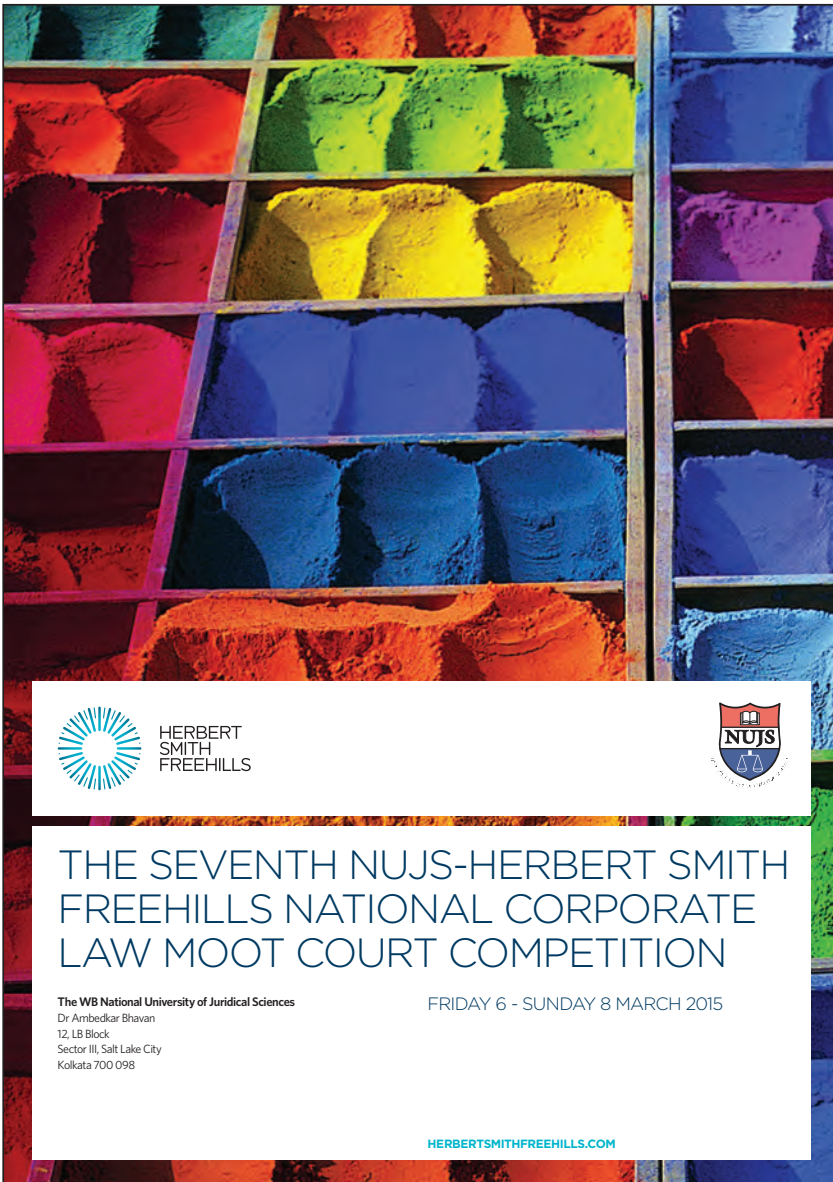


2015 - Problem Seven

Author - Umakanth Varottil



Overview

Winning team

National Law Institute
University, Bhopal
*Raghavi Viswanath, Rohan Hame,
Vaibhavi Tadwalkar*

Runners up team

National Law School of India
University, Bangalore
*Annie Jain, Aniruddh Nigam,
Aditi Shukla*

Best speaker

Naman Singh Bagga
National Law University, Odisha

Best memorandum

National Law School of India
University, Bangalore
*Annie Jain, Aniruddh Nigam,
Aditi Shukla*



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FRIDAY 6 - SUNDAY 8 MARCH 2015

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*Celltone plc (Appellant) v. IndMobile Telecoms Limited,
5G Star Networks (Respondents) Limited, Band Bank &
M/s. Darsh Legal Associates*

1. IndMobile Telecoms Limited is a successful telecom equipment company in India. It manufactures and sells mobile network equipment to various telecom services companies. It has also been a member of the Nifty 50 for the last two years. The company has been piloted by the energetic Mr. Sardar, who is its chairman and managing director. Mr. Sardar and his family are the promoters of IndMobile as they hold a total of 35% shares in the company.
2. Although flush with success, IndMobile set its sight on loftier ambitions. It wishes to become a player in the telecom services industry rather than to be a mere supplier. Hence, when the Government of India announced the grant of licences for the 5G mobile networks to be established in the metro cities in India, it decided to bid for those licences. For this purpose IndMobile Telecoms Limited set up a wholly owned subsidiary 5G Star Networks Limited in Kolkata, in which the telecom services business will be housed.
3. In 2013, the Government of India conducted separate bidding processes for each metro area, with the condition that no single entity or group can submit bids for more than three metros. 5G Star duly submitted the bid documents to the Government of India for the Kolkata, Chennai and Hyderabad areas. The bidding process was highly competitive given the lucrative nature of the market. The Government first shortlisted bidders on the basis of technical criteria. The shortlisted bidders were in turn evaluated on the basis of financial and other criteria, after which the bids were announced. Due to the phenomenal nature of the bids placed by 5G Star, it was successful in bagging the licences for Kolkata and Hyderabad. It was trounced in Chennai by an existing influential telecom service provider. Following the award of the licences, the actual licence agreements were executed between the Government and 5G Star for the Kolkata and Hyderabad metro areas on November 1, 2013.
4. During the bidding process, IndMobile began in parallel to scout for potential partners to be brought into its 5G business. Mr. Sardar was well aware of IndMobile's limitations. Having been a telecom equipment player, he knew that establishing and managing a telecom services company was a different cup of tea altogether for which he did not possess expertise within the company. That expertise necessarily had to be sourced from elsewhere. For this purpose, he approached Vegus Investment Advisors, a boutique M&A investment banking firm. Vegus in turn prepared an information memorandum, which it used to ascertain interest from various telecom players in 5G Star. After discussions with several potential players, IndMobile (based on Vegus' advice) decided to invite Celltone plc, a

leading telecom services company in the UK. The partnership was finalised at a dinner meeting one wintry night in London between Mr. Sardar and Mr. Barrett, the CEO of Celltone. The parties shook hands on a deal in which Celltone would acquire 49% shares of 5G Star at a total value of US\$ 490 million. This was of course subject to the conduct of satisfactory due diligence by Celltone and the drafting, negotiation and execution of definitive deal documentation between the parties.

5. In order to help accomplish the deal in India (particularly as to its legalities), Celltone appointed M/s. Lexman Associates, a leading Indian law firm. It also appointed DBAD Partners, a leading accounting firm, to advice on accounting and taxation aspects. Given that it was Celltone's first foray into the Indian market, it adopted a rather cautious approach, and decided to conduct a full-blown due diligence. It began with a two-day kick-off meeting in Kolkata where Celltone and its advisors attended a series of presentations by 5G Star, IndMobile and their representatives on various matters pertaining to the business of the companies. Celltone was rather interested in understanding the licensing process for the 5G networks and the robustness of the same. During the presentation by 5G Star representatives on licensing, Mr. Gangston, the Celltone project manager leading the deal quizzed intensively on the process and as to what measures were adopted to ensure that the award of licence was foolproof. Specifically, he voiced Celltone's zero-tolerance policy towards corruption. The 5G Star representatives responded to Mr. Gangston's concerns and assured him that the process was transparent and entirely above board. Following the presentations, Celltone and their lawyers and accountants were given full access to all the relevant books and records of 5G Star and (to the extent necessary) those of IndMobile. The lawyers and accountants subsequently prepared detailed due diligence reports and submitted the same to Celltone.



6. Given that Celltone was entering a new market and due to the sensitivities involved in the licensing process, Mr. Gangston decided to conduct a further background check on his own on various matters. Through Vegus, he was able to obtain access to some customers of IndMobile as well as some former and current employees of that company. During one such meeting, a former employee of IndMobile revealed the rather flexible approach of the company towards its dealings with the government. She mentioned that in the past the company had entertained government officials in expensive restaurants and showered them with gifts. She was however unable to tell the value of these gifts and whether they were significant in nature. These revelations were of great concern to Mr. Gangston. However, he was pacified by Mr. Dhanlal, the managing partner of Vegus, who mentioned that this was not uncommon in the developing world, where it is otherwise impossible to do business. Mr. Gangston was somewhat conflicted. On the one hand, there was a lurking fear in his mind given Celltone's strict policies. But, on the other hand, the 5G Star deal was too important to be scuttled. He therefore decided not to escalate this issue to the senior management and board of Celltone.
7. Along with the due diligence, the parties also negotiated and agreed upon the terms of the legal documentation. On October 3, 2013, a Share Acquisition Agreement (**SAA**) was executed between Celltone, IndMobile and 5G Star. Under the terms of the SAA, Celltone was to subscribe to 40% shares of 5G Star, for which the company would undertake a new issue of shares. This would be for a consideration of US\$400 million that Celltone would pay 5G Star. Celltone would acquire the remaining 9% (representing 125,998 shares) from IndMobile for a consideration of US\$ 90 million that it would pay IndMobile. Upon completion of the transaction, Celltone would hold 49% of 5G Star on a fully diluted basis. The relevant terms and conditions of the SAA are contained in **Appendix A**.
8. On November 25, 2013, upon satisfaction of all the conditions precedent, Celltone completed the acquisition under the SAA and became the owner of 49% shares in 5G Star, with the remaining 51% shares being held by IndMobile. Upon closing, the necessary formalities involving the filings with the Reserve Bank of India, the Registrar of Companies, and the like were duly completed. One of the conditions precedent in the SAA related to the issue of a closing legal opinion by the legal counsel representing IndMobile and 5G Star, which was M/s. Darsh Legal Associates. Accordingly, on November 25, 2013, Darsh Legal issued a legal opinion, the relevant paragraphs of which are contained in **Appendix B**. At the time of issuing the opinion, Darsh Legal also obtained the requisite confirmations from IndMobile and 5G Star. It was a condition of the issue of the legal opinion that Darsh had to obtain professional liability insurance worth at least US\$100 million, which it in fact obtained from Prolnsure.



9. Celltone, IndMobile and 5G Star also entered into an Escrow Agreement dated November 25, 2013 with Band Bank. Under this arrangement, Band Bank as the escrow agent is to hold 10% of the consideration payable by Celltone to IndMobile and 5G Star respectively (i.e. the escrow amount). The escrow amount is to be held for a period of three years from the Closing Date to be applied towards satisfaction of any indemnification obligations of IndMobile and 5G Star that may arise under the SAA. In the absence of such claim, the escrow agent is to pay over the respective shares of the escrow amount to IndMobile and 5G Star at the end of the said three-year period.
10. After the acquisition of the 49% stake by Celltone in 5G Star, the parties got down to business to exploit the licence for the Kolkata and Hyderabad metro areas. Orders were placed for millions of dollars' worth of equipment, and loans were arranged from banks and financial institutions. Although the business aspects were proceedings smoothly, the parties experienced a temporary hiccup in December 2013 when Navro Telecom Limited, one of the losing bidders for a licence in the Kolkata metro area filed a writ petition before the Calcutta High Court challenging the award of the licence for the Kolkata metro area to 5G Star. Matters became somewhat compounded by the sensational nature of the allegations made by Navro Telecom. Navro stated in its writ petition that Mr. Bantha Ranga, a project manager in IndMobile (who was subsequently transferred to 5G Star) is alleged to have promised significant favours as well as cash and other gifts to Mr. Debaraya, one of the members of the Government committee that was deciding upon the bids for the Kolkata metro area. It is alleged that Mr. Ranga paid a sum of Rs. 2,50,000 by way of consulting fees to a company fully owned by Mr. Debaraya and his wife on the pretext of obtaining strategic advisory services from that company. This sum was paid from 5G Star and shown towards payment of consulting fees in its books. No details were available regarding the precise nature of the services provided by Mr. Debaraya's consulting company to 5G Star, if at all.

11. Mr. Sardar was livid with these revelations in the writ petition. He did not in his wildest imagination expect his employees to act in such a manner. Of course, he had some inkling about the wayward habits of Mr. Ranga, including making all kinds of promises to government officials, but he never imagined that Mr. Ranga would actually execute those promises and make payment of such significant sums of money from the company's account. 5G Star decided to put up a strong defence against the challenge to its licence for the Kolkata metro area. However, that was not good enough. The Calcutta High Court decided that the allegations made against the bidding process for the Kolkata metro area were rather serious and given the law laid down by the Supreme Court of India in this field, it ordered a cancellation of the licence awarded to 5G Star for the Kolkata metro area. This came as a significant shock to 5G Star and its two principal shareholders. Although the Hyderabad licence was unaffected, this development effectively meant that about half the business of 5G Star was in disarray. 5G Star decided to put up a strong fight and preferred a special leave petition to the Supreme Court, which was dismissed at the admission stage itself.
12. The information regarding the shaky nature of the licence granted to 5G Star came as a shock to Celltone, being a significant shareholder in 5G Star having put in enormous amounts of money into the company. While it was still assessing its situation, Celltone's miseries intensified with a series of further bad news that poured in. During a discussion between Mr. Gangston and the operational personnel of 5G Star, a serious discrepancy was found in the financial projections pertaining to the Hyderabad metro area. Celltone operated on the assumption that the projected monthly average revenue per unit (**ARPU**) for the Hyderabad metro area was Rs. 250. During due diligence, DBAD Partners had advised Celltone that the components that went into the calculation of ARPU may not be uniform across countries or even among different telecom operators. Hence, it would be best to clarify this with 5G Star. Mr. Beanman, the Vice-President (**Finance**) of Celltone, who was leading the accounting due diligence effort, raised this issue during a telephone conference call with the finance personnel of 5G Star. During the conference call, the 5G Star personnel explained that the projected monthly ARPU of Rs. 250 was without regard to discounts and rebates that may be offered to customers. During this discussion, however, the connectivity was poor and the conference call kept getting dropped with the participants having to rejoin a number of times. While 5G Star was under the impression that they had disclosed this information to Celltone, the fact remains that during the frustrating moments of the conference call marred by continuous disruptions, that information was not properly received and assimilated at the Celltone end. In fact Mr. Beanman remarked to his colleagues sitting along with him that if this was the quality of the telecom network in Kolkata and Hyderabad, then 5G Star had a promising outlook with its superior

quality services. As they were subsequently caught up with other sticky negotiation points, neither Mr. Beanman nor his colleagues had the opportunity clarify as to what components went into the computation of the projected monthly ARPU for the Hyderabad metro area. It was only after the closing of Celltone's investment in 5G Star that it was discovered the projected monthly ARPU figure of Rs. 250 provided by 5G Star was without regard to discounts and rebates. The net figure taking these aspects into account would be only Rs. 175, which would significantly alter the valuation of the shares of 5G Star. In other words, Celltone was left with the stark reality that it had considerably overpaid for its stake in 5G Star.

13. When Celltone was still licking its wounds, it was delivered another blow. It received a legal notice from the lawyers of Grovera Inc., a telecom consultancy company based in Greenwich, Connecticut. The legal notice claimed that IndMobile had agreed with Grovera to sell the 125,998 shares in 5G Star that it ultimately sold to Celltone. The notice included a document titled "Letter of Intent", which is set forth in **Appendix C**. The notice claimed that the sale of the 125,998 shares in 5G Star to Celltone was illegal and that Celltone must immediately transfer those shares to Grovera at a price of US\$40 million. No other document was signed between IndMobile and Grovera.
14. Following this series of unsavoury events, Celltone through its legal advisors Lexman Associates decided to undertake remedial actions. It issued instructions to Band Bank to release the escrow amount and pay it to Celltone's designated bank account in the UK on account of the breach of the terms and conditions of the SAA by IndMobile and 5G Star. Band Bank immediately consulted its own lawyers and replied that it has been advised not to so release the escrow amount to Celltone.
15. Celltone filed three civil suits before the Calcutta High Court as follows.
 - (i) Its first suit was against IndMobile and 5G Star pursuant to the SAA. It sought a refund of the purchase consideration of US\$490 million that it had paid for the acquisition of shares in 5G Star, or alternatively damages for an equivalent amount.
 - (ii) It filed a suit against Band Bank seeking release of the escrow amount in favour of Celltone pursuant to the terms of the Escrow Agreement.
 - (iii) It filed a suit against Darsh Legal Associates seeking damages to the tune of US\$490 million against it for rendering an incorrect legal opinion for which it is to be held liable.

16. In parallel, Celltone also initiated an arbitration claim against the Government of India under the Agreement Between the Government of the Republic of India and the Government of the United Kingdom of Great Britain and Northern Ireland for the Promotion and Protection of Investments, on the ground that the action of cancellation of the licence for the Kolkata metro area amounted to an expropriation of its investment in 5G Star. The arbitrators are yet to be appointed.
17. In the meanwhile a single judge of the Calcutta High Court heard Celltone's civil suits and dismissed all of them on their merits. Celltone has preferred an appeal against all the orders to a division bench of the Calcutta High Court, which has decided to club all the appeals and hear them together. None of the parties has raised any issue regarding the jurisdiction of the court, which they all accept.



Appendix A

Extracts from the Share Acquisition Agreement dated October 3, 2013

2. Definitions

"**Company**" means 5G Star Networks Limited;

"**Purchaser**" means Celltone plc;

"**Sale Shares**" means 125,998 shares representing 9% of the share capital of the Company to be sold and transferred by the Vendor to the Purchaser pursuant to this Agreement;

"**Vendor**" means IndMobile Telecoms Limited.

6. Representations and Warranties of the Vendor and the Company

The Vendor and the Company hereby represent and warrant to the Purchaser as follows:

- 6.1 The Vendor is the sole legal and beneficial owner of the Sale Shares, free and clear of all liens and the Vendor is absolutely entitled to sell and transfer the Sale Shares in accordance with the terms and conditions of this Agreement.
- 6.2 The Company and the Vendor are limited liability companies duly incorporated and organised and validly existing under the laws of India having the full corporate power and authority to enter into this Agreement and to perform their respective obligations under this Agreement.
- 6.3 This Agreement and the execution, delivery and performance constitutes a legal, valid, and binding obligation on the Vendor and the Company, and is enforceable against them in accordance with its terms.
- 6.4 There are no rights of first refusal, non-disposal undertakings or other restrictions whatsoever on transfer in respect of the Sale Shares and the Sale Shares are freely marketable by the Vendor, and would create a valid title of the Purchaser to the Sale Shares.
- 6.5 The Company at all relevant times has the corporate power and all licenses, authorisations, consents and approvals required under applicable law to own its assets and to carry on business as conducted now or from time to time and is duly qualified to do business in each jurisdiction where the nature of the assets owned or leased by it or the activities conducted by it and as proposed to be conducted make such qualification necessary.
- 6.6 The latest audited balance sheet and profit and loss account of the Company and the latest unaudited balance sheet provide a true and fair view of the financial condition of the Company and there have been no subsequent events, which, to the best knowledge of the Vendor and the Company, and after due enquiry, would materially alter the financial condition of the Company.

- 6.7 To the best knowledge and bonafide belief of the Company and the Vendor, the Company is neither in, nor has at any time been in, violation of any applicable law or regulation which is likely to result in any material liability or criminal or administrative sanction of a material nature to the Company or otherwise have a material adverse effect on the ability of the Company to conduct its business as currently conducted or as contemplated to be conducted.
- 6.8 All books and records relating to operating income and expenses of the Company furnished or made available to the Purchaser were those maintained by Company in the normal course of business and are true and correct and accurately reflect the matters contained therein.

10. Indemnification

- 10.1 In the event of any breach by the Vendor or the Company of any representation, warranty, covenant or agreement made or given by the Vendor or the Company in this Agreement, the Vendor and the Company undertake to indemnify and hold harmless the Purchaser to the extent of any and all damages (including without limitation all losses, costs, damages, fines, fees, penalties, out-of-pocket expenses under the applicable law, fees and expenses of attorneys, accountants and other expenses) suffered or incurred by the Purchaser, resulting from or consequent upon or relating to such breach of representation or warranty, covenants or agreement by the Vendor or the Company.
- 10.2 Notwithstanding clause 10.1 above, the maximum liability of the Vendor and the Company for purposes of indemnification under this clause 10.2 shall be the fifty percent (50%) of the total consideration paid by the Purchaser to the Vendor and the Company respectively under this Agreement, provided that this clause 10.2 shall not apply in case of fraud or deliberate omission by the Vendor or the Company, as the case may be.
- 10.3 All representations and warranties of the Parties contained in this Agreement shall survive for a period of three (3) years from the closing date (the **Indemnification Period**) and upon the expiration of the Indemnification Period, all representations and warranties to which such Indemnification Period relates shall automatically expire without any action from the Parties hereto.

Appendix B

Legal Opinion dated November 25, 2013 issued by M/s. Darsh Legal Associates

To: Celltone plc

Sub: Acquisition of Shares in 5G Star Networks Limited

1. We have acted as legal advisors to 5G Star Networks Limited (the **Company**) and to IndMobile Telecoms Limited (the **Vendor**) in relation to the acquisition by Celltone plc (the **Purchaser**) of 49% shares in the Company by way of a Share Acquisition Agreement dated October 3, 2013 (**SAA**).
2. For the purposes of this opinion, we have assumed that:
 - (a) All statements as to matters of fact (other than matters on which we are expressing an opinion herein) contained in the SAA are true, accurate and complete.
 - (b) There are no facts or circumstances in existence and no events have occurred, which render the SAA void or voidable, or repudiated or frustrated, or capable of rescission for any reason, and in particular but without limitation by reason of the lack of consideration, default, fraud or misrepresentation. The SAA and other documents perused by us do not indicate any such facts, circumstances or events.
3. Based on and subject to the aforesaid assumptions, we are of the following opinion:
 - (a) The Company and the Vendor have been duly incorporated and have all the requisite corporate power and authority to enter into the Transaction Documents and to perform their respective obligations thereunder.
 - (b) The execution, delivery and performance of the SAA do not, and will not result in a breach of, violate, or otherwise conflict with or contravene any of the terms and provisions of any law, contracts or any of the constitutional documents of the Company and the Vendor, as applicable.
 - (c) Based on confirmation from the Company, it is qualified to carry on its business in all jurisdictions where it carries on such business, except where failure to do so would not have a material adverse effect on the financial condition of the Company.

Appendix C

August 16, 2013

From: IndMobile Telecoms Limited
23 Chowringhee
Kolkata
India

To: Grovera Inc.
34 Office Tower Park
Greenwich, CT USA

Sub: Letter of Intent

This represents our agreement and understanding regarding the purchase by Grovera Inc. from IndMobile Telecoms Limited of 125,998 shares in 5G Star Networks Limited. Grovera shall purchase the said shares from IndMobile for a total consideration of US\$40 million. Prior to the sale of the shares to Grovera pursuant to this arrangement, IndMobile shall be restricted from selling, transferring or creating security over these shares in favour of any other person. The parties shall negotiate in good faith the detailed definitive documentation to give legal effect to the understanding set forth in this letter of intent. The articles of association of 5G Star shall also be amended to reflect the specific terms of the definitive documents. The parties shall work in good faith towards completing and executing the definitive documentation within a period of three months from the date of this letter of intent.

Yours faithfully

Sd/-

(IndMobile Telecoms Limited)

Received and confirmed.

Sd/-

(Govera Inc.)