the company and also compare with the industry trend.
- Whether the Balance sheet have any fictitious assets?
- Whether any assets have been re-valued (particularly of real estates) in current year or in past. Calculate Net worth and its components and compare it with the previous year(s) figures.
- Whether any penalty from Revenue Authorities, Stock Exchanges/ SEBI/ CCI/ FEMA levied in the current / past years?
- Whether any litigation against the company, is pending before any court of law?
- Amount of contingent liabilities

Debtor's aspects:

- Study the demographic profile of the customer
- Study the type of customer base

- Whether sales are made in concentration / very few buyers are available in the market.

Creditor's aspects

- Who are the suppliers?
- What are the terms and conditions for purchase on credit?
- Whether the supplier is unique or discattered or no single supplier can mis-match the supply?

Material Control Aspect

- Make a review of all material contracts and commitments of the target company
- Study various issues pertaining to guaranties, loans, and credit agreements
- Study the Customer and supplier contracts, Equipment leases, Indemnification agreements, License agreements, Franchise agreements, Equity finance agreements, Distribution, dealer, sales agency, or advertising agreements, Non-competition agreements, Union contracts and collective bargaining agreements, Contracts the termination of which would result in a material adverse effect on the company.

Human Aspect

- Study the organization chart and biographical information,
- Type of workforce and expertise involved.
- Summary of any labour disputes, information concerning any previous, pending, or threatened labour stoppage,
- Employment and consulting agreements, loan agreements, and documents relating to other transactions with officers, directors, key employees, and related parties,
- Schedule of compensation paid to officers, directors, and key employees for the three most recent fiscal years showing separately salary, bonuses, and non-cash compensation (e.g., use of cars, property, etc.)

Regulatory Aspects

- Study the revenue returns filed by the company and its assessment orders.
- Whether any penalty has been imposed for contraventions of the provisions of the law and such penalty is still due.
- Whether the company is abiding with the company law compliances.
- Check the various returns filed with the RoC and is there any specific laws applicable and compliance of such laws are regular.

MERGERS AND ACQUISITIONS IN INDIAN AVIATION INDUSTRY

In the present era of liberalization and globalization, questions relating to the impact of mergers and takeovers on the economy of a country, warrant our immediate attention. During the past few years, India has followed the worldwide trends in consolidation amongst companies through mergers and acquisitions. Mergers and industrial restructuring have raised important issues both for business decisions and for public policy information. The daily newspapers are filled with case studies of mergers and acquisitions, tender offers (both friendly and hostile), spin-offs and corporate restructuring, changes in ownership structures, units being hived off and struggles for corporate control.

Mergers are like a marriage in the romantic jargon. Usually there is a period of courtship leading to the joining of two or more separate entities into one, after which the parties hope to live happily ever after, i.e., to say a Merger is said to occur when two or more companies combine to form a new company. Mergers in aviation industry are also very relevant to the present economy because it affects directly the life of large number of people who frequently use airway for commuting from once place to the other place. The direct affect involves the frequency of the number of flights being operated by different airlines in a specific route and the cost that has to be paid by the customer to avail such facility. Mergers in aviation industry would definitely affect both these concerns of the prospective or frequent customer.

Airline mergers and alliances can allow airlines to lower cost and enhance demand by rationalizing the combined networks, and expanding the scope of seamless service. On the other hand, airline mergers and alliances can reduce competition and enhance market power, especially on non-stop routes to and from hub airports. The relative balance of the efficiency benefits and the competition effects depends on a number of factors, including the degree of overlap in the airlines' networks prior to the merger.

The promotion and protection of competition in the airline industry requires attention to both competition and regulatory issues. In particular, competition in the airline industry could be preserved and enhanced through:

- Further liberalization of regulatory constraints on competition, especially at the international level, including for example, the application of international trade principles of transparency and non-discrimination within multilateral context;
- Attention to the mechanisms for investment in and allocation of scarce airport capacity including investment in new airports, expansion of existing airports and mechanisms for ensuring that facilities are available to entrants at key times;
- Careful review of proposals for mergers and alliances, careful use of remedies to offset anticompetitive effects and consideration of divestiture or separation in cases of dominance;
- Close review to frequent- flyer programs and other loyalty schemes;

- Careful control over predatory behaviour and other anti competitive practices.

Jet-Sahara Merger: Heralding the Consolidation in Civil Aviation Industry:

It seek to examine the significance of Jet–Sahara merger against the backdrop of liberalization and privatization of civil aviation sector. Having witnessed a tumultuous journey interspersed with legal hurdles owing to which it was held in abeyance, the resurrected merger has triggered the market driven consolidation of aviation industry. Secondly, it uncover the ramifications of this merger on the health of low cost carrier in the proposed paper. The Jet–Sahara combine will re-assert the leading private airline's supremacy in the Indian skies and empower it to fight the low fares offered by low cost carriers. This deal has erected a conspicuous entry barrier as evidenced by the changing dynamics of low cost carriers with Jet acquiring dominant market share and enhanced airport infrastructure.

Thirdly, it made an attempt to explore the legal underpinnings of this deal to understand the role of mergers and acquisitions in the aviation sector. This deal is saddled with monopolistic traces making Jet the largest player in Indian airspace and the sole private airline to possess international flying rights. (In the current scenario, Kingfisher has attained clearance from the civil aviation ministry to operate international flights courtesy the Kingfisher-Deccan deal). The MRTP Commission gave the green signal to deal silencing all analysts claiming abuse of dominance. The probe was in a way restricted as clauses relating to monopoly, mergers and acquisitions in the MRTP act had been deleted in 1991. With establishment of the new competition regime addressing legal concerns exhaustively, the aviation industry can expect stricter vigilance in future consolidation advances.

Fourthly, it undertakes an analysis of regulatory obstacles that have been exposed through this deal. The transfer of assets such as parking and landing slots were being governed by land lease agreements and couldn't change hands through merger. The civil aviation ministry settled the dust by charting guidelines regulating transfer of airport infrastructure in all merger schemes.

Project Finance in Airlines

In the last few years major structural and organizational changes have been occurring within the air transport industry. Major airlines have been consolidating their services by forming international alliances whilst a new generation of low cost carriers has entered the market. At the same time, a growing number of airports have been privatized which has allowed airport groups, which control a number of airports in different countries, to develop. In the era of globalization, the aviation industry is booming very much and low cost operating airlines are coming up and project financing or we can say that financing in the airlines or like mergers or take over of major carriers in aviation are taking place. If we take the example Kingfisher is a major airline and it took over the small and budget carrier Deccan airways, so many low cost airlines are coming up and investment in this field is very much as we have seen the changes in the recent decade that the purchasing power parity of a common man has increased many times folded, so for increasing demand in the aviation industry so many low cost airlines or we can say budget airlines came up and huge money is being invested in this field, if we look at the past few years only few airlines were there and they were even not permitted by the aviation ministry to fly internationally but now many private airlines are there which are flying internationally. Now financing of the airlines or venturing up the capital in starting the new airlines is booming up, every day we hear of some or the other airline coming up in the market, competition is so high that financing in the aviation sector or like in airlines is a new phenomenon which has been seen in the recent days. Project financing involves various aspects like, first of all the attention required as such the latest techniques in airport traffic forecasting, revenue and cost projection, airport charges regulation, project finance and risk assessment. Key market trends will be evaluated, including the growth in global airline alliances, low cost airlines and increasing concern over environmental issues, together with their potential implications for future airport growth. In the same decade airports have transformed from a public service to a value creator in a transport network. Deregulation of air transport markets has shown that the introduction of competition may have drastic impacts on network configurations of airlines, because of free route entry and exit; airlines will use their route networks to achieve traffic economies and maintain spatial monopolies in a competitive environment, so the major thing is that project finance in airlines is increasing day by day, economy is growing, as the number of growth of airports is also growing, so financing projects related to the aviation industry is seen as a profitable venture. Predatory Pricing is assumed, when an incumbent airline responds to market entry by greatly expanding capacity and low-fare seats. Summing up project finance in airlines is now a seen as a profitable venture as the market trends are changing in the developing country like India, so financing the airlines is also seen as a new phenomenon.

Air France and KLM Merger:

In September 2004, the boards of directors of KLM and Air France announced the merger of the two airlines forming Air France-KLM, the biggest airline in the world in terms of revenues. This paper investigates the effect of the merger on the stock price and operational performance of the merging firms, using three different methods outlined later. An analysis of mergers and acquisitions (M&A) in the airline industry is done to examine the effect that M&A generally has in this industry. While mergers and acquisitions are widely discussed in the economic literature, M&A in the airline industry are generally overlooked, despite their relevance for finance and their big impact on stakeholders of the airlines.

FACTORS THAT INFLUENCE THE SUCCESS OF THE AIR FRANCE-KLM MERGER

Firm size

The firm size has a negative impact on short-term and long-term AR, according to Moeller et al. (2004) and Franks et al. (1991). Dickerson et al. (1997) find the same results for operational performance, although they find that the firms in the 1st quintile (the smallest firms) perform worse than those in the 2nd and 3rd quintile. Although these papers do not directly provide an explanation for the negative correlation between firm size and AR, it is reasonable to assume this is due to the 'firm size effect'; the larger the firm, the harder it is to find investment opportunities that improve overall company performance significantly. Because Air France-KLM is in the 5th quintile when all airlines are ranked from small to big, the firm size might have a negative influence on the success of the merger in all 3 methods.

Method of financing

In many studies on the effect of mergers, a distinction is made between stock-financed M&A and cash-financed M&A. Healy et al. (1992), Fuller et al. (2002) and Heron and Lie (2002), among others, analyzed the difference in CAR and operational performance between these two ways of financing. On this subject, the literature does not seem to reach a single conclusion. Looking at the short-term stock price effect, Healy et al. (1992) find that cash-financed M&A outperform stock-financed M&A in terms of short-term CAR, especially when looking at the acquiring firms. An explanation could be that acquirers using cash take on more debt, for which they are rewarded by shareholders. Heron and Lie (2002) reach the same conclusion. Fuller et al. (2002), however, find that stock-financed M&A outperform cash-financed M&A.

Looking at the long-term stock price effect, significantly better results for cash-financed M&A are found by Abhyankar et al. (2005). The explanation they offer is that when an M&A is financed with stock, this is a signal that the stock price is too high. This explanation is consistent with the findings of Myers and Majluf (1984). Opposed to the Abhyankar et al. results, Franks et al. (1991) find no significant difference between the two methods of financing.

Two studies expand on the impact of the method of financing on long-term operational performance. Heron and Lie (2002) find that stock-financed M&A outperform cash-financed M&A, even though they find opposite returns when looking at the short-term CAR. Unfortunately, they do not provide the reader with possible explanations. A different conclusion is reached by Ghosh (2001), who finds evidence that cash-financed M&A outperform stock-financed M&A, and uses the same reasoning as Abhyankar et al (2005).

Air France acquired KLM by offering 11 Air France shares and 10 Air France call options for 10 KLM shares. According to the majority of the studied literature, this might have a negative impact on the CAR and the operational performance of Air France-KLM.

However, since there is no unanimous conclusion, it is a weaker expectation than was the case for both CARs.

Mergers and Acquisitions in the airline industry

In 1978, deregulation of the airline industry started in the US to spread to the rest of the world in the following years. One consequence of this deregulation was the rise of low-cost carriers (LCCs) and increased competition. This triggered many airlines to merge in order to achieve economies of scale. This consolidation is thought to be crucial in an industry that is still fractioned. Notably, the top five European airlines had a combined market share of only 31% in 2008, four years after the Air France-KLM merger (Buettner and Burger, 2008).

It is surprising how little attention the specific area of airline mergers has received, especially compared to the number of studies addressing effects of M&A in general. Whereas most studies that do address this topic focus on problems related to Industrial Organization, especially market power and price levels, this paper focuses on financial performance. The papers that did focus on financial performance are discussed in the next section. How the possible factors of success relate to the Air France-KLM merger is discussed later.

Short-term stock price effect

As with M&A in general, the literature is fairly conclusive regarding the short-term stock price effect. Singal (1996), Knapp (1990), Slovin et al. (1991) and others report significant AR for target airlines and zero to slightly positive AR for acquiring airlines. Factors that are discussed include firm size, method of payment and overlap of cities serviced by the merging airlines.
Since mergers in the airline industry did not occur frequently before 1978, there was not enough data to analyze airline M&A until the end of the 1980s. One of the first to dive deeper into the airline industry from this point of view was Knapp (1990). Taking the period between 20 days before and 10 days after the merger announcement, he finds significant CARs for target firms of around 25% and significant CARs for acquiring firms between 6% and 12%. The author suggests that a possible explanation is the network overlap between acquirers and targets, but provides no evidence to support this. An article that partly reaches the same conclusion when looking at the short-term stock price effects is Singal (1996). He finds significant CAR for target airlines of up to 22% when using a period between 5 days before and 1 day after the merger announcement, and insignificant AR for acquiring airlines. This seems to confirm the research findings on M&A in general. Singal (1996), too, suggests that a high overlap in the airlines' network results to higher gains, and shows that the coefficient on route overlap is in fact positive, confirming the suggestions made by Kim and Singal (1993).

Slovin, Sushka and Hudson (1991) have the same expectations regarding the explanations for excess returns to target and acquiring airlines around merger announcements, which is that they are significantly positive for both but higher for target firms, and that market power is an important determining factor. While the former seems to be confirmed by their empirical analysis, the latter is not. The authors do indeed find significant CARs of 10.8% for target airlines and 5% for acquirers in the period from 4 days before the merger announcement to the day of the merger announcement itself. A satisfactory reason is not provided. Their tests on the influence of market power (of which overlap of network is a strong indicator) show that this does not have a significant impact on the AR. This could be due to the small sample size that is used and/or the fact that very small mergers are included. In the case of very small mergers, the market power of both parties is unlikely to change even when their networks overlap well, but this overlap could still have a positive effect on the AR. The effect of overlapping networks will in this case be neglected.

Long-term stock price effect

Unfortunately, there is no research done yet on the long-term stock price effect of mergers in the airline industry. The authors that researched the stock price effect looked only at the short-term effect. A predicted effect can still be derived from the existing literature, however, by combining the conclusions of various papers. Singal (1993) draws the important conclusion that the stock price and the operational performance are correlated in the short term. Based on this it can be assumed the long-term stock price is also correlated with the long-term operational performance. The literature on the long-term operational performance is discussed in the next paragraph and is used to support hypotheses that involve both the long-term operational performance and the long-term stock price.

Operational performance effect

Investigating the effect of mergers on the operational performance of the companies, researchers often focus on the higher market concentration caused by the mergers. The general theory is that a higher market concentration results in higher prices and higher profit margins, and thus higher returns on assets (RoA) and returns on equity (RoE). The effect of mergers on the RoA and RoE of airlines is not studied in the existing literature. However, market power is assumed to have a strong correlation with both metrics (Bruner, 2000). Therefore the outcomes found by the studies on the effect of mergers on the market power are used as an indication. Several papers, for example Jordan (1988), Slovin et al. (1991) and Kim and Singal (1993) study the effect of mergers in the airline industry on the market power of the merging companies and the profit margin.

Jordan (1988) finds that market concentration and market power of the merging airlines does not increase after the merger. A reason for this is that merging airlines terminate part of the created overlap on existing routes. However, Jordan does find that operating costs are lower after the merger, which is an indicator for increasing RoA and RoE, and that prices are also lower after the merger, which is an indicator for decreasing RoA and RoE.

As does Jordan (1988), Carlton et al. (1980) find that mergers in the airline industry do not have a significant effect on the market power of the merging airlines, and thus do not impact the long-term operational performance from this point of view. Their theory is that the higher a firm's market power, the higher the price level is and the higher the profit margin. They find that the product is superior after the M&A but that the price level

remains the same.
An author that does find significant average improvement in profit margins is Merkert (2012). An important conclusion from his study is that the success of M&A in the airline industry is strongly influenced by firm size. This relationship seems to be stronger than is the case in mergers in other industries. Merkert (2012) argues that there is an optimal firm size, and that a merger hurts the profit margins if the merged firm becomes too big. The firm size is measured in terms of available seat kilometres (ASK) and the optimal firm size is 34-52 billion ASK.
Kim and Singal (1993) find that market power of merging airlines does increase after M&A. They provide evidence in the form of a significant increase in fares as a result of increased market power. A separate study by Singal (1993) supports these findings and shows that the stock price reaction anticipates on this increase in fares (see above). The increased market power and fares is considered to be an argument for airlines to merge. Possible determinants of the degree of increase are not discussed.

Factors that influence the success of the Air France-KLM merger

The literature on mergers in the airline industry provides little explanation around the drivers of success. Consensus is reached on the influence of market power, but not on firm size and overlap of network. All three factors are discussed in the following section.

Market power

All studies that are discussed above see market power as a critical determinant of success of M&A. They argue that increased market power leads to higher prices and higher profit margins, thus higher RoA and RoE. A possible weakness of the literature is that it does not explain if this relationship is linear, which is probably is not, and what the optimal market share is. It is obvious that the market share and the market power of Air France-KLM was greater than that of Air France and KLM separately. Because no optimal market share is given, the increased market share is considered to have a positive effect on the AR and the operational performance of Air France-KLM.

Firm size

As shown by Merkert (2012), firm size is an important factor for the success of an M&A in the airline industry. He argues that the optimal firm size is 34-52 billion ASK, and that airlines with a capacity of more than 200 billion ASK are too large to operate efficiently. Because Air France-KLM had a capacity of 201 billion ASK in 2004 and 215 billion ASK in 2005, the merger is expected to generate diseconomies of scale.

Overlap of network

There is a big overlap of the network of Air France and KLM. One reason for this is that the hubs of both airlines, Paris and Amsterdam respectively, are only 400 kilometres apart. Before as well as after the merger both airlines serviced many cities in Europe, North America and Asia, which creates an overlap and thus market power and higher profits (Singal, 1993). Termination of a big part of the overlap as suggested by Jordan (1988) is not applicable to Air France-KLM. The overlap of the network is expected to have a positive effect on both the CARs and the operational performance of Air France-KLM.

The Air France-KLM merger

Short-term stock price effect

For the short-term stock price effect for the Air France-KLM merger, the expectation was that the abnormal return (AR) of Air France would not have been influenced significantly by the merger. The expectation was that the AR of KLM would have risen significantly in the 5 days surrounding the announcement of the merger. As can be seen in table 2, the two parts of the first hypothesis are accepted based on the empirical research conducted. The AR on the stock price of Air France was on average 0.007% in the control period before the merger and - 0.875% in the (-2,+2) period, but the test statistic is -0.621 > -1.64. Because -1.64 (or 1.64) is the critical value for the two-sided test with a significance level of 10%, it can be concluded that the change was negative but not significant. The average AR on the stock price of KLM was 0.025% in the control period and 3.056% in the (-2,+2) period with a test statistic of 2.759, which makes the change significantly positive at the 1%-level. The combined effect, where the stock price of both firms is weighted by the value of the total assets, shows a positive effect on the average AR of 0.331%, which is small but significant at the 5%-level.

JOINT VENTURE IN CIVIL AVIATION SECTOR: EMERGING LEGAL ISSUES

The Indian Civil Aviation Sector is in for a major overhaul over the next few years. Major policy changes are taking place because of a shift in the mindset of the government from considering air travel as elitist to making it available for the common man. This has led to the liberalization of air travel services. The airport industry is going through an exceptional transformation that has driven the market towards increasing levels of competition. Additionally, major investment programs are required to meet the expected growth in air travel demand (particularly in some emerging regions, such as India). Nevertheless, governments and city airport authorities are becoming more reluctant to support airport projects, since they have major budgetary constraints.

The New Economic policy Reforms 1991 has paved way for almost all Indian industries to undergo a radical change. The traditional and restrictive Aviation industry is no doubt a part of it. In fact, Indian civil aviation had to immediately nod to liberalization due to its poor and pathetic financial numbers. Airline, being a service industry is facing intense competition after
liberalization. As a result, the various airlines are engaged in consolidation, strategic alliance and privatization, with an aim of improving their competitive positions.

KEY PLAYERS IN INDIAN INDUSTRY

Airlines on International Routes

Air India is the national flag carrier airline of India with a network of passenger and cargo services worldwide. It is one of the two state-owned airlines in the country, the other being Indian Airlines. Air India has 44 world-wide destinations. The airline has been profitable in most years since its inception. In the financial year ending March 31, 2006, Air India has made a net profit of Rs.97 million; earned a revenue of Rs.87, 480 million - representing a growth of almost 15 per cent over the previous year.

Air Sahara is a privately owned airline operating scheduled services1 connecting all metropolitan centres in India. The airline was established on 20 September 1991 and began operations on 3 December 1993 with two Boeing 737-200 aircraft as Sahara Airlines. The uncertainty over the airline's fare has caused its share of the domestic Indian air transport market, from approximately 11% in January 2006 to a reported 8.5% in April. Sahara Airlines was rebranded as Air Sahara on 2 October 2000.

Indian is India's state owned primarily domestic airline, under the federal Union Ministry of Civil Aviation The Company was formerly known as Indian Airlines. On December 7, 2005 the company was rebranded as Indian as a part of a program to revamp the company image in preparation for an IPO. Former Indian Civil Aviation Minister, Praful Patel, announced Government of India's plan to merge Air India and Indian into one giant airline consisting of 130-140 aircraft.

Airlines that provide normal scheduled air transport of passengers and freight Jet Airways a “regular” airline which offers normal economy and business class seats. Jet Airways, along with Air Sahara, is the only airline which survived the dismal period of 1990 when many private airlines in India were forced to close down. Jet Airways operates both in domestic and international routes. The airline operates over 300 flights to 43 destinations across the world. It currently controls about 32% of India's aviation market.

Airlines on Domestic Routes

Spice Jet is a low-cost airline. Their marketing theme is "offering low”, “everyday spicy fares” and “great guest services to price conscious travelers". Their aim is to compete with the Indian Railways passengers travelling in AC coaches.

Air Deccan is an airline based in Bangalore, India. It was India's first LCC (low-cost carrier)/no-frill airlines2, and as of May 2006, it connects 55 cities within India. Air Deccan has grown rapidly since it first started air operations in 2003, and despite its almost disastrous maiden inaugural flight (which caught fire), it continued to grow. The growing Indian economy and the increasing number of middle-class people in India have greatly helped its growth.

GoAir or the People’s Airline, a low cost carrier promoted by The Wadia Group is a domestic budget airline based in Mumbai, India established in June 2004. It’s a relatively small player as compared to other low cost airlines.

Kingfisher Airlines is an airline based in Bangalore, India. Services started on 9 May 2005, following the lease of 4 Airbus A320 aircraft. It initially operates only on domestic routes. The airline promises to suit the needs of air travellers and to provide reasonable air fares. Kingfisher are pushing for an amendment of the present Indian government rule which requires an airline to fly a minimum of five years on domestic routes before it can start flying overseas.

IndiGo Airlines is a new and a private domestic airline based in India. IndiGo placed an order for 100 Airbus A320 aircraft during the 2005 Paris Air Show. The total order was worth US $6 billion; one of the highest by any domestic carrier during the show. The new low-fare carrier has started operations from August 4, 2006.

LCCs are mostly no-frill airlines i.e. they not provide food, beverages or other amenities to passengers

Growth Potential of Aviation Industry

What drives the aviation dream is the growth potential, estimated to be 25 percent with domestic

players like Indian Airlines, Jet Airways, Kingfisher Airlines, SpiceJet, Air Deccan, GoAir and Air Sahara carrying 25million passengers every year. In spite of the downturn, key players are ramping up to fight the battle.

Growth in aviation industry can also viewed from macro economic perspective. A study by NCAER3 pointed out that one per cent increase in GDP required one per cent increase in air passenger traffic and 1.3 per cent increase in air cargo traffic. In the first three years of the Tenth plan, the air transport has grown at an average rate of 7 per cent per annum as against the planned estimate of 5 per cent. During the year 2004-05, air transport witnessed a very high growth of 22 per cent in passenger traffic and 20 per cent in air cargo.

Growth in India's civil aviation sector, for many years stunted by bureaucracy and political interference, is now booming at an estimated 25 percent per year. The intense competition ushered in by new entrants — and the strategic response by existing players — will drive further market growth. This expansion is being fuelled by annual economic growth of about 8 percent, rising incomes, cash-rich middle class, a reformist government and an ambitious plan to modernize the country's aviation infrastructure.

The Indian aviation industry is growing at a rapid pace, thanks to air transport deregulation, emergence of new operators, lower fares and large untapped demand for air travel.

The New Delhi office of the Center for Asia Pacific Aviation (CAPA), a Sydney-based aviation consultancy, says airlines in India may be selling about 50 million tickets a year by 2010, compared with around 19 million now. Another study conducted by KPMG suggests that the air passenger traffic is likely to reach 100 million in 2009-10.

As per the National Council for Applied Economic Research, the main drivers of air traffic are economic upswing, concentration of population, industries and liberalization leading to higher propensity to travel. The spike in air passenger traffic is largely triggered by the emergence of low-cost carriers in the domestic sector. The penetration of low-cost carriers in small towns, coupled with exceptionally low airfares comparable with railway AC fares has raised the competition to a new level. India is the only country where the number of air travellers a year equals the number of rail passengers in a day. The growth potential in this sector is further leveraged by the first-time flyers queuing up to fly.

The Government has also come up with some initiatives in the right direction which aids the growth of aviation industry such as strong political will and improved policy environment:

Electricity Act, Draft Maritime Policy, Draft Civil Aviation policy, ring fencing of funds earmarked for infrastructure, nomination of implementation authorities, urgency to bring about commercial viability, momentum of private participation, innovative financing concepts like

'Public Private Partnerships' and 'Viability Gap Funding'4 etc.

The aviation industry is almost an under penetrated market with total passenger traffic being only 50 million as on 31st Dec 2005 amounting to only 0.05 trips per annum as compared to developed nations like United States have 2.02 trips per annum. Air Cargo has not yet been fully taped in the Indian markets and is expected that in the coming years large no of players would have dedicated fleets The key challenge for Indian aviation companies is to convert strong traffic and revenue growth to profits for which yields need to stabilize.

Civil Aviation: Before and After Liberalization

Before Liberalization:-

The cost of travel in India was amongst the highest in the world. The two state-owned domestic and international carriers, Indian Airlines (IA) and Air India (AI) dominated the market until recently. Built on huge cost and as full-service providers they justified these high airfares.

Viability Gap Funding' – A scheme which is meant to reduce capital cost of projects by credit enhancement and to make them viable and attractive for private investments through supplementary grant funding.

With no competition from any front, the state-run airlines enjoyed a monopoly. From their position of strength, they pressurized the state machinery to obstruct foreign airlines from expanding flights to India and also to restrain the growth of private sector players. As a retaliatory measure foreign players hindered the growth of Indian airlines by not accommodating any deals with them. In the early 1990s, steps were taken to liberalise the aviation sector and the rest what we witness today is history.

After Liberalisation

From the consumers perspective; choice of airlines have increased, fares have reduced significantly, and increased routes is another big major advantages. From the airline perspective; Commercial freedom is the biggest advantage along with increased foreign investment. From the airport perspective; increased number of air passengers and aircraft contributing to increased revenue in form of landing charges and consumer spending at airport is the great advantage. All these factors have directly and indirectly contributed to the economy in form of increased tax revenues, increased employment opportunities and increased inflow of FDI, increased tourism etc.

Problems in Indian Civil Aviation

The most restricted industry faces serious setbacks even after liberalization and privatization. Infact such initiatives have caused new problems.

a. Infrastructure bottlenecks: There is hardly an airport with more than one runway. Also, none of the runways can handle wide bodies like the A380. There is serious shortage of parking bays. Ground facilities are hardly sufficient to process the current passenger volume. While the offer of cheap tickets and the convenience of choosing between different airlines and flight timings are luring domestic flyers, there are other issues that need attention. If one talks to regular flyers today one will come across endless tales of how flights circle above airports, waiting to land, or they are made to wait endlessly in aircraft because of the long queues of planes either waiting to take off or land.

b. Traffic Jam: Airport privatization is facing rough weather. The ground infrastructure of metro-airports is very poor. Delhi and Mumbai together handle around 60 percent of India's passenger traffic. It typically takes 10 to 15 minutes for any flight to land in Delhi or Mumbai airports. Under foggy conditions, it may go up to 40 to 45 minutes. It may be noted that each minute of flying over the airport burns around fuel worth Rs.1000

c. Taxation policy: The taxation policies of the Indian government are also adversely affecting airlines operations. The aviation turbine fuel (ATF) price in India, which is reportedly subject to 8 per cent excise duty, and a high sales tax averaging well above 25 per cent, is on the high side. Airlines in India have to spend 30 per cent of their operating costs on ATF while the international average is 10 to 15 per cent.

d. Productivity: The legacy carriers are replacing their high-cost labour with new blood which would result in lower wages as less senior people means lower wages. At the same time, low cost carriers will be maturing and with older work force comes higher salaries. The most difficult problem facing the legacy carriers will be the transition to higher productivity. Senior workers will be hesitant and it will be difficult tot change the culture. The low-cost carriers will face aircraft that are older. Older aircraft requires more maintenance and more time out of service as the longer maintenance cycles are more intense.

Reasons for Alliances & Joint Venture in Civil Aviation

The salient features that favored the alliances and joint ventures in airlines are as follows: Capital intensity, service orientation, Limited manufacturers, High level of regulation, low margins and tendency to consolidate and outsource.

- Capital intensity: The modern jet aircraft are products of intensive research and commercial application and are hence very costly. This implies that airlines companies should have the ability to mobilise enormous resources for acquisition and maintenance of their fleets.
- Service Orientation: As the basic aircraft gives little scope for product differentiation, airlines are harping on high level of on-time performance, wide network that offers better connectivity, better in-flight services, attractive frequent flyer's programme, superior lounge facilities etc. to attract passengers. Airlines are, thus, dependent on the skills of the flying crew and pleasant behavior of the cabin crew for attracting and retaining passengers.
- Legacy carrier - An airline revolving around a hub & spoke network and a corporate
  structure. Legacy Carriers mainly include:: First Class/Business Class , Lounges , Frequent Flyer Programs , Alliances Frills/Perks throughout the cabin (food, beverage, better service)
- Limited manufacturers: Most of the aircraft are manufactured by two manufacturers: Airbus Industries and The Boeing Company. As a result, basic features like carrying capacity, speed, range and facilities offered are likely to be similar for same type of aircraft operated by different airlines.
- High level of regulation: Operations of the air transport industry are governed by the agreements entered into between countries in which the aircraft are registered. These agreements prescribe the names of the carriers that can operate between the countries, the frequency, seating capacity and rights to pick up and discharge passengers. Countries have to enter into bilateral agreements for these rights. Government support is, therefore, essential for the survival of the airline industry.
- High level of concentration: Although there were more than 700 airlines in the world, the top seven (in terms of revenue) accounted for 33% of the total tonne kilometre performed in 1996. Again, approximately 35% of the total volume of scheduled passenger, freight and mail traffic was accounted for by the airlines of the United States. On international services, about 18% of all traffic was carried by the airlines of United States.

- Low Margins: Almost all the airlines are running under losses. If at all any airlines showed profits, it is only marginal. Generally any capital intensive industry would book low or negligible profits.
- Tendency to consolidate: Faced with intense competition and falling yields, the major players in the industry are moving towards consolidation through block

space arrangements, code sharing alliances and joint ventures. In 1996, six major alliances controlled 59% of the revenue, 56% of the fleet, 55% of employees and 60% of total tonne kilometer for the top 100 airlines in the world. Through alliances, the partners attempt to edge out marginal players on different routes.

- Adding to the salient features, the following reasons contributed for consolidation in Indian airline industry: Weak financials, high cost of operation, poor brand image, lower fleet capacity and inability for differentiation.
- Block space arrangement - reservation of certain number of seats in oneairlines' flight is reserved for sale of another airline
- Code sharing - seats can be sold by two airlines bearing codes allotted to more than one airlines
- Weak Financials: The Laws of supply and demand in economics were not working for civil aviation business. "In the law of economics, lower prices lead to increase in demand and in turn lead to higher revenues. In the airline business, there has been a reduction in fares resulting in an increase in demand for seats. But the industry does not experience a corresponding increase in revenues; in fact, the reverse is happening." Cumulatively, the losses reported by various airlines exceeded Rs.2000 crores in 2006.
- Declining Yield: Intense competition is leading to falling yields. This issue got compounded by the very high prices of aviation turbine fuel (ATF). Airlines are not able make up for the frequent and steep increase in prices of ATF through price adjustments. It is noteworthy to mention that ATF prices account for around 30 - 45% of an airline's operating cost. Hefty taxes imposed by Central and State government is another reason for low margins. The additional service tax imposed on business class and first class passengers also affected custom from a sector that have been paying handsome prices.
- High cost of Operation: The steep decline in fleet strength and the ageing fleet make cost of operations still costlier for Indian Airlines. Today, the average age of the Indian Airlines fleets over 17 years; these include fuel guzzlers like A 300 and B 737. With the new order by IA for 43 aircraft, the average age would fall to less than 8 years.
- Poor Infrastructure: Air transport follows road transport case in India. Development of road infrastructure was not matching the production of cars. Similarly Airport infrastructure is far behind the acquisition of aircraft. Presently, there is increase in demand for air travel and this has stimulated the investments in airport infrastructure. Upgradations with huge investment are carried out at Delhi, Mumbai, Bangalore, Hyderabad, Cochin airport. Due consideration is given to smaller airports.
- Poor brand image: Customer service and network are the main aspects of the product offered by airlines. Since it is a service industry, only the quality of service will ensure success in business. AI's product has suffered on these counts in the recent past due to which it has lost its business to other airlines.
- Lower fleet capacity: AI's fleet size is only 26, which is significantly less when

compared with other international airlines. British Airways has 256 aircraft while Singapore Airlines is having aircraft. Even after the merger between Air India and Indian, there will be only 112 flights in total.

- All other private carriers also don't have commendable fleet size to meet the growing demand. But almost all the airlines have ordered for aircrafts in big numbers. Fleet acquisition will be a successful only if there is access to adequate capital.
- Inability for differentiation: Being a capital intensive industry, it is difficult for the airlines to differentiate in the aircrafts they run. Hence the differentiation has to be in service – with frills or no-frill service.

Strategic Alliance – The modern airline trend

Strategic alliances have been one of the most visible responses of airlines to the intense competition of recent years. The main objective of these alliances is to create competitive advantage for the partners by enabling them to complement each other's services and achieve substantial economies of scale, particularly in marketing and maintenance costs and largely retailing and corporate independence. Inter-airline alliances lead to many competitive advantages:

- Merging of commercial activities in terms of sale and passenger service
- Pooling of intercontinental routes and linking domestic routes
- Providing high quality services
- Giving preferential access to a long haul hub8 for feeder airline partners
- Joint ground handling and maintenance at airports
- Capturing market share
- Joint investments and operating expenditure agreements
- Merging of reservation systems
- Joint fare policy
- Code sharing
- Advantage of global status and transcontinental distribution on partners
- Generate economies and new opportunities
- Risk sharing

Hub –An airport or city in which an airline has a major presence and many flights to other destinations. Many carriers use the hub and spoke system to maximize profits by keeping the aircraft in the air as much as possible. Flights to the hub are many, and from there flights to many other destinations are scheduled.

Such alliances enable the airlines to break regional barriers and explore vast and hitherto untapped business opportunities. In the international front, the first major alliance was established in 1989 between KLM and North West Airlines. The 'Star' alliance was initiated in 1993 between Lufthansa and United Airlines. In 1996, British airlines and American airlines formed the 'One World' alliance. Airline merger permits airline that may be constrained by bilateral regulations to offer a global coverage (Agusdinata and de klein 2002).

In the domestic front, such alliances are going to shape the outlook of entire aviation industry. Jet airways and Air Sahara has set the prelude for alliance and mergers. In years to come there would be one or two alliances formed by merging or amalgamating small airlines like Air Deccan, Go Air, Indigo etc. and one national airline (merged entity between Air India and Indian). Kingfisher airlines is looking forward eagerly for such opportunities.

<u>Strategic Initiatives in Civil Aviation</u>

The Ministry of Civil Aviation has taken some serious steps after privatization which was actually pending for a long duration.

Revenue from Real Estate: All most all the airports, be it be Bangalore International Airport

(BIAl), Cochin international airport (CIAL) or Hyderabad International airport (HIAL) – all of them have unanimous decision to earn diversified revenue from their huge real estate land with them. The promoters of BIAL are planning to lease out a 300-acre corridor along the access road. CIAL expects to attract Rs.3, 500 crore of investment in real estate. It will lease some of its land, enter into joint ventures, and may even pick up equity in some projects. It is the same story for HIAL. All this flows from civil aviation ministry policies on airport infrastructure of 1997 and 2002.

Joint venture for support services: IA's joint venture on maintenance, repairs and overhaul is also being extended to take of the maintenance of air frame and other engineering services. IA has been offering a lot of ground handling operations for other airlines. In all 23 foreign airlines, including British Airways and Lufthansa, are provided ground handling services by IA in 1 stations. Some 25,000 third party flights are covered by these stations.

Alliance with low-cost carrier: Jet airways have acquired Air Sahara for $500 million. It is also trying for an alliance with Air Deccan - the largest low-cost carrier in the country. The alliance would be on various fronts – sharing of engineering infrastructure, exchange of passengers when flights are cancelled, and combination offers and so on.

Merger by authoritative bodies: The Airports Authority of India (AAI) was formed after the merger of the International Airports Authority of India and the National Airports Authority by way of the Airports Authority Act (No.55 of 1994). It came into existence on April 1, 1995. The AAI is keen on establishing world-class airports in the country.

Consolidation approach: Despite competition, there seems to be camaraderie between the private airlines. Air Deccan has given one of its Airbuses to Kingfisher so that its pilots can train.

Also there are strategic alliances especially in sharing infrastructure at airports and inventory.

There are also reports about joint bidding for aircraft manufacturers so as to get a good deal.

Indian Airlines and Air India have decided to jointly tender for ground handling at the GMR Hyderabad International Airport (GHIAL). Singapore air terminal service (SATS) was selected by GMR as the JV partner with 49% share holding, while Air India and

Indian Airlines both jointly hold the remaining 51%.
Perhaps one of the most published deals is stopping poaching of pilots from one other's airlines. As airlines in India find their niches (at home and abroad) the advantages of code-sharing and other joint market approaches will become clearer.

Opportunities in 2007

Indian aviation industry is optimistic to take up pleasant journey in 2007. Though almost airlines have exhibited losses in the past few years, still the industry seems lucrative both for the players and for the changing Indian consumers.

Reduction in Fuel bill: ATF accounts for 35-40% of the cost of an aviation company. Any drop in prices will spare losses. Oil prices have declined from the peak of US$ 78 per barrel. Now it is around US$ 76 per barrel.
More disposable income with the Indian population: IT revolution and earning youth in India are left with high disposable income. Also the LCC have targeted at the first class train travelers who don't mind paying a little extra thereby reducing journey time.
Funds pouring into the sector: Aviation is a capital-intensive business with long gestation. Both domestic and international carriers are in the full swing of expansion to meet the growing demand.
Unlike earlier days, investors are willing to pour in their funds in to this loss making but still but still optimistic sector. The players are adopting different funding strategies. For instance, SpiceJet announced it would raise about US$118.5 million by offering stake to potential investors which include Tata group companies, Texas pacific group ventures, Istithmar PJSC and Goldman Sachs. In August 2006, Spice jet and Babcock & Brown Aircraft management (BBAM), along with a long term strategic partner Nomura Babcock & Brown Co (NBB), signed a sale-and –lease back agreement covering 16 brand-new Boeing 737-800/-900 ER aircraft valued at over US$ 1.1 bn based on the manufacturer's list prices.
Similarly Air Deccan had announced that it had entered into financial structure with a consortium of European banks for US$ 100 mn to be received in four tranches against the assignment of aircraft purchase contract through a special purpose company funded by consortium of European banks. Air Deccan has also issued equity shares to Investec bank (UK) on a preferential basis. Jet airways has successfully launched its IPO and several other airlines are to follow this route.

Own MRO units: Global players like Boeing and Airbus are collaborating to set up MRO units and aeronautical flight training centre in Nagpur with estimated investment of $ 185 mn. Not only airline carriers are pitching in this space. Even infrastructure developers like GMR group have business plans to set up MRO units. There is strong trend of outsourcing in this space. For instance two decades ago, about 85 percent of global engine maintenance was done in-house.
Now, this is reduced to 30 per cent. Locating MRO units in India saves time and resources.
Globally 25 percent of flight delays are maintenance related. A research by Hamco reveals that in India these are as high as 60 per cent.

Case of Air-India Limited

Air-India (AI) was set up on October 15, 1932, as Tata Airlines, the first scheduled airmail service in India. In July 1946, the company was converted into a public limited company and renamed as Air-India. By the end of 1947, Air-India International was launched for international services, with the participation of the Government of India. In 1952, the Planning Commission recommended nationalization of the air transport industry. Nationalization was effected on August 1, 1953 with the creation of two corporations, viz. Air-India for international services (as the nation's flag carrier) and Indian Airlines for domestic services.

The paid up share capital of AI as on 31st March, 1997 was Rs. 153.8crores and is wholly owned by Government of India.

Air India and Lufthansa Sign Strategic Alliance

Lufthansa and Air India have significantly improved their market leadership positions on India-Europe-USA routes with the Strategic Alliance agreement signed between Lufthansa & Air

India. From 1st October 2004, Air India has been a partner of Lufthansa. Within the scope of an extensive agreement covering a far-reaching bilateral cooperation, Wolfgang Mayrhuber, Chairman of the Executive Board of Deutsche Lufthansa AG, and V. Thulasidas, Chairman & Managing Director of Air India, signed a Strategic Alliance agreement in Mumbai. The objective of the partnership is expansion of the offer of flights between Germany and India. All flights between the two countries are operated by the two airlines in code-sharing. New routes are added. Through the cooperation in the area of frequent flyer programs, customers on flights of both airlines can collect and redeem miles for the respective programmes - Miles & More and Flying Returns.

Air India has been accorded the IOSA Audit Certificate by IATA which puts it in the league of a dozen Airlines conforming to quality standards required for joining Global Alliances.

India - Germany/ Europe and India-USA are very important markets for Air India which it plans to serve over Frankfurt in 10. IOSA (International Civil Aviation Organisation) – A specialized agency of the United Nations whose objective is to develop the principles and techniques of international air navigation.

IATA (International Air Transport Association) –

A trade association serving airlines, passengers, shippers, travel agents alliance with Lufthansa. In addition to the code-sharing between Germany and India, the code of Air India will also be bookable on Lufthansa connecting flights from Frankfurt to Berlin, Munich, Stuttgart and Düsseldorf to Amsterdam, Geneva, Zurich and Lyon as well as to Washington, Denver, Detroit, Chicago and Los Angeles.

This cooperation agreement results from a memorandum of understanding which the two carriers signed on 26th August 2003. In it, cooperation in the area of sales and marketing is also foreseen as well as cooperation in the medium term in other areas, for example, in the area of IT.

Lufthansa which was flying from Frankfurt to Delhi (once daily), Mumbai (once daily), Chennai (once daily) and Bangalore (five times a week) as well as from Munich to Delhi (three times a week.) would fly further six weekly flights between Frankfurt and Mumbai as well as three weekly flights between Frankfurt and Delhi which are operated by Air India and can be booked with a Lufthansa code.

Air India served up to 33 destinations from Mumbai and Delhi, including, among others, Frankfurt, Chicago and New York. The fleet of Air India consists of 33 wide bodied aircraft and it had planned to add more to make its Los Angeles & Chicago flights daily. It has also planned to operate daily services between London and Mumbai & London and Delhi and link Bangalore with Frankfurt four times a week from March 2005.

The Lufthansa - Air India pact paves the way for joint development of air services on India-Europe-USA route.

Air India – Indian Airlines Merger

The Indian government has cleared the merger of two state-run carriers Air-India and Indian (Indian Airlines Ltd).Government will continue to be the sole owner of the merger entity and has made it clear that the public sector character of the merged airline would be maintained.

But the Government may look for IPO after getting approval of a committee consisting of Finance Ministry.

The merger of the two airlines would enable them to leverage their combined assets and capital better and build a strong and sustainable business. The potential synergies are expected to enhance the new combined airline's profitability by over US$133 million per annum, or about four per cent, of their current combined assets. By 2010-11, when all the new aircraft ordered by the two carriers are inducted into the fleet, the merged entity's employee-aircraft ratio would come be about 200:1, comparable with any major global airline. While Air-India has ordered Boeing planes, Indian has finalized the acquisition of 43 Airbus aircraft.

According to the report submitted by Accenture, there will be no manpower rationalization as the consultancy has suggested 'careful integration' of manpower at various levels. It has also suggested a top-to bottom integration of the employees. It is proposed that the pay-scales be revised to bring parity in promotion procedures.

The merged entity of state-owned international and domestic carriers Air India and Indian - National Aviation Company Ltd - is now in the process of drafting the Scheme of Amalgamation under Section 391-94 of the Companies Act. This would pave the way for the integration of the two national airlines and their subsidiaries — Air India Express (Air India) and Alliance Air (Indian).

MODULE III

INSOLVENCY, WINDING-UP AND LIQUIDATION OF COMPANIES

BANKRUPTCY AND INSOLVENCY- AN INTRODUCTION

The insolvency resolution process in India has in the past involved the simultaneous operation of several statutory instruments. These include the Sick Industrial Companies Act, 1985, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, the Recovery of Debt Due to Banks and Financial Institutions Act, 1993, and the Companies Act, 2013. Broadly, these statutes provided for a disparate process of debt restructuring, and asset seizure and realization in order to facilitate the satisfaction of outstanding debts. As is evident, a plethora of legislation dealing with insolvency and liquidation led to immense confusion in the legal system, and there was a grave necessity to overhaul the insolvency regime. All of these multiple legal avenues, and a hamstrung court system led to India witnessing a huge piling up of non-performing assets, and creditors waiting for years at end to recover their money. The Bankruptcy Code is an effort at a comprehensive reform of the fragmented regime of corporate insolvency framework, in order to allow credit to flow more freely in India and instilling faith in investors for speedy disposal of their claims. The Code consolidates existing laws relating to insolvency of corporate entities and individuals into a single legislation. The Code has unified the law relating to enforcement of statutory rights of creditors and streamlined the manner in which a debtor company can be revived to sustain its debt without extinguishing the rights of creditors.

Applicability

The Code provides creditors with a mechanism to initiate an insolvency resolution process in the event a debtor is unable to pay its debts. The Code makes a distinction between Operational Creditors and Financial Creditors. A Financial Creditor is one whose relationship with the debtor is a pure financial contract, where an amount has been provided to the debtor against the consideration of time value of money ("Financial Creditor"). Recent reforms have sought to address the concerns of homebuyers by treating them as 'financial creditors' for the purposes of the Code. By a recently promulgated ordinance, the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018 ("the Ordinance"), the amount raised from allottees under a real estate project (a buyer of an under-construction residential or commercial property) is to be treated as a 'financial debt' as such amount has the commercial effect of a borrowing. The Ordinance does not clarify whether allottees are secured or unsecured financial creditors. Such classification will be subject to the agreement entered into between the homebuyers and the corporate debtor. In the absence of allottees having a clear status, there may be uncertainty about their priority when receiving dues from the insolvency proceedings. An Operational Creditor is a creditor who has provided goods or services to the debtor, including employees, central or state governments ("Operational Creditor").

A debtor company may also, by itself, take recourse to the Code if it wants to avail of the mechanism of revival or liquidation. In the event of inability to pay creditors, a company may choose to go for voluntary insolvency resolution process – a measure by which the company can itself approach the NCLT for the purpose of revival or liquidation.

Institutional Framework

The Code proposes the creation of several new institutions, all of which have specialized roles in the insolvency resolution process. The Code has created a regulatory and supervisory body, the Insolvency and Bankruptcy Board of India ("IBBI"), which has the overall responsibility to educate, effectively implement and operationalize the Bankruptcy Code. The IBBI has the added responsibility to facilitate the functionality of the Code by studying practical implications and framing rules/regulations to overcome any difficulty or hurdle. The Code envisages the creation of a cadre of professional insolvency practitioners, known as Resolution Professionals ("RP"), who are tasked with overseeing various aspects of the resolution of insolvency. The Code also sets up Insolvency Professional Agencies, which are professional bodies that will regulate the practice of insolvency professionals. Individual practitioners are required to be enrolled with insolvency professional agencies which are empowered to certify professionals, conduct examinations, and lay out a code of conduct.

Information utilities

The Code envisages the establishment of information utilities, which are tasked with the collection, collation, maintenance, provision and supply of financial data to businesses, financial institutions, adjudicating authorities, insolvency professionals and other relevant stakeholders, which will thereby serve as a comprehensive repository of information on corporate debtors that are of a financial nature. It is optional for operational creditors to provide financial information to the information utility.

Framework of the Code

All proceedings under the Code in respect of corporate insolvency are to be adjudicated by the NCLT, which has been designed as the special one window forum which can tackle all aspects of insolvency resolution. The NCLT is referred to as the Adjudicatory Authority in relation to insolvency of corporate persons under the Code. No other court or tribunal can grant a stay against an action initiated before the NCLT. Appeals from the orders of the NCLT lie before the National Company Law Appellate Tribunal ("NCLAT"). All appeals from orders of the NCLAT lie to the Supreme Court of India. The jurisdiction of civil courts is explicitly ousted by the Code with regard to matters addressed by the Code. Additionally, it is now established that the Limitation Act, 1963 shall be applicable to proceedings under the Code. Thus, time-barred claims are outside the purview of insolvency.

When resolution/restructuring of debts is not viable, the NCLT may direct for dissolution of the company. The Code envisages a two stage process, first, revival and second, liquidation:

1. Corporate Insolvency Resolution Process ("Insolvency Resolution Process")

2. Fast Track Corporate Insolvency Resolution Process ("Fast Track Resolution Process")
3. Liquidation

Insolvency Resolution Process and Fast Track Resolution Process are measures to help revive a company. The Code attempts to first examine possibilities of a revival of a corporate debtor failing which, the entity will be liquidated.

INSOLVENCY

The term "insolvency" notes the state of one whose assets are insufficient to pay his debts; or his general inability to pay his debts. The term "insolvency" is used in a restricted sense to express the inability of a party to pay his debts as they become due in the ordinary course of business.

The word "bankruptcy" the condition of insolvency. It is a legal status of a person or an entity who cannot repay debts to creditors. The bankruptcy process begins with filing of a petition in a court or before an appropriate authority designated for this purpose. The debtor's assets are then evaluated and used to pay the creditors in accordance with law.

Therefore, while insolvency is the inability of debtors to repay their debts, the bankruptcy, on the other hand, is a formal declaration of insolvency in accordance with law of the land. Insolvency describes a situation where the debtor is unable to meet his/her obligations and bankruptcy occurs when a court determines insolvency, and gives legal orders for it to be resolved. Thus insolvency is a state and bankruptcy is the conclusion. The term insolvency is used for individuals as well as organisations/corporates. If insolvency is not resolved, it leads to bankruptcy in case of individuals and liquidation in case of corporates.

INSOLVENCY RESOLUTION PROCESS

CORPORATE INSOLVENCY RESOLUTION PROCESS

Financial Creditors, Operational Creditors and Corporate Debtors can initiate the Corporate Insolvency Resolution Process by making an application to the NCLT. The new code envisages that a company which has gone insolvent cannot start the liquidation process at the primary stage until and unless it has gone through the process of Corporate Insolvency Resolution Process (CIRP). Under the said resolution process, options for revival of the company are looked into and if the said resolution process fails then only the company goes into liquidation.

In corporate insolvency resolution process, the financial creditors assess the feasibility of debtor's business and the options for its betterment and rehabilitation. If the corporate insolvency resolution process fails or the financial creditors decide that the business of the debtor cannot be carried on in a beneficial manner and it should be wound up, the debtor's business undergoes the liquidation process. In the liquidation process, the assets of the debtor are realised and distributed by the liquidator in accordance with the provisions of the Insolvency and Bankruptcy Code, 2016.

Who may initiate Corporate Insolvency Resolution Process?

Where any corporate debtor commits a default, a financial creditor, an operational creditor or the corporate debtor itself can initiate corporate insolvency resolution process in respect of such corporate debtor under Section 6 of the Insolvency and Bankruptcy Code, 2016.

The term "default" means non-payment of debt when whole or any part or instalment of the amount of debt has become due and payable and is not paid by the debtor or the corporate debtor.[3]

Initiation of corporate insolvency resolution process by financial creditor

Section 7 of the Insolvency and Bankruptcy Code, 2016 lays down the procedure for the initiation of the corporate insolvency resolution process by a financial creditor or two or more financial creditors jointly.

Section 7 of the Insolvency and Bankruptcy Code, 2016 reads as follows:

"(1) A financial creditor either by itself or jointly with other financial creditors, or any other person on behalf of the financial creditor, as may be notified by the Central Government may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred.

Explanation. – For the purposes of this sub-section, a default includes a default in respect of a financial debt owed not only to the applicant financial creditor but to any other financial creditor of the corporate debtor.

(2) The financial creditor shall make an application under sub-section (1) in such form and manner and accompanied with such fee as may be prescribed.

(3) The financial creditor shall, along with the application furnish –

(a) Record of the default recorded with the information utility or such other record or evidence of default as may be specified;

(b) The name of the resolution professional proposed to act as an interim resolution professional; and

(c) Any other information as may be specified by the Board.

(4) The Adjudicating Authority shall, within fourteen days of the receipt of the application under sub-section (2), ascertain the existence of a default from the records of

[3] Section 3(12) of Insolvency and Bankruptcy Code, 2016

an information utility or on the basis of other evidence furnished by the financial creditor under sub-section (3).

(5) Where the Adjudicating Authority is satisfied that –

(a) A default has occurred and the application under sub-section (2) is complete, and there is no disciplinary proceedings pending against the proposed resolution professional, it may, by order, admit such application; or

(b) Default has not occurred or the application under sub-section (2) is incomplete or any disciplinary proceeding is pending against the proposed resolution professional, it may, by order, reject such application:

Provided that the Adjudicating Authority shall, before rejecting the application under clause (b) of sub-section (5), give a notice to the applicant to rectify the defect in his application within seven days of receipt of such notice from the Adjudicating Authority.

(6) The corporate insolvency resolution process shall commence from the date of admission of the application under sub-section (5).

(7) The Adjudicating Authority shall communicate –

(a) The order under clause (a) of sub-section (5) to the financial creditor and the corporate debtor;

(b) The order under clause (b) of sub-section (5) to the financial creditor, within seven days of admission or rejection of such application, as the case may be."[4]

Initiation by Financial Creditor

A Financial Creditor may by itself or jointly with other financial creditors or any other person on behalf of the financial creditor, as may be notified by the Central Government, seek to initiate Insolvency Resolution Process by filing an application before the NCLT, once a default has occurred. Interestingly, under the Code, the adjudication process in respect of a Financial Creditor does not require a notice to be served on the debtor. However, the Supreme Court has in its judgement of '*Innoventive Industries v IDBI Bank*' made it mandatory for a notice to be served on the debtor, as well as to provide the debtor with the right to be heard.

Initiation by an Operational Creditor

The Bankruptcy Code envisages a two-step process for the initiation of insolvency proceedings by an Operational Creditor. An Operational Creditor would upon the occurrence of a default have to demand payment of the unpaid debt ("Demand"). The Corporate Debtor may within 10 days of receipt of the Demand either Dispute the debt (as described below) or pay the unpaid debt. In the event the corporate debtor does not

[4] Section 7 of the Insolvency and Bankruptcy Code, 2016

reply or repay the debt, an application could be filed by the Operational Creditor before the NCLT to initiate Insolvency Resolution Process. However, the existence of a dispute can act as a barrier to such application.

Initiation by a Corporate Applicant

In case of default by the corporate debtor, the corporate applicant may file an application for initiation of insolvency proceedings. The applicant must furnish information relating to the books of account and the RP to be appointed. Additionally, a special resolution must be passed by the shareholders of the corporate debtor or a resolution by at least three-fourth of the total number of partners must be passed approving the filing of the insolvency resolution application.

Resolution Plan

A primary objective of the enactment of the Code is to aid a debtor in resolving an insolvency situation without approaching liquidation, by finalizing an insolvency resolution plan ("Resolution Plan"). In an ideal scenario, a properly structured Resolution Plan would provide a strategy for repayment of the debts of the debtor after an evaluation of the debtor's worth, while allowing for the survival of the debtor as a going concern. Specifically, the Resolution Plan must provide for repayment of the debt of operational creditors in a manner such that it shall not be lesser than the amounts that would be due should the debtor be liquidated. Additionally, it should identify the manner of repayment of insolvency resolution costs, the implementation and supervision of the strategy, and should be in compliance with the law. If the terms (including the terms of repayment) under the Resolution Plan are approved by the committee of creditors, and subsequently by the NCLT, the Resolution Plan would be implemented, and the debtor may emerge from the debt crisis with a fresh chance for business and lessened liabilities.

Mandatory Contents of the Resolution Plan

The Mandatory Contents of the Resolution Plan are listed under Regulation 38 of the IBBI Regulations, 2016 which are as follows:

1. A resolution plan shall identify specific sources of funds that will be used to pay the –
   (a) Insolvency resolution process costs and provide that the insolvency resolution process costs will be paid in priority to any other creditor;
   (b) liquidation value due to operational creditors and provide for such payment in priority to any financial creditor which shall in any event be made before the expiry of thirty days after the approval of a resolution plan by the Adjudicating Authority; and
   (c) Liquidation value due to dissenting financial creditors and provide that such payment is made before any recoveries are made by the financial creditors who voted in favour of the resolution plan.

[“(1A) a resolution plan shall include a statement as to how it has dealt with the interests of all stakeholders, including financial creditors and operational creditors, of the corporate debtor.”]

(2) A resolution plan shall provide:

(a) The term of the plan and its implementation schedule;

(b) The management and control of the business of the corporate debtor during its term; and (c) adequate means for supervising its implementation.[5]

With the approval of committee of creditors, the resolution professional invites prospective resolution applicants who fulfil the criteria as laid down by him having regard to the complexity and scale of functions of the business of the corporate debtor.

FAST TRACK INSOLVENCY RESOLUTION PROCESS

According to Section 55 of the Insolvency and Bankruptcy Code, 2016, a corporate insolvency resolution process carried out in accordance with this Chapter IV of Part II of the Code shall be called as fast track corporate insolvency resolution process.

An application for fast track corporate insolvency resolution process may be made in respect of the following corporate debtors, namely: -

a) A corporate debtor with assets and income below a level as may be notified by the Central Government; or
b) A corporate debtor with such class of creditors or such amount of debt as may be notified by the Central Government; or
c) Such other category of corporate persons as may be notified by the Central Government.

The time period for completion of fast track corporate insolvency resolution process is provided under Section 56(1), which is ninety days from the insolvency commencement date. The extension of the fast track corporate insolvency resolution process shall not be granted more than once.

MANNER OF INITIATING FAST TRACK CORPORATE INSOLVENCY RESOLUTION PROCESS

According to Section 57 of the Code, an application for fast track corporate insolvency resolution process may be filed by a creditor or corporate debtor as the case may be, along with-

a) The proof of the existence of default as evidenced by records available with an information utility or such other means as may be specified by the Board; and
b) Such other information as may be specified by the Board to establish that the corporate debtor is eligible for fast track corporate insolvency resolution process.

[5] Regulation 38 of the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016

ISSUES IN AIRLINE INSOLVENCIES IN INDIA

Be it the nature of operations or the complexities of aircraft financing and asset preservation, multiple issues contribute to the difficulties in dealing with insolvencies in the aviation sector. In this section, we discuss some of these issues.

Aircraft Financing

The primary assets of an aviation company are aircrafts. However, owning an aircraft is often not economically feasible for such companies. This leads to airlines engaging in rather complicated financing arrangements not only with financial institutions, but also with the aircraft manufacturers themselves. Being at the shorter end of the deal, airline companies tend to provide heavy collateral to the financiers in such arrangements thereby adding to the encumbrances on its limited assets. The other method of acquiring aircrafts is through leasing. Such leases may either be financial leases or operational leases. The title to the aircraft may or may not pass to the airline company upon entering into a financial lease, depending upon the terms of the lease agreement. Therefore, it is likely that upon default, the lessor would exercise its proprietary interest over the aircraft and obtain possession of such aircraft, thereby further limiting the scope of assets available with the airline.

Further, when the company is undergoing CIRP, there is also the issue of categorising claims under such leases as financial and operational debt and verifying claims which may include accelerated payment of rent. There is also a lack of clarity as to the treatment of costs, expenses and future losses when dealing with such claims. During the CIRP, all claim amounts are admitted as on the insolvency commencement date. However, this may be in conflict with contractual rights of the lessors and the question remains as to whether the Code will override contractual rights of the lessors.

Legal Requirements for Running the Company as a Going Concern

The aviation industry requires a niche set of skills, training and knowledge. This has, in turn, led to the development of licenses, rules, regulations and other requirements essential for running an airline as a going concern. For instance, the Aircraft Rules, 1937 (Aircraft Rules) requires an airline to obtain an Air Operator Certificate subject to compliance with Schedule XI of the Aircraft Rules.

This certificate may be cancelled by the DGCA, in its discretionary powers, when the aircraft stops operating. The airline cannot operate without such certificate. Further, for continuing to be eligible to hold such certificate, the airline requires the appointment of an Accountable Manager (AM). The AM is a person who has full financial authority over the airline. During CIRP, since the Resolution Professional (RP) has such authority, she becomes the AM and has to take over the corresponding risks and liabilities as stipulated by the DGCA. The AM is also required to have a team of skilled, specialised and qualified personnel who must be appointed during CIRP if they cease to provide their services upon commencement of CIRP. It is critical for the RP to have access to a team of skilled professionals and ensure compliance with all applicable laws and regulations to perform its duty of running the Company as a going concern. Very often, the RP or the firm she is associated with may not have in-house expertise in this sector at which stage it becomes critical for the RP to be able to persuade senior management of the airline company to continue to be in employment of the entity so as to ensure regulatory compliances.

Assets Preservation

The most critical assets for an airline are its aircrafts, airport slots and traffic rights. There are various concerns with respect to each of these assets which must be dealt with for preservation of their value.

For instance, every aircraft is required to be registered with the Central Government for it to operate. The primary concern with respect to such aircrafts during the CIRP is the issue of deregistration during the CIRP. Under Rule 30(7) of the Aircraft Rules, registration of the aircraft may be cancelled within five working days, without seeking consent or any document from the operator of the aircraft or any other person, if an application is received from a holder of an Irrevocable Deregistration and Export Request Authorization (IDERA). It is essential for the courts to conclusively decide whether the exercise of such an IDERA would fall within the scope of prohibition under the moratorium under the Code.

In respect of the other assets of the airline, slots and traffic rights are allocated to an airline company pursuant to a fixed process and are not owned by the airline company as such. Once the operation of the airline ceases, there is a risk of these slots and traffic rights being allotted to competing healthy airlines. The civil aviation rules currently do not provide for a due process for reversion of those rights to the restructured airline. Therefore, the RP is required to initiate discussions with the DGCA, the Ministry of Civil Aviation and airport authorities for preservation of such slots and traffic rights on an ad hoc basis. If a viable business plan is plausible for the airline company then the Ministry of Civil Aviation and DGCA are more likely to consider protecting these assets of the airline company. However, the unavailability of these assets during the CIRP and related uncertainty may discourage potential resolution applicants and may adversely affect the resolution of the airline company. It is, therefore, a circular problem where the possibility of asset preservation depends on the preservation of the asset in the first place.

Treatment of Claims

In addition to the claims arising out of debts owed to financiers and lessors, a major portion of the claims against an insolvent airline company are claims of consumers. In the event of insolvency of airline business, consumers face two types of losses – (a) financial loss (because they have paid for tickets that become worthless); and (b) personal welfare losses if they are left stranded abroad (this could be on account of delay and disruption, discomfort, anxiety and stress, and in some cases even health and employment problems). A consumer may suffer further loss basis her specific circumstances. Further, in terms of filing of claims one must look at the source of purchase of the ticket to verify and examine such claims. There are two ways for a consumer to purchase an airline ticket – (a) purchase of a ticket from the airline itself through its physical counters or its website / mobile application; and (b) through a travel agency. If a consumer has purchased a ticket from the airline itself, the consumer will herself have a claim against the insolvent airline company. However, if the consumer has purchased a ticket through a travel agency, it may seek a refund and compensation for loss from the travel agency (subject to the cancellation policy of the travel agency). In such a case, the travel agency will, in turn, file a claim with the airline company for the amount claimed by the consumer. In addition to the above, travel agents in India also have the option of seeking a refund from the IATA. IATA settlement service between airlines and travel agents (known as the BSP or Billing and Settlement Plan), may allow IATA to reimburse travel agents for monies submitted to the airline, depending on the national bankruptcy legislation and the specifics of the airline's participation with IATA. IATA may then file a claim against the airline company. Another entity from which the consumer may claim refund / compensation is the credit card company, if she has purchased the ticket using a credit card. The credit card company may then file a claim with the airline company.

Assessing the scope, nature of debt and amount of such claims may prove to be an onerous task for the RP under the Code, especially in view of the sheer volume of such claims and of the possibility of duplication of claims for the same transaction.

Cross-Border Implications

The very nature of the business of an airline company leads to a situation where the assets of the company may be located in more than one jurisdiction. In such case, it may be possible that insolvency proceedings are initiated in more than one jurisdiction. Such is the case in the insolvency of Jet Airways. If the jurisdictions involved have a legal framework for dealing with cross-border insolvency, it is easier to ascertain how such issues will be dealt with. However, this will be subject to the mutual relationship between such jurisdictions. Where a legal framework for cross-border insolvency is itself not available in either of the jurisdictions, the proceedings rely heavily on voluntary cooperation between the RPs /administrators/judicial fora of such jurisdictions. Matters further complicate when aircrafts of the airline are lying in either jurisdiction. In such case, not only are the operations of the company adversely affected but there is also a possibility that the creditors of the jurisdiction where the aircraft is grounded obtain returns from the proceeds of sale/ auction of such jurisdiction while the estate of the insolvent vis-à-vis the other creditors diminishes.

Sensitive Timelines

Aircrafts depreciate rapidly if not operated and maintained regularly, they lose value at tremendous speed. Further, pilots as skilled workmen with niche technical knowledge have high demand in the market and delays in resolution may cause these pilots to be hired by competing airlines. Both these elements of operating an airline are likely to adversely affect the value of the company from the perspective of potential resolution applicants. Therefore, protection of these two vital elements of running an airline business must be the top priority of all stakeholders. In addition to the above, data suggests that 8 million jobs are supported by the aviation industry. Protection of interests of such employees should also be prioritised during CIRP. If we look at the example of Jet Airways itself, 20000 employees have been adversely affected by the insolvency of the company. The National Company Law Tribunal (NCLT) has also observed this to be a matter of national importance. In view of the above, it is imperative that a decision to resolve /liquidate an airline is taken expeditiously.

Identifying the unique issues mentioned above, various jurisdictions have developed or are in the stage of developing legal provisions focused specifically on dealing with insolvencies in the airline sector. In the next section, we look at the legal framework and practice in some of these jurisdictions.

THE GLOBAL EXPERIENCE

US and Protection of Secured Creditors

The US Congress identified that the great expense of transportation equipment combined with the relative financial instability of the transportation industry justified greater protection for secured creditors and lessors of aircraft. Consequently, section 1110 of the Federal Bankruptcy Code (US Code) forces debtor airlines to make decisions very early in their reorganisation efforts regarding their most important asset – their aircraft. The section also covers aircraft engines, propellers, appliances, or spare parts. It states that the right of a secured party with a security interest in the aircraft and other equipment as mentioned above, or of a lessor or conditional vendor of such equipment, to take possession of such equipment in compliance with a security agreement, lease, or conditional sale contract, and to enforce any of its other rights or remedies, under such security agreement, lease, or conditional sale contract, to sell, lease, or otherwise retain or dispose of such equipment, is not limited or otherwise affected by any other provision of the US Code, 1978. The exception to such exercise of rights by the secured creditor is the fulfilment of all obligations by the airline company under the security agreement, lease or conditional sale contract, within 60 days of the order for relief under the US Code.

UK and Treatment of Consumers

Post the Monarch airline debacle, the UK constituted an Airline Insolvency Review (Review) to assess consumer protection in the event of an airline or travel company failure. As discussed above, insolvency of an airline causes loss to consumers who have purchased flight tickets in advance. The final report of the Review makes recommendations seeking, among other things:

- establishment of a formal repatriation protection scheme to protect any air passenger whose journey began in the UK, and who has a ticket to return on an airline that becomes insolvent while they are already overseas;
- improvement of the availability of rescue fares and enhancement of passengers' ability to claim them;
- the introduction of a more complete regulatory toolkit which would provide for, among other things:
    - Annual certification to confirm financial fitness of the company;
    - Development of repatriation plans and access to data as required;
    - Requirement for the Board of a UK airline to notify the Civil Aviation Authority when there is a material adverse change in its financial situation; and
    - Ability to grant a temporary special purpose license to enable an airline to conduct a repatriation operation, even where the airline does not have a future.
- enhancement of existing refund protection by increasing consumer awareness and uptake of refund protection; minimising unnecessary duplication of protection; and helping passengers to make a claim swiftly and easily.

While the recommendations have not yet been transposed into law, India may derive from the observations made in the Review when dealing with consumer claims.

Cape Town Convention and Opposable Rights to High-Value Aviation Assets

The Convention on International Interests in Mobile Equipment was concluded in Cape Town on November 16, 2001 (CT Convention), as was the Protocol on Matters Specific to Aircraft Equipment (Protocol). The primary aim of the Convention and the Protocol is to resolve the problem of obtaining certain and opposable rights to high-value aviation assets, namely airframes, aircraft engines and helicopters which, by their nature, have no fixed location. Since these assets have no fixed location, there is negligible predictability of outcomes for the financier / lessors in terms of the enforcement of their rights to such assets. Owing to the differences in laws pertaining to leases and security interests across the globe, the enforcement of rights by such financiers / lessors may depend on multiple factors such as (a) where the asset is located; (b) where the insolvency proceedings are conducted; and (c) what is the level of coordination of proceedings between the jurisdictions where the asset is located and the insolvency proceedings are being conducted, if not conducted in the same place. These uncertainties hamper the provision of financing for such aviation assets and increases the borrowing cost.

The CT Convention read with the Protocol permits charges to enforce the following remedies:

- take possession or control of any object charged to it;
- sell or grant a lease of any such object;

- collect or receive any income or profits arising from the management or use of any such object;
- procure the de-registration of the aircraft (to the extent that the debtor has at any time so agreed and in the circumstances specified in the CT Convention); and
- procure the export and physical transfer of the aircraft object from the territory in which it is situated (to the extent that the debtor has at any time so agreed and in the circumstances specified in the CT Convention).

65 countries are parties to the CT Convention and are adopting its provisions by way of legislation. While India is also a signatory of the CT Convention, it has not yet adopted its provisions in the domestic law.

WINDING UP OF A COMPANY

One of the hallmarks of a reliable economy is the time taken for a company to wind-up. India's record in this area was not satisfactory. This was a major sore point for foreign investors who were looking for a way to close down the operations in a reasonable time. With this as one of its intents, the Insolvency and Bankruptcy Code was brought into effect in the year 2016. The Code is a game changer in the way insolvency is dealt with in this country. The entire procedure for bringing a lawful end to life of company is divided into two stages. These two stages are winding up and dissolution. Winding up of company is defined as a process by which the life of a company is brought to an end and its property administered for benefit of its members and creditors. It is the last stage, putting an end to life of a company. The main purpose of winding up is to realize the assets and make the payments of company's debts fairly. Thus, winding up is the process by which management of a company's affairs is taken out of its directors, its assets are realized by a liquidator and its debts are discharged out of proceeds of realization.

Meaning of Winding-up

Winding-up is the process of closing down the legal existence of a company or LLP. During this process, the assets of the entity are realized, its liabilities are paid off and any surplus is distributed amongst the contributories. Once the adjudicating authority is convinced that these processes are completed, the entity is dissolved. During winding up, the management of the company / LLP is in the hands of the liquidator and not the governing body / board of directors. However, the assets and liabilities still belong to the company until dissolution takes place. On dissolution, the entity loses its legal existence. The Insolvency and Bankruptcy Code, 2016 has made significant amendments to provisions relating to winding up in the Companies Act, 2013. The important ones are discussed below:

"Winding up" – The expression "winding up" was not defined in the Companies Act, 2013 or in the erstwhile Companies Act of 1956. The Eleventh Schedule has added sub-section (94A) to section 2 of the Companies Act, 1956. The definition of "winding up" reads as follows: "Winding up" means winding up under the Companies Act, 2013 or liquidation under the Insolvency and Bankruptcy Code, 2016, as applicable." [Section 2(94A)]

Voluntary winding up

Provisions relating to voluntary winding up in the Companies Act, 2013 i.e., sections 304 to 323 have been omitted by the Insolvency and Bankruptcy Code, 2016. Voluntary liquidation is now dealt with under section 59 of the Insolvency and Bankruptcy Code, 2016.

The Insolvency and Bankruptcy Code 2016 (the Code) not only enables the insolvency proceedings of the insolvents but also contains provisions for solvent entities that want to surrender their business and refrain from carrying on their business. To be eligible for voluntary liquidation, the solvent entity must be in a state to pay off its debts. The provisions relating to voluntarily winding up of Companies have been removed from the Companies Act, 2013 (w.e.f April 01, 2017) and are now governed by Insolvency and Bankruptcy Code. A corporate person will be eligible to opt for voluntary liquidation under the Code provided it fulfils the two mandatory conditions i.e.

(i) either the company has no debt or that it will be able to pay its debts in full from the proceeds of assets to be sold in the voluntary liquidation; and

(ii) The company is not being liquidated to defraud any person. Code reduces the intervention of the regulatory authorities drastically that fasten up the process. Once the liquidation process is completed, the liquidator has to make an application to the Tribunal for passing the order of dissolution of the company.

Inability to pay debts – Insolvency and Bankruptcy Code, 2016 has substituted section 271 of the Companies Act, 2013. Winding-up due to inability to pay debts is now governed by the Code.

WINDING UP BY TRIBUNAL

Section 271 of the Companies Act 2013 provides grounds for winding up of the company by the Tribunal.

According to section 271, a company may be wound up by the Tribunal in following cases:

(a) If the company has, by special resolution, resolved that the company be wound up by the Tribunal;

(b) If the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality;

(c) If on an application made by the Registrar or any other person authorized by the Central Government by notification under this Act, the Tribunal is of the opinion that the affairs of the company have been conducted in a fraudulent manner or the company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company be wound up;

(d) If the company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years; or

(e) If the Tribunal is of the opinion that it is just and equitable that the company should be wound up.

For commencing proceedings under section 271, a petition is to be made to the Tribunal.

According to section 272, this petition may be made by any of the following persons:

(a) The company;

(b) Any contributory or contributories;

(c) All or any of the persons specified in clauses (a) and (b);

(d) The Registrar;

(e) Any person authorised by the Central Government in that behalf; or

(f) In a case falling under clause (b) of section 271, by the Central Government or a State Government.

Any petition filed by the company shall be accompanied by a statement of affairs in prescribed form. A petition can be filed by the Registrar only with previous sanction of the Central Government which shall be accorded only after giving to the company a reasonable opportunity of being heard. Any petition filed under this section, apart from that filed by the Registrar himself, shall be served on the Registrar and the Registrar shall submit his views to the Tribunal within 60 days of receipt of such petition.

On a petition filed under section 272, the Tribunal may pass any of the following orders within 90 days of presentation of the petition:

(a) Dismiss it, with or without costs;

(b) Make any interim order as it thinks fit;

(c) Appoint a provisional liquidator of the company till the making of a winding up order;

(d) Make an order for the winding up of the company with or without costs; or

(e) Any other order as it thinks fit.

The Tribunal shall give an opportunity of being heard to the company before appointment of a Provisional Liquidator. The order for winding up of a company shall operate in favour of all the creditors and all contributories of the company as if it had been made out on the joint petition of creditors and contributories.

The liquidator is required to submit to the Tribunal, a report containing the following particulars, within sixty days from the order:

(a) the nature and details of the assets of the company including their location and value, stating separately the cash balance in hand and in the bank, if any, and the negotiable securities, if any, held by the company:

(b) valuation Report of the assets obtained from registered valuers

(c) amount of capital issued, subscribed and paid-up;

(d) the existing and contingent liabilities of the company including names, addresses and occupations of its creditors, stating separately the amount of secured and unsecured debts, and in the case of secured debts, particulars of the securities given, whether by the company or an officer thereof, their value and the dates on which they were given;

(e) the debts due to the company and the names, addresses and occupations of the persons from whom they are due and the amount likely to be realised on account thereof;

(f) guarantees, if any, extended by the company;

(g) list of contributories and dues, if any, payable by them and details of any unpaid call;

(h) details of trademarks and intellectual properties, if any, owned by the company;

(i) details of subsisting contracts, joint ventures and collaborations, if any;

(j) details of holding and subsidiary companies, if any;

(k) details of legal cases filed by or against the company; and

(l) any other information which the Tribunal may direct or the Company Liquidator may consider necessary to include.

When the affairs of a company have been completely wound up, the Company Liquidator shall make an application to the Tribunal for dissolution of such company. The Tribunal shall on an application filed by the Company Liquidator or when the Tribunal is of the opinion that it is just and reasonable in the circumstances of the case that an order for the dissolution of the company should be made, make an order that the company be dissolved from the date of the order, and the company shall be dissolved accordingly.

LIQUIDATION PROCESS

Liquidation of corporate person is considered to be the last resort in order to recover money. When the resolution plan has failed and no other way could be adopted then dissolution of company is the only resort. An auction is conducted where the assets of the company is sold to realize money to return it to the lenders. The provisions dealing with the liquidation of corporate persons are covered in the chapter III of the Part II of the Insolvency and Bankruptcy code.

Sections 33 to 54 of the Insolvency and Bankruptcy Code, 2016 and IBBI (Liquidation Process) Regulations, 2016 lays down the law relating to liquidation process for corporate persons. An attempt is first made to resolve the insolvency of corporate debtor through corporate insolvency resolution process laid down in Chapter II of Part II of the Code. The provisions relating to liquidation in Chapter III of Part II of the Code comes into effect if the attempts to resolve corporate insolvency under Chapter II of the Code fail. Section 33 of the Code lists out the triggers for initiating the liquidation process for corporate persons.

Section 33 of the Code reads as follows:

(1) Where the Adjudicating Authority, –

(a) before the expiry of the insolvency resolution process period or the maximum period permitted for completion of the corporate insolvency resolution process under section 12 or the fast track corporate insolvency resolution process under section 56, as the case may be, does not receive a resolution plan under sub-section (6) of section 30; or

(b) rejects the resolution plan under section 31 for the non-compliance of the requirements specified therein, it shall –

(i) pass an order requiring the corporate debtor to be liquidated in the manner as laid down in this Chapter;

(ii) issue a public announcement stating that the corporate debtor is in liquidation; and

(iii) require such order to be sent to the authority with which the corporate debtor is registered.

(2) Where the resolution professional, at any time during the corporate insolvency resolution process but before confirmation of resolution plan, intimates the Adjudicating Authority of the decision of the committee of creditors approved by not less than 66% of the voting share to liquidate the corporate debtor, the Adjudicating Authority shall pass a liquidation order as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section (1).

(3) Where the resolution plan approved by the Adjudicating Authority is contravened by the concerned corporate debtor, any person other than the corporate debtor, whose interests are prejudicially affected by such contravention, may make an application to the Adjudicating Authority for a liquidation order as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section (1).

(4) On receipt of an application under sub-section (3), if the Adjudicating Authority determines that the corporate debtor has contravened the provisions of the resolution plan, it shall pass a liquidation order as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section (1).

(5) Subject to section 52, when a liquidation order has been passed, no suit or other legal proceeding shall be instituted by or against the corporate debtor: Provided that a suit or other legal proceeding may be instituted by the liquidator, on behalf of the corporate debtor, with the prior approval of the Adjudicating Authority.

(6) The provisions of sub-section (5) shall not apply to legal proceedings in relation to such transactions as may be notified by the Central Government in consultation with any financial sector regulator.

(7) The order for liquidation under this section shall be deemed to be a notice of discharge to the officers, employees and workmen of the corporate debtor, except when the business of the corporate debtor is continued during the liquidation process by the liquidator. Liquidator Section 34 of the Code provides for the appointment of liquidator and the fees to be paid to him.

According to section 5(18) of the Code, a "liquidator" means an insolvency professional appointed as a liquidator in accordance with the provisions of Chapter III or Chapter V of this Part, as the case may be. Section 35 provides a non-exhaustive list of powers and duties of the liquidator to ensure orderly completion of the liquidation proceedings. Liquidation Estate Section 36 provides for the creation of a liquidation estate comprising the assets of the corporate debtor as set out in section 36(3). Section 36 also lists out the assets which are to be excluded from the liquidation estate. The Central Government has been given the power to notify assets, in consultation with the appropriate financial sector regulators, which will be excluded from the estate in the interest of efficient functioning of the financial markets. Section 36(1) provides that for the purpose of liquidation, the liquidator shall form an estate of the assets mentioned in sub-section (3), which will be called the liquidation estate in relation to the corporate debtor. Section 36(2) further provides that the liquidator shall hold the liquidation estate as a fiduciary for the benefit of all the creditors.

VOLUNTARILY LIQUIDATION

The Insolvency and Bankruptcy Code 2016 (the Code) not only enables the insolvency proceedings of the insolvents but also contains provisions for solvent entities that want to surrender their business and refrain from carrying on their business. To be eligible for voluntary liquidation, the solvent entity must be in a state to pay off its debts.

Brief of procedure of voluntary liquidation of a corporate person under IBC is given below:

Step I: Submission of declaration(s) to ROC, stating that the company will be able to pay its dues and is not being liquidated to defraud any person;

Step II: Passing of special resolution for approving the proposal of voluntary liquidation and appointment of liquidator ("Approval"), within 4 (four) weeks of the aforesaid declaration(s). If a corporate person owes debts, approval of two-third majority creditors would also be required;

Step III: Public announcement inviting claims of all stakeholders, within 5 (five) days of such approval, in newspaper as well as on website of the corporate person;

Step IV: Intimation to the ROC and the Board about the approval, within 7 (seven) days of such approval;

Step V: Preparation of preliminary report about the capital structure, estimates of assets and liabilities, proposed plan of action etc., and submission of the same to a corporate person within 45 (forty-five) days of such approval;

Step VI: Verification of claims, within 30 (thirty) days form the last date for receipt of claims and preparation of list of stakeholders, within 45 (forty-five) days from the last date for receipt of claims;

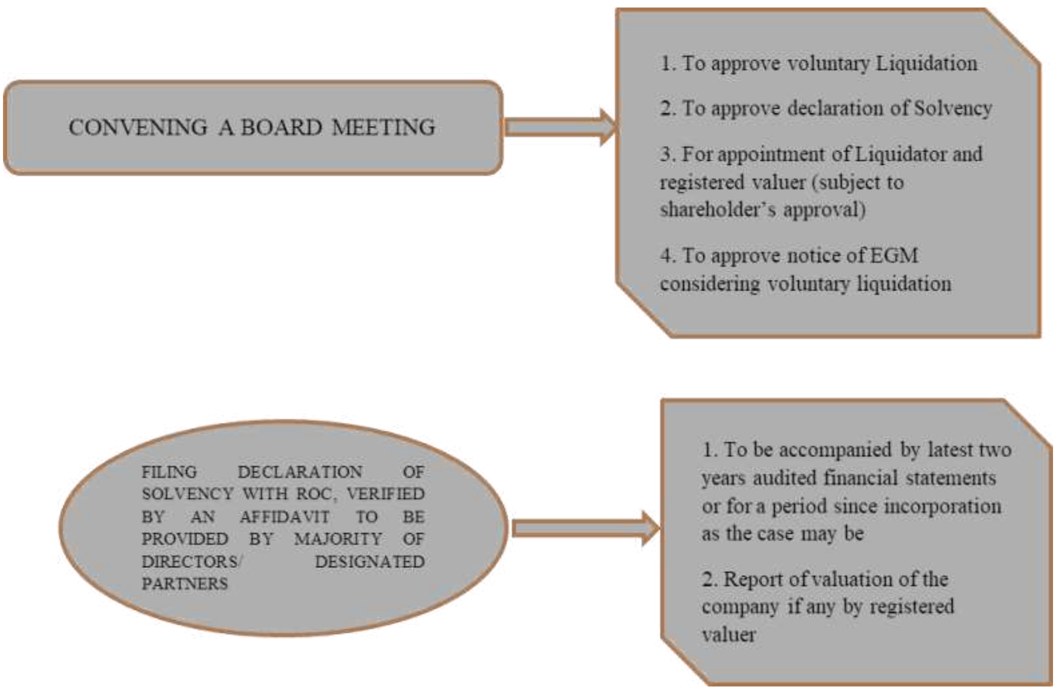
Step VII: Opening of a bank account in the name of the corporate person followed by the words 'in voluntary liquidation', in a scheduled bank, for the receipt of all moneys due to the corporate person

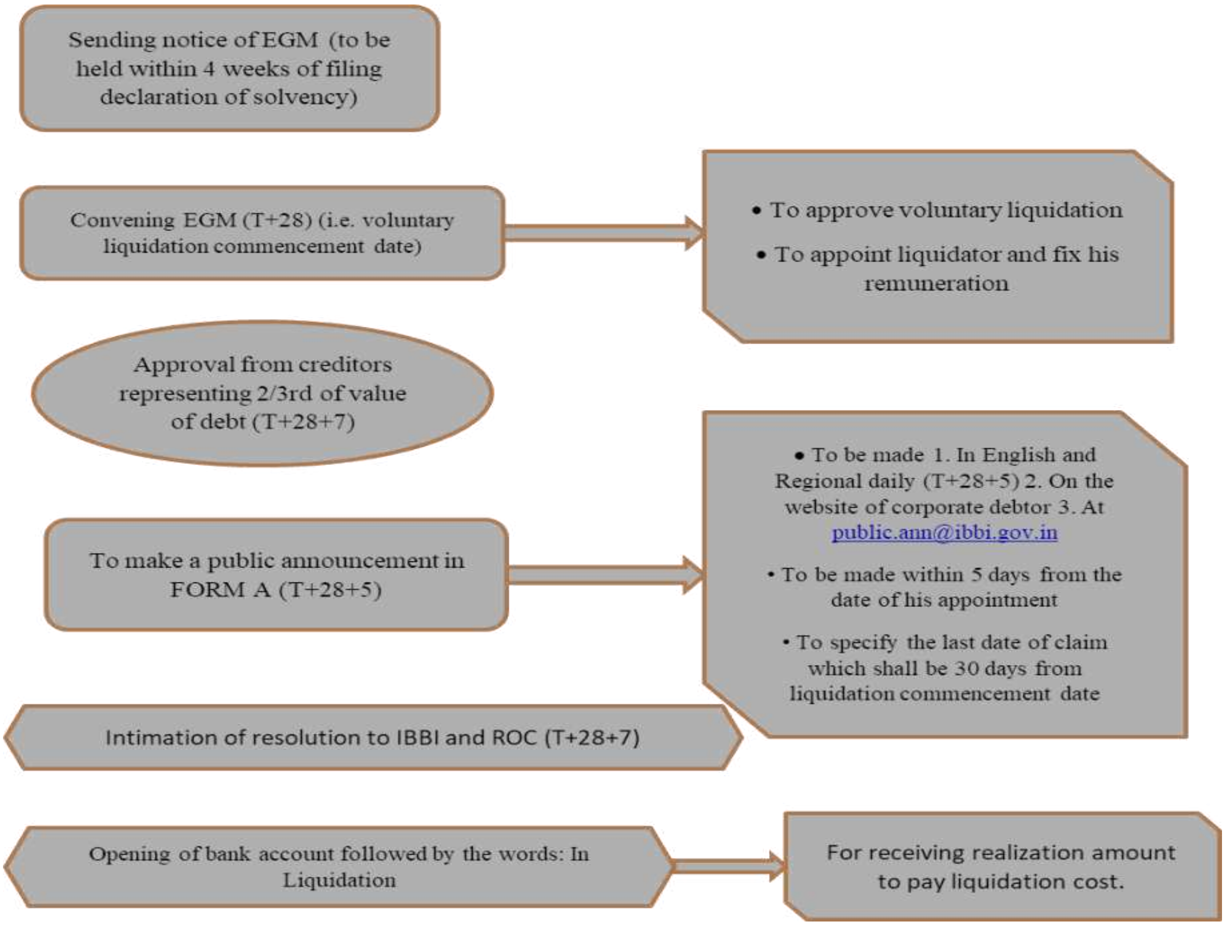
Step VIII: Sale of assets, recovery of monies due to corporate person, realization of uncalled capital or unpaid capital contribution;

Step IX: Distribution of the proceeds from realization within 6 (six) months from the receipt of the amount to the stakeholders;

Step X: Submission of final report by the liquidator to the corporate person, ROC and the Board and application to the National Company Law Tribunal ("NCLT") for the dissolution;

Step XI: Submission of NCLT order regarding the dissolution, to the concerned ROC within 14 (fourteen) days of the receipt of order.




Sending notice of EGM (to be held within 4 weeks of filing declaration of solvency)
Convening EGM (T+28) (i.e. voluntary liquidation commencement date)
• To approve voluntary liquidation
• To appoint liquidator and fix his remuneration
Approval from creditors representing 2/3rd of value of debt (T+28+7)
To make a public announcement in FORM A (T+28+5)
• To be made 1. In English and Regional daily (T+28+5) 2. On the website of corporate debtor 3. At public.ann@ibbi.gov.in
• To be made within 5 days from the date of his appointment
• To specify the last date of claim which shall be 30 days from liquidation commencement date
Intimation of resolution to IBBI and ROC (T+28+7)
Opening of bank account followed by the words: In Liquidation
For receiving realization amount to pay liquidation cost.

MODULE IV

COMPETITION LAW AND COMPETITION ISSUES IN AVIATION

OVERVIEW OF THE COMPETITION ACT 2002

What is Competition?

It is a situation in a market, in which sellers independently strive for buyer's patronage to achieve business objectives such as profits, sales or market share. It is the foundation of an efficiently working market system. Competition and liberalization, together unleash the entrepreneurial forces in the economy. Competition offers wide array of choices to consumers at reasonable prices, stimulates innovation and productivity, and leads to optimum allocation of resources.

Competition is not defined in law but is generally understood to mean the process of rivalry to attract more customers or enhance profit or both. Competition law deals with market failures on account of restrictive business practices in the market. Restrictive business practices can be of many kinds and include inter-alia agreements to restrict competition, cartelization, predatory pricing, tie-in sales, re-sale price maintenance, abuse of dominance etc.

The history of competition law is usually traced back to the enactment of Sherman Act in 1890 in the US. This act was directed against the power and predations of the large trusts formed in the wake of the Industrial Revolution where a small control group acquired and held the stock of competitors, usually in asset, and controlled their business. Gradually, competition law came to be recognized as one of the key pillars of a market economy. This recognition led to enactment of competition law in many countries, including developing countries, and the number now stands at around 105.

Need for Competition

Competition law enhances the innovation in the market.

According to Schumpeter, social theorist of 20th century the business cycle is exclusively the result of innovation in the economy. Innovation does not mean invention rather it refers to the commercial applications of new technology, new material, new methods and new sources of energy. which compels an entrepreneur to innovate or get eliminated, because of the forces of competition. Economies don't grow, they evolve. So the most important factor that stimulates innovation and growth in the economy is competition. In case of competition, firms would have more incentive to innovate because of the need to outperform rivals with new and improved products or services rather than in a monopoly as proposed by Schumpeter.

The competition law encourages the competition in the market, this results in increase in competition among the players in the market. The competition between the players forces them to reduce the cost through innovative technologies. To sustain in the market the players tend to invest more on the research and development, this leads to development of technology in the market in the long run.

Competition law promotes the stability in the economy

The competition law is one of the important factor which promotes the development of the economy. but at the same time it is evident that when the competition is increasing among the players in the market the players are tend to take more risk compared with the controlled environment. This policy may lead to a situation where the market players are unable to face the unforeseen circumstances due to the shocks in the economy. this lead to instability in the economy. it is observed that when we are promoting competition in the market, there is always a possibility of shocks to be faced by the economy due to unforeseen circumstances. But these circumstances may occur once in a decade or for more than that period. The competition promotes the economic development of the economy. it is a continuous process. so we can say that though competition reduces the stability in the economy but it can be avoided with the controlling the mechanism adopted by the government, like prescribing the minimum equity share capital and maintaining the reserves in the company. The above measures may help the companies to maintain the stability in during the unprecedented situations and contribute for the economic development as a whole[6].

Competition law facilitates the appropriate allocation of natural resources

Competition law is the one of the important legislation which aims at achieving an important object of economics. Economics is "*The study how societies use scare resources to produce valuable goods and services and distribute them among different individuals*[7]" The competition law helps the government to maintain the balance in allocation of natural resources. The Competition law helps the government in achieving the object of the economics. This is the reason why the competition law can be considered as an important economic legislation which aims at maintaining pure competition in the market. The basics for maintaining ecological balance and allocation of natural resources was very well understood by our ancestors in ancient times.

Supreme Court in the case Manohar lal sharma v. Principal Secretary held that the distribution of natural resources that vest in the state is to subserve the common good. In Natural Resources Allocation, In re, the constitution bench with reference to Art 39(b), stated as follows:

The disposal of natural resources is a facet of the use and distribution of such resources. Article 39(b) mandates that the ownership and control of natural resources should be so distributed so as to best subserve common good. Article 37 provides that the provisions of Part IV shall not be enforceable by any court, but the principles laid down therein are nevertheless fundamental in the governance of the country and it shall be the duty of the state to apply these principles in making laws. Therefore, this article, in a sense is a restriction on the distribution built into the constitution. The overarching and underlying principle governing distribution of natural resources is furtherance of common good.

The economic principal says that when we are having the competition in the market which leads to proper allocation of natural resources among the players in the market. This is major aim of the competition law in any country. The Constitution of India

[6] http://finance.wharton.upenn.edu/~allenf/download/Vita/compfinstabpublished.pdf
[7] Economics by Paul A Samuelson and William D. Nordhaus, Nineteenth Edition, Page 4

provides that it is the responsibility of the state to ensure the equitable distribution of natural resources among the people in the country. Article 39 of the Constitution of India Provides that it shall be the duty of state to ensure proper allocation of natural resources and the state shall ensure that the economic concentration shall not be there in the market.

The Economic Efficiency requires that the economy shall be in a position utilise the scare resources in the highest combination of quantity and quality of goods and services, so that we can generate the surplus while utilising the scare resources. This is facilitated by the competition policy in the country.

The efficient competition policy enhances the positive externalities which creates benefits to the society as a whole by proper allocation of natural resources. Sustainable consumption can also be achieved by the competition law.

Competition law encourages the consumer welfare

The Supreme Court of United States speaking in favour of consumers in ***Allied Tube & Conduit Co. V. Indian Head, Inc.***[8], held that "Product standardization might impair competition in several ways. It might deprive some consumers of a desired product, eliminate equality competition exclude rival producers, or facilitate oligopolistic pricing by easing rivals' ability to monitor each other's price".

The best definition of competition as provided by Chicago School that competition may be read as designating a state of affairs in which consumer welfare cannot be increased by moving to an alternative state of affairs through the intervention of antitrust law and that, conversely, monopoly designates a situation in which consumer welfare could be so improved so that to monopolise would be to use practices inimical to consumer welfare. This interpretation of competition coincides with everyday parlance as the competition for the man in the street implies low prices, innovation and choice among differing products. Competition thus equates with consumer welfare as the sole meaning thereby that antitrust law's sole goal is the maximization of consumer welfare. Consumer welfare is greatest when society's economic resources are allocated so that consumers are able to satisfy their wants as fully as technological constraints permit. Consumer welfare, in this sense, is merely another term for the economic wealth of the nation.

Competition Policy

The past few years have been challenging for the economy and for businesses world over, making the task of policy makers even more daunting. India, in the pursuit of globalization responded by opening up its economy by removing controls and resorting to liberalization. In the light of this, the obvious need of the hour was that the Indian market be geared to face competition from within the country and outside. The financial crisis which gripped world strengthened the need and highlighted the importance of a strong and effective competition policy, a policy which would encourage markets to

[8] 486 U.S.492 (1988)

work well for the benefit of business and consumers, thereby increasing the country's economic fitness: markets characterized by effective competition makes firms innovate more, keep prices down for consumers and improved total factor productivity drives economic growth. These factors are all the more relevant given the financial challenges faced by the country. It is clear that ultimately, the way out of this crisis – for the financial sector and the wider economy – lies with competitive markets, backed up by a robust competition policy.

Competition policy is defined as those government measures that affect the behavior of enterprises and structure of the industry with a view to promoting efficiency and maximizing consumer/ social welfare. There are two components of a comprehensive competition policy. The first involves putting in place a set of policies that enhance competition or competitive outcomes in the markets, such as relaxed industrial policy, liberalized trade policy, convenient entry and exit conditions, reduced controls and greater reliance on market forces. The other component of competition policy is a law and its effective implementation to prohibit anti competitive behavior by businesses, to prohibit abusive conduct by dominant enterprise, to regulate potentially anti competitive mergers and to minimize unwarranted government/regulatory controls.

In the wake of economic liberalization and wide spread economic reforms introduced by India since 1991 and in conformity with the commitments made at the WTO, in October 1999, the Government of India appointed a High Level Committee (Raghavan Committee) on Competition Policy and Competition Law to advise a modern competition law for the country in line with international developments and to suggest a legislative framework, which may entail a new law or appropriate amendments to the MRTP Act. The Committee submitted its report to the Central government. The Central Government consulted all concerned including the trade and industry associations and the general public. The Central Government after considering the suggestions of the trade and industry and the general public decided to enact a law on Competition to replace the then existing competition law namely, the Monopolies and Restrictive Practices Act (1969) (the MRTP Act) which was primarily designed to restrict growth of monopolies in the market with a modern competition law in sync with the established competition law principles. As the first step towards this transformation, a new Competition Act, 2002 was enacted which received Presidential assent on January 13, 2003

Background to Indian Competition Act 2002

Government of India (GOI) had appointed a committee under the Chairmanship of Shri S.V.S. Raghavan in October, 1999 to examine The Monopolies and Restrictive Trade Practices Act, 1969 for shifting the focus of the law from curbing monopolies to promoting competition and to suggest a modern competition law. Competition Bill, 2001 was introduced in the Lok Sabha on 6 August, 2001 and was referred to Parliamentary Standing Committee for its recommendation. Pursuant to the recommendations of the committee, the Competition Act, 2002 [Competition Act] was enacted.

In an open market economy, some enterprises may undermine the market by resorting to anti-competitive practices for short-term gains. These practices can completely nullify the benefits of competition. It is for this reason that, while countries across the globe are increasingly embracing market economy, they are also re-enforcing their economies through the enactment of competition law and setting up competition regulatory authority.

In line with the international trend and to cope up with the changing realities India, consequently, enacted the Competition Act, 2002. Designed as an omnibus code to deal with matters relating to the existence and regulation of competition and monopolies, the Act is intended to supersede and replace the MRTP Act. It is procedure intensive and is structured in an uncomplicated manner that renders it more flexible and compliance-oriented. Though the Act is not exclusivist and operates in tandem with other laws, the provisions shall have effect notwithstanding anything inconsistent therewith contained in any other law.

Departure from the MRTP Act

In a significant departure from the letter and spirit of the MRTP Act, the Act hinges on the "Effect Theory" and does not categorically decry or condemn the existence of a monopoly in the relevant market, rather the use of the monopoly status such that it operates to the detriment of the potential and actual competitors is sought to be curbed.

- The earlier legislation, considered draconian in the changed scenario, was based on size as a factor, while the new law is based on structure as a factor, aimed at bringing relief to the players in the market.

- The Act empowers CCI to impose penalty on delinquent enterprises, whereas in the MRTP Act there were no provisions regarding such enterprises

- MRTP Act could only pass "cease and desist" orders and did not have any other powers to prevent or punish while the new law contains punitive provisions.

- MRTP Act was applicable to Private and Public sector undertakings only, whereas, the new Act extends its reach to governmental departments engaged in business activities.

- As regards agreements, compulsory registration has been done away with.

- The most path-breaking chapter in the Act has been the emphasis on Competition Advocacy that was not at all contemplated by the MRTP Act.

Objectives of the Act

I. To check anti-competitive practices

II. To prohibit abuse of dominance

III. Regulation of combinations.

IV. To provide for the establishment of CCI, **a quasi-judicial body** to perform below mentioned duties:

- Prevent practices having adverse impact on competition
- Promote and sustain competition in the market

- Protect consumer interests at large
- Ensure freedom of trade carried on by other participants in the market
- Look into matters connected therewith or incidental thereto.

ELEMENTS OF COMPETITION LAW

Typically, a modern competition law has three major elements:

- anti-competitive agreements
- abuse of dominance
- merger control

Anti-competitive agreements

Anti-competitive agreements are those, as the name suggests agreements that restrict competition. Usually, an agreement need not be formal or in writing or justifiable in a court of law necessarily to be dealt with under a competition law. Thus, an informal agreement to fix prices will be hit by provisions of competition law. Agreement between rivals or competitors is termed horizontal agreement. The most pernicious form of anti-competitive agreement is cartelization. When rivals or competitors agree to fix prices or share consumers or do both, the agreements are termed as cartel. Competition laws across the global take cartelization very seriously and there seems to be a convergence in law on dealing strictly with this scourge of competition.

Besides horizontal agreements, there can be anti-competitive agreements between producers and suppliers or between producers and distributors. These are referred to as vertical agreements. By an agreement with the supplier of the most important source of raw material or by having an agreement with the largest distribution channel, the producer forecloses the market to its rivals. Hence, vertical agreements too can undermine competition in the market.

The Competition Act, 2002, deals with anti-competitive agreements in section 3.The provisions specifically deal with cartels and distinguish between horizontal and vertical agreements. While horizontal agreements are dealt with under presumptive rule, i.e. appreciable adverse effect on competition is presumed, vertical agreements are dealt with on a rule of reason basis, i.e. appreciable adverse effect on competition needs to be proved by the Competition Commission of India.

In the US, anti-competitive agreements are dealt with in section 1 of the Sherman Act. In the UK, anti-competitive agreement is covered in Chapter I section 2. In the EU, these are controlled by re-numbered Article 81 of the Treaty of Rome. In Australia, anti-competitive agreements are covered in Part IV of the Trade Practices Act, 1974. In the Canada, Part VI Sec 45 covers anti-competitive agreements.

In the competition laws, anti-competitive agreements are declared to be void. While this is true in the US (where it is illegal), the same is true in the UK, Australia, Canada and also in India.

Most competition authorities rely heavily on leniency or amnesty programmes for detection of the cartels. A member of a cartel is usually granted immunity from criminal sanction (wherever it exists like in the US) and/or the penalty is either waived or reduced. Practically every major industrialized country has some kind of leniency programme and there seems to be a move towards having criminal sanctions for this offence. In India, the leniency programme is contained in section 46 and does empower the Commission to reduce the penalty. However, there are no criminal sanctions for cartelization in the Competition Act, 2002. Monetary fines seem to be common in the competition laws of major countries. Both in India and in UK, the fines can be upto 10% of the turnover. In the US, the fine is fixed at US$ 10 million for a company and US $ 350000 for a person under the Sherman Act, 1890

In modern competition laws, in order to establish abuse of dominance or dominant position, it is first necessary to establish the dominance itself. Ever since the enforcement of section 2 of the Sherman Act in US began, economic analysis came to play an important role. This led to the development of certain key concepts in competition economics namely, market definitions. An enterprise's dominance can be in the relevant market which can be demarcate on the basis of the relevant product market and the relevant geographic market.

The relevant product market is the market constituted by substitute products or services. The relevant geographic market consists of neighboring areas or territories from which products can be supplied profitably at little above the current prices to the area under inquiry. For example, a major supplier of bananas with a large market share of, say, around 50% can be in a dominant position only if the other fruits are not substitutes. As a matter of fact, in one of the landmark cases in the European Union, a banana supplier claimed 6% market share in the fruit market but was found to have market share of 46% among banana suppliers. The European Court of Justice held that banana constituted the relevant product market on account of its non- substitutability by the toothless i.e. infants and old people.

Abuse of Dominance

Dominance is also referred to as market power which is defined as the ability of the firm to raise prices or reduce output or does both independently of its rivals, customers and consumers. The definition of dominance is broadly similar in the competition laws of several countries. When a firm acquires market powers, it can, and usually will, increase prices and reap monopoly profits since it has no fear of rivals or consumers. As and when price is increased or output is reduced by a firm having market power in a non-transitory manner, it is said to abuse its power. Since economists loathe monopoly for its failure to provide any benefits but certainty of its leading to loss of consumer welfare, competition laws also treat abuse of dominance as a restrictive business practice.

The laws of various countries show a lesser convergence while dealing wit abuse of dominance. One major difference seems to be in the need for proving the harm and injury on account of the abuse. There is also variation in what constitutes an abuse.

In the Competition Act, 2002, abuse of dominant position is dealt with in section 4 and the law presumes 5 kinds of abuses including, inter-alia, discriminatory pricing, unfair pricing, predatory pricing, denial of market access, etc. and prohibits such behaviour. Injury or harm is not required to be proved while dominance needs to be proved using

rule of reason test after considering 27
4factors (including factors to be taken into account for market definition), economic
as well as non-economic, stated in the law itself. This is in line with other jurisdictions. Once dominance is established and the dominant firm is found to be indulging in any of the five kinds of behaviour, law presumes such behaviour to be an abuse.

Some of the vertical agreements, namely, tie-in-sales, resale price maintenance etc. are treated under the provisions dealing with abuse of dominance in some jurisdictions since these can only be effective if resorted to by dominant firms.

: Indian Civil Aviation in the past seventy or so years has witnessed three different phases, starting from the initial private regime followed by years of nationalization and the recent era of deregulation. The current de- regularized system, with its inherent competition, has succeeded in providing better consumer services. On the other hand, this has posed several challenges to the competition policy framework, calling for a need to strike a balance between protecting the interests of consumers and hence ensuring free and fair competition.

Areas which need the attention of legal fraternity and policy makers include measures to combat abuse of dominant position, encompassing:

- Predatory pricing
- Denial of market access
- Loyalty Programmes
- frequent flyer programmes
- corporate discount schemes
- travel agents commission

At the first level the paper will focus on the issues relating to abuse of dominant position by airline operators and air navigation service providers. At the next stage an attempt will be made by the authors to examine certain practices adopted by the airlines such as predatory pricing, denial of market access and loyalty programmes which have an adverse effect on the competition in the industry.

This paper will analyze the position of law in India and the existing infirmities to it in this regard. The paper will draw insights from various international instruments like Chicago Convention, 1944, the International Civil Aviation Organization (ICAO) and International Air Transport Association (IATA) and de-regulation laws of various jurisdictions like USA, Australia, Mexico, Canada and European Union which are in consonance with the international law regime and the applicability of the same in the Indian scenario will be examined in detail.

Based on the above appraisal of the current scenario the paper will draw conclusions on the need of a comprehensive policy or the substitution of draft Civil Aviation Policy, 2000 that can assure a conducive competitive regulatory framework for encouraging entry and participation of private airlines and privately run airports with special reference to update policies, guidelines and other regulatory instruments to address recent changes

Merger Control

The third element of modern competition law is merger control. The Indian law uses the word combinations to cover acquisition of control, shares, voting rights and assets, and mergers and amalgamations. This is universally done ex-ant in all jurisdictions. The underlying logic is that it is much easier to stop a combination that is likely to undermine competition than to deal with the situation ex-post, after the damage has been done (which could have been prevented in the first place) and facing the possibility of de-merging, which can be cumbersome. The combinations are stopped or modified (including divestiture) to prevent unilateral action or collusive action. If the combining parties compete in substitute products, and the combination is likely to provide them with market power, it is likely that they will abuse such power. Therefore, such combinations can not be allowed to go ahead by the competition authorities. It is also likely that combination can result into fewer players in the market which can facilitate collusion that can seriously undermine competition. Therefore, even such combinations will not be allowed.

Combinations are usually divided into three categories. The first are horizontal combinations, which are between producers of substitute products and often raise serious competition concerns for obvious reasons. The second category is vertical combinations where the combining parties are at different stages or levels of production e.g. producer of cars merging with distributors. Such combination can in some cases lead to anti-competitive situation and will get a hard look by the competition authorities. The third category is conglomerate combinations where the combining parties are in unrelated businesses and usually do not raise competition concerns. Most of the jurisdictions that have merger control are similar in this regard.

One major difference in handling combinations is the requirement of notifications and having thresholds. Most of the jurisdictions in the world have mandatory merger control where the combining parties are compulsorily required to notify the competition authority. The list of countries having compulsory notification includes Argentina, Brazil, South Korea, Canada, France, Germany, Israel, Japan, South Africa, EU and US. Few countries have voluntary filing regimes where it is left to the discretion of the combining parties whether to notify the competition agency. According to the International Bar Association, the list of such countries in 2006 includes Australia, Chile, Costa Rica, Indonesia, New Zealand, Norway, Panama, UK and Venezuela. Since compulsory notification brings in greater certainty and reduces business risks associated with combining, most countries in the world have opted for compulsory notification.

Since compulsory notification tends to increase the workload of the competition authorities, most of the jurisdictions have sought to reduce their workload by having threshold limits, either in terms of value of assets or value of turnover or both. The Competition Act, 2002 also provides thresholds both in terms of assets as well as turnover. The threshold limits in the Indian law are relatively higher than most jurisdictions.

Under a compulsory notification regime, combinations taking place outside the jurisdiction also need to notify. If the combining parties do not have any effect on competition in markets within the concerned jurisdiction, the burden of imposing notification requirements would not be appropriate. Therefore, most of the jurisdictions having compulsory notification provide for further threshold limit in terms of domestic revenue generated by the combining parties. In effect, domestic nexus provides second level of threshold which would reduce the burden of both the combining parties as well

as the competition agency.
The fourth element is competition advocacy. At the outset, it may be noted that advocacy is not always provided in the statute even in mature jurisdictions. And yet, all the mature jurisdictions display a singular focus on competition advocacy. Competition advocacy has been defined to "include all activities of a competition agency that are intended to promote competition apart from those that involved enforcement of the competition law".
The Competition Act, 2002 mandates the Competition Commission to promote competition advocacy, create awareness
and impart training on competition issues.
While enforcement of competition law is targeted towards commercial activities of private and public players, advocacy is targeted more towards the policy making powers of the government besides creating awareness. Therefore, it is often said, the law enforcement and competition advocacy complement each other.
The Indian competition law enables the government to seek non-binding opinion of the Competition Commission on competition policy. In the UK, all government offices are obliged since 2002 to assess the impact of legislation on competition.
The Office of Fair Trading, the UK competition authority, advises the regulators and the government on their regulatory impact assessments. In the US, the Federal Trade Commission has a competition advocacy programme since 1980s and has actively intervened in a number of sectors including on legislations.

Competition Commission of India

CCI, entrusted with eliminating prohibited practices, is a body corporate and independent entity possessing a common seal with the power to enter into contracts and to sue in its name. It is to consist of a chairperson, who is to be assisted by a minimum of two, and a maximum of ten, other members.

Acts taking place outside India

CCI has the power to enquire into unfair agreements or abuse of dominant position or combinations taking place outside India but having adverse effect on competition in India, provided that any of the below mentioned circumstances exists:

- An agreement has been executed outside India
- Any contracting party resides outside India
- Any enterprise abusing dominant position is outside India
- A combination has been established outside India
- A party to a combination is located abroad.
- Any other matter or practice or action arising out of such agreement or dominant position or combination is outside India.

To deal with cross border issues, CCI is empowered to enter into any Memorandum of Understanding or arrangement with any foreign agency of any foreign country with the prior approval of Central Government.

Benches

For the execution of duties, the Act contemplates the exercise of the jurisdiction, powers and authority of CCI by number of **Benches**. If necessary, a Bench would be constituted by the chairperson of at least two members; it being mandated that at least one member of each Bench would be a "Judicial Member". The Bench over which the chairperson presides is to be known as the **Principal Bench** and the other Benches known as **Additional Benches**. However, the Act further empowers the chairperson to further constitute one or more Benches known as **Mergers Benches** exclusively to deal with combination and the regulation of combinations.

Extension of the executive powers

The Act contemplates the extension of the executive powers of CCI by the appointment of a **Director General** and as many other persons for the purpose of assisting it in conducting enquiries into contraventions of the provisions of the Act as well as conducting cases before the Commission.

CCI is empowered to conduct enquiries into:

1. "Certain agreements and dominant position of enterprise"
2. "Combinations"

CCI, either on its own motion, on receipt of a complaint or on a reference made to it by the Centre or State Government may enquire into any alleged contravention regarding the nature of the agreement, which is suspected to be inherently anti-competitive, or the abuse of dominant position. Any person, consumer, consumer association or trade association can make a complaint.

An enquiry into a combination, existing or proposed, may be initiated upon the knowledge or information in the possession of CCI or upon notice of the person or entity proposing to enter into a combination or upon a reference made by a statutory authority. Limitation of time for initiation of enquiry is one year from the date on which the combination has taken effect when CCI conducts such enquiry.

Jurisdiction

An enquiry or complaint could be initiated or filed before the Bench of CCI if within the local limits of its jurisdiction the respondent\s actually or voluntarily resides, carries on business or works for personal gain, or where the cause of action wholly or in part arises.

CCI has been vested with the powers of a civil court including those provided under sections 240 and 240A of the Companies Act, 1956 on an "Inspector of Investigation" while trying a suit, including the power to summon and examine any person on oath, requiring the discovery and production of documents and receiving evidence on affidavits. CCI is also vested with **certain powers of affirmative action** to act in an expedited manner. Civil courts or any other equivalent authority will not have any jurisdiction to entertain any suit or proceeding or provide injunction with regard to any matter which would ordinarily fall within the ambit of CCI.

Procedure Of Investigation And Order Thereof

If a prima facie case exists with respect to **anti-competitive agreements and abuse of dominant position**, CCI is empowered to direct the Director General to conduct an investigation in the matter.

In determining the nature of agreements, the following factors are to be taken into account:

- Barriers to new entrants in the market
- Driving existing competitors out of the market
- Foreclosure of competition by hindering entry into the market
- Accrual of benefits of consumers
- Improvements in production or distribution of goods or provision of services
- Promotion of technical, scientific and economic development.

In determining the nature of the dominant position enjoyed by an enterprise, following factors are to taken into account:

- Market share of the enterprise and market structure and size
- Size and resources of the enterprise
- Economic power of the enterprise including commercial advantages over the competitors
- Size and importance of the competitors
- Dependence of consumers on the enterprise
- The extent of vertical integration and consumer dependence
- Whether the monopoly was gained by reason of statute or otherwise
- Entry barriers including barriers such as regulatory barriers, financial risk, high capital cost of entry, market entry barriers, technical entry barriers, economies of scale
- "Countervailing buying power" and "social obligations and costs"
- Any other factor which CCI may consider relevant for the enquiry.

The Director General would submit his report with recommendations. If CCI is of the view that there are no merits to the case, the complaint would be dismissed, with costs. However, during the course of enquiry, CCI may grant **interim relief by way of temporary injunctions** restraining a party from continuing with the ant-competitive agreements or abuse of dominant position.

An order of CCI subsequent to an enquiry, could consist of:

- Directing the persons or entities ruled against to desist from abusing a dominant position or discontinuing acting upon anti-competitive agreements
- Imposing penalty to the maximum extent of ten percent of the average turnover for the last preceding three financial years upon each person or entity party to the abuse
- Award compensation
- Modify agreements
- Recommend the division of the dominant enterprise to the Centre, which has the ultimate authority to decide the fate of a dominant enterprise
- Recovery of compensation from any enterprise for any loss or damage shown to have suffered by the other party.

The procedure for investigation of combinations is somewhat different, as the Act contemplates direct investigation to be conducted by CCI rather than by resorting to the via media of the Directorate General. It may call upon any party to furnish all relevant information with regard to their business operation to come to a conclusion as to the nature of the combination.

While the factors to be taken into account_are similar to the parameters to be applied while examining anti-competitive agreements and abuse of dominant position the CCI shall also have due regard to the following factors:

- Actual and potential level of competition through imports in the market
- Extent of effective competition likely to sustain in the market
- Likelihood that the competition would result in the removal of a vigorous and effective competitor or competitors in the market.
- Possibility of a failing business
- Nature and extent of innovation
- Relative advantage, by way of the contribution to the economic development
- Whether the benefits of the combination outweigh the adverse impact of the combination if any

In case of combination, CCI may pass following **orders**:

- Approval of the combination if no appreciable adverse effect on competition is found
- Disapproval of the combination in case of adverse effect
- It may propose suitable modification as accepted by the parties
- During enquiry grant interim relief by way of temporary injunctions
- Award compensation

Penalties

In case of failure to comply with the directions of CCI and Director General or false representation of facts by parties, penalties ranging from Rs 1lac to Rs 1 crore may be imposed as the case may be.

Execution of the order

So far the execution of the order is concerned, it is the responsibility CCI. However, in the event of its inability to execute it, CCI may send such order for execution to the High Court or the principal civil court, as the case may be.

Post-Decisional Options

The aggrieved person may apply to CCI for **review of the order** within thirty days from the date of the order, provided that the below mentioned conditions are fulfilled:

- An appeal is allowed by this Act
- No appeal has been preferred

Provision has been made for an **appeal against any order** or decision of CCI by any aggrieved person. An application for this purpose has to be made to the Supreme Court within sixty days from the date of communication of the decision or order.

Competition Advocacy

Perhaps one of **the most crucial components of the Act** is **competition advocacy.** Intention is to help evolve competition law through review of policy, promotion of competition advocacy, creating awareness and imparting training about competition issues. For this purpose Government may, in its discretion, make a reference to CCI for its opinion thereon but is not bound by it. The power of the Centre to issue directions to CCI is inherent, and such directions would bind it.

Indian Aviation Sector-An Overview

Pre-Liberalization Era

The early years of Indian aviation industry and especially 1949-1950, witnessed soaring prices of aviation fuel, mounting salary bills and disproportionately large fleets. The result was shown in the declining financial health of the airline companies inspite of a slightly favourable and liberal patronage by the government and an increasing trend in air passenger traffic. Further in 1953, the government nationalized the airlines via. The Air Corporations Act, 1953, giving rise to Indian Airlines and Air India. The Act also gave monopoly power to Indian Airlines to operate on domestic scheduled services to the exclusion of any other operator. Air India became the only Indian carrier to operate on international routes except for some routes to the neighboring countries which were given to Indian Airlines.

Air India had the reputation of a boutique airline till 1970s with all its gracious Indian service. But it was unable to sustain this image as it slowly adopted many of the insensitivities of Indian public sector enterprises and appeared to be driven more by the priorities of its large workforce than its paying customers. On the other hand Indian Airlines became unpopular due to its delayed flights, indifferent service, patchy safety record, and high fares.

The period before liberalization of Indian economy was predominantly exposed to higher levels of state control over most of the sectors of the economy. The Airline industry being one of the most important sectors of the economy was no exception. The industry was monopolized by state-run carriers, disallowing private and foreign players from entering Indian market and these state-run carriers which dominated the market were built on huge costs. The monopoly by state carriers led to hindrance of growth in the airline sector. One of the most disadvantageous consequences of such monopoly was the retaliatory measure by foreign players. The foreign airline companies were hesitant in entering into deals with Indian companies due to the monopolistic lock created by state-run carriers resulting in an unwelcoming aviation market.

The cost of air travel in India was amongst the highest in the world owing to rising fuel costs. Further, the monopoly of the state-run carriers restricted the entry of no-frill airlines into the market. No- frill airlines are those low cost airlines which do not provide food, beverages or other amenities to passengers, reducing the cost of travel. But the monopoly of the two airlines had created a dead-lock restricting entry of private players, low-cost airlines, foreign players, etc., resulting in hindrance in the growth of aviation sector. All these factors and features of the era of liberalization resulted in the "open skies" policy of the government.

Reasons for Deregulation

The monopoly of state-run airlines and their deteriorating performance was one of the most important reasons for deregulation in the aviation sector. The rising costs of travel and dissatisfaction amongst consumers and various reasons demanded deregulation of the aviation sector. The restriction on entry of private players disallowing competition and reduced prices was a clear disadvantage for the passengers.

Since the 80s, popular opinion began shifting towards privatization and deregulation of the air transport sector. Many forces including growth in demand for air services, technical changes, emphasis on safety, and changing perceptions of limited Government intervention in commercial activities contributed to the shift. The burgeoning growth in air traffic also put additional strains on the aviation system and its regulatory structure. Increasing passenger demand was not meted out by satisfactory services to cater to the demand. It was not only a trend with increasing passenger demand but the passengers demanded variety and options in aviation services, such as low- cost and no-frill airline services. This need for variety in services fostered the entry of such services into the market post deregulation.

Moreover during the 1980s and 1990s, most of the developing countries witnessed rapid economic development, and this was also reflected in the dynamism of the airline industry. Air traffic witnessed a major boost, both on domestic and on international routes. The development in turn necessitated important reforms in the role of the State. It needed loosening up of the regulations. The divergent needs of business travelers, tourists, shippers of cargo, and the airlines themselves put considerable strain on the regulatory structure.

Liberalization of the sector entailed a combination of both privatization initiatives as well as deregulation as a whole. Privatization of the airlines from Government control would enable the airlines to operate on economic principles, fostering competition and improved efficiency. Worldwide experience showed that privatization of ownership improved efficiency in operations, as the parameters that govern the operations are no more non-economic. Excessive Government control had been one of the weak links of the sector. Private ownership would also facilitate resource mobilization. It was deemed to prove important especially for developing countries because it was perhaps the best way of bringing in financial discipline in the aviation sector.

Therefore, decline in performance as well as profitability of both Air India and Indian Airlines and increased passenger demand from 1990 onwards, necessitated additional capacity creation in the domestic market leading to deregulation. Apart from the reasons related to the monopolistic state carriers, other reasons such as rising fuel prices and the zeal of privatization demanded deregulation of the aviation sector.

Post Liberalization

India reverted back towards an ‘open sky’ policy in the nineties conforming to the worldwide trends in the aviation sector. As a part of this policy, various reforms were brought about in the aviation sector. Private operators were allowed to operate scheduled and non-scheduled services thus removing entry and exit barriers. Since the repeal of the Air Corporations Act and the entry of private operators, seven private airlines were assigned ‘scheduled’ status and were allowed to operate on all domestic routes alongside Indian Airlines. Apart from these there were 27 non-scheduled operators. However there were no private operators on international routes.

The choice of the aircraft type and size were left to the operator to decide. The foreign equity up to 40 per cent and NRI/OCB investment up to 100 per cent was permissible in the domestic air transport services. The deregulation reforms also brought about open sky policy for cargo operators on a permanent basis. Constructions of private airports both for international and domestic operations were being permitted. Private participation including full foreign equity in the development of existing airports was allowed.

One of the most important features of deregulation was that the control over fares had been withdrawn and left to the market forces. This led to a rapid boom in the demand for air transport services. Further, entry of low-cost and no-frill airlines enhanced this demand.

For the systematic development of air transport services, four categories of operator services were defined—Scheduled Airlines, Regional Airlines, Nonscheduled (Air Taxi) Charter Services and Air Cargo Services for transportation of cargo and mail. Scheduled airlines were to operate on routes according to a published timetable each flight being open to use by members of the general public. Regional airlines were to operate between state headquarters and other cities and towns in the region. Nonscheduled services were to cover specialized traffic like business tours, executive flights and special flights to destinations without scheduled flights. Air cargo services were either on a scheduled or a non-scheduled basis but could not carry passengers.

Hence, deregulation brought about rapid developments in the civil aviation sector and revolutionalised the erstwhile industry which was pawned by the government. But gradually, the developmental objectives which were sought to be brought about in the sector began to be defeated by various factors. Firstly, the immediate factors like uneconomic fares and rising fuel costs defeated the developmental objectives of deregulation. Further, in the recent times, strategic alliances by airlines and corresponding anti-competitive behaviour on their part have also started defeating the purpose of deregulation.

The liberalization of the airline industry in the 1990s led to a notable increase in the role of the private sector. No longer were the Indian skies dominated by the state run carrier and the exclusive monopoly of the state carrier came crashing down. Many reasons have been attributed to such crash, which include unplanned expansion as well as interference of government in key policies despite deregulation and ironically deregulation itself has been blamed as a cause.

Another important character of aviation sector in the present situation is that the existence of low cost air carriers. Let us understand about the Low cost air carriers in detail then we will move forward by understanding various competition issues in aviation industry.

Low Cost air carriers - a global perspective

Overview

The low cost carriers in Europe almost captured a 25% share as of now. While the first time air travelers continue to contribute to the growth of LCC, the full services conventional carriers (legacy) do not suffer any appreciable market share.

In general, what we observe in the air travel market today is a fare war ignited by low cost carriers. There is an impression fast gaining momentum that low cost carrier (LCC) means, substandard services, low in performance, low in serviceability and low even in safety standards, and the tickets are sold for a very low price or even ‘zero’ as the hidden surcharges and taxes are unknown to the traveling public, particularly the ‘first time travelers’ who in any case are the target population. It is time that the LCC re- looked at their advertising campaigns to correct the wrong impressions. First time travelers must know the clear difference between a ‘full service’ conventional airline like Emirates Airline and the LCC like Air Arabia. Travelers should be aware that low cost carrier means it will not have certain facilities or full services on board like Emirates and that is why they are low in prices, and not low in service quality. Once this clear message is communicated, then the traveling public should be able to choose the right airline. It is important to create the right impression from the very beginning, otherwise it will create a wrong impression in the mind of a first time traveler and that will spread by word of mouth. It is critical to inculcate the right perspective, as the LCC is growing fast and have a good potential to grow fast in India too.

<u>What is a Low-Cost carrier (LCC)</u>

In airline business, we have a traditional model referred to as 'Legacy Carrier/Conventional' and the Low-Cost Carrier. It is essentially a 'business module' also known as 'no frills' or discount carrier, is an airline that offers low fares but eliminates most traditional services. Legacy carriers operate with multi-class (First, Business and Economy) configuration with 'complimentary in-flight services.

'No-frills' is the term used to describe any service or product for which the non-essential features (or frills) have been removed. Common products and services for which no-frills brands exist include airlines, supermarkets, holidays, automobiles etc. They operate on the principle that if you take away the frills, you get lower prices/fares. No-frills supermarkets are recognizable by their store design and business model. They work on the principle that in most supermarkets,20% of products on sale account for 80% of what people buy and therefore, they stock the most commonly sold product, and they often do not serve branded items.

A typical Low-Cost Carrier business model practices include:

- a single type of aircraft (say, Airbus320 or 'Boeing 737)
- a single passenger class
- a simple fare scheme(typically fare increases as the aircraft fills up, which rewards early reservations-Yield Management)
- unreserved seating (encouraging passengers to board early and quickly)
- short flights and fast turnaround times (allowing maximum utilization of aircraft)
- flying to cheaper/less congested airports
- simplified routes, mostly point-to-point
- emphasis on direct sales of tickets(on line)
- employees working in multiple roles and simple dress code
- 'Free' in flight catering and other 'complimentary' services are eliminated, and replaced by optional paid-for in-flight food and drink

LCC seek to price their fares well below those of traditional airlines to increase demand and encourage consumers to switch to the low -cost carriers. By taking advantage of their lower average seat mile costs and using the increased demand to fill a large percentage of their flights, the low-cost carriers seek to maintain profitability despite offering lower rates.

The first successful low cost carrier was Pacific South West Airlines in the US who pioneered the concept when the first flight took off on 06 May 1949. Often, this credit has been incorrectly given to South West Airlines which began service in 1971 and it has been profitable every year since 1973.. With the advent of aviation deregulation, the model spread in Europe and the most notable one being Ireland's Ryanair which began the low cost operations in 1991 and Easy Jet followed it in 1995. Malaysia's Air Asia and Australia's Virgin Blue came in 2004.

Many traditional carriers tried to introduce the low cost concept by introducing an 'airline within an airline' where in the traditional airlines tried to follow the low cost concept just by introducing no frills such as KLM's Buzz, British Airways' GO Fly, and United's Ted, and most of them found it difficult to establish the low cost model. British Midland's low Cost rival bmi baby has however, successfully operated alongside its full-service counterpart. In Canada, Air Canada found it difficult to compete with low-cost rivals such as Westjet, Canjet and Jetsgo despite its prominent position in the market. Air Canada tried to operate two low cost subsidiaries, Tango and Zip, and both were discontinued. Whereas, Malaysia's Air Asia and Australia's Virgin Blue are some of the good models of growing LCC.

The clear message is that fare alone can not drive an airline, though it could be one of the drivers, there has to be other factors that should join the drivers to make LCC in real terms, 'low in fares but high in service'. Look at airlines like 'Emirates', they are high on fares, superior in service quality, and doing well.

It is also wrong to presume that people look only for food and entertainment on board, more so, on short routes, the main customer concern is service with a smile and from the word go customers should have a feeling of goodwill- a hassle free environment.

As the Government policy is now aimed to encourage Regional Carriers, it is obvious that more and more LCC will take off, while many more are waiting on the wings, some hesitant and frightful whether they can gain the market and be profitable. Why this uncertainty?

The objective of LCC are to woo the rail/road travelers to air travel and create a new environment for this segment of travelers so that more and more such travelers will move over creating a new wave of mass transportation- nothing but an Air Taxi operation. The carriers, planners, and airport operators should accept this concept and mutually assist each other so that air taxi operations (LCC) gain the required momentum.

It is said "strategy with out tactics is the slowest route to victory." There is a need for LCC to re- look at their present strategy to ensure that the model stays on track and sustains with adequate profit margin, with out indulging in fare war, and without coming on the contrails of full service model carriers. What is the way forward?

LCC- New Thrust Areas

Low-cost carriers pose a threat to traditional 'full service' airlines,since the high-cost structure of full-service carriers prevents them from competing effectively on price. Notwithstanding, LCC are to focus on new thrust areas to stay ahead.

There is a need to find a path that the low cost carriers can follow as it seeks out new markets, ways and means to attract and maintain its customers and how to compete with the market rivals. Sustained excellent performance records of LCC like SouthWest and JetBlue in US and Ryanair and EasyJet in the UK are good case studies that will help our existing LCC and the potential low cost carriers to carry out a transformational intervention. Some of the key issues that merit attention are:

Differential Strategy- Uniqueness, Features, Appearance and Perceived Customer Value are some of the factors that help to provide distinguishable marks for which the customer is willing to pay a premium. You have to be something different from your competitors. To gain such a differential strategy, you need to know the market you want to serve, the market segments, customer type, nature of customers, customer needs and their choice and the geographical area and the product niche. You have to constantly work through the customers by way of customer surveys, close scrutiny of customer preferences, their behaviour patterns and the regional characteristics including the cultural bias. Capture these very features and introduce something new and something very different. Though it can be copied by your competitor, but you have the advantage of introducing it for the first time and thereby making it easy for you to market it, and also to bring about quick changes at frequent intervals. Pleasing, unique interiors and appearance, seating configuration, leather upholstery, soft skills of cabin crew and above all, on time performance are some of the features that can differentiate you from your competitors. You may not need to add any tangible value to the product as long as the customer perceives that the product is superior. It is the perception that matters. Perception value is more important than actual value.

Competitive Strategy- It means that a low cost model is doing something different, deliberately choosing a different set of activities than its competitors. Full service carriers serve a large number of destinations on a hub-and-spoke method, clustering around peak hours at hub airports which require coordination of schedules, interlining, extensive screening of baggage etc. Where as, low cost operators should stay away from large, congested airports and offer only short point-to-point services between mid size cities and only to secondary airports in large cities, strategy being- keep fares low and frequency high- so that you are able to attract people who might otherwise travel by car or train.

While introducing hopping flights to attract rail/road users, it should be ensured that they do not waste their time in procedural aspects, instead, it should be straight in and they should gain an impression that air travel really saves time, it is comfortable and convenient, and at an affordable cost.

Popularise the secondary airport/low cost airports concept. They are to be different to achieve the quick turn around time with simplified security/check in procedures; one can even scrutinise the credentials of frequent fliers and high value travelers, and issue them with laminated boarding pass/e-gate facility to reduce the dwell time.

Airport operators and aviation security bureau should be able to come forward with less stringent and quicker ways to screen and even provide an exclusive area for low cost operators. Passengers can be indoctrinated to carry less baggage or just hand baggage only so as to reduce the turn around time. Passengers with only hand baggage can even be encouraged with some incentives so that the practice gets developed. Focus on high frequency and least dwelling time.

Selection of aircraft is crucial. The tendency to go in for the easily available old aircraft or cheaper lease terms should be avoided as it can be costly in due course as they would be less fuel efficient and costly on maintenance, training of air and ground crew. Use of standard aircraft, say a fleet of Air Bus 320 or B737-800 contribute to lowering the operating costs and therefore selection of aircraft is key to the whole issue. In 2006, the cost per available seat mile for full services carrier US Airways was 12.5 cents and 9.6 cents for Continental, where as, it was 7.0 cents for South West and 6.2 cents for Jet Blue, the low cost operators.

Operational Effectiveness- It means performing better than your competitors by keeping the operating cost lower than your competitors by performing the same activities in different ways. A strategic management approach of establishing a corporate Vision, Mission, Objectives, strategic alternatives, implementation of the set out strategies and periodical evaluation, and corrective action wherever necessary will be an effective tool to achieve the operational effectiveness. Vision or Mission says it all. Virgin Atlantic's Mission, "to grow a profitable airline, that people love to fly and where people love to work" has indeed helped the airline to market it very well.

Awareness Build Up- Most of the traveling public, particularly the first time fliers, at least 10 to 20% at any given time are ignorant of the difference between conventional full services airlines except that they are induced by the fare driving advertisements. Best fare does not always explain consumer choice in air transportation. There is a segmentation here one segment is leisure passengers and the other business passengers. While price may rank high in the case of leisure passengers where elasticity of demand is high, when it comes to business travel, demand level is inelastic and depends mostly on convenient schedule than fare. Another factor is passengers may end up paying a higher fare than they would probably because they use a medium to make their reservation that does not have an account to the lowest possible fare. Use of inter net and on-line booking makes it cheaper than booking through a travel agent or direct booking over a telephone. One may choose an airline due to pre-conceived perception of preferred ground services, or safety record or on time performance, or cultural preferences, and therefore, understanding the consumer behaviour is extremely important in establishing a competitive position.

Low Cost Leadership- A low cost leader has two options one, to provide a service at lower fare than its competitors and thereby gaining a large share of market place. In this, the low cost leader is undercutting the competition. If the buyer is cost sensitive, then the buyer will choose the low cost leader. The second option for the low cost leader is to offer the same fares as that of the competitors. In this case, the leader reaps the benefit of a greater profit margin. The leader by virtue of being the leader has been able to keep the cost lower than rivals, and as the costs are lower, the profit is better than rival. However, to be a leader, you should be able to provide customers with a workable schedule as well. In a price sensitive environment, the customers should also know who offers the lowest fare and convenient schedules and then choice will be the leader.

When buyers are price sensitive, low cost leadership position will have a very strong competitive position in the market. The aim is to contain the cost to the lowest, relative to industry rivals and in course to create a sustainable cost advantage over the competitor. Remember, cost is not equal to price. So, one has to gain cost advantage in a manner that is very difficult for the rival carriers to copy. Cost advantage is based totally on the relative ease or difficulty it takes to imitate the product and this is the key to sustainability of competitive edge.

Core Competence – What is your core competence, how to identify them and how to develop them are some of the questions that you need to answer. May be it is better for you to try and identify a competency or set of competencies that helped you to do well in your business, and then it would be easy to exploit them.. We need to recognise that the competitive advantage and core competencies come from within the airline itself. It must also be borne in mind that it is not easy to identify or figure out what exactly is your core competence. It may be skills, process, and corporate identity, combination of skills and knowledge that is embedded in the organisation; because it exists you are able to reach new heights. This helps to initiate value creating activities that can make unique value added contributions to the business. The aim is that your airline should be better at the competencies than all others or at least the vast majority of your competitors. Rareness of the competency makes it difficult for your competitors to imitate you. Competency to meet your customer needs is the key. Being better than your competitor is not enough to have a sustainable competitive advantage, but the reality is to fit and focus is necessary. What make an airline in one market, may not work in another market. Your success in one market segment does not guarantee success in another market segment. It is important for you to focus on your core activities in which you want to excel. This is the reason why the introduction of 'airline with in an airline' tried by some of the major traditional airlines did not succeed. Continental tried to copy South West unsuccessfully, similarly, many others. So copying is not easy.

When the activities are incompatible, it can become confusing to customer if another type of service or value is offered, when the brand is known for one type of service or value. The new image can undermine the reputation of the parent airline (Air India Vs Air India Express). A new activity requires different skills, different equipment, management systems/style and employee attitudes. Use of same travel agents, lack of training on the part of employees while switching from legacy carrier to low cost or even after training, inertia or mind set can affect the brand image. Lack of internal coordination and control can also result out of change of roles.

Sustainability Strategy

- Optimize operating efficiency of facilities
- Pursue cost cutting measures through procedural control
- Avoid or minimize marginal cost activities
- Maintain a close watch on the cost drivers
- Continuous innovation in areas where cost cutting can be achieved. Even the crew uniforms can be made simpler and cheaper. Introduce something to go by the regional accent and smart casuals are optional choices.
- Adaptability to market condition, where inventory can be adjusted rapidly, keeping demand and supply equation
- Quick and efficient on time performance- flexibility to respond quickly and pro-actively to changing needs of the customers
- Out source as much as possible in areas such as finance& accounting, back office functions, reservation process, baggage screening, and resort to e-marketing, snap express reporting and build committed employees.
- Seating and all other services based on what the customers can afford to pay, what ever strategy that can boost the first time travelers' choice and cut down the costs to ensure no seat goes unoccupied and that no space that goes vacant, it should be filled with additional seats.
- Improved revenue management system- some of the airlines have a complex fare structure. Make it user friendly and more manageable, and keep the unfamiliar first time travelers in mind.
- Function exactly as air taxi operations with e-commerce strategy.

Follow what Mr. Roller King, the founder of South West Airline, the most successful low cost carrier said "if you get your passenger to their destination when they want to get there, on time, at the lowest possible fares, and make damn sure that they have a good time doing it, people will fly your airline"

It is important in the context of a developing country like India to keep two posits in mind. The first, no air passenger wishes to return to the days of state dominated control in the aviation airline sector. Second, anti competition behavior on the part of the private players is going to defeat the purpose of deregulation. These two posits are often at conflict with each other. While a remedy against anti competitive behavior is necessary, it must be balanced with the concern to keep the private sector alive and thriving. Price appears to be most important factor for the consumer followed by service provided and flight schedules. So, the astounding reason for air passengers not favouring state dominated control is the price-effective outcome of the open-sky policy of deregulation. Other reasons attributable for consumer's preference over deregulation is the constructive mode of service and schedule-friendly approach.

Further, the regulatory structure inhibits competition in many ways. It can prevent or deter entry, constrain capacity, and limit the potential for airlines to win market share. A problem in assessing regulatory impacts is the structure of aviation markets. The problem arising out of the structure is again attributable to the anti-competitive or collusive behaviour of private players defeating the very purpose of deregulation. However, things have not really been going the consumers' way. The market opening for private players has not brought the desirable stage for the aviation sector.

Factors Defeating The Purpose Of Deregulation:

At the dawn of deregulation, there was a lot of enthusiasm and optimism that accompanied the entry of private operators in the Indian domestic market. However, the private operators could not sustain their operations for long and soon turned sick. There are several factors that contributed towards such a down-turn. Setting up an airline operation required substantial capital investment, and so the number of aircrafts that each of these operators had was limited. Further, the operators had to adhere to the route categorization laid down by the government, or in other words they were forced to ply in certain economically unviable routes. All these factors made the operations uneconomical.
The private operators could not afford to maintain separate aircrafts for flights on category II/III routes. Overall, the private airlines failed to provide a regime of regular, stable and professionally run air transport services in the country. They had also been involved in various disputes relating to lease agreements, payment of dues, lack of schedule integrity, frequent shifting of routes and operations, etc. Gradually, most of the airlines turned sick.

Thus despite liberalization and deregulation of the civil aviation sector, the domestic air transport sector had not grown on expected lines. The private airlines, which had to close down, blamed their sickness on reasons such as :

- Lack of transparent and consistent government policy
- Route Dispersal Guidelines – Operations on uneconomic routes
- High Cost of Aviation Turbine Fuel
- Inland Air Travel tax and Income Tax on leasing of aircraft
- High rates of airport charges
- Lack of adequate airport facilities and limited watch hour problem at minor airports
- Uneconomic fares

All these reasons contributed to the downfall of private airlines. Therefore, the very purpose of deregulation was defeated due to such a downfall. Another important factor was the decline in airfares which triggered losses for the airline companies. The losses worsened the existing deterioration of the private airline companies. Moreover, the rising fuel costs also deteriorated the situation.

Further, there was gradual decrease in the number of passengers, both business and leisure, contributing to the losses suffered by these companies. Due to all these factors, the airline companies faced an inability to meet breakeven and continued to suffer losses. The initial freedom resulting from deregulation, led to competition in the market place following new entry in the business leading to lowering of prices in the markets that put further pressures on the bottom lines of the airlines companies' balance sheets. Subsequently, the focus shifted on economizing the operations so as to reduce the costs and arrest the price increases so as to boost the margins and keep the airlines in business.

As a measure to improve their situation, the airlines brought about an uncontrolled rise in fares with a new break up of the total fare.

- Earlier, Basic Fare = 999 + Tax = 225 , Total = Rs. 1224
- Now, Basic Fare = 99 + Tax = 3250 , Total = Rs. 3349

The new break up of airfare with a deceitful increase in the tax rate is one of the few measures taken up by the airlines to improve its profits and meet breakeven. The amount charged as tax is majorly pocketed by the airlines and only a small amount is actually the tax collected by the government. The break up of the tax includes fuel surcharge, service charge, congestion charge amongst others and these are adjusted according to the rising input costs. This practice had knocked down the aim of deregulation to a great extent but the players in the industry defend themselves by saying that they have no other option if they have to survive. The era of post liberalization has observed the airline industry undergoing constant revision of strategies for growth and to encounter competition. One of the key factors driving this industry is survival since prosperity in this sector is only secondary.

Therefore, the general law of supply and demand has not been applicable to the civil aviation sector, according to which lower prices lead to increase in demand resulting in increasing revenues. Lower fares have led to an increase in demand for seats but at the same time there was an increase in input costs because of which industry did not experience increasing profits. Increasing losses, inability to meet breakeven, constantly rising ATF (Aviation Turbine Fuel), poor infrastructure have forced the airline companies to come up with various strategies to cope up with the situation along with the driving force of survival. One such solution arising as part of such a deliberate action by the airline companies was strategic alliances amongst airlines. This involved alliances between arch rivals to minimise costs and maximise profits, who agreed on various terms and levels of air transport service carried out by alliance agreements.

Market Structure of Air Transportation sector

Indian Air transport sector tarnished from state monopolism to competitive market. While moving from state monopolism it attained Oligopoly market structure. Oligopoly means existence of few sellers. The main characters of Oligopoly are existence of few sellers, product homogeneity with apparent differentiation and high cross elasticity. Cartel formation is major competition issue faced by new entrants in to this market. Cartel formation and high cross elasticity both pressurises the small players to fix low prise and decrease their profitability. At the same time some government policies favours the big players. As there are few companies are existing in Indian Air transportation sector it defiantly comes under Oligopoly market. Two are three companies are dominating the market, as already they are existing from a long period their fixed costs reached lower level, and they can fix lower price. As we discussed above certain rules in our competition law are favourable to the big players and causing further dominant position. Let us discuss the various entry barriers which are having adverse affect on the competition in the Air Transportation market.

Competition Issues in Aviation

Various Entry Barriers in the air transportation sector

Route Dispersal guidelines

The route dispersal guidelines are prescribed by ministry of civil aviation. Accordingly the routes are categorised into category I, Category II, Category IIA, and Category III[9].

- According to guidelines the operator shall deploy at least 10% in category II of the capacity deployed on Category I Routes.
- The operator shall deploy at least 10% in Category IIA of the capacity deployed in Category II.
- The Operator will deploy at least 35% in category III routes of the capacity deployed in Category I routes.

Economic impact

The above guidelines force the new entrants to run the flights in the low profitability routes. This causes the losses in the air transportation company at the initial stage itself. Due to high cost of the entry the new player may not in a position to recover the investment due to the mounting losses due to these route dispersal guidelines. The new entrant may not be interested in operating in these routes but through operation of law they are forced to operate the same.

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[9]Route Dispersal Guidelines, Ministry of Civil Aviation, F.No.AV.18011/1/2016-DT (Aug, 9th 2016) http://civilaviation.gov.in/sites/default/files/order.pdf

Minimum Equity and Fleet Requirements for starting air Transportation Company

As per section 3 of Civil Aviation Requirements a scheduled operator permit can be granted if the following conditions are satisfied[10].

- The applicant must be citizen of India
- In case of company or body corporate then they shall have principal place of business in India.
- Its chairman and at least two-third of its directors are citizens of India and substantial control of the company shall be with the Indian nationals.

Paid up Capital for new applicants for whom the applicant shall submit a certificate from the banker or chartered accountant to confirm the paid up capital of the company:

(i) Airlines operating with aircraft with takeoff mass equal to or exceeding 40,000 kg.

a) Upto 5 aircraft – Rs 50 crores

b) For each addition of up to five aircraft, additional equity investment of Rs 20 crores will be required.

(ii) Airlines operating with aircraft with takeoff mass not exceeding 40,000 kg.

a) Upto 5 aircraft – Rs 20 crores

b) For each addition of up to five aircraft, additional equity investment of Rs 10 crores will be required.

Generally while starting companies the air transportation companies will take the flights on lease basis. The lease may be either dry lease of wet lease, while going for lease there is a possibility that the lessor may behave favourably towards the existing dominant players in the market. This would result in undue advantage to the existing players in the market.

Availability of slots based on the existing practice of "grandfathering"

At present the slot allotment in India is based on the guidelines prescribed by IATA[11]. According to this rule while allotting the slot priority shall be given to existing user. This rule is based on the historical precedent. If existing user used 80% of his allotted slot then priority shall be given to the existing entity only. Only 50% of total slots are available to new entrants. This may create entry barriers to new comers. As the prime slot may be available to only existing players. This rule is called as grandfathering. The IATA guidelines provides that[12] when developing the guidelines for slot allocation plan. The

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[10] Civil Aviation Requirements Series "C" Part II, http://dgca.nic.in/rules/car-ind.htm

[11] Report of the Committee Constituted for the Examination of Recommendations made in the Study Report on Competitive Framework of Civil Aviation Sector India, Ministry of Civil Aviation (June, 2012), http://civilaviation.gov.in/sites/default/files/moca_001870_0.pdf

[12] Worldwide Slot Guidelines Effective from Jan, 1st, 2017, International Air Transport Association, 8th Edition https://www.iata.org/policy/slots/Documents/wsg-8-english.pdf

first priority shall be given the historical slots. Once historical slots completed then the authorities shall give importance to application made by new entrants. 50% of the slot pool shall be allotted to the new entrants unless their capacity is less than the available slots.

Economic Impact and Solution

The existing player can hold the slots allotted to them. The slot allotted to the existing holder automatically transferred when it is taken over by another players. This creates advantage to the new player who is acquiring the existing entity over other new players. This policy shall be reviewed by the government, rather than giving the slot allotment only on the historical precedent, while considering the slot allotment, the player who is having experience of specified period (for Example 5 years) can be allotted prime slot period provided his performance from the incorporation is satisfactory in terms of customers satisfaction.

Cartelization

> *People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices.*
>
> – Adam Smith

'Cartelisation' is a process where enterprises collude to fix prices, limit or control production, share the market or customers, or indulge in collusive bidding. Cartels usually operate in secrecy due to which these are hard to detect, or successfully, investigate and prosecute and because of this competition laws across the globe reserve their most severe treatment for cartels. Almost all the sectors, including the aviation sector are prone to Cartelisation.

Cartelization is when enterprises collude to fix prices, indulge in bid rigging, or share customers. Cartels have the capacity to adversely affect consumer welfare and the economy of a country. The most common activity undertaken by cartels is price-fixing which eventually results into artificial increase in prices.

Chapter IV of the Constitution directs the State policy in matter of concentration of wealth, welfare of consumers' vis-à-vis Fundamental Rights (under chapter III). It is in pursuance of this that the State enacted the Competition Act, 2002. But critics opine that this Act is riddled with loopholes that might condone hard-core cartels and predatory pricing. Section 19 of the Competition Act, 2002 provides that Competition Commission of India may inquire into any alleged cartel (anti-competitive agreement) on receipt of any information from any person, consumer or their association or trade associate.

The aviation industry in India has undergone a sea change from the times when it was the domain of the public sector. Today, the aviation sector is predominantly about the oligopolistic competition among privately owned firms vying for maximum profits.

In the recent years, the privately owned firms decided to reduce fares so as to increase the catchment area and include the common man in their customer base. This cutthroat competition forced the companies to decrease their fares to such an extent that they ended up incurring losses.

In such a scenario it is but obvious that the airline companies would devise plans to pull themselves out of this rut, and since the lack of innovative ideas plague the aviation industry, the firms would come out with methods which have been tried and tested through the course of history. Cartelization is one such method which the Indian private airlines seem to be following. Several economic studies and legal decisions of antitrust authorities have found that the median price increase achieved by cartels in the last 200 years is around 25%.

The result of this cartelization is the increase in air fares among all the privately owned airlines along with other measures, with "route rationalization" being one of them. This increase in air fares across the board has been a lot in the news lately with Jet airways and Kingfisher being accused of forming a cartel and increasing air fares which both the firms have vehemently denied blaming losses being incurred by them due to market forces and also the rise in price of Aviation Turbine Fuel (ATF), thus justifying the increase in fares.

According to Section 3 of Competition Act, 2002, the privately owned airline firms have violated the law if they have formed a cartel and involved themselves in a restrictive trade practice.

Taxation Policy

The beginning of this decade witnessed the boom of no-frills carriers which gave a new thrust to the privatization of aviation sector in the country. At this junction the high prices of Aviation Turbine Fuel (ATF) has become a thorny issue as ATF currently constitutes about 30-45% of the total operating costs. The same has especially become a burning issue for this budget with the rise of cut-throat competition with frequent entries of new players. The same not only attracts accelerating custom and excise duties but varying sales tax at the level of state government. This is because aviation turbine fuel is not yet notified as a 'declared good' and hence does not attract the uniform VAT rate of 4%.

ATF prices in India are 60-100 per cent higher than in other countries. This means that the domestic players are even losing out to international competition. The effect on aviation sector has certain indirect effects as well. It affects the tourism industry which witnessed a boom with the entry of private air carriers. It also discourages the carriers to fly in states with high sales tax. Ultimately it has a negative multiplier effect on the employment and the economy as such.

Taxation of civil aviation

"There is cut-throat competition in this sector and airlines are losing money, mainly because of competition and high taxes."[13]

The Central Government has the power to issue Orders regarding rates, tariffs, and the like under section 5 of the Aircraft Act, 1934 and Rules 134, 13of the Aircraft Rules,

[13] Mr. Praful Patel, Hon'ble Minister for Civil Aviation, Government of India at the First National Civil Aviation Conference, New Delhi, January 18. 2008.

1935. The various taxes being imposed in the aviation sector include Service Tax, Luxury Tax, transport taxes, and excise duty.

The prominent amongst these is the state sales tax levied on Aviation Turbine Fuel (**ATF**) which differs from state to state and ranges from 4 to 34 per cent, because the ATF does not fall under the GST purview but still the government is imposing the taxes under the old sales tax regime which is in turn not uniform in the states[14]. ATF comprises 35-40 per cent of domestic airlines' total operating costs. There is a demand to notify ATF as a declared good so that it attracts a uniform 4% duty all over the country as under section 15 of the Sales Tax Act, 1956. The current ATF prices are 60% higher than the average ATF prices globally. Besides, there is also a levy of 8% excise duty on ATF.

A recent circular issued by the finance ministry to airlines operating international flights out of India has called for a levy of 12.36% service tax on the fuel surcharge on every business class and first class ticket. Such a surcharge was previously not under the ambit of service tax. Non-Economy class international journey has been subjected to service tax vide the Finance Act 1994 as amended vide Finance Act 2006 with effect from 1st May 2006. It must be noted that fuel surcharge is levied at the same rate irrespective of the distance covered by the air journey. Hence, if a fight travels from Bombay to Goa or Bombay to Srinagar the fuel surcharge is levied at the same rate.

Due to the high tax rate there have been instances of airline operators attempting to evade tax; Lufthansa and British Airways are two popular illustrations. Consumers have also filed cases against the hike in airfare due to taxes, surcharge, transaction fees and congestion fees which are prima facie irrational.

Rationalization of taxes, particularly state sales tax, would encourage more airlines to fly into a state, leading to creation of aviation as well as tourism infrastructure that would in turn create jobs and income and have a multiplier effect.

Code Sharing

Code sharing involves one airline advertising and selling the services of another airline as its own and the transportation of passengers and cargo on an airline other than the one identified in the travel documents. The carrier performing the flight is usually referred to as the operating carrier while the other airline is typically identified as the marketing or contracting carrier. Code-Share agreements enable airlines to increase their traffic and revenues thereby profits, network size, service frequency, offering more destinations through its frequent flyer programmes and coordination of operations.

In order to identify the proper defendant claim arising from a code-shared flight, the Guadalajara Convention, which was adopted in 1961, applies to which India is a party. It ensures that a carrier performing carriage without having entered into a contract with the passenger will be liable according to the Warsaw Convention as modified by the Guadalajara Convention. This convention has formally introduced the distinction

[14] Here we may observe that the taxation policy may create concentration of air traffic in a particular region due to favourable taxation in that region, causing regional imbalances.

between a contracting and an actual carrier. As per this convention, both carriers will be jointly liable and the plaintiff is released from the difficulty in proving which carrier caused the damage which could be due to lost baggage, delay in the flight taking off, diversion of the flight due to unavoidable circumstances, passengers been offloaded due to overbooking .etc. especially in congested airports. Jet Airways already has a code-share agreement with Brussels Airlines in order to give its passengers wider destinations in Europe to choose from.

Thus the role of the Guadalajara Convention will increase and become more important with a steadily growing number of flights under Code-Sharing agreements.

Frequent Flyer Programs and Code Sharing Alliances: Competition Concerns:

There are certain factors intrinsic to airline industry that are anti-competitive such as 'Frequent Flyer Programs' ("FFP's") operated by various airlines that is a form of unfair pricing practice and can have adverse effect on competition. Also, the airlines alliances in the industry that inter alia include 'Code Sharing Agreements' tend to restrain competition in the market. The object of the paper is to study nature and impact of Code Sharing Alliances and FFP's on competition.In India, many airlines such as Indian Airlines, Kingfisher, and Jet Airways operate FFP's for its customers and provides various benefits in relation to same. FFP's are basically loyalty inducing programs offered by airlines which rewards customers with free travel on the basis of build up miles and gained points on each travel by that airline. Through these FFP's, the airline tends to enhance the value of subsequent flights on its airline by increasing opportunity for free travel, once the customer flies on FFP.

Such rewarding tends to induce future loyalty among customers and not only strengthens airline's market position, but also tends to fetter competition in market by making it difficult for new entrants to enter market and expand. Such loyalty inducing pricing and rebates programs become abusive when they lead to foreclosure effects. Section 4 of the Competition Act, 2002 ("the Act") prohibits abuse of such dominant position by an enterprise by way of imposition of unfair or discriminatory price in provision of services or by limiting or restricting market. Such loyalty programs also prevent customers from accruing most advantageous offer at a given time thereby denying market access. Further, airlines by way of FFP's raise the switching costs between various airlines –they make traveller keen to continue its services such that, if they switch to another they would not be able to gain points and thus free travel. Switching costs act as barrier for entrants to gain market share and are detrimental to competition in market. Also, the inducement caused by way of FFP to customer by the airline has the effect of stipulation to purchase exclusively from that airline and is related to the law prohibiting exclusive purchasing agreements. FFP's are basically targeted for business class travellers who have less price elasticity demand and therefore treat customers in discriminatory manner over other leisure travellers. Such discriminatory pricing is prohibited under the Act.

In the air industry, alliances constitute a framework for cooperation between airlines such as Code Sharing Alliances that allows one airline to sell seats under its own name and code on another airline's flight. However when two main competitors in the market enter into such code share agreement on overlapping networks, it dampens competition which may also lead to price collusion and rise by the two airlines. For example in 2006, Air Deccan signed an alliance with Jet Airways for code sharing and pooling engineering resources. This Jet-Sahara-Air Deccan alliance can have severe impact on competition as both of them have a very heavy domestic presence and overlapping networks with a combined market share of over 50 per cent, which may lead to monopoly on some routes. Further, if Computer Reservation System displays each alliance partner's flight under each partner codes, independents or entrants shall have more difficulty in getting their flights listed prominently. Also, considering the issue that customers may be unaware of code sharing when purchasing ticket and may find themselves on carrier which they consider to offer low quality of service and would not have been willing to choose, it can be said that code sharing operations act as detrimental to fundamental issue of transparency in consumer information and interests.

To conclude, competition in airline industry could be preserved and enhanced through, inter alia, close and careful review of FFP's and such alliances and careful use of remedies to offset such anti-competitive effects. Remedies such as, requiring incumbent airlines to grant new entrants access to their FFP and control on merging airlines to keep their FFP separate and in case of code share alliances, to assess such alliances on the basis of increase in fares and elimination of competition on the basis of market power or network effects, that should be discouraged and also pro competitive effects of economic efficiencies that can outweigh potential competitive harm.

Market Concentration in the Aviation Industry

One of the important method while assessing the market concentration is through HHI (The Herfindahl-Hirschman Index), which enables the authorities to assess the concentration in the market so that the authorities can take the remedial measures accordingly.

The Herfindahl-Hirschman Index (HHI) is the technique which is used to identify the market concentration. The market concentration helps us in identifying how market is moving in a particular period. If the HHI is moving towards 10000 point it indicates that the market is highly concentrated and the monopoly is there in the market. If the HHI is moving towards '0' it indicates there is a perfect competition in the market. As per the anti-trust law guidelines if HHI shows 2000 points or above there is a possibility that the market may move towards monopoly. This situation has to be controlled by the government under the competition law or anti-trust law in US

How HHI is calculated?

For calculating the HHI the market share of a particular player is taken and then the market concentration is identified. As per section 19 of the competition Act, 2002 when the adjudicating authority conducts the enquiry into the anti-competitive practices or abuse of dominant position, the adjudicating authority shall take into consideration the market share of the player then accordingly they shall determine whether particular player is abuse of dominant position or entered into any contract which has appreciable adverse effect on the competition.

Example: in a particular sector Firm A is Having 30% market share, Firm B is having 20%, Firm C is Having 25% and Firm D is having 25% market share respectively. Then

HHI is calculated as follows

$$HHI = 30^2+20^2+25^2+25^2 = 900+400+625+625$$

$$HHI = 2550$$

The HHI of above industry is 2550, which shows that at present situation the market is in the oligopoly market and there is a possibility that the market may towards the monopoly if the market concentration continues to be the same. The HHI helps us in estimating the market concentration in the industry, which in turn helps us in ascertaining the competition issues in particular industry.

HHI Calculation in Air Transportation sector

Year	HHI
1980-1986	10000
1987-1991	10000
1992-1995	8192.02
1996-2002	3561.367
2003-2011	1502.683
2011-2016	2075.371

The above table shows us that the concentration in the aviation industry is slowly increasing though not at rapid speed. It is time for the competition authorities to take positive initiation so that we can maintain the healthy competition in the aviation sector, which is main aim of the competition policy.

MODULE V

BUSINESS OPPORTUNITES IN AVIATION SECTOR: RECENT DEVELOPMENTS

The Aviation Industry is facing the challenges on account of the global economic recession. The industry has undergone paradigm shift over a period of time in the Asia Pacific Region including India. Indian Aviation has recorded over 23% growth just prior to the economic meltdown. There is no doubt that the present setback is only a pro-tempore phase and there is ample evidence that industry is regaining its momentum and bouncing back at a higher rate where it was left. Whenever there is a slight demonstrated decline in the air traffic and loss of revenue, unfortunately the first casualty is training budget and when the industry bounce backs there is acute shortage of professionals and a visible gap between the trained manpower and the required manpower. Here again unfortunately there is no worthwhile aviation education institutions/ universities who could meet the projected deficiencies of the industry. The industry by itself cannot meet their own training requirement due to financial constraints and displace priorities. Per se, it is for the leaning universities/ educational institutions to come to rescue of the industry.

In India, so far, much of the Aviation related programmes were confined to IATA Travel and Tourism, and hardly any courses covering the core areas of Aviation Management. Airline sectors is in need of Airline Managers, Business Development Managers, Marketing Managers, Safety and Security Managers, Operations Managers, Air Transport Managers, Human Relations Managers, Finance Managers, Environmentalists etc. similarly Airport and Aerospace sectors, we need hundreds of such Professional Managers to meet the day to day Managerial Activities. Air Transport Industry is one of the unique business entity providing direct, indirect and induced employment opportunities. While every direct employment creates an additional thirteen indirect employment induces another nearly 100 in the induced sector thereby providing the largest employment opportunity in the global aviation market.

Projected Aviation growth in India, Asia Pacific and Middle East Region opens up equally challenging opportunities for the lawyers who were hitherto ignorant of the immense job opportunities in the aviation sector where not in a position to acquire a specialization in the aviation law. With the rapid expansion of airport, airline, aerospace sector, the global aviation market has opened up plethora of aviation opportunities for legal professionals. Aviation Law which essentially related to the international law and specific aspects related to the aviation industry is generally identified as aviation law. It is a fact that barely two or three universities across the globe the much desired qualification in aviation law. Legal Professionals with specialization in air law would easily be able to enter into the much coveted aviation industry in the managerial areas as well as in the legal departments. Legal professionals with specializing in aviation law would be in a much better position to enter into legal consultancy, legal advising, litigation, for drafting contracts, negotiating bilateral and multilateral treaties, handling of traffic rights and other and regulatory functions. Now hundreds of job vacancies are also waiting for air law experts because of Globalization, Liberalization and Privatization of aviation industry in India and abroad.

CHOOSING BETWEEN BILATERALISM AND MULTILATERALISM: APPROACHES FOR IMPROVING MARKET ACCESS IN THE INDIAN CIVIL AVIATION INDUSTRY

The air transport industry in India is not in its nascent stage, though it is in its nascent stage of liberalization. India is pursuing phased liberalization as recommended by the Naresh Chandra Committee Report and is in the second phase, negotiating for more liberal bilateral agreements and vying for full access to wider markets by entering into regional and multilateral agreements with countries with similar liberalization agendas. However, there have been major limitations, which have created distaste for the newer airline companies from entering the Indian Civil Aviation industry. According to recent reports, newer airlines, which choose to fly out of the major hubs of Delhi and Mumbai, have to park their aircraft overnight at nearby airports like Lucknow or Pune, leading to higher costs and misalignment with the peak traffic. Blame in this regard, has been attributed to the bilateral system of negotiations for market access. This paper deals with reconciling the conflict between the bilateral and multilateral approaches for entering the Indian civil aviation regime in the light of the air transport annex of the General Agreement on Trade in Services.

In the present contextual matrix, air traffic rights of scheduled air services are negotiated and exchanged on a strict quid pro quo basis under the framework of the Convention on International Civil Aviation, notwithstanding the presence of a multilateral framework under the Convention. It appears that the model of bilateralism has so far been a more widely and successfully used tool of gaining market access through the exchange of traffic rights vis-à-vis the multilateral avenues available for the same under the Chicago Convention framework. Taking this as the core argument, the paper shall argue upon the outcome of providing trading access rights through the GATS route in the form of a multilateral convention and its effects upon India.
However, at this stage the factors affecting market access should be taken into account. A nation while choosing between a bilateral model (bilateral air traffic agreement) and multilateral model (commitment to be made under the GATS Annex on Air Transport Services) will have to consider certain shortcomings of both of these, in the form of onerous cabotage restrictions, debilitating ownership and control clauses, debilitating state aid programs, vexatious slot allocations; and environmental restrictions, which may restrict market access. Elaborating upon these, the paper shall weigh the adequacy of both the models and establish as to which one be the best one for India.

In conclusion, it should be noted that acceding to GATS-specific commitments relating to a market access regime now might not seem such a distant dream, but it is still a difficult one to realize because India shows reluctance to end its protection of flag carriers. It seeks to encourage and nurture the growth of private enterprise, but not at the cost of allowing its flag carriers to fall to stiff competition from India and road. Further, India's aviation market is hobbled by third-world realities such as the dismal state of its infrastructure, policy rigidities, and protectionist tendencies towards its flag carriers. The few bold steps taken in the past to increase market access will prove to be inconsequential if India does not adequately address its infrastructural and policy rigidities.

Therefore, unless India confronts these realities soon, it will also be difficult for it to benefit from entering into liberal, bilateral or multilateral arrangements with other nations.

AVIATION INSURANCE: HAVE A SAFE FLIGHT

Insurance in the aviation sector has become an area of much review particularly when the magnitude of the problem was demonstrated in the 9/11 attacks. The insurers covering those aircrafts faced the prospect of claims for loss of hulls, liability for passengers and crew, and last but not the least, liability for on-the-ground third-party fatalities. Thus the risk and liability may rise up to mammoth proportion. Therefore it is obvious that the general principles of insurance laws in rating of premiums are insufficient in the case of the aviation sector because of the presence of high risk and liability.

Aviation Insurance in India: Aviation insurance is a very specialized branch of insurance. This unique class of business is characterized by high risk, high values and sophisticated technology. Aviation technology has developed rapidly during the last few decades. As a result, air travel these days had grown to be significantly safer than was the case a few decades ago. Emerging complexities in finance and lese arrangements, coupled with the criticality of optimum management of finances in this capital-intensive field, lend more challengers to the Aviation Insurer than ever before. This field of insurance has turned truly global in view of its inherent nature and characteristics.

Aviation insurance policies offer a wide variety of cover ages to take care of almost every conceivable situation that may bear an adverse financial impact. The aviation portfolio encompasses cover normally availed of by airline operators which includes (1) Aircraft Hull All Risks; (2) Aircraft Liabilities; (3) Aircraft Hull War Risks; (4) Spare Risks; (5) Personal Accident Cover for Crew; and (6) Loss of Licence cover for Pilots. There also exist cost effective insurance covers that are available to agencies allied to aviation industry.

Since nationalization of General Insurance Business in India, Aviation business has been under-written by the General Insurance Corporation of India (GIC) and its four Subsidiary Companies—National insurance Co. Ltd., Calcutta, New India Assurance Co. Ltd., Bombay, Oriental Insurance Co. Ltd., New Delhi, and United India Insurance Co. Ltd., Madras. While GIC writes the aviation insurance business of Air India Ltd., Indian Airlines Ltd., Vayudoot Ltd., all the divisions of the Hindustan Aeronautics Ltd., (HAL), and the Airport Liability Cover of the Airports Authority of India (AAI), the four subsidiary companies write aviation business pertaining to all other aircraft operators and Allied Agencies including Pawan Hans Ltd., and other private operators.

GIC has insured the national flag carriers since their infancy from the time they operated with small sized fleets and has seen them through their growth and acquisition of the modern and technologically advanced fly-by-wire aircraft. During this period, GIC had gained considerable technical expertise and have a proven track record tested by time and circumstances in this class of business.

The Global Connections: Aviation is a technology that has grown by leaps and bounds during the past few decades and aircrafts today are highly sophisticated. In addition, Lease and Finance arrangements involved in procurement of aircraft have grown in complexity and bear international implications. Considering fact that aircraft operations involve heavy outlays both on capital as well as on working finance, aircraft operators justifiably demand and expect more and more from insurers. Further, with new operators having tight cash flows and critical break-even operations, insurance outlays assume even greater significance. Aviation insurance has, all through, kept pace with the changing scenario and has today emerged as a very specialized and technical branch of General Insurance.

Insurance companies have constantly strived to attain one of the prime objectives of nationalization byway of maximization of retentions. Aviation insurance, however, being a high exposure and high risk branch, increasing aircraft values and limited financial risk bearing capacities have left insurance companies with no option but to share large portions of the risks with several reinsures world wide in a large number of cases.

This process of reinsurance on a global basis also insures adequate and much needed spread of the risks and is one of the fundamental principles of insurance. Lloyd’s at London is one of the larges Aviation Reinsurance Markets. Relatively large markets also exist in France, elsewhere in the European Continent and in the USA. Terms in respect of major Aviation Operators/Agencies in India are, therefore, negotiated by the GIC and its subsidiary companies with Underwriters at London and other Aviation Insurance Markets.

The world Aviation Market has reeled from recurrent losses since 1985, despite hikes in premiums. For example, in 1994 losses touched a peak of US dollars 2.4 billion. These losses have eroded the reserves of Aviation Insurance and Reinsurance worldwide. As a result, several syndicates and companies have wither gone into liquidation or merely ceased writing aviation insurance business or merged with other entities. Underwriting capacity of aviation insurance stands considerably reduced. The aviation insurance market has hardened considerably leading to large increases in premium rates during the last few years. Selective underwriting practices with due recognition for good loss records and good growth potentials remain underwriting keys.

The aviation insurance portfolio in India has, in a manner of speaking, really taken off since 1991 with the introduction of the Government's Open Sky Policy and with the consequent liberalization in National Economic policies. The scenario today points to sustained growth of aircraft operators in India in the coming years.

GIC has on number of occasions lived up to their reputation as judicious insurers sensitive to the needs of the operators by way to timely interventions in expeditious claim settlements and their pragmatic approach in this regard. As a part its diversified activities, GIC also aids operators in their loss minimization, risk assessment and management programmes and also propagates effective client awareness. With this objective in mind, GIC has, during the recent past, organizes seminars of officials of Air India dealing with cargo claims. These efforts have been well received.

The expertise gained centers around various technical and related aspects of the acquisition, administration, development and management of healthy aviation insurance portfolio. These strengths are available to the subsidiary companies for the overall advantage of the Indian market as a whole. The Indian market has come of age and has presently developed substantial expertise in this effective management of this class of business with their tackling of complicated financial and technical issues. These features have put the Indian aviation insurance industry on the world map.

The adept and efficient handling of situations, including in adverse circumstance like operation to the Gulf Areas during war, and more recently the September 11th terrorists attack in the United States of America, flexibility and practical approach have earned GIC an enviable reputation in aviation circles. Constant interaction and prolonged exposures with the world markets have enabled sensitization of operations and transformed Indian aviation insurance operators and agencies into the Global Aviation Insurance Market. Several fruitful business relationships have been established where good faith, reliability and long-term relations remain key parameters.

The Indian aviation insurers, in their continued pursuit of customer satisfaction, have intertwined their business handling with educating the buyers of aviation insurance in India. Besides human resource development interventions, several client seminars and training sessions are extensively used to enhance awareness and take the aviation insurance product to where it belongs- the customer.

India is often said to be a at the threshold of a aviation revolution, but for the wings to fly high, and more importantly safe much needs to be done to improve the insurance of the aircraft. If once this is secured, India's aviation market, one of the fastest in the world, will be all set to take wings.

TRAIN THE PILOTS – BRAIN THE ECONOMY

With the air and the land going into the private hands, the dotted link between the two needs to be submitted to the safe carriers. The paper talks about, how the establishing of the new flying schools within India can strengthen our economy. The need of the hour is grooming sharper pilots with sound skills. Its for everyone to see the aviation boom and its expanding grasp over the expanding population of our country, this very India. It certainly calls for more pilots to enter the arena and in a way pilots who receive better training facilities. What can be more jubilant for us than the fact that we have an unexplored bracket to bank upon in a way to brain our economy. This in turn will boost the economy of our country to the core. What India needs after business schools, technical schools and law schools phase is the phase of flying schools (with world class flying facilities). Why we need them can best be explained with the fact that so many aspiring pilots leave the shore to gain advantage. If we are able to check this drain, we can certainly brain our economy with virtuous inflows .This can be supported by the strong and astounding technical hold India has on the markets of the world. Why not make ourselves self-potent even on the front of pilot training imparting hubs ? The creeping in of the LPG (model) which takes into account the liberalization, privatization and globalization spheres .We must also base ourselves on these .At present there are only two flying schools that hold the national status, i.e. IGRUA and Ragiv Gandhi Flying School.Better flight simulators need to find a place to catapult the over-growing needs and fill up the deficiency .Having a say at the (technical know-how) field will provide the best platform to the aviation industry. A green flag will be the sign for the new day.

3. Shortage of Pilots in India: What Steps We Need

Due to the era of Globalization, Liberalization and Mergers and Acquisitions of several medium and small sizes aviation companies like Sahara- Jet airways, Air Deccan and Kingfisher Airlines the size of Indian Aviation sector become multi times; simultaneously there are several other foreign players like Lufthansa, British Airways, and Singapore Airways who wants to trap the huge Indian aviation industry.

On the other hand India has only one government sponsored flying school and its tuition fee is not within the reach of every person. The entire Indian Aviation Industry is struggling from the acute shortage of Skilled and experienced pilots. With the aviation boom underway, and an estimated shortage of 450 pilots, many feel the Directorate General of Civil Aviation (DGCA) must facilitate an easier licensing process. The DGCA, however, insists that students must have maths and physics as subjects in Class 12; 200 hours of flying, including 25 hours of multi-engine flying; and strong theoretical knowledge of aircraft, aviation, and aerodynamics.

The DGCA says it is aware of the changing needs and is planning to phase out certain portions of the syllabus. “The profiles of commercial pilots are changing, and so is the business of aviation and the technology of aircraft: we are trying to update study material accordingly. But this won’t happen overnight. About the DGCA exams being the toughest to clear, well, that’s because we maintain quality.

To curb the problem of shortage of pilots, India should open at least 10 to 15 Flying schools and simultaneously also attract the foreign trained pilots, who have enough flying experience. The Government should sponsor financially to the students pursuing the Student Pilot License and Commercial Pilot License. On the patterns of United States of

America and Canada, Government should promote more and more private players in the pilot training institutions.

Indian flying schools don’t have the foreign collaborations with the countries like Russia, USA and Canada. The problem of flying of bulky size jets by Indian Pilots can only be curbed by the introduction of new multiple engine trainers.

Shortage Of Pilots: What Steps Do We Need

With aviation industry occupying a prime position in the Indian transport sector and having a crucial role to play in India's march to emerge as global economic hub, it is incumbent upon the civil aviation to play a proactive role. One of the several problems which it is facing is the acute and continuous shortage of pilots in the country which will tarnish the industry with the associated costs.

A lot of hue and cry is what can be witnessed in the Indian aviation industry. The dire need now is to take immediate steps so as to counter the crisis of shortage of pilots and hence putting a halt on the consequential problems like dwindling expansion rate of aviation market. This has to be rectified immediately because the rolling Indian economy at this crucial hour has to expand its flying base and meet the burgeoning demand of the aviation industry and its consumer palette.

Over the past several years the growth of air traffic in the Middle East and Asia and the proliferation of budget airlines in Europe and the United States have created a drastic shortage of airline pilots. With global air traffic predicted to grow by 5 to 6 per cent annually over the next two decades, the shortage will only become more acute, especially in country like India.

The situation demands urgent reforms in the sector with rising demand for pilots, cabin crew and maintenance staff . The cut throat competition which has arisen with private players coming into picture cannot afford abrupt flight cancellations and indiscriminate poaching activities. Hence, significance of this topic cannot be ignored. Though the government has taken measures to combat the shortage, there is a need to go beyond the conventional measures and reform the procedural and substantive laws in place.

- Ameliorate Infrastructure- The Government should implement the recommendations of M.K. Kaw Committee report on reorganising the DGCA. The report had favoured setting up a central air university, State air universities, a DGCA training academy, and better supervision over flying clubs. The DGCA be given a sufficient budget and administrative and financial autonomy. The flying clubs in existence need to be open to privatisation at a faster pace. The fresh talents from the flying clubs have to be targeted upon coupled with restructuring the 17 defunct flying schools in the country levelling it to the international standards. The mushrooming private flying schools have to be given proper assistance and lucrative tax concessions on buying of aircraft, simulators, land, aviation turbine fuel etc. The Civil Aviation Requriements relating to infrastructure, procedures and manpower for grant of approval for training activities have to be relaxed..

•Reorganising Training- The primary need is to re-think pilot training and qualification to further improve safety and increase training capacity. The influx from the instituites have to be increased. The training is an expensive proposition. On the lines of other central universitites government should offer proper subsidies so as to attract the students and provide incentive to newer training institutes. The DGCA office regualtions for selection and training which are on lines of Sec 7 of the Civil Aviation Act, 1937 have to be eased. The examination procedure set is tough in comaprison to foreign universities. Examination intervals, number of examinations, high percentage have given rise to backlogs and hence the passing percentage is shockingly low. India lacks adequate number of training aircrafts owing to strict norms in the EXIM policy and high excise duties. Also, Flight Duty Time Limitations(FDTL) for trainee pilots needs to be increased from 6 to 8 hours. IATA proposition of providing a multi-crew pilot licensing (MPL) training which would reduce cost and aslo allow trainees to put in less hours of flying and more in a simulator can prove to be of great help

•Other Measures- The New FDTL Rules issued by DGCA, increasing the pilot rest period from eight to ten hours and other norms are worsening an already acute pilot shortage. The Government may consider the implementation of a transparent regulatory structure, which could reduce uncertainties, ensure a level playing field and improve the quality of services taking into account the interest of consumers. Instead of direct intervention, the Government should act as a facilitator, leaving it to the private sector to take operational and management decisions. This will enable the country to achieve the desired objectives of growth, capacity-enhancement and efficiency in both the public and private sectors. Also, facilitating an easier licensing process, hike in salaries and assuring job assurance would ensure inflow of newer ones and retaining the existing ones who have lucrative offers all over the world.

EMERGING REGULATORY ISSUES AND CHALLENGES

Air Transport is one of the world's most vital resources. Its development as an industry and its technical and service achievements rank air transports as one the greatest contributors to the advancement of modern society. Since the first jet airliner flew in 1949, use of commercial aviation has grown more than seventy-five fold. This is a rate of progress unmatched by any other major form of transport. Air Transport is essential to economic progress.[1] In an increasingly global community and marketplace, air transport makes possible the rapid movement of millions of people and billions of dollars worth of goods to markets around the world. With regarding to regulations, the International aviation was highly regulated till mid 1970s. However, late seventies and early eighties, global aviation is undergoing the most dramatic changes in its history.

Since the passing of the De Regulation Act of 1978 in the USA, the international air transport is undergoing the dramatic changes in its history. Globalization, deregulation, liberal bilateral air transport agreements, international alliances, privatization of airlines and airports, and economic constraints are some of the factors challenging established management and business practices[2]. In this process each region plays variations on a common theme. In North America, air travel is the normal way of moving people, mail and increasingly, freight. In the European Union, we have liberalization, consolidation, concentration and decentralization. Civil aviation in Eastern Europe and the Former Soviet Union is being restructured and needs strengthening –while adjusting to a free market economy. Impressive Aviation expansion is seen in India, China and ASEAN. Latin America shows promise. Everywhere, these regional trends co-exist with an intensification of global ties across the Atlantic, the Pacific and the Eurasian Continent.

The process of the Liberalization Privatization and Globalization (LPG) has become the buzzword in today's world, and aviation industry is no exception to this general norm. Deregulation, liberalization and privatization started for the last two and half decades. This process has led to the independent states increasingly becoming inter-dependent states and the roles of governments are changing form regulators to facilitator. The concept of sovereignty thus suffered a massive dilution; thereby the states have become law-takers rather than law-makers. It is also well-known that though multilateral treaties such as the Chicago Convention in many aspects governed the international air transport but the major part was dealt with by the bilateral treaties. WTO provides a classic example of this emerging trend in the arena of international trade. Since there was a pressure for movement for the present system to plurilate framework there is also growing recognition of the need to define the industry 'sub sector' for trade purposes; to keep the airline industry 'on-board' and to generate new thinking, inter-alia on whether the concept of 'conditional most-favored nation' (MFN) could be applied to air transport in the context of GATS. However the main reasons for limiting GATS coverage of air transports was that at an initial stage the Uruguay round negotiators recognized that the air transport was governed by a large number of bilateral agreements based on balanced and reciprocal exchange of rights between states coupled with fair and equal opportunity.

With this scenario privatization of airlines and airports, and liberal and open "open skies" bilateral agreements, are the some of the new trends emerging on the horizon. Deregulation and intensified global competition are forcing airlines to become responsive, competitive and efficient by focusing more closely on their customers and operations. The technological, infrastructural, institutional, economic and human challenges have prompted those in charge of airlines and aviation-related agencies to effect a shift in their polices and approaches pursued for years. In fact, civil aviation in the new millenium would be one of the biggest growth sectors.

The attitude of the government and industry towards the regulation of air transport has undergone a profound change over the past few years in almost all parts of the world. The worldwide impact of deregulation, privatization and globalization forced all parties to rethink the ground rules by which the airline industry had been regulated since the

Chicago Convention 1944. Even many countries in Africa, Asia which once adopted a defensive position against liberalization, have recognized powerful pressures for changes in the regulatory system.

The global economic forces are compelling the governments and airlines everywhere to redefine their respective roles in air transport. the entire industry is undergoing a drastic transformation from regulation to deregulation, mergers, acquisitions, alliances, consolidations, and allied issues of privatization, liability, insurance and infrastructure, code-sharing arrangements, computer reservation systems and other inter-airline agreements are changing the structure of the airline industry. On the other hand, new concepts of ownership, financing, management and operation of airports are emerging. Traditional patterns of state involvement are increasingly being questioned. Many governments have begun to pursue competitive policies domestically - including the continuing movement to privatize many government-owned airports - and to expand foreign holdings in airport equity. As a result, there is a significant growth in the number of alliances over marketing, code sharing and computer reservation system.

The beginnings of reform process in civil aviation in India.

Regulatory frameworks have had significant impact on the evolution of the Indian aviation industry since its very beginning. The first generation of aviation regulations were created in the colonial era to ensure that growth of aviation did not pose a threat to the colonial government and served the strategic interests of the imperial government. In the post-independence era the aviation industry was nationalized and the second generation of aviation regulations were introduced to cater to this state monopoly.

The Narasimha Rao government faced with an impeding economic crisis in the early 1990's changed course and an era of liberalization and deregulation was ushered in. The aviation sector, which had been struggling as state monopoly, has also been slowly deregulated and private players are making their presence felt in the industry. However experiences in the past fifteen years have shown that as the industry moves increasingly away from the stated-centric model of the nationalization era to a multi-player model with large scale participation from private players in the post-liberalization era, crucial issues relating to regulation of the rapidly evolving civil aviation industry need to be addressed, in a manner, that would ensure effective and sustainable growth of the industry

The reform process in civil aviation in India was in response to the global developments, particularly after Deregulation Act 1978 in USA which followed because of new global economic philosophy to promote privatization , liberalization, and globalization in economic relations. Civil aviation is an international commodity which provides means for international economic relations between states. The ICAO also held important conferences inviting states to discuss new measures to introduce privatization and liberalization in global air transport. The Planning Commission in India made a study of deregulation in international air transport and lessons for India. There was a national debate on this subject. There was no alternative but to go with the global developments. Some reforms were introduced in stages. The domestic and international airports were merged for administration. Private enterprise was introduced for airports developments .The national airlines Air India and Indian Airlines were made into holding companies and private airlines were permitted to fly for public transport purposes. Besides there was new look being given to aviation policy to promote national economy through civil airlines and airports. An open sky policy was adopted to promote greater entry for foreign airlines to India. There was a proposal to merge Indian airlines and Air India into one single national carrier for domestic and international services and to provide a better competition with foreign airlines. Some GATT principles were adopted to promote free trade through civil aviation. Air India joined a group of airlines for common pool for cargo services. Code- sharing was introduced to promote joint marketing by national carrier with foreign airlines. Some times unilateral permission was given to foreign airlines to operate to India. In a way therefore the Government and the regulatory authorities had responded creatively to the challenges to the global civil aviation and made use of reforms to promote national economy.

In the aviation sector, the liberalization /open skies policy started in India in the late 1980s. A strong consumer demand and constraints on the rapid expansion of national carriers and tourism potential have favoured this policy. India first introduced the open skies policy in cargo services and chartered flights for domestic and foreign carriers. The open skies policy in cargo has facilitated the emergence of all-cargo airlines in India. India's new economic policies in the early 1990s have triggered far-reaching fiscal, trade, industrial and economic reforms, aimed at accelerating growth, employment, productivity and technical innovations. In civil aviation sector, the government repealed the Air Corporations Act 1953 and passed the Air Corporations (Transfer of Undertakings and Repeal) Act in 1994. This Act ended 40 years of state monopoly and a large number of private domestic airlines are now operating in the Indian skies.

The new legal issues in the area of airlines & airports activities have been growing every single day. Though we have existing aviation laws in place, it is not adequate enough to address all of them satisfactorily. So we have emerging issues like the privatization/commercialization of airport activities, intellectual property rights, questions of liability, Airport privatization areas & concerns, Due diligence consultancy & other issues, growing importance & legal issues involved in air cargo, commercial issues in civil aviation, safety , security& environmental issues , emerging issues and issues arising from the lack of Aviation legislation in most countries, our very own country, India, for example. As lawyers, we have to handle them, and handle them well. It is with this hope and heartfelt desire that I have envisaged the proceedings for the day and I am sure at the end of all the interesting presentations and discussions, each one of us would go home, aware and enlightened of all the facets that constitute and contribute to space law.

M.K. Law National Committee Report on Civil Aviation March 2006.

The terms of reference of above mentioned committee were to examine functions of DGCA as envisaged by ICAO, authorize DGCA to carry out its functions , comparison of regulations in India with other countries, organization of DGCA and its manpower and training requirements, procedures adopted by DGCA for a) Licensing of airlines, b) licensing of personnel that is pilots ,engineers, flight dispatchers etc. c) examination system d) clearance of international scheduled and non-scheduled flights, administrative and financial autonomy of DGCA for its functions, to conduct audit as per ICAO Protocols for air safety etc. The above committee invited top level experts from aviation world during its deliberations to complete the terms of reference.

The Kaw Committee made the following recommendations which have been approved by the Government of India and are being implemented ever since they were made.

4.1 There is need for overall civil aviation policy and the civil aviation act.

4.2 There is need for flexible use of Indian air space by both military and civil air traffic.

4.3 The Government should establish a National Advisory Committee on Civil Aviation with Secretary civil aviation as chairman and DGCA as member- secretary.

4.4 DGCA to act as aviation safety and aviation economic regulator. However, the Ministry of civil aviation has opted for a separate economic regulatory body.

4.5 The DGCA to act as a facilitator for developmental activities in operational and manufacturing fields.

4.6 DGCA to be catalyst for aviation manufacturing and training activities.

4.7 Urgent need for National Training policy and National Aviation University.

4.8 Streamlining of DGCA procedures for grant of clearances of flight schedules, licensing of airlines and aviation personnel.

4.9 Review of examination systems of DGCA and its central examination organization

4.10 Setting up DGCA Governing Council and its empowered committee with Secretary Civil Aviation as chairman to exercise administrative and financial autonomy for DGCA.

4.11 DGCA as an empowered arm of the Government rather than a civil aviation authority.

4.12 Need for a comprehensive manpower policy for DGCA and introduction of new all India civil aviation service.

It may be said, that the civil aviation law and policy are a reflection of the national economic policy for development and growth. Aviation in the modern world is a means for economic development. In the report by ICAO made in 1996(ICAO Doc 9687 dated May 1996), the Asia and the Pacific Region has the highest growth rate during period 1996 -2010.This forecast has been proved right. In the Annual Report of the Council 2005 the ICAO informed its strategic objectives and business plan for period 2005 -2007. It made six following important strategic objectives:-Safety, security, environment protection, efficiency, continuity, and the rule of law.

The ICAO recommends for the business plan that it should be achieved by requirements-driven, results-oriented organization, and there is need to introduce new methods for optimal use of limited resources.

PROJECT FINANCE IN AVIATION

India is one of the fastest developing country with poor infrastructure. Infrastructure of a country is backbone of the country. Airport being a nuclei of economic activity assume a significant role in national economy. Now there is dire need to develop the infrastructure. Airports are the very important part of infrastructure. The finance of infrastructure development projects is generally sought to be done through an approach termed as 'Project Finance'.

Project Finance can be defined as the method of financing of the development or implementation of any project where lenders look at the project for recovery of amount due to them rather than at the borrower or assets of them. Project finance is not financing a project. Project finance is defined as raising funds to finance an economically separable capital investment project in which the providers of fund look primarily to the cash flow from the project as the source of funds to service their loans and provide a return on their equity invested.

Passengers carried by domestic airlines increased by 36.47 per cent (to 317.29 lac passengers) in the first three quarters of 2007, against 232.49 lac in the same period last year. Overall aircraft movements also increased by 27.2 per cent in April 2006 – August 2007, as compared to the same period in 2005-06. International movement was up by 12.9 per cent and the domestic, by 31 per cent. Simultaneously, overall passenger traffic increased by 28.5 per cent, while the freight traffic was up by 11.9 per cent.

The International Air Transport Association (IATA) in its latest estimates this year reckons India to be a driving force behind the world's civil aviation business that is globally expected to grow from US$ 5.1 billion to US$ 5.6 billion this year.

Air Traffic

India's air passenger travel is expanding at about 25 per cent a year, and. Growth in this sector will outpace the global average until 2025, according to government estimates.

Domestic air traffic is likely to more than double and touch 86.1 million passengers by 2010, up from 32.2 million passengers in 2007, states the market research firm PhoCus.

According to data compiled by the Airports Authority of India (AAI), 16.21 million people flew on international routes to and from India during April-October 2007-08. This was a growth of 17.1 per cent over the same period last fiscal.

So there is a need of more airport infrastructure but government have limitations to finance the new airport infrastructure and develop the existing airports up to international standards. So project finance by private players is the best way to develop airport infrastructure according to requirement.

Issues:

Negotiation considerations such as identification of the project, drafting of the Memorandum of Understanding with State and Central Government officials, location of feasibility study funding, determination of project feasibility, and interaction with Central Government officials to move projects through required official clearances. I will examine foreign investment considerations such as a review of the Indian political, legal and business systems; the identification of major investors into India; an analysis of equity, export performance, local content, currency conversion, technology licensing agreements, dividends repatriation, and direct taxation requirements; an overview of government concessions and incentives; the identification of specific indirect taxation through import duties; and review of contract requirements.

Legal Feasibility- Here the most important aspect is the security for the loan

1. Term loans are usually fully secured

2. The term lending institution will have to examine the loan proposal from the 3. 3. view point of the nature and the extent of security offered

4. Term loans are secured by creating a charge on the immovable and movable properties of the plant

Project Finance In Airlin

In the last few years major structural and organisational changes have been occurring within the air transport industry. Major airlines have been consolidating their services by forming international alliances whilst a new generation of low cost carriers have entered the market. At the same time, a growing number of airports have been privatised which has allowed airport groups, which control a number of airports in different countries, to develop. In the era of globalisation, the aviation industry is booming very much and low cost operating airlines are coming up and project financing or we can say that financing in the airlines or like mergers or take over of major carriers in aviation are taking place. If we take the example Kingfisher is a major airline and it took over the small and budget carrier Deccan airways, so many low cost airlines are coming up and investment in this field is very much as we have seen the changes in the recent decade that the purchasing power parity of a common man has increased many times folded, so for increasing demand in the aviation industry so many low cost airlines or we can say budget airlines came up and huge money is being invested in this field, if we look at the past few years only few airlines were there and they were even not permitted by the aviation ministry to fly internationally but now many private airlines are there which are flying internationally. Now financing of the airlines or venturing up the capital in starting the new airlines is booming up, every day we hear of some or the other airline coming up in the market, competition is so high that financing in the aviation sector or like in airlines is a new phenomenon which has been seen in the recent days. Project financing involves various aspects like, first of all the attention required as such the latest techniques in airport traffic forecasting, revenue and cost projection, airport charges regulation, project finance and risk assessment. Key market trends will be evaluated, including the growth in global airline alliances, low cost airlines and increasing concern over environmental issues, together with their potential implications for future airport growth. In the same decade airports have transformed from a public service to a value creator in a transport network. Deregulation of air transport markets has shown that the introduction of competition may have drastic impacts on network configurations of airlines, because of free route entry and exit; airlines will use their route networks to achieve traffic economies and maintain spatial monopolies in a competitive environment, so the major thing is that project finance in airlines is increasing day by day, economy is growing, as the number of growth of airports is also growing, so financing projects related to the aviation industry is seen as a profitable venture. Predatory Pricing is assumed, when an incumbent airline responds to market entry by greatly expanding capacity and low-fare seats. Summing up project finance in airlines is now a seen as a profitable venture as the market trends are changing in the developing country like India, so financing the airlines is also seen as a new phenomenon.

SPECIAL ECONOMIC ZONES AND AIRPORTS

It could be another `chicken-and-egg' story, if we say infrastructure investment would follow investment by SEZ (Special Economic Zone) users, or can be said other way around. The rapidly growing number of SEZ across the country, after viewing the progression records of various other nations (like China, Philippines, UAE, Indonesia and Polland) fuelled by the establishment of SEZ, is evidencing the interest of Indian Government to make the units a successful and progressive step for the nation. These are export promoting zones identifying themselves as 'free' and 'special', distinguishing themselves from other regions by relaxed tariffs, taxation and administrative regimes.

To accomplish the success of the zones, a synergism on the part of government and developers can be seen. The SEZ providing an internationally competitive and hassle free environment for exports. Connectivity of each SEZ thus becomes a significant factor to be undertaken which make the project more efficient and cost effective. In order to create world class trade-related infrastructure facilitating import and export of goods aimed at making India a global trading hub, the multi-modal connectivity has already been a focus of the developers. The economic rationale behind the promotion of SEZ is to deal with infrastructural deficiencies, procedural complexities and attempts can be seen very well on part of developers providing high infrastructure. For instance- creation of logistic parks inside SEZ and enjoying world class logistic support, which is not only a part of infrastructure but indeed a grave requirement. For the time critical and time sensitive logistic platforms, the developers of SEZ/ Unit are confidently dependent on the airway. It has been noticed that an important factor which has been considered, while setting up SEZ, is the distance between SEZ unit and the airport, supplying a smooth access to airports.

The prevailing tendency of development of SEZ near airports is already being followed; further the priority of developing the airports near or inside SEZ can be seen in future being adopted as a frequent trend. Although in India in many of these units, the zone's private aerodrome with air strip of international class is fully functional which receives private/chartered flights. Establishment of international airports inside SEZ is a new source of energy, as the conception of establishment of SEZ unit inside an airport have already been adopted by the developers in many states. The idea is to provide the highest and fullest degree of infrastructural facilities in and around the SEZ. The easy and convenient air linkages to these units will result in maximum efficiency and will exhibit high ratio of output. Many Infrastructure development companies are also planning to set up an airport-based SEZ near the newly constructed International Airports, in which aircraft component manufacturing industries and high-end aircraft engineering support activities will be carried.

After the introduction of concept of privatisation of airports and commercialisation, new developers and private companies are investing in India's infrastructural development. Specially, in the field of airports, we can see many domestic and foreign companies interested in investing in Indian airports, which is a featured attraction for the confident and bold investments made by SEZ investors and developers. Without such facility of availing convenient air transport service, it would have been difficult for the SEZ developers to gain confidence on the heavy monetary investments made on the development of these export zones.

AIRCRAFT LEASING IN INDIA: AN OVERVIEW

The increasing popularity and possibility of leasing is dictated by the rapid growth of technical developments and the need for bigger and faster aircrafts. The airline companies had to face steeply rising costs and often could not afford to buy new aircrafts. At the same time these larger aircrafts contributed to temporary overcapacity, thereby reducing the profit of the airline companies. Thus one can say that privatization of aircrafts has led to the development of aircraft leasing and financing. An aircraft is an expensive commodity and aviation is a sector with great prospects so many private entities have started running airlines by acquiring aircrafts either through leasing or by getting it financed. As the aviation industry is growing by introduction of more and more airlines so is the business of leasing and financing of aircrafts. Therefore there arose an urgent need to regulate the aircraft leasing and financing industry. The article also briefly discusses the Cape town convention and the Protocol which can be called the mother convention of aircraft leasing and financing.

Owning the "Big Bird" is an expensive deal. Purchasing new aircrafts further makes it an attentive proposition in exchange of monetary. It is a common practice in the airline business to take aircrafts on lease. Leasing not only assists in increasing the paradigm of airline sector, and more importantly, reduces the instant cost of airline operators. Universally aircraft leasing is quite prevalent and practiced. In India, There is an entire gamut of legislations dealing this business, viz. Directorate General of Civil Aviation

("DGCA"), the Reserve Bank of India ("RBI"), Taxation Department, which parties entering into aircraft leasing transaction have to consider.

Leasing of aircraft is a extensive portion of financing and accounting of airline operators in terms of both the magnitude of capital and the complexity of lease classification. Leasing is an important instrument used by Aviation companies dealing in capital management, especially when facing financial distress. Basically aircraft leasing provides two main purposes that is to have aircraft without the financial burden of buying them, and to provide temporary increase in capacity of business and services. In this regard lease classification and the related accounting treatments are critical and necessary to the airline industry.

Leasing has become a common and important technique to acquire an aircraft, which is governed by various law and regulations. One of its prime advantages of leasing is that it helps to manage the finance investment. Leasing of aircraft is most common in private as well as in public aviation sector. Both short and long term aircraft leasing options are available to aviation industry.

Aircraft leasing are classified into finance and operating lease. Finance lease is required to meet criteria like: a lease term greater than 75% of the aircraft's estimated life, option to purchase it at less than fair market value, or transfer of ownership to the lessee when lease expires. It also enhances tax benefits and is explicit on the balance sheet of the lessee. Generally, it's for a long term period. On the other hand, an operating lease is meant for a short term period. Presently, most of the aircraft leasing is on the basis of this type of lease. According to data, there are about12,500 commercial aircrafts over the world, among which about 2500 flying on operating lease. It's always a constructive and beneficial deal to relish aircraft leasing service from Commercial Aircraft Sales and Leasing, a collective term given to organizations involved in marketing airliners from manufacturers of like Boeing and Airbus. A innumerable number of other providers, such as commercial banks, financial institutions, and hedge funds, are also in the scenario to provide aircraft leasing services. Of which noticeable are GE Commercial Aviation Services (GECAS) and International Lease Finance Corporation (ILFC). Besides, some companies offer leasing as well as financing packages for commercial and corporate aircrafts. Customized aircraft leasing packages are also designed to meet the demands of the market.

Despite the high growth of the Indian aviation market, the legal, tax and regulatory environment continues to be a challenge for lessors and financiers of aircraft –both at domestic and international levels. A variety of issues comes to non-Indian lessor or financier of an aircraft to an Indian operator.

MEANING, DEFINITION AND CONCEPTS

Meaning of Aircraft Leasing: Aircraft leasing is a contract whereby the owner (lessor) of an asset agrees to another party (lessee) the exclusive rights to the use of asset (aircraft) for an agreed period of time, in return for of rent or premium which is to be paid periodically. In Indian context the word 'lease' is defined under section 107 of Transfer of Property Act, 1882 which deals with only immovable property only. Aircraft being the movable property so the appropriate word to be used is 'Bailment' of an Aircraft which is defined under section 148 of Indian Contract Act, 1872. In foreign context the word 'lease' could be used as the ICAO document (Manual of procedures for operations inspection, certificate and continued surveillance) and Regulation (EC) No. 1008/2008 (common Rule for the operation of Air service in community defines following :

Lease: a "...contractual agreement whereby a properly licensed air operator gains commercial control of an entire aircraft without transfer of ownership "

Lessor: "…the party from which aircraft is leased "

Lessee: "…the party to which aircraft is leased "

Concepts of Aircraft Leasing: The nature of leasing is a contract between the lessor and lessee where lessor provides the right to use asset to lessee. The contract has its own specified time, referred to as the lease term for which the lessee is obliged to pay the installment as agreed between the lessor and lessee. Generally, a lease contract may not be cancelled by either party unless certain terms and conditions specified in the contract switch to its termination. A lease automatically terminated on the completion of the lease term unless renewed. At the expiry of the lease term, the lessee is usually required to return the asset (aircraft) to the lessor, unless the lessor provides an option to the lessee to purchase of the asset (aircraft). No separate act exit to do aircraft leasing. Neither the aircraft Act nor the Aircraft Rules contain any specific provision in this regard. As with leases in general, therefore, the provisions of the contract act will apply. In order for there to be a valid lease there must be an offer and acceptance together with consideration . The parties must be competent to contract .

Most airlines increasingly rely on aircraft leasing to large up front capital requirements and efficient way to purchase the aircraft. According to report , major airlines across the world had accumulated approximately 13,458 aircraft. The international Lease Finance Corporation (ILFC), estimates that one out of every three commercial aircraft is leased one. Thus the leasing is becoming more prevalent in the airline sector.

TYPES OF AIRCRAFT LEASING

Basically there are two types of Aircraft Leasing: Dry lease and Wet lease.

Dry Lease: A dry lease agreement is "… an agreement between undertakings pursuant to which the aircraft is operated under AOC of the lessee… "In Dry lease, an aircraft is leased without insurance, crew, ground staff, supporting equipments, maintenance etc. Airlines enter into dry lease agreement which has its own flight and maintenance department and need aircraft only and no other services. Dry lease is used by the leasing companies and banks, requiring the lessee to put the aircraft on its own AOC and provide aircraft registration i.e. Aviation Regulation becomes the responsibility of the lessee. The tenure of the aircraft lease is more than two years and consist certain conditions regarding depreciation, maintenance, and insurance etc. and also depending upon the geographical and political circumstances etc.

Requirements of Dry lease in India

Registration of aircraft: - Operation of foreign aircrafts on dry lease requires registration of aircraft in India. The leased aircraft ought to have a valid Certificate of Registration ("CoR") and must be entered in the operating permit of the operator. According to Civil Aviation Requirement ("CAR") regulations , registration of aircrafts can be done either in Category A or B. For leased aircrafts, the registration falls under Category A. the registration of the aircraft is valid as long as the lease is in force and the aircraft is maintained in accordance with (i) the DGCA Regulations; (ii) the terms and conditions specified in the operator's permit; and (iii) the operator's maintenance control and operations manuals. The operator can apply to DGCA for extension of validity of the CoR. Airworthiness of the aircraft- once the aircraft is registered, the owner of his authorized representative has to apply to DGCA in a prescribed form together with the requisite fees prescribed in rule 62 of Aircraft Rules 1937 for obtaining CoA . An application for issue of Aircraft Noise Certificate is also to be made along with the CoA application. CoA is valid for a period of Twelve months. In case of imported aircraft, the validity begins from th date of issue of Export Certificate of Airworthiness and is restricted to the validity specified in the standard certificate of Airworthiness issued by the country of export.

Two types of Dry lease: There are two types of dry lease:

(a) An Operating lease; and (b) A finance lease.

An Operating lease: In case of an operating lease, the aircraft is leased for short period of time as compared to its total economic life. An operating lease is commonly used to acquire aircraft for a term of 2-8 Years. For instance, if the total economic life of aircraft is 20 years then under operating lease it may be leased upto 8 years, upon the end of the lease period, the lessee returns the leased aircraft to the lessor and there is no option of purchasing the aircraft. The lessee does not show aircraft into his balance sheet under operating lease.

Finance lease: The finance lease is also known as Capital Lease. Finance lease is long term lease and the lessee has the option to purchase the leased aircraft upon the expiration of leasing date and also includes:

- Lease payment more than 90% of the market value of the aircraft.
- The term of the lease is over 75% of the aircraft's usage life.

Wet lease: "… an agreement between air carriers pursuant to which the aircraft is operated under the AOC of the lessor… ".A Wet lease provides the aircrew, maintenance, aircraft logs and other support function with the leased aircraft to lessee. A wet lease is beneficial to a company that wants an aircraft at its disposal but does not want the burden of hiring a flight department to fly and maintain aircraft. Over the years the aircraft leasing terminology has gone through many changes which may not reflect the service provided; for instance, in U.K wet lease use to mean, quite logically, ‘including fuel’.

Requirements of Wet Lease in India : Operation of foreign aircraft leased by Indian operators is normally permitted on dry lease basis. Import of aircraft for domestic air transport operations on wet lease basis is not permitted except in emergency situations and in the following circumstances such as the existing aircraft of an operator is grounded for maintenance/inspection checks or due to any other unforeseen reasons.(in such cases, wet leasing is permitted only for the duration of grounding of aircraft); or the existing aircraft is involved in some accident/ incident or due to expiry of existing lease and delay in finalization of new lease agreement, there is a reduction in capacity of the operator; or for revival of sick operators who should have an agreement with the lessor initially for wet lease for a period not exceeding six months and, thereafter, automatic conversion to dry lease for the remaining period of lease; or short term induction of capacity required to meet emergency situation such as natural calamity, industrial unrest or any other similar situation .

Other important provisions pertaining to operation of aircrafts on wet lease are discussed below:

- The state of registry has to confirm that their legislation enables them to divest themselves of the functions and duties which are the object of the transfer agreement, agree for surveillance of aircraft operations and maintenance by DGCA , and should furnish a letter from the concerned regulatory authority in this regard;

- There should be well stated agreement between the lessee and lessor stipulating that the Indian operator and DGCA will have the authority to exercise airworthiness and operational control on the wet lease aircraft operation:

- The lessee and the lessor must have a valid and effective operation permit or AOC for the type of operations.

Type of Wet Lease: Damp Lease: a “…wet leased aircraft that includes a cockpit crew but not cabin attendants” . Under Damp lease, the lessee will provide cabin crew. However, in order to give initial guidance to the crew of the lessee, sometimes, the lessor provides a trainer on board for a limited period of time to give SEP (Safety and Emergency Procedure) training to the cabin attendants.

General requirements applicable to both dry and wet leases: For leased aircraft operations in India, the aircraft should have been type-certificated by Federal Aviation Administration of USA or Joint Airworthiness Authority of Europe or Civil Aviation Authority of UK or any other authority acceptable to DGCAA. It is operator’s responsibility to confirm that the lease agreement does not contain any provision which will be binding on the DGCA. The lessor, on his part, has to give an undertaking in the lease agreement that he would comply with all the application accordance to “CAR” rules.

Tests for lease classification In terms of criteria for lease classification, the following four tests are generally applied.

- Transfer of ownership test
- Bargain Purchase option test
- Economic life test: 75% rule.
- Rule of investment test: 90% rule.

ADVANTAGES AND STRUCTURE OF AIRCRAFT LEASING

Advantages: The advantages of aircraft leasing is as follows:

1. Full financing at fixed rates: The lessee is entitled to use an asset (aircraft) Without paying full cost-up-front which helps to conserve score cash.

2. Protection against Obsolescence: Leasing and asset reduces risk of obsolescence, and in many cases passes the risk in residual value to the lessor. If the asset value changes in a short period of time, lease is effective way to avoid such risk from lessee’s end.

3. Less costly financing: Tax benefits that accrue to the leasing company or financial institution may sometimes be transferred to ht e lessee in lower rent payment form.

4. Flexibility: The agreement of lease may less restrictive provision as compared to other debt agreements. For e.g., a lease payment schedule can be structured to meet financial condition of the lessee. If you own the aircraft, you may have virtually complete control over its use. Depending upon the resale market for the aircraft and how long you are willing to hold it, you may be building equity. However, there is less flexibility with ownership. The aircraft you purchase may become obsolete or the company's aircraft needs may change over time. A substantial down payment may be required to purchase an aircraft, depleting the company's working capital and adversely affecting your debt-equity ratio. In addition, payments towards purchase may be higher than available lease arrangements. Some companies may be subject to requirements prohibiting aircraft ownership due to shareholder or insurance liability concerns.

A lease arrangement may be more flexible than purchase of an aircraft. A lease can enable a company to get in and out of aircraft use more easily through shorter-term commitments and without the prepayment penalties that might be triggered upon sale of a leased aircraft and the risks and responsibilities of aircraft ownership.

5. Attractive minimum tax problems: As the ownership of equipment results in an increase in tax liability under alternative minimum tax rules, companies can avoid the onerous alternative tax provisions by way of leasing equipment.

6. Off Balance Sheet Financing: depending on the type of leases, the lessee can treat lease transactions as off-balance sheet. This is critical to those companies wishing to increase borrowing capacity. Companies can avoid increasing balance sheet liability by leasing equipment instead of purchasing. One reason to choose a lease over purchase is that it can minimize the cash flow required to provide what is, in effect, a service (transportation), rather than an asset, necessary to company operations. In most cases, the company has no inherent interest in owning aircraft, only in using aircraft. Even companies in business directly involving aircraft, such as the airline industry, often lease. Currently, about half of the commercial aircraft operating worldwide are leased.

7. Tax-Advantage: Ownership of an aircraft will generally give you the right to depreciate it for tax purposes. However, only interest, not principal, will be deductible. For some companies facing potential Alternative Minimum Tax issues, a lease with fully-deductible payments could present advantages. Or, if the company has insufficient tax liabilities to take advantage of depreciation deductions, leasing might provide a cheaper method of acquiring use of an aircraft. Also, a company with international operations may have options, in terms of structuring the acquisition of aircraft that make the option of leasing more desirable than purchase.

8. Since lessors assume a residual value to the aircraft being leased, they can typically offer a lower rental payment. However, to optimize the cash flow benefit, leases usually must be for a longer term. In addition to freeing up cash, leasing also may help keep your lines of credit open.

9. Leasing also can remove long-term debt from the balance sheet. Under many lease agreements, lease rental payments will qualify as an expense, not debt, under applicable accounting rules. Companies looking to clean-up their balance sheets may prefer leasing to purchase of aircraft. You may, however, have to reflect your lease obligations in the footnotes to your financial statements.

CHARGES AND TAXES UNDER AIRCRAFT LEASING

Fees and Charges: There are no fees or charges payable in respect of the creation of an aircraft lease. Registration of the lease (in case it gives rise to a charge) with the Registrar of Charges will entail a nominal fee. So too, will registration of the lease with the Sub-registrar of assurances.

Taxes: The usual taxes and duties on aircraft leases are described below:

VAT: This was introduced in April 2005 and has replaced Sales Taxes in all 29 States and six Union territories of India. However the following sales are exempt:

a)If made in the course of inter -state trade or commerce;

b)If made outside the state;

c)If made in the course of import of the goods into or export of the goods out of India.

Custom Duty: No customs duty is payable on import of aircraft by Scheduled/ Non-Scheduled Operators, Flying Clubs and Training Institutes into India.

Capital allowances: Capital allowances are in the nature of tax depreciation allowances arising on the purchase of certain plant and machinery, including aircraft. Capital allowances may be claimed in respect of aircraft by the owner.

Corporation tax: In the case of a non-resident assesses, engaged in the business of operation of aircraft, the income chargeable to tax in India under the head "Profits and gains of business or profession", is calculated at the rate of 5 per cent of the aggregate .

Stamp duty: Stamp Duty is levied in India on instruments in accordance with the Indian Stamp Act. If the instrument is executed overseas and relates to a property located overseas, there is no stamp duty.

DIRECTOR GENERAL OF CIVIL AVIATION'S (DGCA) REQUIREMENTS IN INDIA

DGCA Permission: For leasing an aircraft in India DGCA's permission is mandatory. A lessee can either take an aircraft on lease from a) foreign operator b) Indian operator.

Aircraft Lease from a Foreign Operator: Where the Indian operator intends to take a foreign registered aircraft on lease, charter or any similar arrangement for a person holding Air Operator Certificate (AOC) issued by another State, the following information has to be provided by the Indian Operator to the DGCA at least 45 days prior to the proposed date of operation with the eased aircraft. i.e. Name and Address of the Indian Operator and the lessor, aircraft details, AOC details along with operations specifications, if any, of the lessor, name and contact information of the State of Registry, a copy of the letter of intent, planned arrangements for operation and maintenance of aircraft during the lease period, proposed date of import into India.

Aircraft Lease from an Indian Operator: In the event an Indian Operator intends to borrow an aircraft on lease from an Indian Operator the following information has to be provided to the DGCA at least 45 days prior to the proposed date of operation with the leased aircraft, ie. The name and address of the operator from whom the aircraft is intended to be leased, AOC details along with operations specifications of the lessee and the lessor, aircraft type, registration number and its main base, maintenance agency with scope of approval, a copy of the draft lease agreement and maintenance agreement, any amendment proposed to be made in the Operations Manual or other relevant documents, a document giving details of the respective responsibilities of compliance with regulatory requirements such as arrangements for Flight Operations Quality Assurance, Flight dispatch and responsibilities of the lessor and the lessee with regard to operation, maintenance and quality system of the aircraft.

Upon receipt of the aforesaid information, the DGCA finalizes the modalities for operation of the leased aircraft at a meeting with the Indian Operator. Where the aircraft is taken on lease from a foreign operator, the representatives of the foreign operator and the regulatory authority are also allowed to participate in the meeting. The DGCA can conclude an agreement under Art. 83 with the State Registry and the State Operator for transfer of certain regulatory functions. It has also the discretion to impose conditions while granting permission to the Indian Operator for operations with the leased aircraft.

Lease agreement and stamp duty: Pursuant to the DGCA permission, the Indian operator can conclude a formal lease agreement with the lessor. The agreement should include the conditions decided by the State of Registry and the State of Operator and the ones imposed by the DGCA. A copy of the lease agreement has to be, thereafter, filed with the DGCA at New Delhi (the DGCA usually asks for a notarized copy from the airlines). The copy of the lease agreement does not attract stamp duty in the State of Delhi but it is necessary to stamp the lease agreement in the relevant state, (the state in which the airline is incorporated or has its operational base), prior to filing with the DGCA. Stamping is necessary to ensure that the lease agreement is enforceable in a court of law. In India, the stamp duty rates vary from state to state.

DRAFTING OF LEASE OF AIRCRAFT

While drafting a Lease Agreement of an Aircraft the following are considered at the time of execution of the deed between the parties. Information to be given regarding Aircraft which includes Aircraft Make and Model, Aircraft Manufacturer's Serial Number, Aircraft Registration Mark, Made and Model of Engines, Serial Number of Engines etc., Summary of the Transaction, Place and Date of Delivery, Lease Term, Security Deposit, Transaction Fee, Rent, Reserves and other payments, Involvement with Aircraft Manufacturer, Pre-Delivery, Delivery and Post-Delivery Documentary and other requirements, Disclaimers, Manufacturers and Vendors' Warranties, Operation of Aircraft, Subleases, Maintenance of Aircraft, Use of Reserves, Title and Registration, Identification Plates, Taxes, Indemnities, Insurance, Loss, Damage and Requisition, Representation, Warranties and Covenants of Lessee, Representations, Warranties and Covenants of Lessor, Financial and Related Information, Return of Aircraft, Assignment, Default of the Lessee, Notices, Governing Law and Jurisdiction and Miscellaneous.

OWNERSHIP INTEREST, LEASE INTEREST AND COMPETING INTEREST

OWNERSHIP INTEREST:

Ownership interest includes the following requirement:

1. Registration: It is likely record a lessor's exclusive interest as the owner of an aircraft with the Indian Directorate General of Civil Aviation (DGCA) & this will be redirected on the aircraft's certificate of registration.
2. Registration documents: The type of documents to be submitted to the DGCA in connection with any transfer of title and/or the issuance of the certificate of

registration will be determined by the nature of the transaction: new delivery; sale and leaseback; or sale of aircraft subject to existing lease.

3. Registration fees: No registration fees are payable to the DGCA in connection with the recordation of an ownership interest, although a nominal fee of 1,000 Rupees is payable in relation to the issuance of a new certificate of registration upon change in aircraft ownership.
4. DGCA approvals: Depending on the nature of the transaction, a variety of DGCA approvals might be required
5. Effective title transfer: Indian law will generally recognize as effective an English law title transfer pursuant to an English law aircraft purchase agreement and an English law bill of sale.
6. Sales tax and VAT: Sales tax or VAT will apply if the aircraft is located in India at the time of title transfer.
7. Stamp Duty: As with a variety of other transaction documents, stamp duty might be payable in relation to a sale and purchase agreement and/or bill of sale as a condition to its enforceability in India.

LEASE INTEREST

It requires the following things:

1. Registration: It is possible to record the lease agreement with the DGCA.
2. Registration documents: A copy of the lease agreement must be filed with the DGCA in New Delhi.
3. Registration fees: No registration fees are payable to the DGCA in connection with the filing of the lease agreement, although a nominal fee of 1,000 Rupees is payable in relation to the issuance of a new certificate of registration upon change in aircraft ownership.
4. DGCA approvals: Depending on the nature of the transaction, certain DGCA approvals might be required. In the context of the sale of an aircraft subject to an existing lease, these are likely to include a formal approval in relation to the change of ownership and a formal approval for the continued leasing of the aircraft pending the issuance of a new certificate of registration.
5. Stamping requirement: Stamping is necessary so as to ensure that the lease agreement can be used in the relevant Indian courts in case of need.
6. Place of stamping: Careful consideration will invariably need to be given to the right State or States in which to stamp so as to balance the need to stamp against the cost of stamping.
7. Alternative to stamping: If the cost of stamping is prohibitive, a lessor or financier might decide to proceed without stamping on the basis that a judgment under an English law lease agreement would be obtained in the English courts and then enforced by the relevant Indian courts.

COMPETING INTERESTS

The supremacy of a lessor's interest can be threatened for a variety of familiar reasons. These will include:

- Detention rights in favour of the Airports Authority of India for unpaid landing, parking, navigation and x-ray charges.
- Arrest and sale rights in favour of the Customs Authority of India for unpaid import duties or for unpaid inland air travel tax.
- Governmental ability to detain and/or requisition aircraft under sections 6 and 8 of the Aircraft Act 1934 in certain circumstances (e.g. if it is in the interests of public safety to do so).
- Governmental ability to introduce legislation for the detention and/or requisition of aircraft under Article 352 of the Constitution in a state of emergency.

Needless to say, it will be important for a lessor and/or financier to be able to agree appropriate monitoring provisions with the lessee. This might include (a) a letter addressed by the airline to the Airports Authority authorising the release of payment/account information to the lessor and/or financier (although there is no guarantee of a response to any request made), (b) a similar letter addressed to the Customs Authority (although such a letter is only likely to be or real value if inland travel tax is reintroduced) and/or (c) a regular certificate from the airline's auditor confirming that all relevant amounts have been paid in full within the applicable time limits (a lessee will often baulk at such a request).

In terms of requisition risk, it will be advisable to assess whether or not state of registration risk is excluded from the insurance coverage. Local advice might also be sought as to the level of compensation payable by the government in the event of any state requisition.

Enforcement & Repossession

No self-help remedies: In the non-appearance of a consensual repossession of the aircraft succeeding any lease termination, an aircraft can only be repossessed via the courts - Indian law doesn't recognize self-help remedies.

Foreign judgments: A lessor / financier should if possible certify that the lease agreement is governed by a user friendly law & that a familiar court system has jurisdiction (English law & English jurisdiction being a mutual choice for leases to Indian airlines). Indian courts will usually uphold any choice of English law as the overriding law of the lease agreement (& any related submission to English jurisdiction), except the choice is not made in good faith or is opposing to Indian public policy. The Indian courts will normally recognise a judgment gotten against an Indian lessee in the English courts, subject to a number of familiar exceptions set out in Section 13 of the Civil Procedure Code 1908 (the "CPC"). A feasible mode of enforcement (particularly if the airline operates internationally) will thus be for the lessor or financier to obtain a ruling in the English courts & have it enforced (without the requirement for a separate action) by the pertinent Indian courts.

Service of process: The lessor & financier will need to guarantee that any court proceedings can be authentically served on the lessee in the proper jurisdiction. This will, in the instance of English proceedings, involve the nomination of an agent to receive service of process on account of the lessee. Without a binding appointment, the English courts would have preference as to whether or not to consent jurisdiction. While all participants are acquainted with process agent appointment letters in cross-border transactions, some precaution needs to be taken when selecting or agreeing to the process agent.

Enforcement timeframe: It is hard to accurately forecast the likely timeframe for the contested retrieval of an aircraft run by an Indian airline. Observers propose that it could take between 10 - 15 years to exhaust all legal avenues, as well as any rights of appeal. However, the usual measure for the granting of an order for repossession is anything between 2 - 24 months.

Repossession: It is possible that the following consents or approvals will be required so as to permit the export of an aircraft from India after lease termination:

- an export permit from the DGCA
- an export certificate of airworthiness issued by the DGCA
- consent from the RBI
- consent from the Airports Authority of India
- consent from the Customs Authority of India

Even if the Indian courts would grant a court order for repossession / enforce the judgment of an English court, experience indicates that the relevant Indian authority may nevertheless refuse to issue the pertinent consent or approval. The DGCA, the Airports Authority & the Customs Authority would be uncooperative if there are unpaid charges, duties or taxes. Negations to consent are however open to face by the affected lessor / financier, & have been successfully confronted in the Indian courts.

<u>Lease & Guarantee Payments</u>

Withholding Tax Exemption: Indian lessees currently benefit (under section 10(15A) of the Income Tax Act 1961) from a rental withholding tax exemption dispensed by the Indian tax authorities, which would expire on 31 March 2006. Without the exemption, withholding tax at a rate equal to 40% would be in effect to lease rental payments to a non-Indian lessor (subject to the terms of any applicable double tax treaties).

So as to profit from the exemption, it is essential to file the signed lease agreement with the Indian Ministry of Finance, plus a letter requesting exemption under section 10(15A) of the Income Tax Act 1961. It is not at all times possible to predict with any precision how long it would take to obtain the exemption, although waiting periods of 2 to 3 months are not uncommon. Consequently, the parties would need to carefully plan the transaction agenda so as to accommodate this latent time lag (except if the lessee is willing to undergo the risk associated with an application for exemption following closing). Pending receipt of the exemption, the airline would have to deduct tax at the appropriate rate & pay it to the tax authorities (while this requirement may not always be constant with practice).

Exchange Control Approval: A lessor / financier will have to ensure that the lessee takes active responsibility for the exchange control approvals that are expected to be required from the Reserve Bank of India (RBI) in relation to the lease agreement & any payment guarantee that is given by an Indian entity in the framework of the transaction.

RBI exchange control approval is required for:

- any guarantee payments
- cash security deposits of more than US$1,000,000
- non-scheduled lease payments

RBI exchange control approval is not required for:

- rental & other scheduled lease payments
- cash security deposits of US$1,000,000 or less letters of credit in any amount

The applicable underlying legislation is the Foreign Exchange Management Act 1999 which controls the payment of foreign currency duties in India.

Lease rental payments & L/Cs: Subject to certain due assiduousness in relation to the pertinent transaction (like confirming that all required DGCA approvals have been acquired), an "authorized dealer" in foreign exchange (in most cases, the airline's Indian banker) is legalized to allow a lessee to send lease rental payments (& other scheduled lease payments, like maintenance reserve payments) & open letters of credit regarding aircraft imported into India on an operating lease basis. There is no particular limit on the amount of lease rentals that could be paid or the amount in which a letter of credit could be issued without exchange control approval. It should be noted that approvals for finance leases should be sought on a case by case basis.

Cash security deposits :Authorized dealers may license airlines (other than certain public sector companies & governmental entities) to remit up to US$1,000,000 per aircraft as a security deposit (for the payment of lease rentals) to a non-Indian lessor in relation to the import of an aircraft or an aircraft engine on operating lease. If the cash security deposit exceeds US$1,000,000 per aircraft, then the lessor would have to arrange for the lessee with a standby letter of credit or a guarantee dispensed by either (a) a foreign international bank or (b) an authorised dealer in India backed by a counter-guarantee from a foreign international bank.

Other payments: Without the consent of a clarification from the RBI, an authorised dealer is not allowed to permit a lessee to remit any other monies to a lessor (payments which are not explicitly covered by the Circulars referred to above). This would include (without limitation) the following non-scheduled payments which are typically provided for in lease agreements: default interest, any amount owed pursuant to any gross-up provision & any insurance payments. RBI approval in relation to such payments can only be attained at the time the relevant payment becomes due (means there can be no pre-approval).

Guarantees: The sanction of the RBI is also mandatory for payments to be made under any guarantee. It should be noted that the guarantee can't be executed until RBI approval has been acquired. To the extent that the advantage of a guarantee executed in favour of the lessor is allocated by way of security to the financier, the RBI approval should also cover the security assignment to enable guarantee payments payable to the financier.

Security Documents

Indian Law Aircraft Mortgage: Indian statutory law doesn't make delivery for mortgages over moveable possessions (including aircraft). As such, it is not likely under statutory law to take an Indian law loan over an aircraft. Indian courts do however know mortgages over moveable property.

The interest of a mortgagee cannot therefore be listed with the DGCA under the supplies of the Aircraft Act and/or the connected rules & regulations. Accordingly, no footnote of the interest of a mortgagee can be made on an aircraft's certificate of registration under constitutional law in India (subject to the comments made in the following sentence). The DGCA has however generally in certain instances marked the mortgagee's interest on an aircraft's certificate of registration.

English Law Aircraft Mortgage: The Indian courts will usually recognise the efficiency of an English law mortgage to create a security importance in an aircraft in agreement with its terms & will generally recognise a judgement got against an owner in the English courts, subject to Section 13 of the CPC.

As Indian constitutional law doesn't anticipate mortgages over aircraft, the mortgage need not satisfy any Indian (being the lex situs) legal necessities, except that the document might be liable to stamp duty if (a) executed in India or (b) if, while the aircraft is situated in India, executed outside India & then brought into India. If the aircraft were situated in an Indian State at the time of implementation of the aircraft mortgage, the rate of stamp duty would be the rate appropriate in that state. Stamp duty concerns connecting to the aircraft mortgage represent another aim for the parties to seek to ensure that the aircraft is positioned outside India at closing.

Lease Security Assignment: For a financed aircraft, the security suite will (assuming fundamental English law rights & obligations) usually include an English law security task in relation to, inter alia, the rights of the owner under the contract agreement & any related contract document (such as any guarantee).

As with an English law aircraft loan, the Indian courts will generally identify the effectiveness of an English law security task to create a security interest in relation to the contract agreement & any other related collateral in accordance with its terms & will identify a judgment gained against the owner in the English courts, subject to the exceptions set out in Section 13 of the CPC.

Insurance Security Assignment: For a financed aircraft, a standard security package would typically include an English law security assignment in relation to certain of the airline's rights in relation to the insurances and/or reinsurances. The lessor's & financier's aim will of course be to ensure, through appropriate registration against the relevant debtor, that the security is creditor & insolvency-proof if at all possible. An assignment of insurances is register against an Indian airline with the Registrar of Companies in the airline's state of registration. As a condition to registration, the assignment of insurances must however be stamped.

Deregistration Power of Attorney: The DGCA has in most instances refused to distinguish the exercise of powers under deregistration powers of advocate. The Civil Aviation Requirements also deliver that, in the case of a dispute, the DGCA will only deregister an aircraft pursuant to a court order.

It is however usual for the lessor/financier to necessitate that the airline execute a de-registration power of attorney in favour of the lessor & the sponsor as several attorneys. This (Indian law) article would have to be implemented under the airline's company seal, notarized & stamped (nominal stamp duty of 100 Rupees will apply). It is recommended that a replica of the de-registration power of attorney be filed with the DGCA. Once India has approved the Cape Town Convention (and opted in to the applicable deregistration provisions), deregistration powers of attorney that are "Cape-Town compliant" will of course enable a lessor or sponsor to deregister & export an aircraft without DGCA or other interference.

PDP Financing

RBI Exchange Control Approval: Although it is likely for a PDP financing to qualify for involuntary exchange control approval under the RBI's Guidelines on External Commercial Borrowings (the "ECB Guidelines"), it is unlikely since a PDP financing will usually not satisfy the following criteria for involuntary approval:

- the term of the mortgage must be more than 3 years (for mortgages of less than US$20m) & more than 5 years (for mortgages of more than US$20m)
- the "all-in-cost" (which includes interest, fees & expenditures) must not exceed 200bps (for mortgages of less than US$20m) & 350bps (for mortgages of more than US$20m), in each case above 6-month US$ LIBOR

Withholding Taxes: Withholding tax will usually apply in relation to interest expenditures made by an Indian airline to a non-Indian lender. PDP Security: A key element of any PDP security suite is likely to be the security assignment by the airline to the sponsor of its relevant rights under the manufacturer purchase contract.

AIRCRAFT LEASING BY AIR INDIA

Leasing aircraft on loss-making routes cost Air India Rs. 4,234 crore : An investigation by Air India's internal vigilance department found the airline lost a staggering Rs. 4,234.28 crore between 2005 and 2010 because it leased 16 aircraft to enhance capacity on routes that were already making losses, documents obtained by The Hindu show

The investigation, whose findings were submitted for review by Air India's Board on November 29, 2011, shows the leasing losses accounted for a third of the airline's total losses of Rs. 13,835 crore.

Earlier, a report by the Comptroller and Auditor-General said the airline had also lost Rs. 68,000 crore because it committed itself to purchasing aircraft far beyond the recommendations of its own feasibility studies.

Air India officials declined to comment on the report. However, in a leaked communication to the Cabinet Secretary that became public earlier this month, the former Air India chief, Sunil Arora, alleged that key decisions had been colored by "unprecedented" interference by the former Civil Aviation Minister, Praful Patel.

In his May 28, 2005 letter, Mr. Arora said Air India's Board had been steamrollered into purchasing more jets than required. In some cases, Mr. Arora alleged, even seat configuration requirements had been changed to suit particular manufacturers. Indian Airlines, similarly, had been pulled out of profitable routes to make way for private operators.

Air India's Board, a briefing note on the investigation prepared for it states, was told a variety of reasons were assigned for leasing aircraft despite the negative returns on the routes, such as protecting slots at airports and maintaining schedule integrity. However, "no viability study was carried out of these futuristic issues vis-a-vis the loss that was going to be caused, which would justify taking the aircraft on dry lease at an estimated loss."

"From the actual operating results, it is seen that revenue earned by operating leased aircraft was about 50 per cent lesser than the revenues estimated in the Economic Viability Report," the report states.

"In a particular case," the note states, "[an] aircraft was taken on fresh dry lease five months before the lease period of the then operating dry leased aircraft came to a close, and that too when this route was making loss. Subsequently, operations on the same route were terminated."

The note also records that key documents on the decision-making process are missing.

Criticism to Aviation management: The concept Aircraft leasing is very efficient and successful for the aviation industry, but inspite of having so good mechanism due to mismanagement and lack of forecasting the aviation industry in India bears losses. The aviation industry should study the concept and nature of market before investment because aircraft leasing sector is very flexible concept it can give you good fruits if managed well and on the contrary can take it in huge loss if mismanaged.

CONCLUSION

The aircraft leasing & financing industry essentials to develop to a complete new level in India. Considering the prompt growth of the aviation industry, it is forecast that aircraft flotilla would nearly twofold in the coming years as India holds the rank of having the ninth largest aviation market in the world, showing the capability of international aviation traffic to reach a breath-taking value of 50 million & the domestic traffic reaching to more than three folds of international traffic. This would require more fleet than ever needed in the past, which can very efficiently be conceived by proper leasing & financing. Proper leasing & financing definitely requires extremely non-complicated procedures & solutions. The role of the Cape Town Convention & the Aircraft Protocol ratified by India has been of immense significance in ensuring security for both lessor & the lessee.

One very prominent reason for the lack of involvement from foreign investors to India & vice versa is the complexity of laws & policies governing the aircraft leasing in the country. Preservation of the domestic as well as international interest of parties by International Registration System is possible via enactment of the Cape Town Convention. Basic priority rule, which protects the right of first lessor or lessee, is applied. A few issues have still been left to the Contracting Parties, i.e. Court's decision upon any default committed by any party. This, & many other issues discussed previously in the paper have to be addressed if India is to become a prominent leader in aviation sector by executing flawless leasing & financing processes to feed the surge in requirement of aircraft in the coming years.

LEASING AND FINANCING OF AIRCRAFT: A CRITICAL ANALYSIS

Given the staggering costs of large commercial airplanes, even made more critical in the wake of the recent US subprime crisis, airlines around the world have adopted new methods of financing their acquisitions of aircraft. In recent years, leasing - a legal concept developed in the United States - has become more and more important in financing expensive capital goods globally. Although leasing does not yet play a vital role in most aircraft financing comparable to its importance in the United States, the general opinion and trend is that it is having increasing significance on the market. This is especially so with the latest trend of low-cost carriers taking the airline industry by storm. Aircraft are already considered as “classical leasing objects”.

It is in this light that this paper seeks to investigate the nature and role of different modern methods of aircraft financing. Particularly, this paper will focus on three forms of aircraft finance namely debt finance; cross border leasing and operating leasing. These have emerged on the face of redundancy of such traditional methods of aircraft finance such as secured lending and leasing with no cross border element. The value of these modern methods of aircraft finance as a financial tool will be explored with reference to their unique capabilities and pitfalls. The paper will describe the aforementioned methods of aircraft finance in a multi-jurisdictional perspective including their legal and tax aspects. The analysis will extend to international and regional conventions on aircraft finance. It will also include an examination of the future prospects, issues and impediments with respect to the use of these methods in the global arena as well as local markets.

Airlines wishing to expand their fleet may either go in for a lease or go in for an outright purchase of new aircraft if finance is available on attractive terms. A 'dry lease' includes only the aircraft whereas a 'wet lease' includes both aircraft and crew. The airlines are also charged for maintenance and insurance apart from the rentals.

A lease is beneficial for an airline as it can be treated as expenditure. On the other hand a plane is generally purchased on credit and therefore treated as debt. Thus a leased aircraft helps the airline raise debt for other expenditure. The popularity of lease over purchase has resulted in lease rentals jumping by over 20 per cent in the past one year.

Purchasing marks the progression from leasing to owning the aircraft. As most purchases are made on credit the airlines' ability to raise future capital is evaluated before closing the sale. For the airlines price is the most critical factor. Discounts are given based on order size, future prospects of the airline and the prospects for the aviation industry in the operating country. Next the airline needs to consider various options as far as raising of finance is concerned. Usually one per cent of the aircraft costs have to be paid upfront by the airline. Export credit agencies like EXIM Bank and European Credit Agencies (ECA) also provide credit guarantees for a maximum of 85 per cent of the purchase price. Commercial loans are also available but work out to be more expensive. The airline may also raise finance from Private Equity players to fund the purchase.

Two options are available to an airline wishing to purchase a plane. A 'hire-purchase' lease allows the aircraft to be owned through a special purpose vehicle. At the end of the term of the lease the airline owns the asset and the last payment is made in a lump sum.

Another option for purchasing is a sale-and-lease-back. The airline sells the aircraft to a leasing company, who then makes all the remaining payments. The leasing company leases the aircraft back to the airline and eventually becomes the owner of the aircraft.

<u>The Cape Town Convention: A New Era For Aircraft Financing</u>

On November 16, 2001, the Convention on International Interests in Mobile Equipment (Convention) and the Protocol thereto on Matters Specific to Aircraft Equipment (Protocol) were opened for signature following three weeks of intensive work at a diplomatic conference in Cape Town, South Africa. Twenty-two other countries signed the treaty and are in the ratification process. Much of the Cape Town Convention is still uncertain as to its application.

The Cape Town Convention was drafted under the auspices of the International Institute for the Unification of Private Law (Unidroit). It is primarily intended to extend the benefits of a consistent registration and lien recordation and enforcement system to jurisdictions other than the U.S. that have less clear legal systems for financing. It was strongly supported by the U.S. State Department and the Export-Import Bank which is giving favored rates for aircraft financings to jurisdictions that adopt the Cape Town Convention.

The purpose is to facilitate aircraft financings by bringing a consistent system of creditors' rights and remedies to ratifying nations that do not have legal systems as comprehensive as in the U.S. The Cape Town Convention itself deals only with financing terms, not purchase and sale terms. The Protocol applies the Cape Town Convention to aircraft purchases and sales as a necessary part of the International Registry system.

The Convention contains the basic aspects of a legal regime for secured financing of equipment and the Protocol, then, contains the specialized provisions necessary to adapt the Convention to the financing of aircraft and aircraft engines. The Convention is not intended to operate on a stand-alone basis; it can be effective only in conjunction with a protocol covering a specific type of equipment.

The Convention and Protocol establish an international legal system for security interests in aircraft equipment (called "international interests" in the Convention). The goal is to facilitate efficient secured financing. During the next several years, manufacturers of commercial aircraft equipment hope to sell-and airlines worldwide hope to buy-trillions of dollars' worth of products. Yet, the local legal regimes in many states are inadequate to support secured asset-based financing. In the absence of legal reform, fewer transactions will take place and those that are completed will feature higher costs of financing and in some cases will require the sovereign credit of states in which airlines are based. The researchers in this paper would like to highlight the issues pertaining various matters pertaining to the financing of an aircraft under the Convention and Protocol and provide the necessary reforms.

MODULE VI

AVIATION START-UPS: PRACTICAL AND LEGAL ISSUES

WHAT IS START-UP COMPANY?

A start-up company (start-up or start-up) is an entrepreneurial venture which is typically an emerging, fast growing business that aims to solve an unmet need by developing a viable business model around an innovative product, service, processor a platform. A start up is usually a company designed to effectively develop and validate a scalable business model. Start-ups may have high rates of failure, but the minority of successes includes companies that have become large and influential.

Evolution Start-up companies can come in all forms and sizes. Some of the critical tasks are to build a co-founding team to secure key or complementary skills, know-how, financial resources, and other elements to build the product for the target market. Typically, a start-up will begin by building a first minimum viable product (MVP), a prototype, to validate, assess and develop the new ideas or business concepts. In addition, start-ups founders do research to deepen their understanding of the ideas, technologies or business concepts and their commercial potential.

A Founders' agreement are often agreed early on to confirm the commitment, ownership and contributions of the founders and to deal with the intellectual properties and assets that may be generated by the start-up. A Shareholders' Agreement (SHA) is entered into between the founders and investors to confirm investment terms, rights of investors, exit clauses and any other important agreement terms. Business models for start-ups are generally found via a "bottom-up" or "top-down" approach. A company may cease to be a start-up as it passes various mile stones, such as becoming publicly traded on the stock market in an Initial Public Offering (IPO), or ceasing to exist as an independent entity via a merger or acquisition. Companies may also fail and cease to operate altogether, an outcome that is very likely for start-ups, given that they are developing disruptive innovations which may not function as expected and for which there may not be market demand, even when the product or service is finally developed.

Given that start-ups operate in high-risk sectors, it can also be hard to attract investors to support the product/ service development or attract buyers. A number of organisation and/or organised activities exist with Start-up activities. To name a few, Universities, Advisory and mentoring organizations Start-up incubators, Start-up accelerators, Co working spaces, Service providers(Consulting, Accounting, Legal, etc.), Event organizers, Start-up competitions, Startup Business Model Evaluators, Business Angel Networks, Venture capital companies, Equity Crowd funding portals, corporates (telcos, banking, health, food, etc.), other funding providers (loans, grants etc.), Start-up blogs and social networks and other facilitators.

START-UP INDIA POLICY

The "Startup India" initiative announced by the Hon'ble Prime Minister on 15.08.2015 aims at fostering entrepreneurship and promoting innovation by creating an ecosystem that is conducive to growth of Startup. Startup India is a flagship initiative of the Government of India, intended to build a strong ecosystem for nurturing innovation and

Startups in the country that will drive sustainable economic growth and generate large scale employment opportunities. The efforts of the government are aimed at empowering Startups to grow through innovation and design. It is intended to provide the much needed impetus for the Startups to launch and scale greater heights. In order to meet the objectives of the initiative, the Hon'ble Prime Minister on 16th January 2016 launched the Startup India Action Plan.

The Startup India Action Plan consists of 19 action items spanning across areas such as "Simplification and handholding." "Funding support and incentives" and "Industry-academia partnership and incubation". Since the launch of the programme, a number of forward looking strategic amendments to the existing policy ecology have been introduced, like:

1. Fund of Funds

For providing fund support for Start-up's, Government has created a „Funds for Startups (FFS) at Small Industries Development Bank of India (SIDBI) with a corpus of Rs 10,000 crore. The FFS shall contribute to the corpus of Alternative Investment funds (AIFs) for investing in equity and equity linked instruments of various Startups. The FFS is managed by Small Industries Development Bank of India (SIDBI) for which operational guidelines have been issued. In 2015- 16, Rs.500 crores was released towards the FFS corpus.

2. Credit Guarantee Fund for Start-ups

Since debt funding for Start-ups is perceived as high risk activity, a Credit Guarantee Fund for Startups is being setup with a budgetary corpus of Rs.500 crore per year, over the next four years, to provide credit guarantee cover to banks and lending institutions providing loans to Startups. Once rolled out, the scheme in the lines of credit guarantee scheme for MSME, is likely to provide a huge impetus for enabling flow of much needed credit to the Startups which may run into several thousands of crores.

3. Relaxed Norms in Public Procurement for Startups

Provision has been introduced in the procurement policy of Ministry of Micro, Small and Medium Enterprises (Policy Circular No. 1(2)(1)/2016-MA dated March 10, 2016) to relax norms pertaining to prior experience/ turnover for Micro and Small Enterprises. Department of Expenditure has issued a notification for relaxing public procurement norms in respect of all Startups (including medium enterprises) by all central Ministries/ Departments.

4. Tax Incentives

(i) Income Tax Exemption on profits under Section 80-IAC of Income Tax (IT) Act.

The Inter-Ministerial Board of Certification is a Board set up by Department for Promotion of Industry and Internal Trade (DPIIT) which validates Startups for granting tax related benefits. A DPIIT recognized Startup is eligible to apply to the Inter-

Ministerial Board for full deduction on the profits and gains from business (exemption under Section 80IAC of the Income Tax Act) provided the following conditions are fulfilled. The entity should be a private limited company or a limited liability partnership, Incorporated on or after 1st April 2016 but before 1st April 2021, and Products or services or processes are undifferentiated, have potential for commercialization and have significant incremental value for customers or workflow. The deduction is for any three consecutive years out of seven years from the year of incorporation of start-up.

(ii) Tax Exemption on Investments above Fair Market Value. –

DPIIT Recognized Startups are exempt from tax under Section 56(2)(viib) of the Income Tax Act when 212 EP-SBEC such a start- up receives any consideration for issue of shares which exceeds the Fair Market Value of such shares. – The startup has to file a duly signed declaration in Form 2 to DPIIT {as per notification G.S.R. 127 (E)} to claim the exemption from the provisions of Section 56(2)(viib) of the Income Tax Act.

(iii) Introduction of Section 54EE in the Income Tax Act, 1961.

Exemption from tax on long-term capital gain if such long-term capital gain is invested in a fund notified by Central Government. The maximum amount that can be invested is Rs. 50 lakh.

(iv) Amendment in Section 54GB of the Income-tax Act

Exemption from tax on capital gains arising out of sale of residential house or a residential plot of land if the amount of net consideration is invested in prescribed stake of equity shares of eligible Start-up for utilizing the same for purchase of specified asset:

a. The condition of minimum holding of 50% of share capital or voting rights in the start-up relaxed to 25%

b. The period of extension of capital gains arising from for sale of residential property for investment in start-ups has been extended up to 31st March 2021.

(v) Amendment in Section 79 of Income Tax Act.

Start-ups can carry forward their losses on satisfaction of any one of the following two conditions: a. Continuity of 51% shareholding/voting power or b. Continuity of 100% of original shareholder.

5. Legal Support and Fast-tracking Patent Examination at Lower Costs

A scheme for Startups IPR Protection (SIPP) for facilitating fast rack filing of Patents, Trademarks and Designs by Startups has been introduced. The scheme provides for expedited examination of patents filed by Startups. This will reduce the time taken in getting patents. The fee for filing of patents for Startups has also been reduced up to 80%.

6. Setting up Incubators

Under Atal innovation Mission, Niti Aayog will set up Atal Incubation Centres (AICs) in Public and Private sector. Niti Aayog has received 3658 applications (1719) from academic institutions and 1939 from non-academic institution) for setting up Atal Incubation Centres (AICs) from both Public and Private sector organizations. Under the Mission, a grant in aid of Rs.10 crore would be provided to scale up an existing incubator for a maximum of 5 years to cover the capital and operational costs in running the centre. Niti Aayog has received 233 applications for providing scale up support for established incubation centres.

7. Setting up of Startup Centres and Technology Business Incubators (TBIs)

14 Startup Centres and 15 Technology Business incubators are to be set up collaboratively by Ministry of Human Resource Development (MHRD) and the Department of Science and Technology (DST). Out of the 14 Startup Centres, 10 have been approved. Once MHRD releases its share of Rs.25 lakhs each for the Startup centres, the Startup centres would be supported by DST by December, 2016. Against the target of sanctioning 15 TBIs, 9 TBIs have been approved and other 6 TBIs, 9 TBIs have been approved and other 6 TBIs are under process of being approved.

8. Research Parks

7 Research Parks will be set up as per the Startup India Action Plan. Out of these 7 IIT Kharagpur already has a functional Research Park. Further, DST will establish 1 Research Park at IIT Gandhinagar and the remaining 5 shall be set up by Ministry of Human Resource development (MHRD) at IIT Guwahati, IIT Hyderabad, IIT Kanpur, IIT Kanpur, IIT Delhi and IISc Bangalore.

EXEMPTIONS FOR STARTUPS

To promote growth and help Indian economy, many benefits are being given to entrepreneurs establishing start-ups.

1. Simple process

Government of India has launched a mobile app and a website for easy registration for startups. Anyone interested in setting up a startup can fill up a simple form on the website and upload certain documents. The entire process is completely online.

2. Reduction in cost

The government also provides lists of facilitators of patents and trademarks. They will provide high quality Intellectual Property Right Services including fast examination of patents at lower fees. The government will bear all facilitator fees and the startup will bear only the statutory fees. They will enjoy 80%reduction in cost of filing patents.

3. Easy access to Funds

A10,000 crore rupees fund is set-up by government to provide funds to the startups as venture capital. The government is also giving guarantee to the lenders to encourage banks and other financial institutions for providing venture capital.

4. Tax holiday for 3 Years

Startups will be exempted from income tax for 3 years provided they get a certification from Inter-Ministerial Board (IMB).

5. Apply for tenders

Startups can apply for government tenders. They are exempted from the "prior experience/turnover" criteria applicable for normal companies answering to government tenders.

6. R&D facilities

Seven new Research Parks will be set up to provide facilities to startups in the R&D sector.

7. No time-consuming compliances

Various compliances have been simplified for startups to save time and money. Startups shall be allowed to self-certify compliance (through the Startup mobile app) with 9 labour and 3 environment laws.

8. Tax saving for investors

People investing their capital gains in the venture funds setup by government will get exemption from capital gains. This will help startups to attract more investors.

9. Choose your investor

The startups will have an option to choose between the VCs, giving them the liberty to choose their investors.

10. Easy exit

In case of exit, a start up can close its business within 90 days from the date of application of winding up

11. Meet other entrepreneurs

Government has proposed to hold 2 startup fests annually both nationally and internationally to enable the various stakeholders of a startup to meet. This will provide huge networking opportunities.

Tax Exemptions for the Startups, Effective from 2017-18

Following tax exemptions for the startups had been introduced that was made effective from 2017-18. The proposed incentives and exemptions are:

• Under Section 80-IAC, the Startup incorporated after April 1, 2016 is eligible for getting 100% tax rebate on profit for a period of three years. The startups recognized under the Startup India policy can now claim tax benefits in three out of the first seven years under Section 80-IAC of the Income-tax Act, 1961. Also, the annual turnover must not exceed Rs. 25 crores in any financial year up to 31 March 2021.

• The start-ups have to pay Minimum Alternate Tax [MAT] at 18.5% along with the applicable surcharge and cess. The FM has assured to provide MAT exemptions for the first 5 years in case the start-up fails to make any profit.

• Exemptions have been made against capital gains. Long term capital gains (LTCG) will be invested by the Government's special funds within a period of six months from the date of transfer of the asset. The investment may go up to INR 50 Lakh and the exemptions will be applied for three years. • If the individual holds 50% equity then the company may utilize the invested amount for buying assets before the due date of filing the return.

• The domestic companies who hold turnover less than INR 5 Crore in the FY 2014-15 will be liable for 29% tax along with surcharge and other cess. It will be covered under the chapter VI-A

• The Finance Minister has also proposed different taxes for the new domestic manufacturing companies that have been setup on or after 1st March, 2016. Such companies will be taxed at 25% plus with cess and surcharge. The tax is proposed on the condition that the company do not claim any incentive under profit or investment.

REGISTRATION STEPS

What form should your Start-up Venture have?

Formation of a Company in India

The law of companies in India is governed by the Indian Companies Act, 2013 which is a comprehensive legislation and provides for provisions relating to all phases of a company's life, i.e. incorporation, management, mergers, winding up, etc. A Registrar of Companies ('ROC') is appointed under the Act for designated regions, who is the nodal authority for affairs related to companies in that particular region.

Types of Companies in India

Any person can choose to incorporate either a company with unlimited liability or one with liability limited either by shares or guarantee.

An incorporated company may take one of the following three forms:

Private Company

With restrictions on transfer of shares, and limited number of members, a private limited company enjoys greater flexibility, less legal formalities, and the small shareholders body facilitates prompt decisions. A private company must have a minimum of two directors. A private company may be converted into a public company for raising capital from the public, if need arises, by completing certain legal formalities as specified in the Companies Act.

Public Company

Public companies are subject to stricter legal formalities. However, the free transferability of the shares of a public company and unlimited membership provides a larger base for raising of capital. Shares of a listed public company can be traded on stock exchange, which may open it to the scrutiny and watch of Securities and Exchange Board of India. A public company must have a minimum of seven members and three directors. Certain classes of public limited companies must have at least one third of the total number of directors as independent directors out of which one director has to be a woman director. Minimum authorized and paid up share capital requirement of a private and public company: The criteria of having minimum paid up share capital for both private public company, as stated in the erstwhile Companies Act, 1956, has been omitted in the revised Companies Act. This is a significant advantage to start-ups with respect to the requirement of maintaining minimum share capital under the Companies Act since inception.

One Person Company

This concept has been brought by the new Companies Act and states that One Person Company is in the nature of a private company which has only one person as its member/director At the time of incorporation, the memorandum of association must name a nominee for the sole member of an OPC. The minimum number of directors for an OPC is also one. OPC provides the option of limited personal liability of proprietors (as opposed to unlimited liability in sole proprietorship). Businesses which currently run under the proprietorship model could get converted into OPC's without any difficulty. The questions of consensus or majority opinions do not arise in case of OPCs, and is suitable for small entrepreneurs with low risk taking capacity.

Legal formalities for incorporation of a company

Pre-incorporation formalities:

The below mentioned compliances are required to be carried out with regard to setting up of company in India:-

a. Digital Signature Certificates ('DSC') for the proposed directors of the company by preparing and filing of Incorporation documents as required under the provisions of the Companies Act, 2013.

b. Any person (not having DIN) proposed to become a first director in a new company shall have to make an application through eForm SPICe. The applicant is required to attach the proof of Identity and address along with the application. DIN would be allocated to User only after approval of the form.

c. The next step is filing of online Incorporating a company through Simplified Proforma for Incorporating Company electronically (SPICe -INC-32), with eMoA (INC-33), eAOA (INC-34), is the default option and most companies are required to be incorporated through SPICe only.

d. However, Application for allotment of DINs to the proposed first Directors in respect of new companies shall be made in SPICe form only and any person intending to become a director in an existing company shall have to make an application in eForm DIR-3 for allotment of DIN.

e. The final step of the incorporation process and obtaining a certificate of incorporation of the company.

Post incorporation formalities:

Once the certificate of incorporation has been issued by ROC, the company becomes a separate legal entity in the eyes of laws in India, and requires certain basic registrations to initiate the business which includes filing of application for obtaining a permanent account number, tax deduction account number in the name of the company and any other business specific registrations from the relevant government authorities i.e. Import–Export Code Number in case of company carrying out the business of import and/or export. Further, every company shall be required to carry out certain compliances, as required under the provisions of the Companies Act, for their day to day activities which includes holding of first board meeting immediately after incorporation, convening the annual general meeting every year, maintaining all the secretarial records at the registered office of the company, maintaining of statutory registers, minutes books etc. of company in compliance with the Companies Act, 2013.

Following are the important points for a Start-up:

1. Choose the right legal structure for your start-up:

Choosing an appropriate legal structure is one of the most crucial decisions for any start-up. The decision should be taken based on individual circumstances and a host of factors such as nature/sector of business operation, business trajectory, regulatory and tax considerations, costs of formation and ongoing administration, external capital requirement and type of funding sought, of legal liability protection required, number of stakeholders, balance required between ownership and management, proposed mechanism for profit sharing or distribution amongst stakeholders, et al. Preferred entity structures for start-ups in India are limited liability partnership and private limited company.

2. Registrations and business licenses:

Post incorporation of a business entity in India, some necessary registrations are required and mandated by law. Any user who intends to incorporate company through SPICe eform can now also apply for GSTIN / Establishment code as issued by EPFO / Employer Code as issued by ESIC through this eform (INC-35).

Business licenses are permits issued by government authority that allow startups to start/continue to operate a particular business within its territorial jurisdiction lawfully. The nature of business activity determines most license requirements. Other determining factors may include the number of employees, location of business and the form of business ownership. Some examples are Food safety license, Health/Trade license, Shops & Establishment License etc.

3. Founder Equity –

Split and Vesting: Founder equity should be split amongst founders based on the nature of role played by each founder along with their time, effort and capital contribution to the start-up. Splitting founder equity equally by default without a through discussion on expectations and contribution generally leads to tension and unhappiness amongst founding teams as the start-up matures. Founder shares should be always subject to vesting schedule – typically over a period of three to four years. When vesting is imposed on a founder equity, the unvested shares held by the founder become subject to a contractual right to repurchase/transfer often at a nominal value, if one of the founders is terminated or voluntarily leaves the start-up. This is very important to ensure future viability of the business.

5. Founder agreements:

The founders agreement is the most valuable tool to establish the relationship between the founders of a startup. The agreement should represent a clear understanding between the founders on all key issues related to the startup. Founder agreements should clearly mention the roles and responsibilities of the founders and have clauses detailing the decision making and operating structure of the startup, founder equity split with vesting (explained above), assignment of all intellectual property in favour of the startup, termination of a promoter and exit process etc.

6. Employment contracts:

Startups must ensure to enter into clear employment contracts detailing terms and conditions of employment with their employees. While employment contracts are certainly valuable to the employees as it details terms regarding description of job profile, compensation and other associated benefits, a number of clauses may be inserted to safeguard and protect the interest of the startup – such as stopping employees from setting up competing entities (non- compete clause), poaching other employees/clients/customer (non-solicitation clause), preventing employees from claiming any intellectual property right on the work done/developed during the course of employment (assignment of intellectual property rights).

7. Employee Stock Option Pool (ESOP):

ESOP's are incentives given to employees/directors of a company to attract talent and retain employees by rewarding them. ESOPs create a sense of ownership amongst employees. It is important to note that ESOPs are not shares. They are structured in a way that they are option to buy shares at a discounted price and can be exercised only after a certain vesting period which is decided by the company granting the ESOPs.

8. Third Party Agreements:

Prior to entering into a third-party agreement and while negotiating the terms, it is advisable to execute a nondisclosure agreement. If creation/development of intellectual property is a component of such a third-party agreement, it must clearly state that all rights to the intellectual property rights shall vest and be owned by the startup and the third-party shall not stake any claim on the same and will do all acts to ensure the protection of the intellectual property. Clauses related to breach, termination and dispute resolution should be well negotiated and captured in all third-party agreements.

9. Investment structuring:

One of the most challenging and time consuming aspects of operating a startup is to raise capital for working capital requirement and growth. In India, Investors (HNIs/Angels/Funds) invest in early and growth stage companies in different structures and on varied terms. It is imperative for startups to seek proper legal advice while negotiating the deal terms for investment and the rights of the investors.

10. Compliance management:

Compliance and its importance is often overlooked by many startups. There are multiple laws applicable to specific entity structures under which separate event based and annual compliance is mandated. It is extremely critical for the sustainable growth of any business that the startup is in compliance with legal, secretarial, accounting, taxation, employee related and other associated compliances. The consequences of noncompliance can be levy of punitive fines on the startup.

SEED CAPITAL

Startup business needs the nurturing of finance to explore and grow. The funding done at the nascent stage is called seed funding and the capital is known as a seed capital. Technically, seed capital is the initial capital used at the time of starting the business. This capital can come from the founders, families or friends. It is required for the market research, product development, and other initial stage operations. Seed funding permits exploration of the business idea and converting it into a viable product or service that further attracts venture capitalists. A business founder must be clear on how to utilise seed capital in the most optimum manner to ensure smooth transition to the advanced stage of the business.

Seed funding is a risky investment option, as most funding agencies would like to adopt a wait and watch approach to see whether the idea has a business potential. From the founder's point of view, the option of obtaining seed funding has to be carefully utilised as obtaining seed funding may result in dilution of ownership of the founder. The paperwork involved in seed funding is relatively less and straightforward, compared to advanced rounds of funding. Even the legal fees required are also quite less as compared to the seed equity. The interest rates too are usually lower and there are mostly no restrictions in the manner of business working as it is still in the nascent stage.

Financing is generally of two types i.e.

(a) Equity financing; or

(b) Debt-financing.

A. EQUITY FINANCING

Startups are usually equity financed/funded by way of a venture capital/ private equity investors and/or angel investors.

(i) Venture Capitalist/Private Equity
Venture capital ("VC") / Private Equity ("PE") is often the first large investment a startup can expect to receive. Convertible instruments are usually the preferred option and most commonly used securities for VC/PE investment which includes compulsory convertible preference shares and compulsory convertible debentures. The investor and startup will normally enter into a non-binding offer based on the preliminary valuation of the startup usually followed with a financial, legal and technical due diligence on the startup as required by the investors.

Funding Procedure

A Term Sheet / Letter of Intent /Memorandum of understanding is entered into, setting out the following:

▪ basic commercial understanding between the VC and the startup; and

▪ legal terms for the agreements to follow the due-diligence;

(b) The contracting parties will enter into a Share Subscription Agreement/ Debenture Subscription Agreement.

It usually captures the following:

▪ The issuance of shares in the share capital or debentures at subscription amount determined based on the valuation of the startup;

▪ Condition precedents to completion of transaction or conditions subsequent to be completed within the agreed time frame after the completion date;

▪ sets of representation and warranties and indemnification resulting from due-diligence exercise or otherwise, etc.

(c) Thereafter, the contracting parties may enter into a Shareholders' Agreement providing for the following:

▪ Nomination/representation rights on the board of investee;

▪ Information and reporting right and disclosure obligation of investee to the investors;

▪ Redemption rights on debenture or preference shares;

▪ Pre-emption rights, Right of First Refusal or Right of First Offer, Tag Along Right, Drag Along Rights, Lock-in-period for the investor or promoter's holding, put and call options, affirmative vote rights on certain reserved matters, anti-dilution provisions;

▪ Exit options to investors after the lock-in-period; etc.

(d) Issuance of Securities through Private Placement process;

(e) Filing of necessary eForms with ROC for completing the process of issuance and allotment of securities.

(f) Amendment of AOA as per Shareholders' Agreement;

(g) Completion of Condition Subsequents;

(ii) Angel Investors

Angel investors are usually individuals or a group of industry professionals who are willing to fund the venture in return for an equity stake. Under the SEBI (Alternative Investment Funds) Regulations, 2012 which was subsequently amended in 2013, SEBI has made the following restrictions applicable to angel funds investing in an Indian company:

a. An investee company has to be within 3 years of its incorporation, not listed on the floor of a stock exchange, and should have a turnover of less than INR 250 million and not be promoted by or related to an industrial group (with group turnover exceeding INR 3 billion).

b. The deal size is required to be between INR 5 million and INR 50 million.

Separately, it is required that an investment shall be held for a period of at least 3 years.

Bridge Round

Series Funding

After Seed Funding Round or Angel Funding Round and Bridge Funding Round, Series Funding Round will start like Series A to Z. Series preferred stock is the first round of stock offered during the seed or early stage round by a portfolio company to the venture capital investor. Series preferred stock is often convertible into common stock in certain cases such as an Initial public offering (IPO) or the sale of the company.

Series rounds are traditionally a critical stage in the funding of new companies. A typical series A round is in the range of $2 million to $10 million, purchasing 10% to 30% of the company. The capital raised during a series round is usually intended to capitalize the company for 6 months to 2 years as it develops its products, performs initial marketing and branding, hires its initial employees, and otherwise undertakes early stage business operations:

Sources of capital

Because there are no public exchanges listing their securities, private companies meet venture capital firms and other private equity investors in several ways, including warm referrals from the investors' trusted sources and other business contacts; investor conferences and demo days where companies pitch directly to investor groups. As equity crowd funding becomes more established, startups are increasingly raising part of their Series round online using platforms such as Onevest or Seed Invest in the USA and Seedrs in the UK, VCCircle, Private Circle, Lets Vanture and Tracxn Labs, etc. in India. These blended rounds include a mix of angel investors, strategic investors and customers alongside the offline venture capital investors.

B. Debt Financing

i. Loan from Banks & NBFCs

Loans from banks and NBFCs help finance the purchase of inventory and equipment, besides securing operating capital and funds for expansion. More importantly, unlike a VC or angels, which have an equity stake, banks do not seek ownership in your venture. However, there are several drawbacks of such funding option. Not only do you pay interest on loan but it also has to be done on time irrespective of how your business is faring. They require substantial collateral and a good track record, besides the fulfilment of other terms and conditions and a lot of documentation as follows: a. Application for loan sanction by borrowers;

b. Issue of sanction letter by the Bank;

c. Agreement of Loan;

d. Security/collateral documentation, such as

(i) Deed of Mortgage;

(ii) Deed of Hypothecation;

Iii Deed of guarantee;

(iv)Share pledge agreement;

(v) Memorandum of Entry; etc.

ii. External Commercial Borrowings

External Commercial Borrowings (ECB) in form of bank loans, buyers' credit, suppliers' credit, securitized instruments (e.g. non-convertible, optionally convertible or partially convertible preference shares, floating rate notes and fixed rate bonds) can also be availed from non-resident lenders to fund the business requirement of a company. ECB can be accessed under two routes, viz., (i) Automatic Route; and

(ii) Approval Route depending upon the category of eligible borrower and recognized lender, amount of ECB availed, average maturity period and other applicable factors.

iii. CGTMSE Loans

Under the Credit Guarantee Trust for Micro and Small Enterprises scheme launched by Ministry of Micro, Small & Medium Enterprises (MSME), Government of India to encourage entrepreneurs, one can get loans of up to 1 crore without collateral or surety. Any new and existing micro and small enterprise can take the loan under the scheme from all scheduled commercial banks and specified Regional Rural Banks, NSIC, NEDFi, and SIDBI, which have signed an agreement with the Credit Guarantee Trust.

C. Start-ups and Stability

During the IPO, the Company raises funds by offering and issuing equity shares to the public. An IPO allows a company to tap a wide pool of stock market investors to provide it with large volumes of capital for future growth. The existing shareholding will get diluted as a proportion of the company's shares. However, existing capital investment will make the existing shareholdings more valuable in absolute terms. Companies can also issue of American Depository Receipts ("ADRs") or Global Depository Receipts ("GDRs") to raise funds from international stock investors. The promoter has certain obligations such as (a) meeting minimum contribution requirements; and (b) is generally subject to a 3 year lock-in once the IPO is concluded. Various parties such as investment bankers, underwriters and lawyers need to be engaged as part of the procedure of IPO.

D. **Unconventional modes of financing options which are now becoming popular in India**

i. Crowd Funding

This is recent phenomena being practiced for getting seed funding through small amounts collected from a large number of people (crowd), usually through the Internet. Now we have companies existing in India which are specializing in "Crowd Funding". The entrepreneur can get money for his venture by showcasing his idea before a large group of people and trying to convince people of its utility and success. The entrepreneur needs to put up on a portal his profile and presentation, which should include the business idea, its impact, and the rewards and returns for investors. It should be supported by suitable images and videos of the project. SEBI in 2014, even rolled out a 'Consultation Paper on Crowd funding in India' proposing a framework in the form of Crowd funding to allow startups and SMEs to raise early stage capital in relatively small sums from a broad investor base.

ii. Incubators

These set-ups precede the seed funding stage and help the entrepreneur develop a business idea or make a prototype by providing resources and services in exchange for an equity stake ranging from 2-10%. Incubators offer office space, administrative support, legal compliances, management training, mentoring and access to industry experts as well as to funding through angel investors or VCs.

MUDRA BANKS

Micro Units Development and Refinance Agency Bank (or MUDRA Bank) is a public sector financial institution in India. It provides loans at low rates to micro-finance institutions and non-banking financial institutions which then provide credit to MSMEs. It was launched by Prime Minister Narendra Modi on 8 April 2015. It will provide its services to small entrepreneurs outside the service area of regular banks, by using last mile agents. About 5.77crore (57.6million) small business have been identified as target clients using the NSSO survey of 2013. Only 4% of these businesses get finance from regular banks. The bank will also ensure that its clients do not fall into indebtedness and will lend responsibly. The bank will classify its clients into three categories and the maximum allowed loan sums will be based on the category:

Shishu: Allowed loans up to Rs.50,000 (US$780) Kishore: Allowed loans up to Rs.5 lakh (US$7,800) Tarun: Allowed loans up to Rs.10 lakh (US$16,000)

Those eligible to borrow from MUDRA bank are:

• Small manufacturing unit

• Shopkeepers

• Fruit and vegetable vendors

• Artisans

The basic criteria of age should be 18 years old. Loan under the scheme of the Pradhan Mantri Mudra Bank Loan will be available if and only if it is for commercial and business purposes and not for personal purposes. At the most, borrower can buy vehicle from mudra loan, given that it is used for commercial purposes. Lastly, this loan is for new business and is only applicable for small business owners.

STRATEGIES FOR PROTECTION AND EXPLOITATION OF INTELLECTUAL PROPERTY RIGHHTS (IPR) FOR STARTUPS

Trade secrets include any confidential business information which provides an enterprise a competitive edge over others. Trade secrets encompass manufacturing or industrial secrets and commercial secrets, formula, practice, process, design, instrument, pattern, commercial method, or compilation of information which is not generally known or reasonably ascertainable by other.

The unauthorized use of such information by persons other than the holder is regarded as an unfair practice and a violation of the trade secret. There are no specific statutes under the Indian law for the protection of trade secrets and the same are protectable under the common law rights.

1. **Make Intellectual Property protection a priority:** Start-ups cannot afford the complete protection available under the intellectual property regime. The first step for any startup is to evaluate and prioritize the IP Rights involved in its business. Depending upon the type of industry involved, IP Rights play an important role. Failure to identify or prioritize IP Rights, is likely to create problems for startup's business, especially during negotiations with future investors or exiting its business. Sometimes IP Rights are the only asset available with a startup.
2. **Register Intellectual Property Rights:** It is important to note that certain IP Rights like patents and designs are required to be registered before claiming any protection under the respective statutes. On the other hand, certain IP Rights like trademark and copyright need not be mandatorily registered for protection under. Nevertheless, a registered IP Right carries a greater value and acts as evidence of use of the IP Rights before courts as well as enforcement agencies;
3. **Due Diligence of IP Rights:** For any startup, it is indispensable that it does not violate IP Rights of any other person. This will ensure safety from unwarranted litigation or legal action which can thwart its business activities. This makes it even more important for startups to make careful IP decisions in the initial phase and conduct proper due diligence of IP Rights, which it is using or intends to use.
4. **Implement clear and effective policies and strategies for protection of IP Rights:** It is in the long term interest of startups to have an Intellectual Property Policy for management of various IP rights which may be presently owned, created or acquired in future by startups. The aim of such a policy is to ensure that there are no inter-se dispute between the promoters of the startups, which remains till date to be one of the main concerns for failure of startups.

5. **Agreements related to Intellectual Property:** It is pertinent to note that having proper documentation in the form of agreements like non-disclosure agreements, agreements with employees or independent contractors, can make all the difference between the success and failure of startups. Usually, intellectual property is created either by the founders or some key employee or a third party. The intellectual property so created, must be protected through a proper agreement between the founder or key employee or a third party, as the case may be and the startup. If the agreement, with founders or employees or a third party, , under which a novel idea was/is created, is overlooked, it could create bottlenecks later after such idea becomes successful. Accordingly, the startups need to ensure that anything created on behalf of the startup, belongs to the startup and not the Employee or a third party. Further, it is advisable to enter into elaborate assignments, licensing or user agreements, and care should be taken to make provisions for all post termination IP Right issues.

FOREIGN EXCHANGE MANAGEMENT ACT, 1999

Section 6 of the Foreign Exchange Management Act, 1999 provides powers to the Reserve Bank to specify, in consultation with the Government of India, the classes of permissible capital account transactions and limits up to which foreign exchange is admissible for such transactions. Section 6(3) of the aforesaid Act provides powers to the Reserve Bank to prohibit, restrict or regulate various transactions referred to in the sub-clauses of that sub-section, by making Regulations. In exercise of the above powers conferred under the Act, the Reserve Bank has in supersession of the earlier Notification No.FEMA19/RB-2000 dated 3rd May 2000 and subsequent amendments thereto, issued Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2004 vide Notification No. FEMA.120/RB-2004 dated July 7, 2004.

The Notification seeks to regulate acquisition and transfer of a foreign security by a person resident in India i.e.

• Investment (or financial commitment) by Indian entities in overseas joint ventures and wholly owned subsidiaries as also investment by a person resident in India in shares and securities issued outside India.

• Overseas Investment (or financial commitment) can be made under two routes viz.

(i) Automatic Route and
(ii) Approval Route.

Reporting requirement under Master Direction – Reporting under Foreign Exchange Management Act, 1999

Overseas Direct Investment (ODI) Overseas investments (or financial commitment) in Joint Ventures (JV) and Wholly Owned Subsidiaries (WOS) (Part VIII) have been recognised as important avenues for promoting global business by Indian entrepreneurs.

The reporting formalities are as provided in Master Direction – Reporting under Foreign Exchange Management Act, 1999 are as under:

1. Form ODI (Annex I): An Indian Party and a Resident Individual making an overseas investment is required to submit form ODI.

2. The structure of the Form ODI comprise the following parts:

Part I – Application for allotment of Unique Identification Number (UIN) and reporting of Remittances / Transactions:

Section A – Details of the IP / RI.

Section B – Capital Structure and other details of JV/ WOS/ SDS.

Section C - Details of Transaction/ Remittance/ Financial Commitment of IP/ RI.

Section D – Declaration by the IP/ RI.

Section E – Certificate by the statutory auditors of the IP/ self-certification by RI.

Part II - Annual Performance Report (APR)

Part III – Report on Disinvestment by way of a) Closure / Voluntary Liquidation / Winding up/ Merger/ Amalgamation of overseas JV / WOS;

b) Sale/ Transfer of the shares of the overseas JV/ WOS to another eligible resident or non-resident;

c) Closure / Voluntary Liquidation / Winding up/ Merger/ Amalgamation of IP; and

d) Buy back of shares by the overseas JV/ WOS of the IP / RI. 3.

An annual return on Foreign Liabilities and Assets (FLA) is required to be submitted directly by all the Indian companies which have made FDI abroad (i.e. overseas investment) in the previous year(s) including the current year, to the Director, External Liabilities and Assets Statistics Division, Department of Statistics and Information Management (DSIM), Reserve Bank of India. The form can be duly filled in, validated and sent by e-mail, by July 15 every year.

4. Further, a new reporting format has also been introduced for Venture Capital Fund (VCF) / Alternate Investment Fund (AIF), Portfolio Investment and overseas investment by Mutual Funds as per the format in Annex II and Annex III of the Master Direction.

5. In case of reporting purchase and repurchase of ESOPs, the AD banks may continue to report the same in the existing format (Annex IV).

a) Annual Statement shares allotted to Indian employees/ Directors under ESOP Schemes:

This statement is required to be submitted to the Central Office of the Reserve Bank of India by the Indian Company through its AD bank.

b) Annual Statement of shares repurchased by the issuing foreign company from Indian employees/ Directors under ESOP Schemes : This statement is required to be submitted to the Central Office of the Reserve Bank of India by the Indian Company through its AD bank. Any post investment changes subsequent to the allotment of the UIN are required to be reported as indicated in the operational instructions on submission of Form ODI Part I (Annex I).

7. In case of RI undertaking ODI, certification of Form ODI Part I by statutory auditor or chartered accountant need not be insisted upon. Self-certification by the Resident Individual concerned may be accepted.

Foreign Direct Investment (FDI) in Start-up Companies

Start-ups can issue equity or equity linked instruments or debt instruments to FVCI against receipt of foreign remittance, as per the FEMA Regulation.

In addition, start-ups can issue convertible notes to person resident outside India subject to the following conditions:

1. A person resident outside India (other than an individual who is citizen of Pakistan or Bangladesh or an entity which is registered/incorporated in Pakistan or Bangladesh), may purchase convertible notes issued by an Indian startup company for an amount of twenty five lakh rupees or more in a single tranche. 'Startup Company' means a private company incorporated under the Companies Act, 2013 or Companies Act, 1956 and recognised as such in accordance with notification issued by the Department of Industrial Policy and Promotion (Now, Department for Promotion of Industry and Internal Trade), Ministry of Commerce and Industry, and as amended from time to time.

2. A startup company engaged in a sector where foreign investment requires Government approval may issue convertible notes to a non-resident only with approval of the Government.

3. A startup company issuing convertible notes to a person resident outside India shall receive the amount of consideration by inward remittance through banking channels or by debit to the NRE / FCNR (B) / Escrow account maintained by the person concerned in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016, as amended from time to time. However an escrow account for the above purpose shall be closed immediately after the requirements are completed or within a period of six months, whichever is earlier. However, in no case continuance of such escrow account shall be permitted beyond a period of six months.

4. NRIs may acquire convertible notes on non-repatriation basis.

5. A person resident outside India may acquire or transfer, by way of sale, convertible notes, from or to, a person resident in or outside India, provided the transfer takes place in accordance with the pricing guidelines as prescribed by RBI. Prior approval from the Government shall be obtained for such transfers in case the startup company is engaged in a sector which requires Government approval.

6. The startup company issuing convertible notes shall be required to furnish reports as prescribed by Reserve Bank of India.

ENTRY ROUTES FOR INVESTMENT

An Indian company may receive Foreign Direct Investment under the two routes as given under:

Automatic Route

FDI is allowed under the automatic route without prior approval either of the Government or the Reserve Bank of India in all activities/sectors as specified in the consolidated FDI Policy, issued by the Government of India from time to time. 80 EP-EB&CL Government Route FDI in activities not covered under the automatic route requires prior approval of the Government. Proposals for foreign investment under Government route, are considered by respective Administrative Ministry/Department. Foreign investment in sectors/activities under government approval route will be subject to government approval where:

(i) An Indian company is being established with foreign investment and is not owned by a resident entity or

(ii) An Indian company is being established with foreign investment and is not controlled by a resident entity or

(iii) The control of an existing Indian company, currently owned or controlled by resident Indian citizens and Indian companies, which are owned or controlled by resident Indian citizens, will be/is being transferred/ passed on to a non-resident entity as a consequence of transfer of shares and/or fresh issue of shares to non-resident entities through amalgamation, merger/demerger, acquisition etc. or

(iv) The ownership of an existing Indian company, currently owned or controlled by resident Indian citizens and Indian companies, which are owned or controlled by resident Indian citizens, will be/is being transferred/passed on to a non-resident entity as a consequence of transfer of shares and/or fresh issue of shares to non-resident entities through amalgamation, merger/demerger, acquisition etc.

(v) It is clarified that Foreign investment shall include all types of foreign investments, direct and indirect, regardless of whether the said investments have been made under Schedule 1 (FDI), 2 (FII), 2A (FPI), 3 (NRI), 6 (FVCI), 9 (LLPs), 10 (DRs) and 11(Investment Vehicles) of FEMA (Transfer or Issue of Security by Persons Resident

Outside India) Regulations. FCCBs and DRs having underlying of instruments which can be issued under Schedule 5, being in the nature of debt, shall not be treated as foreign investment. However, any equity holding by a person resident outside India resulting from conversion of any debt instrument under any arrangement shall be reckoned as foreign investment.

(vi) Investment by NRIs under Schedule 4 of FEMA (Transfer or Issue of Security by Persons Resident outside India) Regulations will be deemed to be domestic investment at par with the investment made by residents.

(vii) A company, trust and partnership firm incorporated outside India and owned and controlled by non-resident Indians will be eligible for investments under Schedule 4 of FEMA (Transfer or issue of Security by Persons Resident Outside India) Regulations and such investment will also be deemed domestic investment at par with the investment made by residents.

FDI Policy on Aviation Sector

Airport (Greenfield projects)	100%	Automatic
Airport (Existing projects)	100%	Automatic
Scheduled Air Transport Service/ Domestic Scheduled Passenger Airline	100%	Automatic up to 49% (Automatic up to 100% for NRIs) Government route beyond 49%
Regional Air Transport Service	100%	Automatic up to 49% (Automatic up to 100% for NRIs) Government route beyond 49%
Non-Scheduled Air Transport Services	100%	Automatic
Helicopter services/seaplane services requiring DGCA approval	100%	Automatic
Ground Handling Services subject to sectoral regulations and security clearance.	100%	Automatic
Maintenance and Repair organizations; flying training institutes; and technical training institutions.	100%	Automatic

PROHIBITED SECTORS

START-UPS AND LABOUR LEGISLATIONS

Genesis of application of Labor Laws to Start-ups

Over the past decade, India has seen a rapid growth of vibrant new start-ups in different sectors, where young entrepreneurs are dominating the start-up scene with their new age and innovative businesses. Though these ideas as well as the promoters are of new age, all the business enterprises in India have to comply with a wide variety of laws and statutes, especially labour laws, that specifically deal with the employer-employee relationship, compensations, working conditions, medical benefits, discrimination and retirement benefits. One of the many challenges faced by any entrepreneur or organization is the prevalence of year old laws governing labour employment such as benefits and terminations, even though the working culture and economy has progressed with time. While most of the legislations have undergone amendments as per to suit the convenience of present day businesses, for example Companies Act 2013, there still exists a need for a labour law framework which shall be suitable for present day start-ups and MSMEs.

Due to decentralization of power in India, there are various Central and State level labour and employment legislations which govern the conditions of employment, social security, health, safety, welfare, wages, trade unions and industrial disputes, etc. Many of these statutes become applicable only upon fulfilment of prescribed thresholds, such as number of employees in the organisation, wages of an employee(s), etc, while other legislations may be applicable only to specific/specified industries or to certain types of employees. This implies that a start-up needs to be on a constant vigil regarding the compliance with the central and the state legislations, including the stage at which any one or more statutes may become applicable. Some non-compliances may pose a limited financial risk as well as loss of goodwill and may become a source of continuous inconvenience due to inspections by the concerned authorities and actions as a result thereof.

Another important problem that poses inconvenience to start-ups is the lack of uniformity in some of the common terms used across different labour and employment legislations applicable to an organisation. For example, a large number of labour legislations have different applicability criteria, definition of 'employee', definition of 'wages' and also what is included and excluded from the wages and manner of calculation of wages. Further, some of the basic aspects, such as the components that need to be taken into consideration while computing wages for the purposes of identifying provident fund contributions, could be different from components taken into account while accounting bonus entitlement of an employee, etc.

Another issue that arises is with respect to the relationship matters of an enterprise. Currently, most of the start-ups not only hire employees on their payrolls, but until they are certain of their growth and business needs, also use independent consultants, direct or indirect contract employees and various other vendors, etc., to meet with their manpower needs. In absence of labour laws governing and addressing each manpower arrangement, enterprises will depend upon professional guidance to ensure that any such arrangement does not expose it to the risk of claims or demands of compensation or/and permanent employment. Thus, there is an urgent need for laws that allow start-ups to agree short or long-term arrangements or engagements with individuals, without being worried about the possibility of such individuals making burdensome demands.

Recent Developments in the compliance framework for the Start-ups

Recommendations for relaxation of compliance requirements

In 2016, the Ministry of Labour and Employment issued an advisory to all states, union territories and the central labour authorities recommending that there could be implemented a compliance regime for start-ups based on self-certification under different labour legislations.[15] Further, there would also be restrictions imposed on inspections that could happen under such labour laws. This initiative of the Government has been aimed at promoting the development of start-up companies in India and incentivizing entrepreneurship.

[15] PRESS INFORMATION BUREAU, GOVERNMENT OF INDIA, Notification dated 25 April 2016, Available at – *https://www.pib.nic.in/newsite/PrintRelease.aspx?relid=14119*.

Laws applicable to a start-up

Statute	Scope & Application
Factories Act, 1948	**Factories Act embodies the law relating to regulation of labour in factories. It prescribes the terms of health, safety, working hours, benefits, overtime ad leave. This Act has been enforced by state governments in accordance with the state specific rules as framed under the Factories Act.**
Shops and Commercial Establishments Acts	**These are state specific statutes, regulating the conditions of work and employment in shops, commercial establishments, residential hotels, restaurants, eating houses, theatres, places of public amusement/ entertainment and other establishments located within the state. These statutes prescribe the minimum condition of services and benefits for employees, including working hours, rest intervals, holidays, overtime, holidays, leave, termination of service, rights and obligations of an employer and employees, etc.**
Payment of Wages Act, 1936	**The Act regulates the conditions of payments of wages and is applicable to factories, railways, tramways, motor transport services, docks, wharves, jetty, inland vessels, mines, quarries and oil fields, workshops, establishments involved in construction work and other establishments as notified by the appropriate state governments.**
Maternity Benefit Act, 1961	**The Act prescribes conditions of employment for women employees, before and after childbirth and also provides for maternity benefits along with other benefits. The Act is applicable to** all shops and establishments in which 10 or more persons are employed; and factories, mines, plantations and circus.
Sexual Harassment of Women at Workplace (Prevention, Prohibition and Redressal) Act, 2013	**This Act aims to provide protection to women against sexual harassment at the workplace and prescribes guidelines to be adhered by the employers and employees for the prevention and redressal of complaints of sexual harassment. The Act applies to both organized and unorganized sector, including government bodies, public and private sector organizations, non-governmental organizations and organizations carrying on commercial, vocational, educational, etc. activities. It also applies to all the places visited by the employee during the course of employment or for reason arising out of employment.**
Minimum Wages Act, 1948	**The Act provides for fixing and revision of minimum wage rates by the respective state governments periodically for both organized and unorganized sectors.**
Payment of	**Thee Act provides for payment of bonuses under certain defined**

Bonus Act, 1965	**circumstance, thereby enabling the employees to share the profits earned by the establishment. The Act applies to every factory and establishment in which 20 or more persons are employed on any day during an accounting year.**

<u>Labour Laws exempting Start-ups</u>

Since the labour and environment law compliances are time consuming and cumbersome in nature and that the start-ups are often caught unaware as to the issues pertaining to such laws, the Government has proposed a self-certification mechanism for certain compliances as mentioned before. Under this initiative the Government has set up a mobile application as well as a dedicated web portal where start- ups can complete this self-certification process. After the self-certification process, it is proposed that there will be no inspection for a period of 3 years, unless instances of specific violations are reported. Even in such a case, prior approval from a senior officer would be required for any inspection.

Following are the labour laws legislations from which the start-ups are exempted from-

Statute	**Scope and Application**
Industrial Employment (Standing Orders) Act, 1946	**The Act is applicable to factories, railways, mines, quarries and oil fields, tramway or motor, omnibus services, docks, wharves and jetties, inland steam vessels, plantations and workshops, where 100 or more persons are employed. It mandates every employer to lay down clear terms and conditions of service which is to be certified by the concerned labour department and thereafter enacted.**
Trade Unions Act, 1926	**Trade Unions Act provides for the registration of trade unions and lays down the law relating to registered trade unions.**
Industrial Disputes Act, 1947	**The Industrial Disputes Act prescribes and governs the mechanism of collective bargaining and dispute resolution between employer and employees. The Act contains provisions related to unfair labour practices, strikes, lock-outs, lay-offs, retrenchment, transfer of undertakings and closure of business.**
Employees' State Insurance Act, 1948	**The Act applies to all factories, industrial and commercial establishments, hotels, restaurants, cinemas and shops. Employees drawing wages below Rs. 15,000 per month are eligible for benefits under the Act. The Act provides for benefits in cases of sickness, maternity and employment injury and certain other related matters.**
Employees' Provident Funds and Miscella-neous Provisions	**It is an important social security legislation, providing for an institution of provident funds, pension fund and deposit-linked insurance fund for employees in factories and other prescribed establishments. The Act applies to establishments having at least**

Act, 1952	**20 employees, the basic salary of the employee should be less than Rs. 15,000 per month or who has an existing provident fund membership based on previous employment arrangement.**
The Payment of Gratuity Act, 1972	**The Act is applicable to every factory, mine, oil field, plantation, port, railway company, shop and commercial establishment where 10 or more persons are employed or were employed on any day of the preceding 12 months. Employees are entitled to receive gratuity upon cessation of employment, irrespective of the mode of cessation. The eligible employee should have completed a 'continuous service' of at least 5 years (interpreted to mean 4 years and 240 days) at the time of employment cessation.**
Building and Other Construction Workers (Regulation of Employment and Conditions of Service) Act, 1996	**The Act applies to establishments employing 10 or more building workers in any building/ construction work and regulates the conditions of employment and service of the workers and imposes obligations on the employer, with respect to health, safety and welfare of the construction workers.**
Contract Labour (Regulation and Abolition) Act, 1970	**The Act applies to all** establishments employing 20 or more persons (or that have employed 20 or more persons) on any day of the preceding 12 months and contractors employing (or have employed) 20 or more workmen on any day of the preceding 12 months. The Act regulates **the conditions of employment of contract labour, the duties of a contractor and principal employer and provides for abolition of contract labour in certain circumstances.** It **does not govern establishments where work of a casual or intermittent nature is carried out.**
Inter-State Migrant Workmen (Regulation of Employment & Conditions of Service) Act 1996	The Act applies to all "establishments" that have been defined under section 2(1)(d) of the Act. It prohibits the employment of inter-state migrant workers in the establishment without having registered the establishment and prescribes protection to level the playing field between local workers and migrant workers.

ENVIRONMENTAL LAW RELATED TO START-UPS

With the recognition of Right to Healthy Environment as a human right under the Universal Declaration of Human Rights and its related covenants, measures are taken at full force to enforce these rights and guard the right to environment at parity. With the endowed protection to environment under the Constitution and Specific Statutes, all the person as be it natural or legal including a Company owes a duty to conduct themselves in such a manner that their act or omission should not pollute the environment. Therefore, a company is necessitated to abide by various laws in order to protect the environment.

Water (Prevention and Control of Pollution) Act, 1974

The Water Prevention and Control of Pollution Act, 1974 (the "Water Act") has been enacted to provide for the prevention and control of water pollution and to maintain or restore wholesomeness of water in the country. It further provides for the establishment of Boards for the prevention and control of water pollution with a view to carry out the aforesaid purposes. The Water Act prohibits the discharge of pollutants into water bodies beyond a given standard, and lays down penalties for non-compliance. At the Centre, the Water Act has set up the CPCB which lays down standards for the prevention and control of water pollution. At the State level, SPCBs function under the direction of the CPCB and the State Government. Further, the Water (Prevention and Control of Pollution) Cess Act was enacted in 1977 to provide for the levy and collection of a cess on water consumed by persons operating and carrying on certain types of industrial activities. This cess is collected with a view to augment the resources of the Central Board and the State Boards for the prevention and control of water pollution constituted under the Water (Prevention and Control of Pollution) Act, 1974.

The Act was last amended in 2003.

It necessitate to:

• Provide information to the SPCB

• Provide access to the SPCB for taking samples

• Allow entry to the SPCB to ascertain that the provisions of the Act are being compiled with. Responsibilities:

• Obtain "Consent to Establish"

• Obtain "Consent to Operate"

• Apply for renewal of the "Consent to Operate" before the expiry of validity period

• Consent to be deemed as granted automatically and unconditionally after four months from the date of application already given or refused before this period

• Refusal of "Consent" to be recorded in writing

• Pay Water Cess as indicated in the assessment order

• Affix water meters of the prescribed standards

• Provide access to SPCB

• Pay interest in case of delay in paying the Water Cess

• Pay penalty for non-payment of Cess

• Industry is entitled to 25% rebate if meeting certain conditions

AIR (PREVENTION AND CONTROL OF POLLUTION) ACT, 1981

The Air (Prevention and Control of Pollution) Act, 1981 (the “Air Act”) is an act to provide for the prevention, control and abatement of air pollution and for the establishment of Boards at the Central and State levels with a view to carrying out the aforesaid purposes. To counter the problems associated with air pollution, ambient air quality standards were established under the Air Act. The Air Act seeks to combat air pollution by prohibiting the use of polluting fuels and substances, as well as by regulating appliances that give rise to air pollution. The Air Act empowers the State Government, after consultation with the SPCBs, to declare any area or areas within the State as air pollution control area or areas. Under the Act, establishing or operating any industrial plant in the pollution control area requires consent from SPCBs. SPCBs are also expected to test the air in air pollution control areas, inspect pollution control equipment, and manufacturing processes.

Under this statute, one has to comply,

• Comply with the conditions in the “Consent to Establish” or “Consent to Operate”

• Not to discharge air pollutant(s) in excess of the prescribed standards

• Furnish information to the SPCB of any accident or unforeseen act or event

• Allow entry to the SPCB to ascertain that provisions of the Act are being complied with

• Provide information to enable SPCB to implement the Act

• Provide access to the SPCB for taking samples

• Comply with the directions issued in writing by the SPCB

• Obtain “Consent to Establish”

• Obtain “Consent to Operate”

• Apply for the renewal of “Consent to Operate” before expiry of the validity period

• Consent to be deemed as granted after four months from the date of receipt of application if no communication from the SPCB is received

• A prior “Notice of Inspection” to be served by the SPCB

• Industry to ensure that specified emission sampling procedure is being followed by the SPCB

• Opportunity to file objections with the SPCB within 15 days from the date of service of notice

• PCB to record reasons in writing in case it does not provide an opportunity to the industry to file objections.

REAL ESTATE SECTOR

Legislative Framework

Laws governing the real estate sector in India are substantially codified. However, recently there have been talks of a real-estate regulator being introduced. Real estate laws are contained in different enactments pertaining to transfer of property rights, rent control and land ceiling among others. These enactments deal with areas such as:

- aspects related to real estate contracts;
- declaratory relief and injunctions in respect of property rights;
- transfer and conveyance of property in terms of sale, lease and mortgage;
- requisite covenants and terms and conditions to be incorporated in the documentation pertaining to such transfers and conveyance;
- testate and intestate succession;
- grant of letters of representation such as probate, letters of administration and succession certificates pertaining to property;
- total or partial partition of properties; stamp duties payable in respect of property transactions;
- modalities for computation and quantification of such duties;
- compulsory and optional registration of documents in respect of property transactions;
- consequences arising from non-registration of transactions with the registering authorities and procedural laws in respect of enforcement of legal rights pertaining to properties

The principal enactment in India pertaining to the sale of immovable property is the Transfer of Property Act, 1882 (“TPA”). Under the TPA “Sale” (with respect to immovable property), is a transfer of ownership, by one living person to another living person in exchange for price paid or promised or part paid or part promised. The TPA contains detailed provisions with respect to implied terms and conditions of such transfer by sale. Typically transactions of sale of immovable properties are spread out over a period of time commencing from the negotiations between the parties, perusal and scrutiny of the title deeds (for examination of title of the vendor), finalizing the terms and conditions of the prospective sale such as, quantum of price and the payment installments and completion of the transaction by the execution and registration of the formal deed or indenture of transfer. Importantly, under Indian law a contract of sale does not, of itself, create any interest or charge on the property as equitable estates are not accorded recognition under Indian law.

<u>Growth and Development</u>

Recent developments in the real estate sector in India have highlighted its tremendous potential and contributed to its phenomenal growth. This has caused the sector to appear on the agenda of all major international funds and developers. Today, the sector is witnessing a wide spectrum of advancements that are transforming India into a preferred and sought after destination for real estate activity.
Two major steps taken by the GoI have been the core catalysts in fuelling growth in the real estate sector in India:

1. *FDI in Real Estate in India*

   The first step comprises of the initiatives that have been taken to allow FDI in real estate in India in townships, housing, built-up infrastructure and construction development projects. Under these, the minimum area to be developed is (i) 10 hectares in case of development of service housing plots, (ii) a minimum built-up area of 50,000 sq. meters in case of construction-development projects and (iii) in case of a combination project, any one of the two conditions mentioned above. These projects are required to be designed keeping in consideration the local by laws and regulations. The minimum required capitalization amounts to US$ 10 million for a wholly owned subsidiary and US$ 5 million for a joint venture with an Indian partner[18].

   In terms of the Consolidated FDI Policy, the whole of the original investment cannot be repatriated before the end of a period of three years from the date of completion of minimum capitalization. The GoI has recently clarified that the original investment means the entire amount brought in as FDI. The lock-in period of three years will be applied from the date of receipt of each installment / tranche of FDI or from the date of completion of minimum capitalization, whichever is later. The investor may be permitted to exit earlier with prior approval of the Government through the FIPB.

2. *Introduction of Real Estate Mutual Funds*
   The second set of initiatives is the introduction of Real Estate Mutual Funds ("REMFs") in India by way of amendments to the SEBI (Mutual Funds) Regulations, 1996 which permit mutual funds to launch REMFs. As per the amendment, REMFs are close-ended with units requiring compulsory listing on stock exchanges. REMFs are further required to file a declaration of net asset value requirements on a daily basis. As a part of the initiative SEBI has also approved guidelines for the REMFs (yet to come into force) relying on the recommendations of the committee on real estate investments scheme.

Real Estate Bill

In June 2013, the Union Cabinet approved the Real Estate (Regulation and Development) Bill, 2013. The Bill will provide for a uniform regulatory environment, to protect consumer interests, help speedy adjudication of disputes and ensure orderly growth of the real estate sector.