Escrow Mechanism under Foreign Direct Investment

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ESCROW MECHANISM UNDER FDI¹

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CHAPTER – I

INTRODUCTION

An escrow has been technically defined as an instrument which by its terms, imports a legal obligation, and which is deposited by the grantor with a third party to be kept by the depository until the performance of a condition, or the happening of a certain event; and then to be delivered to the grantee.

Firstly, with respect to the above definition, there is a need to emphatically define and explain few basic terms and provide a simple example which would be essential in understanding the concept of escrows in the first place.

It has to be understood that an escrow agreement is generally a tripartite agreement, consisting of a depositor, an agent and a beneficiary. The simple way to understand the relation among them, their role and their functions would be in the form of the following statement, ‘the depositor is required to entrust money or shares or any other commodity with the escrow agent and the escrow agent in turn would hold such deposit until it can be released to the beneficiary upon the happening of some future event, or the performance of a contractual condition.

Hence, a suitable example to substantiate the above statement would be, considering A and B have entered into a Sale and purchase agreement (SPA) for 100 equity shares of A’s Company. The SPA would contain a clause which would refer to the escrow agreement between the parties and outline the condition in which the escrow agreement would come into the picture. Hence the first basic principle is that the escrow agreement between the parties would be triggered off by the fulfilling of some condition in the definitive agreement, i.e. the SPA.

Thereafter, A and B in consensus would have the option to choose whether they would want to maintain a Cash Escrow Account or a Security Escrow Account for their transaction. After that has been decided, they would approach the decided escrow agent, and upon his consensus to act as an escrow agent between them, the designated party may deposit the security or the cash along with a copy of their escrow agreement. Thereafter, the escrow agent would act upon the terms of the agreement and upon the fulfilling of the condition set forth in the agreement give effect to the escrow.
It is however, significant to note that with respect to FDI in India, in accordance with the latest escrow circular (No. 58 of 2nd May, 2011) of the RBI, a security escrow account can be operated only with a SEBI authorized Depository participant, and with respect to the cash escrow account, only the designated AD category-I Banks specified by the RBI.

After giving a preliminary understanding of the concept of escrows on the macro framework, the researcher would like to then take a deep dive into the ambit of cash escrows, more particularly those maintained for the purpose of foreign direct investment by the specified AD Category- I Banks in India. Lastly, the researcher would take up the escrow agreement drafted and which incidentally forms the main part of this seminar paper and explain the need of inserting each particular clause and the relevance it has in the escrow agreement as a whole.

1.1 Research scheme

The researcher in the course of this paper would venture out to discuss the escrow mechanism under foreign direct investment. It needs to be mentioned that the basic premise of this research paper is to draft a cash escrow agreement for a foreign direct investment transaction in India and substantiate and explain each clause inserted in it. However, before drafting the agreement as such, the researcher felt the need of explaining the basics of escrow first. Hence, the preliminary chapters in the paper would include explaining the basics of escrow mechanism, laying down the laws governing escrows in India, the need and purpose of escrows, emphasizing the standard clauses of the escrow contract, and the international perspective of escrows to an extent before arriving at the contract drafted.

1.2 Research Techniques for Data Collection

Research technique of analysis, critique, and review of the theories would be intended to be employed.

1.3 Research Methodology

The researcher has followed the doctrinal method of research throughout the project and the MLA system of formatting has been adopted by him.
1.4 Footnoting Style to be adopted

National Law University standard style of footnoting will be followed throughout the project.
CHAPTER – II

THE ESCROW MECHANISM

Escrow is derived from the old French term ‘escroue’, which refers to a roll of parchment paper or a small scrap of paper held by a third party until the transaction of property or arrangement was made complete by full payment of the agreement. In modern times, the term escrow still has the same base meaning as it did in 15th to 16th century in France.

Escrow account in common parlance means a ‘trust account’ held by the third party on behalf of the borrower. An escrow is a legal device by virtue of which a third party is entrusted with an asset, who holds it until the conditions or contingencies in the contract are met, and then proceeds to deliver the asset to the party prescribed in the contract. The contract that sets into place this legal mechanism is called an escrow agreement. This kind of legal arrangement helps parties to secure satisfactory performance and avoid legal battles. Escrow agreement has three parties, i.e. depositor, escrow agent, and beneficiary.

As a legal device, escrow agreements were developed in the United States primarily as a tool of safeguarding party interests in real-estate transactions.

Escrow agreements came into vogue in India in 1991, post the privatization of power sector. The Information Technology industry boom also led to the frequent application of escrow agreement, mostly called software escrow agreements.

Laws governing Escrow Agreements with respect to FDI

Escrow is a contractual arrangement between the parties. However, it is governed and regulated by specific laws in United States. In India, this legal instrument is still in a nascent stage and is mostly self-regulated, that is, governed by the terms of the contract. However, the provisions of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 apply to some particular kinds of escrows in India. i.e. the Cash escrows maintained by the AD Category Bank. Further, the Securities Escrow is also partly governed by Reserve Bank of India, which has issued a notification permitting non-residents, subject to certain terms and conditions, to hold and maintain escrow accounts and special
accounts with authorized dealers in India without prior approval of the Reserve Bank for acquisition/transfer of shares/convertible debentures through open offers/delisting/exit offers.

Need for opening an Escrow Account

To provide structured flexibility and easiness to the resident/non-resident shareholders of Indian Company, Reserve Bank of India vide its Circular RBI/2010-11/ 498 A. P. (DIR Series) Circular No. 58 dated May 02, 2011 decided to permit AD category -1 banks to open and maintain, without prior approval of the Reserve Bank, non-interest bearing Escrow accounts in Indian Rupees in India on behalf of residents and/or non residents, towards payment of share purchase consideration and / or provide Escrow facilities for keeping securities to facilitate FDI transactions subject to the terms and conditions.

Escrow account mechanism gives the foreign investors a chance to reclaim their investment and exit if the local firms fail to comply or meet certain requirements.

Generally a foreign investor insists on the escrow mechanism under FDI because of their past bitter experiences they had when the local party refused to honour the option and buy back the shares. It is not a water tight arrangement; the whole purpose is to provide comfort and security to the foreign investors as well as the local firms. The escrow process provides the peace of mind necessary when transferring valued property.

Taking the example of FDI in real estate sector, escrow mechanism plays a pivotal role in facilitating the inflow of foreign currency in the local market. The Reserve Bank of India asked banks to put in place the escrow mechanism that can ring fence their loans to real estate firms and keep a close tab on the end use of funds.

Procedure for operation of escrows

It is imperative to lay down the scheme for the formation of semi automated escrow mechanism for any FDI transaction. It works by the participation of two party working through a third party acting as an escrow agent i.e. an authorized dealer which has a fiduciary responsibilities in the transfer of collateral security from one party to another.

In a transaction where both parties are honest, the escrow business can essentially be automatic since the buyer gets his shares and approves release of funds, however when there is a
dispute does human interaction become necessary. So, the need is felt to provide for a semi automated escrow mechanism i.e. intervention of any human entity in the form of guidelines, notifications or norms issued by RBI or FEMA to resolve the disputes and allow for the repatriation or remittance of funds held in escrow account to either of the parties.

The procedure for allotment of shares of Indian Companies to NRIs is governed by the RBI regulation. It is a two stage reporting procedure.

a. Within 30 days from the receipt of money from the investor, the Indian Company will have to report to the Regional Office of RBI under whose jurisdiction it’s registered office is located.

b. Within 30 days from the date of issue of shares, a report in form FC- GPR (Foreign Currency General Purchase Register) should be filed with the regional office along with other documents. A certificate from the Company Secretary of the company accepting investment will be issued certifying that all the requirements of the Companies Act have been complied with.

When the shares are transferred to the NRI, the payment is made to the concerned person who was holding the share and not to the company. Foreign strategic investors on a regular basis enter into an agreement where they keep aside some assets that can be sold from a special account to buy out the shares of the local firm or promoter. The foreign investors can have a put option where they, either, exercise their right to purchase the shares or refuse to make the payment for the said transaction. In such a situation, the asset held in the escrow account act as a security for the local promoters.

There could be other situation where the local promoters failed to allot the shares to the foreign investors then the whole amount has to be repatriated back to the foreign investors. The repatriation is done through the escrow account by the authorize dealers as per the directions given by RBI.

The circulation no.58 issued by RBI dated 3rd May, 2011 regarding the procedure for the opening of an escrow account for FDI transaction according to the researcher, is a reflection of a smart move to facilitate the inflow of foreign currency in the Indian economy. When it comes to financing economic growth and development in the emerging Markets, the overall consensus seems to suggest that this notification will no doubt offer a better and overwhelmingly platform
for raising capital globally to finance their economic growth and development in the Emerging Economies.

Keeping the above issue in mind, escrow account seems to be a good option as that gives comfort to not only the client but also the providers/designers that if delivered, money is on the table. However importantly the provider is assured of the fact that money is there on the table and client is sure of the fact that it is in safe hands.
CHAPTER – III

THE STANDARD CLAUSES IN AN ESCROW AGREEMENT

The foundation of any escrow service is the agreement. A typical escrow is a tripartite one signed between the seller, purchaser, and the escrow agent, thereby enmeshing the parties into the framework created under the agreement. The depositor is required to entrust money with the escrow agent. The escrow agent holds the escrow deposit until it can be released to the beneficiary upon the happening of some future event, or the performance of certain contractual conditions. If any or both the parties withdraw their obligations under the agreement, the escrow agent is required to return the down payment to the purchaser. The main clauses of an escrow agreement are the following:

a. It would specify who the escrow agent is;
b. It would describe the asset or thing that is to be put in escrow;
c. It would detail the events which would trigger the release of the ‘thing’ held in escrow;
d. It will contain a clause indemnifying the escrow agent;
e. It may contain a confidentiality clause; and
f. It will specify the governing law.

Negotiating the inclusion and scope of the escrow agreement is just a prelude to the actual drafting; it is also likely to be the most difficult part of bringing the agreement into existence. Generally, only the buyer will want an escrow agreement. The seller will never be eager to relinquish any control over its own possession. However, very few sellers will abandon an acquisition merely because the buyer insists on a reasonable escrow agreement. The buyer should never get greedy and demand an unreasonable scope for the agreement, or that an exorbitant portion of the purchase price be placed in escrow. In determining the scope of the agreement, the buyer should pinpoint which representations and warranties are likely to pose the most serious problems, and be sure that they are subject to the agreement.
The Preamble

The parties and the type of the escrow agreement are laid down under the preamble of the agreement. The name of the escrow agent is also stated in the agreement and the specialized nature of subject matter is specified.

Material contents of the Escrow

An escrow agreement varies in its structure according to the nature of the item/thing/money being deposited into the escrow. This factum, however, also impacts the extent and nature of the obligation imposed on the escrow agent. The escrow agent is responsible for safeguarding the escrow amount and specific documents deposited in the escrow, as per the agreement, for example, title documents in a real estate transaction.

Thus, in case of a real estate transaction where an escrow agent is entrusted with title documents, he would be under an obligation to protect them. In cases where the escrow agent is entrusted with money, such money must be deposited in a special bank account separate from the escrow agent’s personal and business accounts.

The Time period of the Escrow

The time period for completing an escrow is generally set out in the sale and purchase agreement, or agreed upon by the seller and purchaser. Generally, the date should be mutually convenient for both parties. In some instances it might take some time for the purchaser’s loan to be processed and approved by the bank. In other instances, when the purchaser is purchasing off-plan, there is a time delay while the building is being constructed. In these instances payment will only be made after a period of time has lapsed.

Escrow Agents

With respect to Escrow agent’s compensation, the matters of fees and reimbursement of expenses should be clearly set forth in the escrow agreement. This fee may be paid in a lump sum or in case of more lengthy escrows, over one year in duration are arranged, the parties may agree that one or the other will pay the escrow agent’s fees on a periodic (often quarterly) basis.
However, an escrow agent cannot be compensated through the interest of the escrow property as it would be against the fiduciary duty.

**Notice on Breach of Agreement**

If any party has a claim to the escrow amount/deposits, due to a contractual breach by the other party, he should notify it to the escrow agent—within a certain time. This time period is stipulated and known as notice period.

**Liability Provision**

A provision which is universal to all escrow agreements is what is commonly referred to as the ‘liability provision’. This provision sets forth the purpose of the agreement including the language stating that an escrow fund has been established to indemnify, defend, and hold harmless the buyer from any and all claims, liabilities, and damages arising from an inaccuracy in or breach of any representation or warranty made by the seller in a share transfer agreement. This provision should also clearly establish that the escrow fund is a trust fund that will not be subject to any lien or attachment by any creditor.

**Dispute Resolution**

In case of a dispute on the notice period or otherwise, the procedure for mediation/arbitration should be clearly laid down, including the governing law and place of arbitration. Litigation is another option though it is generally not preferred as it is more time consuming than alternative dispute mechanisms.

The agreement should incorporate determination by an independent expert as the mechanism to settle disputes arising out of a **trigger claim**. If properly set up, such a mechanism would be outside the framework of the Arbitration and Conciliation Act, 1996, and, hence, would avoid the delays and expense a court or arbitration process would involve.

The seller should generally insist on a contractual term providing that if the amount claimed is less than the total in the escrow fund, the excess should promptly be released to the seller at the end of the fixed escrow period. This would ensure that he secures access to the part of the purchase money that is not being disputed.
**Indemnification**

Indemnification clauses are usually insisted upon by escrow agents in order to limit their liability for actions under the escrow agreement. Agreements usually contain a clause that the buyer and seller shall jointly indemnify the agent for any loss or expense incurred due to a claim relating to his actions under the escrow agreement. The justification for providing this sort of immunity to the agent is that he performs a limited function under the agreement, usually limited to safekeeping of the escrowed property in accordance with the terms of the agreement. However, care must be taken to ensure that the indemnification clause is narrowly worded and excludes indemnity in cases of the agent’s own negligence or fault.

**Confidentiality**

Most escrow agreements do not contain a confidentiality clause. The need for an explicit confidentiality clause is especially important in cases where there is a need to access that if a liability occurs due to the negligence of the escrow agent, which party would bear the loss.

In the United States this question has come to be addressed by the *entitlement rule*. Simply put the rule mandates that in case of a loss due to the actions of the agent, the loss must, as between the parties to the escrow transaction, be borne by the one who, at the time of its occurrence, was lawfully entitled to the right or property affected. The inevitable result of this analysis is that one blameless party will suffer a substantial loss while the other will still reap the benefits of the escrow.
CHAPTER – IV

INTERNATIONAL TRADE PERSPECTIVE OF ESCROWS

International trade creates a need for buying and selling or borrowing foreign currencies. When for example a Public Limited Company in India sells equity shares to a buyer in Japan, the sale will be priced in Indian Rupees, Yen or perhaps third universal currencies like the U.S Dollar for exchanging shares of the Indian Co.

In the above example if the sale is priced in Indian Rupees, the buyer in Japan will purchase Indian rupees with Japanese Yen in order to make the payment. In the second situation, if the sale price is in Japanese Yen, the buyer normally will wish to convert the receipts in his domestic currency and will sell the Japanese yen in exchange of Indian Rupees. In the third situation, if the sale price is in some third currency, such as the U.S Dollar, the buyer will purchase USD in exchange of Yen and make the payment and then the Indian Co. will sell those USD in exchange of Indian Rupees.

The above example highlights the ideal hypothetical situations which occur in case of a foreign exchange transaction with respect to share purchase.

On occasion, International trade transactions do not result in the sale or purchase of foreign currency because companies either have foreign currency bank accounts for receipts and payments, or might pay for a purchase with foreign currency bank loan. To counter these situations the RBI has appointed designated Authorized Dealer category-I banks in India which are entitled to open a special type of accounts known in common parlance as ‘escrows’ to facilitate the process of foreign direct investment transactions easily.

Trading is also done in other forms like derivative instruments, swaps, options and futures. These are more sophisticated instruments for trading in foreign exchange that are derived from an underlying foreign exchange market.

Generally, the price at which one currency is traded in exchange in the foreign exchange market is the exchange rate between two currencies. In a free market these prices move up or down according to demand and supply. In such a situation, the government of a developing
country would want to achieve stability in terms of such transaction which involves huge foreign exchange. One of the mechanisms for achieving such stability is offered under the escrow mechanism of transactions, whereby with the mechanism of forward exchange contract or hedging clause the transaction can be locked to the present exchange rates without allowing it to fluctuate according to the market developments. The elaboration on such a mechanism would be taken up in due course of this paper.
CHAPTER – V

FORWARD EXCHANGE CONTRACTS AND ESCROWS

In a forward transaction the purchase or sale is agreed but the actual transaction takes places sometime in the future, thereby the fixation of rate of interest for a future exchange. These forward transactions are known as forward exchange contracts or forward contracts and they very clearly resemble the one of the essential process undertaken under the Escrow mechanism as provided by the RBI.

A forward exchange contract as the name implies is binding upon the parties, generally a bank and a non bank customer or two banks. Once made, a customer cannot back out of it or alter its terms, except by arrangement with the contractual bank.

A forward contract has three main elements, two of which feature as elements of escrow mechanism too. They are-

a. It is a binding agreement to exchange a specific quantity of currency in exchange for currency or assets of another.

b. The rate of exchange is fixed when the contract is made.

c. The contract is for the performance, delivery of the exchange at an agreed future date, either a specific date or any time between two specific dates, depending on the contractual terms.

Utility of Forward Contracts

The forward contracts lock in exchange rates for a future purchase or exchange. It should be remembered that once made, the contract is binding and must be honoured, whatever happens to the spot rate, i.e. present prevailing rate of interest in the period up to the settlement date.

The above situation can be understood more easily by the following illustration. For example and non-resident decides to purchase of 10,000 equity shares of a Public listed Co. in India through automatic route for FDI. The Spot exchange rate between the Indian Rupee and the non-resident’s currency, i.e. USD is 1:0.02.
If the buyer had to pay 50,000 INR for the above transaction, he would agree to lock in the amount at (50,000 X 0.02=10,000 USD). Thus if after a month, the spot exchange rate between the Indian Rupees and the USD become 1:1, then even though the buyer should have ideally ended up paying 50,000 USD, however because of his forward exchange contract with an authorized bank, irrespective of the spot exchange rate he would only pay 10,000 USD.

**How the Bank covers a forward deal contrasted with the position of an AD Category Bank**

When a bank deals with an individual or Co. for an outright forward date, in other words when it arranges a forward contract for a specific future date, it usually considers that it has a position in the currency and often will wish to cover its own exposure.

Generally the process adopted by the Bank, it that it covers both the spot and the forward deals. The bank’s spot dealer will cover the spot side and the forward dealer would cover the forward. In case a bank had transacted a forward contract of 3 months for 50,000 Indian Rupees in exchange of USD, it can arrange to sell 50,000 INR for spot immediately and would cover the forward exposure by means of swap, buying 50,000 INR spot and simultaneously selling the same amount forward.

On the other hand, with respect to escrow, an AD Category bank in India engages in no such processes because the variables are shares on hand. Hence, the bank’s exposure to loss is minimal. Also, the escrow agreement further minimizes the risk of the bank through a ‘duties of escrow agents’ clause and an indemnity clause.
CHAPTER –VI

DRAFT OF AN ESCROW AGREEMENT FOR SHARE PURCHASE UNDER FOREIGN DIRECT INVESTMENT

BETWEEN:

Party A – i.e. the SELLER

and

Party B – i.e. the BUYER

WHEREAS:

A Pursuant to a sale and purchase agreement (the "SPA") entered into on 01.01.2011 between the Seller and the Buyer, the Seller has agreed to sell and the Buyer has agreed to purchase, subject to conditions precedent which have now been satisfied, 50,000 shares (the "Shares") in XYZ India Private Limited, a private company incorporated under the laws of the Republic of India, having its principal place of business at New Delhi (the "Company").

B The Buyer and the Sellers have resolved to enter into this escrow agreement (the "Agreement") to define the terms and conditions of the escrow to be constituted as provided in Clause ● of the SPA.

2 This clause forms the most important clause of the escrow agreement because it highlights the definitive agreement, i.e. SPA upon which the escrow agreement is based. It is only the trigger clause in the SPA which would make the escrow agreement come into the picture in the first place, otherwise the escrow agreement would be dormant.

3 Hence clause B too substantiates the earlier clause A by stating that this agreement is entered upon to define the T&C of the escrow which would be constituted as according to a particular clause of the definitive agreement, i.e. the SPA.
IT HAS BEEN AGREED AS FOLLOWS:

1. DEFINITIONS

Terms defined in the SPA shall have the same meaning herein, unless otherwise defined herein or the context otherwise requires.4

2. SECURED LIABILITIES

This Agreement secures the due performance of all obligations (present or future, actual or contingent) of the Sellers owing to the Buyer under the SPA as amended or extended from time to time (the "Secured Liabilities").5

3. DEPOSIT AND PLEDGE

3.1 The Sellers have opened an account under No. [____________] with Bank [____________] (the "Bank"), [_____] Branch, [address] (the "Account").6

3.2 The Sellers shall upon execution hereof, deliver a confirmation from the Bank, by way of a letter substantially in the form of Annex 1 hereto, that they are aware of the terms hereof in accordance with Article[_____] hereof, shall not transfer or pay, or allow any transfer or withdrawal of, any monies standing to the credit of the Account without the

4 The definitions section has been purposely not emphasized by the researcher as they generally are the same as the definitive agreement barring a few exceptions, hence, a reference to the SPA has been also made by the researcher too.

5 An important clause inserted by the researcher in order to emphasize the principal purpose of this escrow agreement, i.e. secure the due performance of all the obligations of the seller to the buyer, i.e. securing the liabilities.

6 This is the first reference to the escrow account, i.e. the Cash escrow account in this case which would be maintained by an assigned AD Category- I Bank in India.
prior written consent of the Buyer, provided that such consent shall be given forthwith by the Buyer where a transfer, payment or withdrawal is expressly permitted hereunder.\(^7\)

3.3 Upon receipt of such confirmation, the Buyer shall pay an amount of [USD] [____] (being a portion of the Price) into the Account, as provided by Clause [____] of the SPA.\(^8\)

3.4 The Sellers hereby pledge to the Buyer, as security for the Secured Liabilities, all claims of the Sellers against the Bank for the repayment of the credit balance of the Account (the "Pledge").\(^9\)

4. INTEREST

The escrow account would be maintained on a non interest bearing basis only.\(^{10}\)

\(^7\) In this clause the researcher has emphasized the very existence of the escrow account, i.e. the non transfer of the money by the escrow agent, i.e. The AD Category – I Bank, from the account without the prior approval of the depositor, i.e. the Buyer in this case. Hence, the Seller in this respect hereby undertakes to communicate the confirmation from the AD Category Bank to the Buyer.

\(^8\) This clause highlights thereby that upon the letter of confirmation being received from the AD Category Bank, the Buyer shall deposit the money amount in the Bank in accordance with the specific clause of the SPA.

\(^9\) This clause has been inserted by the researcher in order to highlight the security by the seller for the secured liabilities. In this particular case the Seller promises to pledge all his claims against the Bank for the repayment of the credit balance of the Account to the buyer.

\(^{10}\) As according to the latest direction to the RBI to the AD Category Banks, the escrow maintained by it would be on a non-interest bearing basis.
5. **REPRESENTATIONS, WARRANTIES AND UNDERTAKINGS**\(^{11}\)

5.1 The Seller represent and warrant to the Buyer that:

5.1.1 the Seller is the sole holders of the Shares, free and clear of any liens and encumbrances, and the Account is not subject to any seizure or attachment;

5.1.2 this Agreement does not violate any contractual or other obligation binding upon the Seller; and

5.1.3 there is no security in existence on the businesses of the Seller.

5.2 The Seller undertake as follows:

5.2.1 they shall not dispose of the Account, shall not create any other pledge, charge or encumbrance in respect of the Account, and shall not permit the existence of any such pledge, charge or encumbrance; and\(^{12}\)

5.2.2 they and the Buyer shall co-operate with each other and with the Bank and sign or cause to be signed all such further documents and take all such further action as the Buyer and the Bank may from time to time reasonably request to perfect and protect the Pledge of the claims of the Sellers against the Bank for repayment of

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\(^{11}\) The most highlighted clause of any contract agreement. In this particular case the seller represents and warrants that, he has authority to sell the shares, value shown for the shares are correct and they are free from any legal implications, whereas the buyer would also mention the same that he has authority to buy and all details about the purchase shares have been made known to him.

\(^{12}\) This particular clause highlights that the Seller truthfully undertakes not to create any further pledge, charge or encumbrance in respect of the Bank Account and would neither allow any such pledge to be created upon the account.
the credit balance of the Account, and to carry out the provisions and purposes of this Agreement.\(^{13}\)

6. **SCOPE OF THE PLEDGE**

6.1 The Pledge shall be a continuing security, shall remain in force until expressly released in accordance with Clause 7.1, and shall in particular not be discharged by reason of the circumstance that there is at any time no Secured Liability currently owing from the Seller to the Buyer.\(^{14}\)

7. **RELEASE OF THE PLEDGE**

7.1 The Buyer shall agree to a transfer / withdrawal from the Account and accordingly a release of the Pledge, without delay upon demand of the Sellers,\(^{15}\)

7.1.1 as to [USD] [_____] at the end of the period referred to in Clause[____] of the SPA, and

7.1.2 as to the balance at the end of the period referred to in Clause [_____] of the SPA,

*provided in each case that* at the end of such period no Claim by the Buyer against the Sellers is outstanding. If a claim is outstanding, the foregoing amounts shall be reduced

\(^{13}\) This clause has been inserted to substantiate the earlier clauses under the Reps by the Seller. It in a way sums up the Reps and establishes that the Seller in consonance with the Buyer and the Bank, shall cooperate with each other and effect the any requirements which may arise for the perfection of the pledge or for the carrying out of the agreement as a whole.

\(^{14}\) This clause pertains to highlight that the Pledge would remain in force on a continuous basis and would be discharged on the express order of release by the buyer only and not by any other reason.

\(^{15}\) This clause is a corollary to the preceding one, whereby it lays down that the buyer undertakes to release the pledge and instruct the AD Category –I Bank of transfer the amount to the Seller free of any encumbrances in two installments.
by the amount of any such claim and the balance shall then remain on the Account and remain subject to the Pledge.

8. **RIGHTS CUMULATIVE**

The rights of the Buyer hereunder are cumulative with all its rights under the SPA and any other documents ancillary thereto.\(^\text{16}\)

9. **MISCELLANEOUS PROVISIONS**

9.1 **Notices**

Any notice in connection herewith shall be made in accordance with Clause [____] of the SPA.\(^\text{17}\)

9.2 **Severability**

The invalidity or unenforceability of any provisions hereof shall not affect the validity or enforceability of this Agreement or of any other provision hereof.\(^\text{18}\)

9.3 **Waiver**

Failure on the part of a Party to exercise, or delay on its part in exercising, any right shall not operate as a waiver thereof, nor shall any single or partial exercise by a Party of any

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\(^\text{16}\) This clause thus lays down that any rights of the buyer are to be assessed cumulatively with the SPA and other agreements in their contract, and not assessed just on the basis on the escrow agreement.

\(^\text{17}\) The Misce Provisions clause hereby lays down firstly that any notice which is made by either parties with respect to the escrow shall be in accordance with the underlying definitive agreement, i.e. the SPA.

\(^\text{18}\) A very important clause in any contract agreement. The researcher hereby has included this provision in order to make this escrow agreement enforceable even if any particular clause over time becomes inapplicable or redundant.
right preclude any further or other exercise of such right or the exercise by a Party of any other right.\textsuperscript{19}

9.4 **Transferability**

The benefit of the Pledge and of this Agreement shall pass automatically to any permitted transferee of all or part of the Secured Liabilities.\textsuperscript{20}

10. **APPLICABLE LAW AND JURISDICTION**

This Agreement shall be governed by English Law. Any dispute arising from this Agreement shall be submitted for final and binding arbitration to an arbitration tribunal comprised of three arbitrators appointed and deciding in accordance with the rules of the International Chamber of Commerce. The arbitration procedure shall take place in Singapore, and shall be conducted in the English language.\textsuperscript{21}

Made in three originals on 01.01.2011

[_____] EUROPE LTD.

\textsuperscript{19} This clause has been included by the researcher in order to rule out any provision of a deemed waiver by any party in any circumstances.

\textsuperscript{20} This clause gives the right of inheritance as to the benefits of the Pledge to the permitted transferee.

\textsuperscript{21} This is a standard clause in any agreement which has been included by the researcher. It lays down the applicable law to the Contract and if any dispute arises, it would be subject to Arbitration process, and the details of the same have been emphasized.
Annex 1 - Form of confirmation by the bank

[_____] INDIA PRIVATE LIMITED
For the attention of [name], Chairman
[address]
[address]

(the "Seller")

[_____] EUROPE LTD.
For the attention of [name], Chairman
[address]
[address]

(the "Buyer")

[date] 2011

Dear Sirs,

Escrow Arrangement

1. An account [____________________] (the "Account") has been opened with our bank in the name of the Sellers.

2. We understand and acknowledge that the Account is intended to operate as a pledged escrow account pursuant to arrangements between the Seller and the Buyer, in accordance with the terms of an Escrow Agreement dated [_____] 2011, a copy of which is attached hereto and initialled by us.

__________________________

22 This Annex refers to the letter which would be made by the AD Category Bank upon the opening of the escrow account and would be subsequently delivered by the Seller to the Buyer. Upon the receiving of this letter, the Buyer would transfer the amount to the Bank Account, and thereby the Banker would assume the liability to take care of the same in accordance with the agreement from thereon.
3. We understand that the Buyer will, upon receipt of this letter transfer the sum of [USD] [_____] into the Account.

4. We confirm that we will not effect any transfer or payment, or accept or give effect to any instructions for the transfer or withdrawal of any monies standing to the credit of the Account from time to time otherwise than in accordance with the provisions of the Escrow Agreement.

Yours sincerely,

For and on behalf of [bank]

.................................................................

Name:

Title:
CHAPTER – VII

CONCLUSION

To conclude, the researcher would like to highlight that escrows have become a very essential tool to facilitate business transactions nowadays especially when the transaction involves two entities from two different countries or when the transaction is cross border.

The advantages are many in such an arrangement, the most important one being that it increases business expediency. The researcher believes that one of the primary problems faced by Indian business community is that there is no law which governs escrow agreements especially with respect to escrow agents, and this should be rectified at the earliest if the government is serious about facilitating more foreign investments coming in the country.

Moreover, with respect to the drafting of the escrow agreement, the wording of the clauses, especially in relation to damages caused by the negligence of escrow agents should be more carefully worded and should be fair to both the parties as is the course of the research, the researcher found that this clause forms the matter of dispute in most escrow agreements.

Also, a very important trend which the researcher noticed in the course of research was that there seems to be a recent trend that is going within the Reserve Bank of India’s policy formulation, which is to relax the rules pertaining to foreign direct investment in India. It appears that RBI is virtually making the sector automatic with very minimal regulations only in certain sectors. The reason for the above can be basically two, i.e. firstly, there are international and external pressures upon India to formulate an FDI policy which to a great extent allows easy transaction for non-resident investors, and secondly, the need for infusion of external investment into the domestic market which would help in the growth and development of emerging economy of India.

Lastly, the above objective also seemed to be the vital element in the thought process of policy makers with respect to the circular on escrows. Pursuant to the circular no. 58 issued by the RBI on May, 3rd, 2011, the overall consensus seems to suggest that the notification would no doubt offer a better and overwhelming platform raising capital globally to finance India’s economic growth and the development of the emerging economy.
All of the above are a reflection of a smart move to facilitate the inflow of foreign currency in Indian economy. These relaxations would definitely lead to facilitating more foreign direct investment into India and also ease out the mergers and acquisitions transaction in the country.
BIBLIOGRAPHY

- Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India, Consolidated Foreign Direct Investment Policy- Circular 2 of 2011.
- Paul J. Malak, Escrow Agreements in Business Acquisitions, Garrett & Egler, Pittsburgh.

Note: Due to the dearth of available literature on the pertinent issue relating to the topic of this Seminar paper, the researcher has mostly only been able to take a deep dive into the policy documents on the issue.