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Question Paper – Nov 19

Ch. 1 - Appointment and Qualification of Directors

Company to have Board of Directors (Section 149)

Question 1

As per their Articles of Association, the maximum number of Directors of each of the following companies is 9:

i) Goodheart Company Limited.
ii) Frontline Trading Private Limited.
iii) Hindustan Zink limited (a Government company under section 2(45) of the Companies Act, 2013).

The Board of Directors of the aforesaid companies proposes to increase the number of Directors to 15. Advise, whether under the provisions of the Companies Act, 2013, the Board of Directors can do so?

Answer

Under **section 149(1)** of the Companies Act, 2013, every company shall have a Board of Directors consisting of individuals as directors and shall have a minimum number of **3 directors in the case of a public company**, **2 directors in the case of a private company**, and **1 director in the case of a One Person Company**. The maximum number of directors shall be **15.**

The proviso to section 149(1) states that a company may appoint more than 15 directors after passing a **special resolution**.

From the provisions of section 149 (1) as above, though the minimum number of directors may vary depending on whether the company is a public company, private or a one person company, the maximum number of directors is the same for all types at 15 directors.

In the case of the first two companies in the question above, the maximum permissible limit is 15 directors. Hence, the Board of Directors of these two companies can increase the number by **simply appointing the additional 6 directors at the general meetings** of the company after following the prescribed procedure and conditions. However, if the number of directors was proposed to have been increased beyond 15 directors, such authority must be obtained from the members through a special resolution and only after that approval, new directors could be appointed.

Further, the **maximum number of directors being increased to 15 will require the Articles of Association to be altered**. Hence, the special resolution of members will be required to alter the Articles of Association under section 14 of the Companies Act, 2013 and comply with other provisions in the said section.

In case of a Government company, the Ministry of Corporate Affairs has clarified vide Notification G.S.R. 463(E) the **limit of maximum of 15 directors and their increase in limit by special resolution shall not apply to Government company**. Thus, in the case of Hindustan Zink limited (a Government company under section 2(45) of the Companies Act, 2013), the Board of Directors can increase the number the directors.

Question 2 ***(May 10)***

The Articles of Association of Rajasthan Toys Private Limited provide that the maximum number of Directors in the company shall be 10. Presently, the company is having 8 directors. The Board of directors of the said company desire to increase the number of directors to 16. Advise whether under the provisions of the Companies Act, 2013 the Board of Directors can do so.

Answer

Under **section 149(1)** of the Companies Act, 2013 every company shall have a Board of Directors consisting of individuals as directors and shall have a minimum number of 3 directors in the case of a public company, 2 directors in the case of a private company, and one director in the case of a One Person Company. The maximum number of directors shall be 15.

The proviso to section 149(1) states that a company may appoint more than 15 directors after passing a special resolution.

From the provisions of section 149 (1) as above, though the minimum number of directors may vary depending on whether the company is a public company, private or a one person company, the maximum number of directors is the same for all types at 15 directors.

In the given case since the number of directors is proposed to be increased to 16, the company will be required to comply with the following provisions:

i) **Alter its Articles of Association** under section 14 of the Act, so as to increase the number of directors in the Articles from 10 to 16;

ii) Approval shall also be taken to be authorised to increase the maximum number of directors to 16 by means of a **special resolution of members passed at a duly convened general meeting of the company.**

Question 3 ***(May 15)***

Examine the validity of the following appointments with reference to the provisions of the Companies Act, 2013:

i) The Board of Directors of MNP Limited appointed Ms. Neha as a Women Director in the Board Meeting held on 10th September, 2014. The said appointment was made to fill the vacancy of the Woman Director, which had occurred as a result of resignation of Ms. Sheela on 30th June, 2014. Will your answer differ if the Board Meeting of the company was held on 8th November, 2014?

ii) LKG Limited was incorporated on 5th May, 2014 under the Companies Act, 2013. Mr. Ramanujam was appointed as the first Resident Director of the company in the Board Meeting held on 30th September, 2014.

Answer

i) **Woman Director**: At **least one** woman director shall be on the Board of such class or classes of companies as may be prescribed (second proviso to section 149(1) of the Companies Act, 2013).

Further, any intermittent vacancy of a woman director **shall be filled up by the Board** at the earliest but not later than **immediate next Board meeting or three months from the date of such vacancy, whichever is later.**

As per the above provisions, the appointment of Ms. Neha is valid. The vacancy of a woman director of MNP Limited which arose on 30th June 2014, due to the resignation of Ms. Sheela, should be filled up latest by 29th September 2014 or the day of the next Board Meeting, whichever is later. Since Ms. Neha was appointed in the next Board Meeting after the vacancy arose, i.e. on 10th September 2014, her appointment is valid.

The answer will remain the same, even if MNP Ltd. appoints Ms. Neha in the Board Meeting held on 8th November 2014, provided the said meeting is the first meeting of the Board after 30th June 2014 i.e. after the resignation of Ms. Sheela.

ii) **Resident Director**: As per **section 149(3)** of the Companies Act, 2013, every company shall have at least one director who has stayed in India for a total period of **not less than one hundred and eighty two days in the previous Financial year.**

The MCA vide General Circular No. 25/2014 dated 26th June, 2014 has given a clarification on applicability of requirement for resident director in the current calendar /financial year. Regarding newly incorporated companies, it is clarified that companies incorporated between 1st April, 2014 to 30th September, 2014 should have a resident director either at the incorporation stage itself or within six months of their incorporation.

Since, LKG Ltd., was incorporated on 5th May 2014, it should have a resident director either at the incorporation stage itself or within six months of their incorporation. Thus accordingly, **the appointment of Mr. Ramanujam as a first Resident Director of the company in the Board Meeting held on 30th September, 2014 is valid.**

Question 4

Explaining the regulatory provisions of the Companies Act, 2013 and the rules thereof regarding the appointment of independent directors on a company's Board, state whether BCD Company Ltd. is required to appoint Independent directors in the following situations:

i) The company has a paid up share capital of ₹ 10 crore.
ii) What shall be your answer in case the company's paid up share capital is only ₹ 2 crore.
iii) Whether a person who holds the position of a Key Managerial Personnel can be appointed as an Independent Director?

Answer

In accordance with the provisions of the Companies Act, 2013, as contained under **Section 149(4)** every **listed public company** shall have a**t least one-third of the total number of directors as independent directors**. The Central Government may prescribe the minimum number of independent directors in case of any class or classes of public companies. Any **fraction contained** in such one-third numbers shall be **rounded off as one**.

According to the Companies (Appointment and Qualification of Directors) Rules, 2014, the following class or classes of companies shall have at least 2 directors as independent directors:

i) the **Public Companies having paid up share capital of ₹ 10 crore rupees or more; or**
ii) the **Public Companies having turnover of ₹ 100 crore rupees or more; or**
iii) the **Public Companies which have, in aggregate, outstanding loans, debentures and deposits, exceeding ₹ 50 crore**

However, in case a company covered as under the above rule is required to appoint a higher number of independent directors due to composition of its audit committee, such higher number of independent directors shall be applicable to it.
Accordingly, the sub-questions can be answered as under:

i) Since, the company has a paid up share capital of ₹ 10 crore, it is mandatory to appoint atleast2 directors as Independent Directors.
ii) Since, the paid up share capital is only ₹ 2 crore, it is not mandatory to appoint the Independent Directors.

As per the provisions a person who has been or is a one of the key Managerial Personnel cannot be appointed as an independent director in the given case.

Question 5 ***(May 17, RTP May 18)***

i) The composition of the Board of Directors of a listed company as on 31-03-2017 comprised of (i) Mr. A, Director, (ii) Mr. B, Director (iii) Mr. C, Director (iv) Mr.· D, Director, (v) Mrs. E, Independent Director, (vi) Mr. F, Independent Director and (vii) Mr. G, Independent Director.

You are required to **examine** with reference to the provisions of the Companies Act, 2013 the vacations of the offices of Mr. D & Mrs. E and **discuss** the course of action that can be taken up by the Company in this regard?

ii) **Discuss** the legal position in the given situations with reference to the provisions of the Companies Act, 2013:

a) Mr. Arthav, a director resigns after giving due notice to the company and he forwards a copy of resignation in e-form DIR-11 to the Registrar of Companies (RoC) within the prescribed time. Besides, the company fails to intimate about the resignation of Mr. Arthav to RoC.

b) The Board of Directors of Superwood Limited decides to appoint on its Board, Mr. Ramakant as a nominee director upon the request of a bank which has extended a long term financial assistance to the company. The Articles of Association of the company do not confer upon the Board any such power. Also, there is no formal agreement between the company and the bank for any such nomination.

Answer

i) The provision of the Companies Act, 2013 governing the appointment of **Women Director and Independent Directors are as under:**

(a) The **second proviso to section 149(1)** of the Companies Act, 2013 provides that such class or classes of companies as may be prescribed, shall have **atleast one women director**. Rule 3 of Companies (Appointment and Qualification of Directors) Rules, 2014 provides that the following class of companies shall appoint at least one women director –

(1) every listed company;

(2) every other public company having-

i) paid-up share capital of one hundred crore rupees or more; or

ii) turnover of three hundred crore rupees or more:

It further provides that any intermittent vacancy of a women director shall be filled-up by the Board at the earliest but not later than immediate next Board meeting or three months from the date of such vacancy whichever is later.

In this case the Company is a listed and under the provisions of the Companies Act, 2013, it is required to **have at least 1 Women Director in its Board.**

(b) The provision of **section 149(4)** provides that every listed company shall have at least 1/3rd of the total number of Directors as Independent Directors.

As per the facts stated in the question, composition of board of directors of listed company as on 31-3-2017 comprised of total 7 directors. Out of which 4 were directors and 3 were independent directors. Later Mr. D (Director) and Mrs. E (Independent Director) vacated their offices of director on 15 -4-2017.

So accordingly, listed company as stated above, **shall have at least one women director and one-third of the total number of directors as independent directors in the Board**. However, on 15-4-2017, total number of directors left were 5 due to vacation of Mr. D and Mrs. E. Further, Rule 3 of

the Companies (Appointment and Qualification of Directors) Rules, 2014, provides that if there is an intermittent vacancy of a women director, it shall be filled up by the Board at the earliest but not later than immediate next board meeting or three months from the date of such vacancy whichever is later.

As per the requirement of the above sections, there is compliance of section 149(4) as 1/3rd of the total number of directors comprises of (1/3x5) 1.6 rounded off as 2, which complies with the minimum requirement of 2 independent directors in the board, however, pertaining to women director, **Board have to fill up the intermittent vacancy at the earliest but not later than immediate next board meeting or three months from the date of such vacancy whichever is later.**

ii) a) **Resignation of Director (Section 168 of the Companies Act, 2013)**

A director may resign from his office by giving a notice in writing to the company. The Board shall on receipt of such notice take note of the same. **The company shall within 30 days from the date of receipt of notice of resignation from a director, intimate the Registrar in Form DIR -12 and post the information on its website, if any.**

Such director shall also forward a copy of his resignation along with detailed reasons for the **resignation to the Registrar within 30 days from the date of resignation in Form DIR-11** along with the prescribed fee. The resignation of a director shall take effect from the date on which the notice is received by the company or the date, if any, specified by the director in the notice, whichever is later.

In the present case, Mr. Arthav, a director resigns after giving due notice to the company and he forwards a copy of resignation in e-form DIR-11 to the ROC within the prescribed time.

If the company fails to intimate about the resignation of Mr. Arthav to RoC, even then the resignation of Mr. Arthav shall take effect from the date on which the notice is received by the company or the date, if any, specified by Mr. Arthav i n the notice, whichever is later.

b) **According to section 161 (3)** of the Companies Act, 2013, **subject to the articles of a company**, the **Board may appoint any person as a director nominated by any institution in pursuance of the provisions of any law** for the time being in force or of any agreement or by the Central Government or the State Government by virtue of its shareholding in a Government company.

The Articles of Association of Superwood Limited do not confer upon the Board of Directors any such power. Hence, the **Board cannot appoint Mr. Ramakant as a nominee director even on the request of a bank which has extended a long term financial assistance to the company.**

Question 6 ***(May 2018)***

CTC Limited is an unlisted public company having a paid up capital of ₹ 100 crores as on 31st March, 2017. The company made a turnover of ₹ 300 crores for the financial year ended 31st March, 2017. The Articles of Association of the company provides for payment of sitting fee to Directors for each Board Meeting/Committee thereof subject to a maximum of ₹ 40,000 per meeting. The Board of Directors is comprised of Independent Directors and Women Directors also. The Company is having 7 directors in its Audit Committee. Shri PKV, working as Financial Advisor of the company, was designated as Chief Financial Officer from 1st April, 2015. He retired from service on superannuation on 31st March, 2016, He is in receipt of monthly pension of ₹ 80,000 from the company. It is proposed to appoint Shri PKV as Independent Director of the Company. The Board of Directors proposes to fix sitting fee of ₹ 50,000 per meeting to Independent Director and ₹

30,000 per meeting to Woman Director, taking into consideration their experience & qualification.

In the light of the provisions of the Companies Act, 2013, advise the Board of Directors in the following matters :

(1) Appointment of Mr. PKV as Independent Director.

(2) Fixing sitting fee of ₹ 50,000 to Independent Director and ₹ 30,000 to Woman Director.

(3) Minimum number of Independent Directors.

(4) Maximum sitting fee to a Director.

Assuming CTC Ltd. is a Government Company, what will be your advise in the matter of appointment of Mr. PKV as Independent Director.

Answer

(1) Appointment of Mr. PKV as an Independent Director

According to **Section 149(6)(e)(i)** of the Companies Act, 2013, an **Independent Director shall be a person who, neither himself nor any of his relatives holds or has held the position of a Key Managerial Personnel (KMP) or is or has been an employee of the Company or its Holding, Subsidiary or Associate Company in any of the 3 financial years immediately preceding** the financial year in which he is proposed to be appointed.

In the instant case, the Company, CTC Limited is proposing to appoint Mr. PKV as an Independent Director who was working as Financial Advisor in the Company and then was designated as Chief Financial Officer for the financial year 2015 -2016. Since, he was an employee and also a Key Managerial Personnel in one of the 3 financial years immediately preceding the financial year in which he is proposed to be appointed, Mr. **PKV shall not be appointed as an Independent Director in CTC Limited.**

(2) Fixing sitting fee to Independent Director and Women Director

As per **Section 197(5)** of the Companies Act, 2013 along with the Companies (Appointment and Remuneration of Managerial personnel) Rules, 2014, a Company may pay a sitting fee to a Director for attending meetings of the Board or Committees thereof, such **sum as may be decided by the Board of Directors thereof which shall not exceed one lakh rupees per meeting of the Board or Committee thereof.**

However, **for Independent Directors and Women Directors, the sitting fee shall not be less than the sitting fee payable to other directors**.

In the instant case, the Articles of Association of the Company provides for payment of sitting fee to Directors of ₹ 40,000.

Hence, the sitting fee of ₹ 50,000 can be paid to the Independent ₹ ₹ 40,000. So, the amount of Sitting fee payable to Woman Director has to be increased from ₹ 30,000 (as proposed) to minimum ₹ 40,000.

(3) Minimum number of Independent Directors

According to the Rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014, the following class or classes of Companies shall have at least 2 directors as Independent Directors:

(1)	The **Public Companies having paid up share capital of 10 crore rupees or more; or**
(2)	the **Public Companies having turnover of 100 crore rupees or more; or**
(3)	the **Public Companies which have, in aggregate, outstanding loans, debentures and deposits, exceeding 50 crore rupees.**

However, in case a Company covered as under the above Rule is required to appoint a higher number of Independent Directors due to composition of its Audit Committee, such higher number of Independent Directors shall be applicable to it.

As per **Section 177(2)** of the Companies Act, 2013, the Audit Committee shall consist of a minimum of three directors with Independent Directors forming a majority.

In the instant case, CTC Limited shall appoint at least 2 directors as Independent Directors as it is covered under Rule 4 of the above Rules since the Company is having a paid up capital of ₹ 100 crores and a turnover of ₹ 300 crores for the financial year ended 31st March, 2017. But **since the Company is having an Audit Committee having 7 directors, therefore 4 directors out of 7 must be Independent directors (4 is forming majority).**

(4) Maximum sitting fee to a Director

As per **Section 197(5)** of the Companies Act, 2013 along with the Companies (Appointment and Remuneration of Managerial personnel) Rules, 2014, a Company may pay a sitting fee to a Director for attending meetings of the Board or Committees thereof, such sum as may be decided by the Board of Directors thereof which shall **not exceed one lakh rupees per meeting of the Board or Committee** thereof. Accordingly, the maximum sitting fee payable to a Director shall not exceed one lakh rupees.

(5) Appointment of Mr. PKV if CTC Ltd is a government company

If CTC Ltd. is a Government Company, then also Mr. PKV shall not be appointed as an Independent Director in CTC Limited because, he was an employee and also a Key Managerial Personnel in one of the 3 financial years immediately preceding the financial year in which he is proposed to be appointed.

Question 7 ***(RTP Nov 18)***

M/s. Bosch and Lawrence Limited, an unlisted company has a paid up equity share capital of ₹ 11 crores as on 31st March, 2013. Mr. Robert was appointed as an Independent Director at the Annual General Meeting of the company held on 29 -09- 2015 for a period of one year. Again, he was appointed in the subsequent Annual General Meeting held on 28-09-2016 for a period of two years as his second consecutive term. Examine under the provisions of the Companies Act, 2013 whether he can be again appointed in the Annual General Meeting to be held in September 2018 for another period of 2 years to complete his total term of 5 years?

Answer

As per **Section 149(10)** of the Companies Act 2013, an **Independent Director shall hold office for a term up to five consecutive years on the Board of a company**. He shall be **eligible for re-appointment on passing of a special resolution** by the company and disclosure of such appointment in the Board's report.

As per **section 149(11)** no independent director shall hold office for **more than two consecutive terms.** However, such independent director shall be **eligible for appointment after the expiration of three years** of ceasing to be an independent director.

The Ministry of Corporate Affairs in its General Circular 14/2014 dated June 09, 2014 clarified that **section 149 (10)** of the Act provides for a term of "**up to five consecutive years**" for an independent director. As such while appointment of an independent director for a term of less than five years would be permissible, appointment of any term (whether for five years or less) is to be treated as one

term under section 149 (10) of the Act.

Further under **section 149 (11)** of the Act, **no person hold office of independent director for more than 'two consecutive terms'**. Such a person shall have to demit office after the consecutive terms even if the total number years of his appointment in such two consecutive terms is less than 10 years.

Therefore **Mr. Robert cannot be appointed as an Independent Director at the AGM proposed to be held in 2018**. In such case the person completing **'consecutive terms of less than 10 years'** shall be eligible for appointment only after the expiry of the requisite cooling-off period of three years.

Question 8

Sky Limited, a listed company has been incorporated under the Companies Act, 2013. An intermittent vacancy of a woman director has arisen on 15th June, 2016. Advise the company to fill the vacancy as per the provisions of the Companies Act, 2013. The Board meeting was held on 14th August, 2016.

Answer

According to second proviso to **section 149(1)** of the Companies Act, 2013, **at least one woman director shall be on the Board of such class or classes of companies as may be prescribed**.

Further, any intermittent vacancy of a woman director shall be filled up by the Board at the earliest but not later than immediate next Board meeting or three months from the date of such vacancy, whichever is later.

An intermittent vacancy of a woman director has arisen in Sky Limited on 15th June, 2016. The **said vacancy shall be filled up by the Board at the earliest but not later than immediate next Board meeting** (14th August, 2016) **or 3 months from the date of such vacancy** (14th September, 2016), whichever is later. Thus, the vacancy can be filled by 14th September, 2016.

Question 9

XYZ Limited is an unlisted public company having a paid-up capital of twenty crore rupees as on 31st March, 2015 and a turnover of one hundred fifty crore rupees during the year ended 31st March, 2015. The total number of directors is thirteen.

Referring to the provisions of the Companies Act, 2013 answer the following:

i) State the minimum number of independent directors that the company should appoint.
ii) How many independent directors are to be appointed in case XYZ Limited is a listed company?

Answer

i) According to Rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014, the following class or classes of **companies shall have at least 2 directors as independent directors:**
   a) the **Public Companies** having **paid up share capital of 10 crore rupees or more**; or
   b) the **Public Companies** having **turnover of 100 crore rupees or more;** or
   c) the **Public Companies** which have, in **aggregate, outstanding loans, debentures and deposits, exceeding 50 crore rupees.**

   In the present case, XYZ Limited is an unlisted public company having a paid-up capital of Rs. 20 crores as on 31st March, 2015 and a turnover of Rs. 150 crores during the year ended 31st March, 2015. Thus, as per the Companies (Appointment and Qualification of Directors) Rules, 2014, XYZ Limited shall have at least 2 directors as independent directors.

ii) According to **section 149(4)** of the Companies Act, 2013, every **listed public company shall have at least one-third of the total number of directors as independent directors.**

In the present case, XYZ Limited is a listed company and the total number of directors is 13. Hence, in this case, XYZ Limited shall have atleast 5 directors (1/3 of 13 is 4.33 rounded as 5) as independent directors.

The explanation to **section 149(4)** specifies that any fraction contained in such one-third numbers shall be rounded off as one.

As the explanation to rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014 specifies that for the purpose of the assessment of the paid up share capital or turnover or outstanding loans, debentures and deposits, as the case may be, their existence on the last date of **latest audited financial statements shall be taken into account.**

In the present case, it is mentioned that paid up capital of XYZ Limited is Rs. 20 crore on 31st March, 2015 and turnover is Rs. 150 crore during the year ended 31st March, 2015. So, it is assumed that 31st March, 2015 is the last date of latest audited financial statements.

Question 10

In XYZ Ltd., an intermittent vacancy of the women director arises on 15th June 2019. By what time the vacancy so created should be filled the immediate Board Meeting was held on (a) 14th August 2019 (b) 14th Oct. 2019.

Answer

Filling of casual vacancy in case of Woman Director:

a) Rule 3 of Companies (Appointment and Qualification of Directors) Rules, 2014 provides that any intermittent vacancy of a woman director shall be filled-up by the Board at the earliest but not later than immediate next Board meeting or 3 months from the date of such vacancy whichever is later

b) In the present case, an intermittent vacancy of the women director arises on 15th June 2019.

Conclusion: Applying the provisions of Rule 3, following conclusions may be drawn:

a) If after the vacancy, the immediate next Board meeting was held on 14th August, 2019, then the vacancy shall be filled-up by 14th August, 2019 or by 14th September 2019 (3 months from the date of such vacancy) whichever is later. In this case, it shall be filled up by 14th Sep. 2019.

b) If after the vacancy, the immediate Board meeting was held on 14th October, 2019 then the vacancy shall be filled-up by 14th Oct., 2019 or by 14th Sep. 2019 whichever is later. In this case it shall be filled up by 14th Oct., 2019.

Question 11

Royal limited is company listed at Madras Stock Exchange, incorporated on 1st January, 2018. The Board of Directors of the company decides to appoint in its Board 'Women Director' and the **'**Resident Director':

i) Explaining the provisions of the Companies Act, 2013, state whether it is mandatory for the company to appoint such directors in its Board.

ii) What would be your answer in case the company is a non-listed company and the Board of Directors decided not to have the Women Director in the company's Board?

What shall be your answer in case the company in question is not listed at any of the Exchanges. The paid up share capital of the company is ₹ 50 crore and the turnover of the company is ₹ 200 crores. Decide whether the company is mandatorily required to appoint the woman director.

Answer

Requirement of Woman Director and resident Director:

- Proviso to Sec, 149(1) read with Rule 3 of Companies (Appointment and Qualification of Directors) Rules, 2014 provides that following class of companies shall appoint atleast one women director

i) Every listed company;

ii) Every other public company having:
   a) paid-up share capital of 100 Cr. or more; or
   b) turnover of 300 Cr. or more.

- The paid-up share capital or turnover as on the last date of latest audited FS shall be considered for this purpose.
- In case of newly incorporated companies covered under prescribed criteria of Rule 3, appointment shall be made within six months from the date of incorporation
- Sec. 149(3) of Companies Act, 2013 provides that every company shall have at least one director who stays in India for a total period of not less than 182 days during the financial years
- Provided that in case of a newly incorporated company the requirement u/s 149(3) shall apply proportionately at the end of the financial year in which it is incorporated.
- Conclusions: Applying the provisions of Sec. 149(1), 149(3) and Rule 3, following conclusions may be drawn:

i) It is mandatory to appoint women director (as company is a listed company) and resident director (as required by Sec. 149(3)]

ii) in case of unlisted company, appointment of women directors is not mandatory provided company is not covered under Rule 3.

Appointment of woman director is not mandatory as company does not fall under the categories prescribed in Rule 3.

Question 12 ***(May 19)***

KMR Limited, a listed public company, has 15 directors on its Board. The Articles of Association of the said company provide for the maximum number of Directors in the company to be 15. Due to diversification and expansion of activities, the Board of Directors of the said company desire to increase the number of Directors to 18. Decide with reference to the applicable provisions of the Companies Act, 2013:

i) Whether the Board of Directors can do so?

ii) Will your answer differ if the said Company would have been a Government Company?

Answer

Increase in number of Directors:

- Sec. 149(1) of the Companies Act, 2013 provides that every company shall have a Board of Directors consisting of individuals as directors and shall have a minimum number of 3 directors in the case of a public company, 2 directors in the case of a private company, and one director in the case of a One-Person Company. The maximum number of directors shall be 15.
- However, a company may appoint more than 15 directors after passing a special resolution.

- Limit of Maximum directors and their increase is not applicable to Government Companies and Sec. 8 Companies provided these companies has not committed a default in filing of their financial statements u/s 137 or annual return u/s 92 with the Registrar:
- In the present case, the number of directors is proposed to be increased to 16, company will be required to comply with the followings:

i) Alter the Articles of Association u/s 14, so as to increase the number of directors in the Articles from 10 to 16;

ii) A special resolution is to be passed at a duly convened general meeting of the company to increase the number of directors to 16.

- Conclusion – Applying the provisions of sec 149(1) and exemption available, following conclusions may be drawn:

i) BOD can increase the number of directors after altering AOA u/s 14 and by passing a special resolution u/s 149(1)

ii) In case of Govt. companies limit of maximum directors not applicable, hence, BOD can increase the number.

Question 13

Mr. Azad, an independent director of X company, was appointed in the AGM to a period of three years. After the expiry of 3 years he was re-appointed for a period as re-appointed for a period of 5 years. Considering that though Mr. Azad has completed two tenures /terms but hasn't completed ten years in total, therefore he may be appointed in the upcoming AGM for another 2 years to complete his total term of 10 years. Conferring in the light of the Companies Act, 2013, State the validity of reappointment of Mr. Azad for further term in the company.

Answer

Tenure of Independent Director

- Sec. 149(10) of Companies Act, 2013 provides that an independent director shall not hold office for a term up to 5 consecutive years on the Board of a company but shall be eligible for reappointment on passing of a special resolution by the company and disclosure of such appointment in the Board's report.
- Section 149(11) of Companies Act, 2013 provides that no independent director shall hold office For more than 2 consecutive terms, but such independent director shall be eligible for appointment after the expiration of 3 years of ceasing to become an independent director, provided that he Shall not, during the said period of 3 years, he appointed in or be associated with the company in any other capacity, either directly or indirectly,
- It is clarified by MCA that one tenure of independent directors may be for a period less than 5 years and if tenure of independent directors is fixed for a period less than 5 years, than cooling period of 3 years arises on completion of two tenures even if the total number of years of his appointment in such two consecutive terms is less than 10 years.
- In the present case, Mr. Azad, an independent director, has completed two tenures in the company, one for three years and second for 5 years
- Conclusion: Reappointment for third term is not allowed in continuation, a cooling off period of 3

years will be required after completion of two tenures, irrespective that period served under two tenures is less than 10 years.

Question 14

MLtd. is an unlisted company engaged in TMCG sector having 11 directors on its Board. The company has paid-up share capital of 300 crore and a turnover of 500 crore. The provisions contained in the Companies Act, 2013 require the companies to have the following categories of Directors on their Board

a) Woman director
b) Independent director

Keeping in view of the provisions of the Companies Act, 2013, M Ltd. appointed the directors as required by the Act. State the relevant provisions.

Answer

Appointment of Woman Director:

- Proviso to Sec. 149(1) read with Rule 3 of Companies (Appointment and Qualification of Directors) Rules, 2014 provides that following class of companies shall appoint atleast one women director:

i) Every listed company;
ii) Every other public company having;
   a) paid-up share capital of 100 Cr. or more: or
   b) turnover of 300 Cr. or more.

   The paid-up share capital or turnover as on the last date of latest audited F.S. shall be considered for this purpose.

- In case of newly incorporated companies covered under prescribed criteria of Rule 3, appointment shall be made within six months from the date of incorporation.

Appointment of Independent Director:

- As per Sec. 149(4) of Companies Act, 2013, every listed public company shall have at least one-third of the total number of directors as independent directors.
- As per Rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014, the following class or classes of companies shall have at least 2 directors as independent directors:

i) the Public Companies having paid up share capital of 10 crore rupees or more; or
ii) the Public Companies having turnover of 100 crore rupees or more; or
iii) the Public Companies which have, in aggregate outstanding loans, debentures and deposits, exceeding 50 crore rupees.

- Conclusion – considering the requirements of sec 149(1) read with Rule 3 and sec 149(4) read with Rule 4, company must have one woman director and two independent directors.

Question 15 ***(RTP - May 19)***

Rudraksh Ltd., a public company, was incorporated for supply of solar panels for the emerging project of government for construction of highways. However, the said project did not turn up for two years due to some legal implications. During the said period, no any significant accounting transaction was made and so the company did not file financial statements and annual returns during the last two financial years. In the meantime, the Board proposed for Mr. Ram & Mr. Rahim to be appointed as an

Independent Directors for their independent and expertise knowledge and experience for better working and improvement of financial position of the company.
Evaluate in the light of the given facts, nature of the proposal for an appointment of Mr. Ram & Mr. Rahim in the Rudraksh Ltd. for improvement of the company,

Answer

Requirement of Independent Directors:

- As per sec. 149(4) of Companies Act, 2013, every listed public company shall have at least one-third of the total number of directors as independent directors
- As per Rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014, the following class or classes of companies shall have at least 2 directors as independent directors:

i) the Public Companies having paid up share capital of 10 crore rupees or more; or
ii) the Public Companies having turnover of 100 crore rupees or more; or
iii) the Public Companies which have, in aggregate, outstanding loans, debentures and deposits exceeding 50 crore rupees.

- Where a company ceases to fulfil any of the above 3 conditions for 3 consecutive years, it shall not be required to comply with these provisions until such time as it meets any of such conditions.
- However, following classes of unlisted public companies shall not be required to have minimum independent director:

i) A Joint venture
ii) A wholly owned subsidiary, and
iii) A dormant company.

- In the present case Rudraksh Ltd. has not filed financial statements or annual returns for 2 financial years consecutively, status of the company will be of dormant company.
- Conclusion: Proposal for appointment of Independent Director (Mr. Ram & Mr. Rahim) is not necessitated as a dormant company is not required to have independent director.

Appointment of Directors Elected by Small Shareholders (Section 151)

Question 16

M/s. Bharat Pharma Limited is a company listed with Bombay Stock Exchange. The company were having 500 small shareholders in the said company, so they wanted to appoint Mr. A as a Director as their representative on the Board of Directors of the said company. Mr. A is holding 1000 equity shares of 10 each in the said company. State in the light of the Companies Act, 2013 whether the proposal to appoint Mr. A as a Small Shareholders' Director can be adopted by the company. Examine, if Mr. A is already holding a position of small shareholders' director in more than two companies.

Answer

Section 151 of the Companies Act, 2013 provides that a **listed company** may have **one director elected by such small shareholders** in such manner and with such terms and conditions as may be prescribed. Further, the explanation to section 151 clarifies that for the purposes of this Section **small shareholders means a shareholder holding shares of nominal value of not more than twenty thousand rupees** or such other sum as may be prescribed.

The Companies (Appointment & Qualifications of Directors) Rules, 2014 clearly provides that a **listed company, may upon notice of not less than one thousand small shareholders or one- tenth of the total number of such shareholders, whichever is lower**, have a small shareholders' director elected by the small shareholders.

In the given case, the company is a listed one, hence the provisions of section 151 will apply. Therefore, the number of small shareholders who can send the notice for the appointment of a small shareholders director must not be less than 1,000 or one tenth of the total number of small shareholders i.e., 50 small shareholders may propose a person as a candidate for the post of small shareholders. They must give **14 days notice** to the company under their signatures specifying the **name, address, shares held and folio number** of the person whose name is being proposed for the post of director and of the small shareholders who are proposing such person for the office of director.

Thus, as per the above provision, Company may appoint Mr. A as small shareholders' director in the company. Also, that Mr. A shall not hold the position of small shareholders' director in more than two companies at the same time. Provided that the second company in which he has been appointed shall not be in a business which is competing or is in conflict with the business of the first company.

Question 17 ***(Nov 2011)***

Neemuch Pharma Limited is a company listed with Malhargarh Stock Exchange. Some small shareholders of the said company want to appoint Mr. Avadhesh as a Director as their representative on the Board of Directors of the said company. Mr. Avadhesh is holding 1000 equity shares of 10 each in the said company. State the provisions of the Companies Act, 2013 in relation to the proposal to appoint Mr. Avadhesh as a Small Shareholders' Director.

Answer

Section 151 of the Companies Act, 2013 provides that a listed company may have one director elected by such small shareholders in such manner and with such terms and conditions as may be prescribed. Further, the explanation to section 151 clarifies that for the purposes of section 151 **"small shareholders"** means a **shareholder holding shares of nominal value of not more than ₹ 20,000 or such other sum as may be prescribed.**

In the given case, the company is a listed one; hence the provisions of section 151 will apply.

The Companies (Appointment & Qualifications of Directors) Rules, 2014 clearly provides that a listed company, may upon notice of **not less than 1,000 small shareholders or one- tenth of the total number of such shareholders, whichever is lower, have a small shareholders' director elected by the small shareholders.**

Therefore, the number of small shareholders who can send the notice for the appointment of a small shareholders director must not be less than 1,000 or one tenth of the total number of small shareholders. This is not clarified in the question. Presuming that the small shareholders meet the criteria, they must give 14 days' notice to the company under their signatures specifying the name, address, shares held and folio number of the person whose name is being proposed for the post of director and of the small shareholders who are proposing such person for the office of director.

Further, the notice shall be accompanied by a statement signed by the person whose name is being proposed for the post of small shareholders' director stating -

i) his **Director Identification Number**;
ii) that he is **not disqualified** to become a director under the Act; and
iii) his **consent to act as a director** of the company

From the above, it is clear that Mr. Avadhesh who holds 1,000 shares in the company is not debarred from being appointed the small shareholders' director in the company.

Question 18 ***(May 2016)***

DD Ltd. is a listed company and it has been served with notice for appointment of small shareholders' director. Referring to the provisions of the Companies Act, 2013, advise on the following:

i) Define the expression 'small shareholder' and specify the number of small shareholders who may serve notice on the company for a director representing them.

ii) Is it possible to appoint a person who does not hold any share in the company, as small shareholders' director?

iii) What is the tenure of small shareholders' director and whether he can be re- appointed as such, after expiry of his tenure? Also state whether he can be appointed as an officer of the company on expiry of his tenure as small shareholders' director.

Answer

i) According to **section 151** of the Companies Act, 2013, a listed company may have one director elected by small shareholders in such manner and on such terms and conditions as may be prescribed.

Here, "**Small Shareholders**" means a shareholder **holding shares of nominal value of not more than Rs. 20,000** or such other sum as may be prescribed.

A listed company may upon notice of not less than

a) **one thousand small shareholders**; or

b) **one- tenth of the total number of such shareholders**,

whichever is lower, have a small shareholders' director elected by the small shareholders.

ii) The small shareholders intending to propose a person as a candidate for the post of small shareholders' director shall leave a notice of their intention with the company **at least fourteen days before the meeting under their signature specifying the name, address, shares held and folio number of the person whose name is being proposed for the post of director and of the small shareholders who are proposing such person for the office of director.**

However, if the person being proposed does not hold any shares in the company, the details of shares held and folio number need not be specified in the notice.

Further, the notice shall be accompanied by a statement signed by the person whose name is being proposed for the post of small shareholders' director stating-

a) his **Director Identification Number;**

b) that he is **not disqualified to become a director under the Act; and**

c) his **consent to act as a director of the company**

iii) The tenure of small shareholders' director **shall not exceed a period of 3 consecutive years and on the expiry of the tenure, such director shall not be eligible for re-appointment.**

A small shareholders' director shall not, for a period of 3 years from the date on which he ceases to hold office as a small shareholders' director in a company, be appointed in or be associated with such company in any other capacity, either directly or indirectly.

Question 19 ***(Nov 2016)***

Mr. Intelligent, was appointed as a small shareholder's director of XYZ Limited, which is in the business of Oil refining. Subsequently, A Limited and B Limited have also appointed him as small shareholder's director. Is the appointment valid?

Answer

Appointment of small shareholder's director:

As per the Rule 7(8) of the Companies (Appointment and Qualification of Directors) Rules, 2014, read with section 151 of the Companies Act, 2013 regarding the appointment of small shareholders' director, no person shall hold the position of small shareholders' director in more than 2 companies at the same time. However, **the second company in which he has been so appointed shall not be in a business which is competing or is in conflict with the business of the first company.**

In the given case, Mr. Intelligent was appointed as a small shareholder's director of XYZ Ltd. Subsequently A Ltd. and B Ltd. have also appointed him as small shareholder's director.

Considering the above provision, appointment of Mr. Intelligent in both A Ltd. and B Ltd. is invalid. However, **he can accept appointment in either A Ltd. or B Ltd., subject to the maximum limit of 2 companies provided either A Ltd. or B Ltd. is not having a business which is competing or is in conflict with the business of the XYZ Ltd.**

Question 20

The Board of directors of M/s ABC Limited, an unlisted company having Limited, an unlisted company having a paid-up capital of 6 crores consisting of equity share capital of 5 crores and preference share cap also 1,100 'Small Shareholders' holding equity shares seeks seeks your advice on the following:

"Is it necessary for the Company to appoint a Director to represent the 'Small Shareholders"? Advise explaining the relevant provisions of the Companies Act, 2013 and the Rules.

Answer

Requirement of Small Shareholder's Director:

Section 151 of Companies, Act, 2013 read with Rule 7 of the Companies (Appointment and Qualification of Directors) Rules, 2014 provides that a listed company may have one director elected by such small shareholders in such manner and with such terms and conditions as may be prescribed.

In the present case, the Board of directors of M/S ABC Limited, an unlisted company having a paid-up capital of 6 crores consisting of equity share capital of 5 crores and preference share capital of 1 crore and also 1,100 'Small Shareholders' holding equity shares seeking advice for requirement of director to represent the small shareholders.

Conclusion: Requirement of Small shareholder director applies in case of listed company. Whereas in the present case, ABC Ltd. is an unlisted company, so requirement of director to shareholder is not applicable.

Question 21

ABC Ltd. is a listed company having 50,00,000 equity shares of 100 each as its paid up capital. of the

total shareholders of the company there are 20000 shareholders who are holding shares of nominal value of not more than ₹ 20000 each. A group of shareholders who had applied for shares at the time of issue of such shares by the company by issuing prospectus and been allotted these shares, wants to appoint a small shareholder's director to safeguard their interest and to get a proper representation in the company. A total number of 1500 such small shareholders decided to propose Mr. X as their candidate for this post.

In the light of the Companies Act, 2013 on the basis of the facts provided, determine the following situations-

a) What procedure should be followed by group of shareholders to have Mr. X, a small shareholder director in the Board of Directors of the company?

b) What are the provisions related to his (Mr. X) status as an independent director and what exceptions are available to him in relation to his appointment as a director?

Answer

Procedure for appointment of director elected by small shareholders:

Sec. 151 of Companies Act, 2013 provides that a listed company may have one director elected by such small shareholders in such manner and with such terms and conditions as may be prescribed.

Rule 7 of the Companies (Appointment and Qualification of Directors) Rules, 2014 provides that a listed company, may upon notice of not less than 1,000 small shareholders or 1/10th of the total number of such shareholders, whichever is lower have a small shareholders' director elected by the small shareholders.

Small shareholders intending to propose a person as a candidate for the post of small shareholders shall leave a notice of their intention with the company at least 14 days before the meeting under their signatures specifying the name, address, shares held and folio number of the person whose name is being proposed for the post of director and of the small shareholders who are proposing such person for the office of director.

If the person being proposed does not hold any shares in the company, the details of shares held and folio number need not be specified in the notice.

The notice shall be accompanied by a statement signed by the person whose name is being proposed for the post of small shareholders' director stating -

a) his Director Identification Number;
b) that he is not disqualified to become a director under the Act; and
c) his consent to act as a director of the company.

A person shall not be appointed as small shareholders' director of a company, if the person is not eligible for appointment in terms of Sec 164.

Status of Small Shareholder Director:

Rule 7 of the Companies (Appointment and Qualification of Directors) Rules, 2014 provides that such director shall be considered as an independent director subject to, his being eligible u/s 149(6) and his giving a declaration of his independence in accordance with Sec. 149(7).

Exceptions subject to which small shareholder directors are appointed:

The appointment small shareholders' director shall be subject to the provisions of section 152 except that-

a) such director shall not be liable to retire by rotation;
b) such director's tenure as small shareholders' director shall not exceed a period of 3 consecutive years; and
c) on the expiry of the tenure, such director shall not be eligible for re-appointment.

Question 22 ***(Nov 2018)***

The Board of Director of M/s. Diya Steels and Aluminium Limited, a listed company having a paid up equity share capital of 15 crores and preference share capital of 1 crore and 1100 small shareholders holding equity shares, seeks your advice on the following:

i) Is it mandatory for the company to appoint a Director to represent Small Shareholders?
ii) If the company decides to appoint such a Director, the procedure to be followed by the company for such appointment and the tenure for which such appointment can be made.
iii) Whether such a Director be considered as an Independent Director?
iv) When does a person appointed as a small shareholders Director vacate his office?

Advise suitably in the light of the provisions of the Companies Act, 2013 and the rules framed thereunder:

Answer

Provisions as to appointment of directors elected by Small Shareholders:

a) Mandatory Requirement to appoint a Director to represent Small Shareholder:

Sec. 151 of Companies Act, 2013 provides that a listed company may have one director elected by such small shareholders in such manner and with such terms and conditions as may he prescribed.

Rule 7 of the Companies (Appointment and Qualification of Directors) Rules, 2014 provides that a listed company may upon notice of not less than 1,000 small shareholders or $1/10^{th}$ of the total number of such shareholders, whichever is lower, have a small shareholders director elected by the small shareholders.

Conclusion: Use of the term 'may' make it clear that there is no mandatory requirement for a listed company to have a director elected by such small shareholders on its Board.

b) Procedure to be followed for appointment of director to represent small shareholder:

The small shareholders intending to propose a person as a candidate for the post of Small Shareholder's Director shall leave a signed notice of their intention with the company at least 14 days before the meeting specifying their details and proposed director's details.

The details shall include name, address, shares held and folio number etc. of small share- holders and proposed director. If the proposed director does not hold any shares in the company, the details of shares held and folio number need not be specified in the notice.

The notice shall be accompanied by a statement signed by the person whose name is being proposed for the post of small shareholders' director stating –

a) his Director Identification Number;
b) that he is not disqualified to become a director under the Act; and
c) his consent to act as a director of the company.

Tenure: Rule 7 of the Companies (Appointment & Qualification of Directors) Rules, 2014 provides that the tenure of small shareholders director shall not exceed a period of 3 consecutive years & on the expiry of the tenure, such director shall not be eligible for re-appointment.

c) Status of Small Shareholder Director:

Rule 7 of the Companies (Appointment and Qualification of Directors) Rules, 2014 provides that such director shall be considered as an independent director subject to his being eligible u/s 14916) and his giving a declaration of his independence in accordance with Sec. 149(7).

d) Vacation or office by Small Shareholder Director:

A person appointed as small shareholders director shall vacate the office if-

a) he incurs any of the disqualifications specified in Sec. 164;
b) the office of the director becomes vacant in pursuance of section 167;
c) he ceases to meet the criteria of independence as provided in Sec. 149(6).

Question 23 ***(May 2019)***

B Ltd. is a listed Company and it has been served with a notice for appointment of a small share-holders director, Referring to the provisions of the Companies Act, 2013, examine the following;

i) The tenure of small shareholders' director and whether he can be re-appointed as such, after expiry of his tenure?

ii) Whether he can be appointed as an officer of the Company on expiry of his tenure as small shareholders' director.

Answer

i) Tenure of Small Shareholder Director:

Sec. 151 of Companies, Act, 2013 provides that a listed company may have one director elected by such small shareholders in such manner and with such terms and conditions as may be prescribed.

Rule 7 of the Companies (Appointment and Qualification of Directors) Rules, 2014 provides that the tenure of small shareholders' director shall not exceed a period of 3 consecutive years.

Rule 7 further provides that on the expiry of the tenure, such director shall not be eligible for re-appointment.

ii) Eligibility for being appointed as an officer in the company after expiry of tenure:

A small shareholders' director shall not, for a period of three years from the date on which he ceases to hold office as a small shareholders' director in a company, be appointed in or be associated with such company in any other capacity, either directly or indirectly.

Appointment of Directors (Section 152)

Question 24

Annual general meeting of Hero Ltd. has been scheduled in compliance with the requirements of the Companies Act, 2013. In this connection, it has some directors who are rotational and out of which some have been appointed long back, some have been appointed on the same day.
Decide in this connection:

i) Which of the directors shall be retiring by rotation?
ii) In case two directors were appointed on the same day, how would you decide their retirement

by rotation?

iii) In case the meeting could not decide how the vacancies caused by retirement to be dealt with, what shall be consequences?

Answer

Rotational Directors and Retirement:

i) According to **section 152(6)(a)(i)** of the Companies Act, 2013, unless the articles provide for the retirement of all directors at every annual general meeting, **not less than two- thirds of the total number of directors of a public company shall be persons whose period of office is liable to determination by retirement of directors by rotation.**

Further, section 152(6)(c) of the Act states that **one-third of such of the directors for the time being as are liable to retire by rotation,** or if their number is neither three nor a multiple of three, then, the number nearest to one-third, shall retire from office.

From the above provisions, it is clear that the directors who are liable for rotation at every annual general meeting shall be one third of those directors who constitute the two thirds of the total number of directors and who are liable for rotation at every AGM.

ii) Under **section 152(6)(d)** the directors to retire by rotation at every annual general meeting shall be those **who have been longest in office since their last appointment**, but as between persons who became directors on the same day, those who are to retire shall, in default of and subject to any agreement among themselves, be **determined by lot**. Therefore, the directors who will retire by rotation shall be those who have been in office for the longest term since their appointment. **In case of two or more directors who were appointed on the same date at the same AGM**, the retiring directors will be **mutually agreed by them or in the absence of such agreement, will be determined by lots.**

iii) Under **section 152(6)(e)** of the Companies Act, 2013 the Vacancy caused by the retirement of directors at the AGM may be filled in the same annual general meeting by appointing either the retiring directors or some other person. The annual general meeting may also decide not to fill the vacancy arising from the retirement of one or more directors.

Section 152(7) (a) provides that if the vacancy of the director retiring by rotation, is **not so filled-up and the meeting has not expressly resolved not to fill the vacancy**, the meeting shall stand **adjourned till the same day in the next week, at the same time and place**, or if that day is a national holiday, till the next succeeding day which is not a holiday, at the same time and place.

Section 152 (7)(b) further provides that if at the adjourned meeting also, the vacancy of the retiring director is not filled up and that meeting also has not expressly resolved not to fill the vacancy, the **retiring director shall be deemed to have been re-appointed at the adjourned meeting, unless:**

a) At that meeting or at the previous meeting **a resolution for the re-appointment of such director has been put to the meeting and lost;**
b) The retiring director has, by a **notice in writing** addressed to the company or its Board of directors, expressed his unwillingness to be so re-appointed;
c) He is **not qualified or is disqualified** for appointment;
d) A **resolution, whether special or ordinary, is required for his appointment** or re-appointment by virtue of any provisions of this Act; or
e) **Section 162** (appointment of directors to be voted individually) is applicable to the case.

Question 25

ABC Ltd. in its First General Meeting appointed six Directors whose period of office is liable to be determined by rotation. Briefly explain the procedure and rules regarding retirement of these directors. Will it make any difference, if ABC Company Ltd. does not carry on business for Profit?

Answer

Under **section 152(6) (a)** unless the articles provide for the retirement of all directors at every annual general meeting, **not less than two-thirds of the total number of directors of a public company shall be persons whose period of office is liable to determination by retirement of directors by rotation.**

In the given case, it is assumed that the 6 directors appointed at the first general meeting of the company constitute at least two thirds of the total number of directors.

Section 152(6)(c) further states that at every annual general meeting**, one-third of such of the directors for the time being as are liable to retire by rotation,** or if their number is neither three nor a multiple of three, then, the number nearest to one-third, shall retire from office.

Therefore, in the given case 2 directors will be liable to retire by rotation at the next AGM of the Company.

Section 152(6)(d) further states that the directors to retire by rotation at every annual general meeting shall be those who have been longest in office since their last appointment, but as between persons who became directors on the same day, those who are to retire shall, in default of and subject to any agreement among themselves, be determined by lot.

In the given case, all the 6 directors were appointed on the same date. Hence, the choice of the 2 directors who would retire at the next AGM of the company will be made either mutually by these 6 directors failing which; it will be decided by lots.

It will not make any difference under the Companies Act, 2013 if the company is a non-profit organization.

Question 26

ADJ Limited has 10 directors on its board. Two of the directors have retired by rotation at an Annual General Meeting. The place of retiring directors is not so filled up and the meeting has also not expressly resolved 'not to fill the vacancy'. Since the AGM could not complete its business, it is adjourned to a later date. At this adjourned meeting also the place of retiring directors could not be filled up, and the meeting has also not expressly resolved 'not to fill the vacancy'.

Referring to the provisions of the Companies Act, 2013, decide:

i) Whether in such a situation the retiring directors shall be deemed to have been re- appointed at the adjourned meeting?

ii) What will be your answer in case at the adjourned meeting, the resolutions for re- appointment of these directors were lost?

iii) Whether such directors can continue in case the directors do not call the Annual General Meeting?

Answer

Retiring director – When to be deemed director?

In accordance with the provision of the Companies Act, 2013, as contained in **section 152(7)(a)** which provides that if at the annual general meeting at which a director retires and the **vacancy is not so filled up and the meeting has not expressly resolved not to fill the vacancy**, the meeting

shall stand adjourned to **same day in the next week, at the same time and place**, or if that day is a national holiday, till the next succeeding day which is not a holiday, at the same time and place.

Section 152(7)(b) further provides that if at the adjourned meeting also, the **place of the retiring is not filled up and that meeting also has not expressly resolved not to fill the vacancy**, the **retiring director shall be deemed to have been re-appointed at the adjourned meeting**, unless at the adjourned meeting or at the previous meeting a resolution for the re-appointment of such directors was put and lost or he has given a notice in writing addressed to the company and the Board of Directors expressing his desire not to be re-elected or he is disqualified.

Therefore, in the given circumstances answer to the questions as asked shall be:

i) In the first case, applying the above provisions, the retiring directors shall be deemed to have been re-appointed.

ii) In the second case, where the resolutions for the reappointment of the retiring directors were lost, the retiring directors shall not be deemed to have been re-appointed.

iii) Section 152(6)(c) states that 1/3rd of the rotational directors shall retire at every AGM. They retire at the AGM and at its conclusion. Hence, they will retire as soon as the AGM is held. Further, as per section 96 (dealing with annual General Meeting) of the Companies Act, 2013, every company other than a One Person Company shall in each year hold an Annual General Meeting. Hence, it is necessary for the company to hold the AGM, whereby these directors will be liable to retire by rotation.

Question 27 ***(Nov 2015)***

A and B were appointed as first directors on 4th April, 2014 in Sun Glass Ltd. Thereafter, C, D and E were appointed as directors on 6th July 2014 and F, G and H were also appointed as directors on 7th August 2014 in the company. In the Annual General meeting (AGM) of the company held after the above appointments, A and B were proposed to be retired by rotation and re-appointed as directors.

At the AGM, resolution for A's retirement and re-appointment was passed. However, before the resolution for 'B' could be taken up for consideration, the meeting was adjourned. In the adjourned meeting also, the said resolution could not be taken up and the meeting was ended without passing the resolution for B's retirement and re- appointment.

In the light of above and with reference to relevant provision of the Companies Act, 2013, answer the following:

i) Whether proposals for retirement by rotation and re-appointment of A and B only were sufficient?

ii) What will be the status of B as a director in the company?

Answer

According to **section 152(6)(a)(i)** of the Companies Act, 2013, unless the articles provide for the retirement of all directors at every annual general meeting, **not less than two- thirds of the total number of directors of a public company shall be persons whose period of office is liable to determination by retirement of directors by rotation.**

Further, **section 152(6)(c)** of the Act states that at the first annual general meeting of a public company held next after the date of the general meeting at which the first directors are appointed and at every subsequent annual general meeting, one-third of such of the directors for the time

being as are liable to retire by rotation, or if their number is neither three nor a multiple of three, then, the number nearest to one-third, shall retire from office.

Section 152(6)(d) further states that the directors to retire by rotation at every annual general meeting shall be those who have been longest in office since their last appointment, but as between persons who became directors on the same day, those who are to retire shall, in default of and **subject to any agreement among themselves, be determined by lot**.

Section 152(7) (a) provides that if the vacancy of the director retiring by rotation, is not so filled-up and the meeting has not expressly resolved not to fill the vacancy, the **meeting shall stand adjourned till the same day in the next week, at the same time and place, or if that day is a national holiday**, till the next succeeding day which is not a holiday, at the same time and place.

Section 152 (7)(b) further provides that if at the adjourned meeting also, the vacancy of the retiring director is not filled up and that meeting also has not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been re-appointed at the adjourned meeting, unless:

a) at that meeting or at the previous meeting a **resolution for the re-appointment of such director has been put to the meeting and lost;**
b) the retiring director has, by a notice in writing addressed to the company or its Board of directors, **expressed his unwillingness to be so re-appointed**;
c) he is not qualified or **is disqualified for appointment;**
d) a resolution, whether **special or ordinary, is required for his appointment or re- appointment by virtue of any provisions of this Act**; or
e) section 162 is applicable to the case.

i) In the given case there are total 8 directors, out of which A and B were appointed as first directors of Sun Glass Ltd.

As per the provisions of **section 152** of the Companies Act, 2013, the number of directors liable to retire by rotation at the next Annual General Meeting are 2 [1/3 of (2/3 of 8)].

Therefore, in the given case, **2 directors will be liable to retire by rotation** at the next AGM of the Company, which in this case will be A and B as they are who have been longest in office since their last appointment. Thus, the proposals for retirement by rotation and re-appointment of A and B only were sufficient.

ii) According to **section 152(6)(c)**, at the annual general meeting, one-third of rotational directors shall retire from office. Thus, B shall retire at the Annual General Meeting in which he was due to retire even though it was adjourned without the resolution for B's retirement could have been taken up.

Further, at the adjourned meeting also, the vacancy of the retiring director is not filled up and that meeting also has not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been re-appointed at the adjourned meeting as he does not fall in the category of any of the exceptions mentioned in section 152(7)(b). Hence, B will be deemed to be re-appointed as a director in the company.

Question 28 ***(RTP Nov 18)***

The Promoters of M/s Frontline Limited, a listed public company propose to have the strength of the Board of Directors as eleven. They also propose to make the Managing Director and Whole Time directors as directors not liable to retire by rotation. Advice on the following matters as per the provisions of the Companies Act, 2013:

(a) Maximum number of persons, who can be appointed as directors not liable to retire by rotation.

(b) How many of the remaining directors will have to retire by rotation every year at the Annual General Meeting (AGM)?

(c) For the purpose of increasing the strength, certain nominations were received to nominate candidates for contesting elections. One of the nominations was rejected by the directors as it was received after sending the notice of AGM and that too after the working hours of the last day on which nomination should have been received.

(d) Can the Board of Directors increase the strength of companies' directors to 18 from 11 by appointing additional directors through passing single resolution?

Answer

(a) According to **Section 152(6)** of the Companies Act, 2013, unless the articles provide for the **retirement of all directors at every annual general meeting, not less than two-thirds of the total number of directors of a public company shall be persons whose period of office is liable to determination by retirement of directors by rotation** Directors liable to retire by rotation: 11 * 2/3 =7.3 or 8

So, maximum number of persons, who can be appointed as directors not liable to retire by rotation: 11-8 = 3.

(b) According to **Section 152(6)(c)** of the Companies Act, 2013, **1/3rd of such of the Directors for the time being as are liable to retire by rotation**, or their number is neither three nor a multiple of three, then, the number nearest to the 1/3 rd shall retire from office. Therefor the Directors liable to retire by rotation are 11*2/3 i.e. 7.3 or 8.

No. of directors to retire at AGM: 8 * 1/3 i.e.2.67. Hence nearest to 1/3 rd is 3.

(c) According to **Section 160** of the Companies Act, 2013, a person who is not a retiring director in terms of Section 152 shall, subject to the provisions of this Act, **be eligible for appointment to the office of a director at any general meeting, if he has, not less than 14 days before the meeting**, left at the registered office of the company, a notice in writing under his hand signifying his can didature as a director.

In the instant case, one nomination was rejected by the directors as it was received after sending the notice of AGM and that too after the working hours of the last day on which nomination should have been received i.e. 14th day. Hence, the contention of the directors are valid.

(d) According to **Section 149(1)** of the Companies Act, 2013, if the **company wants to appoint more than 15 directors, it can do so after passing a special resolution**. Hence, the Board of directors of Frontline Limited, before increasing the strength of directors from 11 to 18 by **appointing additional directors, have to pass a special resolution.**

But, these appointments cannot be done through single resolution. Each director shall be appointed by a separate resolution unless the meeting first agreed that the appointment shall be made by a single resolution and no vote has been cast against such agreement. A resolution moved in contravention of this provision shall be void, whether or not objection thereto was raised at the time it was so moved. [Section 162 of the Act].

Question 29

A company has 11 directors on the Board consisting of the following:

a) Mr. Active, Mr. Archive as nominees from two Public Financial Institutions.

b) Mr. First, Mr. Second, Mr. Third appointed at the 2nd AGM.

c) Mr: Fourth, Mr. Fifth appointed at the 3rd AGM.
d) Mr. Addition was appointed as additional director subsequent to 3rd AGM
e) Mr. Casual was appointed as director in place of Mr. Soul who died and was earlier appointed during the 3rd AGM.
f) Mr. Excellent was appointed as Managing Director for 5 years w.e.f. 2nd AGM.
g) Mr. One more was appointed as additional Director soon after Mr. Addition was appointed as Additional Director.

List out in order, who shall be vacating the office at the 4th AGM of the company

Answer

Determination of order in which directors have to vacate the office:

Section 152(6) of the Companies Act, 2013 provides that unless the Articles provide for retirement of all the directors at every general meeting, not less than 2/3rd of the total number of directors of a public company, shall be persons whose period of office is liable to determination by retirement of directors by rotation.

At the first AGM of a public company held next after the date of the general meeting at which the first directors are appointed and at every subsequent AGM, 1/3rd of such of the directors for the time being as are liable to retire by rotation, or if their number is neither 3 nor a multiple of 3, then, the number nearest to 1/3rd, shall retire from office.

The directors to retire by rotation at every annual general meeting shall be those who have been longest in one since their last appointment, But as between persons who became directors on the same day those who are to retire shall in default of and subject to any agreement among themselves be determined by lot.

Sec. 161(1) of Companies Act, 2013 provides that additional director shall hold office upto the date of next AGM should have been held, whichever is earlier.

The position in regard to the 11 directors was under:

i) Provisions regarding appointment and removal of directors does not apply over the nominee directors. Hence, Mr. Active & Mr. Archive, who are nominees of Public Financial institution respectively, will not be considered for total number of directors for the purpose of 152(6)
ii) Mr. First, Mr. Second Mr. Third. Mr. Fourth Mr. Fifth are appointed in AGM and hene considered as rotational directors for the purpose of Sec. 152(6)
iii) Mr. Additions Me One More who were appointed as Additional Directors subsequent to 3rd AGM will be considered as Non-Rotational directors who, shall vacate office of the date of 4th AGM.
iv) Mr. Casual was appointed in place of Mr. Soul who died and will, therefore, hold office till the date Mr. Soul would have held office
v) Mr. Excellent the Managing director may be rotational or non-rotational director depending upon terms of appointment.

Total number of directors for the purpose of Sec 152(6) counted as 9. 2/3rd of 9, i.e. 6 should be rotational director and 1/3rd of 6, i.e. 2 directors shall retire by rotation. It is assumed that Mr. First, Mr. Second Mr. Third, Mr. Fourth, Mr. Fifth and Mr. Casual are rotational directors, two amongst Mr. First. Second and Third who were appointed in 2nd AGM and have been longest in office, shall vacate office. Amongst themselves, either they can decide by mutual consent or by draw of lots.

Conclusion: Any two out of Mr. First, Mr. Second and Mr. Third (either by mutual consent or by draw a lot) shall retire by rotation. Mr. Addition and Mr. One More being the additional directors shall vacate the office on the date of 4th AGM.

Director Identification Number (Section 153 to 159)

Question 30

What do you understand by the term "Director Identification Number" (DIN)? Describe the procedure to obtain the same as enumerated under the Companies Act, 2013 read with the relevant Rules.

Answer

Director Identification Number (DIN) is a Unique Identification Number issued by the Ministry of Corporate Affairs. It is required to be obtained by every person who is intending to become a director of any company. DIN is a pre-requisite for filing various forms with the Registrar of Companies. The electronic system of the Ministry of Corporate Affairs will not allow filing / submitting of forms if DIN of the signatory director is not mentioned in the form being filed / submitted.

Under section 153 of the Companies Act, 2013 every individual intending to be appointed as director of a company shall make an application for allotment of Director Identification Number to the Central Government in such form and manner and along with such fees as may be prescribed.

1. Under rule 9 sub rule 1 of the Companies (Appointment & Qualification of Directors) Rules, 2014 every individual, who is to be appointed as director of a company shall **make an application electronically in Form DIR-3, to the Central Government** for the allotment of a Director Identification Number (DIN) along with such fees as provided in the Companies (Registration Offices and Fees) Rules, 2014.
2. Under rule 9 (2) of the said rules The Central Government shall provide an electronic system to facilitate submission of application for the **allotment of DIN through the portal on the website of the Ministry of Corporate Affairs.**
3. The applicant shall download Form DIR-3 from the portal, fill in the required particulars sought therein, verify and sign the form and after attaching copies of the following documents, scan and file the entire set of documents electronically-
   i) photograph;
   ii) proof of identity;
   iii) proof of residence; and
   iv) specimen signature duly verified.
4. Form **DIR-3 shall be signed and submitted electronically** by the applicant using his or her own Digital Signature Certificate and shall be verified digitally by -
   i) **a chartered accountant in practice** or a company secretary in practice or a cost accountant in practice; or
   ii) a **company secretary** in full time employment of the company or by the managing director or director of the company in which the applicant is to be appointed as director.

   Section 154 of the Companies Act, 2013 states that the Central Government shall, within one month from the receipt of the application under section 153, allot a Director Identification Number to an applicant in such manner as may be prescribed.

   Rule 10 (1) of the Companies (Appointment & Qualifications of Directors) Rules, 2014 states that

on the submission of the Form DIR-3 on the portal and payment of the requisite amount of fees through online mode, an application number shall be generated by the system automatically.

Rule 10 (2) further provides that after generation of application number, the Central Government shall process the applications received for allotment of DIN and decide on the approval or rejection thereof and communicate the same to the applicant along with the DIN allotted in case of approval by way of a letter by post or electronically or in any other mode, within a period of one month from the receipt of such application.

Question 31 ***(May 2017)***

Surya, a director in New Age Limited holding Directors Identification Number (DIN) wants to make certain changes in the particulars of his DIN. What procedure would you follow to get changes incorporated in the DIN already allotted to Surya?

Answer

Intimation of changes in particulars specified in DIN application

1) **According to Companies (Appointment and Qualification of Directors) Rules, 2014**, every individual who has been allotted a DIN under these rules shall, in the event of any change in his particulars as stated **in Form DIR-3**, intimate such change(s) to the Central Government within a period of thirty days of such changes(s) in form DIR – 6 in the following manner, namely:
   a) The **applicant shall download Form DIR – 6 from the portal, fill in the relevant changes, verify the Form (DIR-7) and attach duly scanned copy of the proof of the changed particulars and submit electronically**.;
   b) The **form shall be digitally signed by a Chartered Accountant in practice or a Company Secretary in practice or a Cost Accountant in practice**;
   c) The applicant **shall submit the Form DIR -6.**
2) The **Central Government**, upon being satisfied, after verification of such changed particulars from the enclosed proofs, shall incorporate the said changes and inform the applicant by **way of a letter by post or electronically or in any other mode confirming the effect of such change in the electronic database maintained by the Ministry**.
3) The DIN cell of the Ministry shall also intimate the change(s) in the particulars of the director submitted to it in **Form DIR-6** to the concerned Registrar(s) under whose jurisdiction the registered office of the company(s) in which such individual is a director is situated.
4) The concerned individual shall also intimate the change(s) in his particulars to the company or companies in which he is a director **within 15 days of such change.**

Question 32 ***(Nov 2017)***

Mr. Vinay Kumar, applied for the first time for allotment of a Directors identification Number (DIN) on 1st November, 2016 as he is planning to incorporate a private limited company in Form No. DIN-3 under The Companies Act, 2013. The status of his DIN applications presently is showing as "Put Under Resubmission". He seeks your guidance as to whether his application has been rejected and is he required to obtain a fresh DIN. Advice.

Answer

Allotment of DIN: According to **Section 154** of the Companies Act, 2013, the Central Government shall, within one month from the receipt of the application under section 153, allot a Director

Identification Number (DIN) to the applicant in such manner as may be prescribed. The status of the DIN applications showing "Put under resubmission": According to Rule 10 of the Companies(Appointment and Qualifications of Directors) Rules, 2014 of the Companies Act, 2013, if the DIN application is put under Resubmission due to following reasons, one can submit additional documents for rectifying DIN application, **within a period of 15 days from the date on which it is marked as Resubmission**.

a) **Proof of Identity/ residence is not enclosed or expired.**
b) **Proof of Date of Birth is not enclosed.**
c) **Supporting documents are not properly attested.**
d) **Non-submission of affidavit (if required).**

On resubmitting with the additional documents, same DIN will be approved, if documents are found in correct order as per marked in resubmission.

So, accordingly the application of Mr. **Vinay Kumar has not been rejected and does not require to obtain a fresh DIN.**

Appointment of Additional Director, Alternate Director & Nominee Director (Section 161)

Question 33

Prince Ltd. desires to appoint an additional director on its Board of directors. The Articles of the company confer upon the Board to exercise the power to appoint such a director. As such M is appointed as an additional director. In the light of the provisions of the Companies Act, 2013, examine:

i) Whether M can continue as director if the annual general meeting of the company is not held within the stipulated period and is adjourned to a later date?
ii) Can the power of appointing additional director be exercised by the Annual General Meeting?
iii) As the Company Secretary of the company what checks would you make after M is appointed as an additional director?

Answer

Section 161(1) of the Companies Act, 2013 provides that the articles of association of a company may confer on its Board of Directors the power to appoint any person, other than a person who fails to get appointed as a director at the general meeting, as an **additional director at any time and such director will hold office upto the date of the next annual general meeting or the last date on which such annual general meeting should have been held, whichever is earlier.**

i) **M cannot continue as director till the adjourned annual general meeting**, since he can hold the office of directorship only up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier. Such an additional director shall vacate his office latest on the date on which the annual general meeting could have been held under Section 96 of the Companies Act, 2013. **He cannot continue in the office on the ground that the meeting was not held or could not be called within the time prescribed**.
ii) The power to appoint additional directors vests with the Board of Directors and **not with the members of the company**. The only condition is that the Board must be conferred such **power by the articles of the company**.
iii) As a Company Secretary, I would put the following checks in place in respect of M's

appointment as an additional director:

a) He must have got the **Directors Identification Number** (DIN);
b) He must furnish the DIN and a declaration that he is **not disqualified** to become a director under the Companies Act, 2013;
c) He must have given his consent to act as director and such consent has been filed with the **Registrar within 30 days of his appointment**;
d) His appointment is made by the Board of Directors;
e) His name is entered in the statutory records as required under the Companies Act, 2013.

Question 34

Examine the validity of the following:

Mr. Q, a Director of PQR Limited proceeding on a long foreign tour, appointed Mr. Y as an alternate director to act for him during his absence. The articles of the company provide for appointment of alternate directors. Mr. Q claims that he has a right to appoint alternate director.

Answer

Under **section 161(2)** of the Companies Act, 2013 the Board of Directors of a company may, **if so authorised by its articles** or by a resolution passed by the company in general meeting, appoint a person, not being a person holding any alternate directorship for any other director in the company, to **act as an alternate director for a director during his absence for a period of not less than three months from India**.

From the above provision it is clear that the authority to appoint alternate director has been vested in the board of directors only and that too subject to empowerment by the Articles.

Therefore, **Q is not authorized to appoint an alternate director** and the **appointment of Mr. Y is not valid.**

Question 35

The Board of directors of XYZ Limited appointed Mr. A as a Director in the casual vacancy caused by resignation of Mr. X. Mr. A is proposed to be re-appointed as a Director at the Annual General Meeting, when he vacates his office. Examine with reference to the relevant provisions of the Companies Act, 2013 whether Mr. A can be considered as a 'Retiring Director' and state the legal requirements to be fulfilled to give effect to the proposed appointment of Mr. A as a Director at the Annual General Meeting.

Answer

In the given case, Mr. A was appointed as a director of XYZ Ltd. to fill a casual vacancy. His appointment would have been made under **section 161(4)** of the Companies Act, 2013 which provides that in the case of a public company, if the office of any director appointed by the company in general meeting is vacated before his term of office expires in the normal course, the resulting casual vacancy may, in default of and subject to any regulations in the articles of the company, be filled by the Board of Directors at a meeting of the Board.

Provided that any person so appointed **shall hold office only up to the date up to which the director in whose place he is appointed would have held office if it had not been vacated**.

Therefore, in the given case, **Mr. A would be eligible to hold office till the date upto which Mr. X would have held office. Mr. A will not automatically be considered as a "retiring director" at the next AGM of the company**.

In case he has to retire at the forthcoming Annual General Meeting and wants to be reappointed as a director he will have to follow the provisions of Companies Act, 2013 relating to the appointment of a person other than a retiring director as a director of the company which are as under:

a) **Section 152(2)** of the Companies Act, 2013 provides that unless expressly provided in this Act, every director **shall be appointed by the company in general meeting**.

b) **Section 152 (3)** further provides that no person shall be appointed as a director of a company unless he has been **allotted the Director Identification Number** under section 154.

c) **Section 152 (4)** states that every person proposed to be appointed as a director by the company in general meeting or otherwise, shall furnish his Director Identification Number and a **declaration that he is not disqualified to become a director** under this Act.

d) **Section 152 (5)** states that a person appointed as a director shall not act as a director unless he gives **his consent to hold the office as director** and such consent has been filed with the **Registrar within thirty days** of his appointment in such manner as may be prescribed.

e) Further under **section 160(1)** of the Companies Act, 2013 a person who is not a retiring director may be appointed a director at the general meeting of the company including the AGM by following the below mentioned procedure:

   i) He or any other member intending to propose him as a director, **has given a notice of not less 14 days in writing** under his hand signifying his candidature as a director or, as the case may be, intention of such member to propose him as a candidate for that office;

   ii) The above referred notice has been delivered at the **Registered Office of the Company**;

   iii) The notice should be accompanied by a **deposit of Rs. 1,00,000** or such higher amount as may be prescribed;

   iv) The deposit will be refunded to such person or to the member, as the case may be, in case the person is appointed as a director at the meeting or **gets more than 25% of total valid votes cast either on show of hands or on poll on such resolution**.

   v) Under **section 160(2)** on receipt of the notice as referred above, the company shall inform its members of the candidature of a person for the office of director under sub-section (1) in such manner as may be prescribed. Rule 13 of the Companies (Appointment & Qualification of Directors) Rules, 2014 prescribes, the company shall, **at least 7 days before the general meeting**, inform its members of the candidature of a person for the office of a director or the intention of a member to propose such person as a candidate for that office by serving individual notices, on the members through electronic mode to such members who have provided their email addresses to the company for communication purposes, and in writing to all other members; and by placing notice of such candidature or intention on the website of the company, if any.

Question 36

The Board of directors of XYZ Ltd. filled up a casual vacancy caused by the death of Mr. P by appointing Mr. C as a director on 3rd April, 2014. Unfortunately Mr. C expired on 15th May, 2014 after working about 40 days as a director. The Board now wishes to fill up the casual vacancy by appointing Mrs. C in the forthcoming meeting of the Board. Advise the Board in this regard as per the provisions under the Companies Act, 2013.

Answer

Section 161(4) of the Companies Act, 2013 provides that in the case of a public company, if the office of any director appointed by the company in general meeting is vacated before his term of office expires in the normal course, the resulting casual vacancy may, in default of and subject to any regulations in the articles of the company, **be filled by the Board of Directors at a meeting of the Board.**

Provided that any **person so appointed shall hold office only up to the date up to which the director in whose place he is appointed would have held office if it had not been vacated**.

In view of the above provisions, in the given case, the appointment of Mr. C in place of the deceased director Mr. P was in order. In normal course, Mr. C could have held his office as director up to the date to which Mr. P would have held the same.

However, Mr. C expired on 15th May, 2014 and again a vacancy has arisen in the office of director owing to death of Mr. C who was appointed by the board to fill up the casual vacancy resulting from P's demise. Vacancy arising on the Board due to vacation of office by the director appointed to fill a casual vacancy in the first place, does not create another casual vacancy as section 161 (4) clearly mentions that such vacancy is created by the vacation of office by any director appointed by the company in general meeting. Hence, the Board cannot fill in the vacancy arising from the death of Mr. C.

The Board may however appoint Mrs. C as an additional director under section 161 (1) of the Companies Act, 2013 provided the articles of association authorises the board to do so, in which case **Mrs. C will hold the office up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier**.

Question 37 ***(Nov 2014)***

Referring to the provisions of the Companies Act, 2013, examine the validity of the following:

i) The Board of Directors of AJD Limited appointed Mr. N as an alternate director for a period of two months against a director who has proceeded abroad on leave for a period of six months. Articles of Association of the company are silent.

ii) Mr. P who is not qualified to be appointed as an independent director is appointed by the Board of Directors of XYZ Company Limited, for an independent director, as an alternate director.

iii) On the request of bank providing financial assistance the Board of Directors of PQR Limited decides to appoint on its Board Mr. Peter, as nominee director. Articles of Association of the Company do not confer upon the Board of Director any such power. Further, there is no agreement between the company and the bank for any such nomination.

Answer

Appointment of alternate Director (Section 161 of the Companies Act, 2013)

i) According to **section 161(2)** of the Companies Act, 2013, the Board of Directors of a company may, if so authorised by its articles or **by a resolution passed by the company in general meeting,** appoint a person to act as an alternate director for a director (original director) during his absence for a period of not less than three months from India.

In the present case, the Board of Directors of AJD Limited appointed Mr. N as an alternate director for a period of two months against a director who has proceeded on leave for a period of six months and Articles of Association of the company are silent. The said appointment is not valid because the power to appoint alternate director is not authorised by its articles or by a resolution passed by the company in general meeting.

ii) According to **first proviso to section 161(2)** of the Companies Act, 2013, no person shall be appointed as an alternate director for an independent director unless he is qualified to be appointed as an independent director under the provisions of this Act.

In the present case, **Mr. P who is not qualified to be appointed as an independent director is appointed by the Board of Directors of XYZ Company Limited; for an independent director, as an alternate director**. Thus, the said appointment is not valid.

iii) According to section 161(3) of the Companies Act, 2013, the Board may appoint any person as a director nominated by any institution in pursuance of the provisions of any law for the time being in force or of any agreement or **by the Central Government or the State Government by virtue of its shareholding in a Government company, subject to the articles of a company.**

In the present case, on the request of bank providing financial assistance the Board of Directors of PQR Limited decides to appoint on its Board Mr. Peter, as nominee director. **Articles of Association of the company do not confer upon the Board of Directors any such power and further there is no agreement between the company and the bank. Thus, the appointment of Mr. Peter as nominee director is not valid as Articles do not confer upon the Board of Directors any such power**.

Question 38 ***(Nov 2015)***

Queens Limited is a company listed at Bombay Stock Exchange. Company's Articles empower the Board of Directors to appoint additional director. The Board of Directors, therefore, appoints Mr. K. as the additional director. It may, however, be pointed out that earlier, the proposal to appoint Mr. K. as a director on the Company's Board was rejected by the members at the company's Annual General Meeting.

Examine the provisions of the Companies Act, 2013, answer the following:

i) Whether Mr. K's appointment as additional director by the Board of Directors is valid?

ii) Whether the Company's Annual General Meeting can appoint Mr. K. as the additional director when the proposal to appoint comes before the meeting for the first time?

iii) In case the AGM of the company is not held within the stipulated time, decide whether Mr. K. who was appointed by the Board as additional director, for the first time, can continue to act as a director?

Answer

Problem as asked in the question is based on the provisions of the Companies Act, 2013 as contained under section 161 (1) according to which:

A) The **Articles of a company** may confer upon its Board of Directors the power to appoint any person as an additional director at any time.

B) A person, who **fails to get appointed as a director in a general meeting** of the company **cannot be appointed as an additional director in the same company**.

C) Additional director shall hold office up to the date of the **next AGM or the last date on which the AGM should have been held, whichever is earlier.**

In the given case, the answers to sub-questions are:

i) The appointment of Mr. K. as additional director by the Board of Directors is **not valid** because before appointing him as an additional director, the proposal to appoint Mr. K. as a director on the Company's Board was rejected by the members at the company's Annual General Meeting.

ii) The **power to appoint additional directors vests with the Board of Directors** and not with the

members of the company. The only condition is that the Board must be conferred such power by the articles of the company. Therefore, in the present case, the company's Annual General Meeting cannot appoint Mr. K. as the additional director when the proposal to appoint comes before the meeting for the first time because the company's Articles empower the Board of Directors to appoint additional director.

iii) In case the AGM of the company is not held within the stipulated time, Mr. K. cannot continue as additional director, since he can hold the office of directorship only up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier. Such an additional director shall vacate his office latest on the date on which the annual general meeting ought to have been held under Section 96 of the Companies Act, 2013. He cannot continue in the office on the ground that the meeting was not held or could not be called within the time prescribed.

Question 39 ***(May 2017)***

Mr. Abhi was appointed as an additional director of Pioneer Limited on 14th March, 2016. The annual general meeting of the company was scheduled to be held on 29th September, 2016 but due to heavy rains and floods all records of the company were destroyed. In order to rebuild the records, the company approached the Registrar of Companies for extension of time for holding the annual general meeting till 30th December, 2016. In the light of the Companies Act, 2013 advise Mr. Abhi, who was appointed as additional director during the year.

Answer

Problem related to appointment of additional director: Section 161(1) of the Companies Act, 2013 provides for appointment of additional director. According to this section:

i) The **articles of a company may confer on its Board of Directors the power to appoint any person as an additional director at any time**.

ii) A person, **who fails to get appointed as a director in a general meeting, cannot be appointed as an additional director**.

iii) **Additional director shall hold office up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier.**

As per the stated fact, before the scheduled annual general meeting of 29 th September 2016 takes place, due to heavy rains and floods all the record of the company were destroyed. So, company to rebuild the records, approached the Registrar of Companies for extension of time for holding of the Annual General Meeting till 30 th December 2016.

As per the third provision to the section 96 of the Companies Act, 2013, Registrar may, for any special reason, extend the time within which any annual general meeting, other than the first annual general meeting, shall be held, by a period not exceeding three months.

So, accordingly **Mr. Abhi may continue as an additional director of Pioneer Limited till 30th December, 2016.**

Question 40 ***(May 2017)***

Mr. Narayan, a Director of KPR Limited who is proceeding on a long foreign tour, appointed Mr. Shankar as an alternate director to act for him during his absence. The Articles of the company provide for appointment of alternate directors. Mr. Narayan claims that he has a right to appoint an alternate director.

Answer

According to **section 161 (2)** of the Companies Act, 2013, the **Board of Directors** of a company may, **if so authorised by its articles or by a resolution passed by the company in general meeting, appoint a person, not being a person holding any alternate directorship** for any other director in the company, to act as an alternate director for a director during his absence for a period of not less than three months from India.

Hence, the Board of Directors of KPR Ltd. may appoint a person, **not being a person holding any alternate directorship for any other director in the company, to act as an alternate director for a director** during his absence, as:

a) The Articles of KPR Limited provides for appointment of alternate director.
b) Mr. Narayan, director of company is proceeding for a long foreign tour.

However, the power to appoint alternate director lies with the Board of Directors and not with the director himself. Hence, Mr. Narayan cannot himself appoint Mr. Shankar as an alternate director to act for him during his absence.

[**Presumption:** The duration of 'long foreign tour' is not less than three months.]

Question 41 ***(May 2017)***

The Board of Directors of Sakthi Limited decides to appoint on its Board, Mr. Ravi as a nominee director upon the request of a bank which has extended a long term financial assistance to the company. The Articles of Association of the company do not confer upon the Board any such power. Also, there is no formal agreement between the company and the bank for any such nomination.

Answer

According to **section 161 (3)** of the Companies Act, 2013, **subject to the articles of a company, the Board may appoint any person as a director nominated by any institution in pursuance of the provisions of any law for the time being in force or of any agreement or by the Central Government or the State Government by virtue of its shareholding in a Government company**.

The Articles of Association of Sakthi Limited do not confer upon the Board of Directors any such power. Hence, the Board cannot appoint Mr. Ravi as a nominee director even on the request of a bank which has extended a long term financial assistance to the company.

Question 42

In ABC Ltd. three Directors were to be appointed. The item was included in agenda for the Annual General Meeting scheduled on 30th September, 2014, under the category of 'Ordinary Business'. All the three persons as proposed by the Board of directors were elected as directors of the company by passing a 'single resolution' avoiding the repetition (multiplicity) of resolution. After the three directors joined the Board, certain members objected to their appointment and the resolution. Examine the provisions of Companies Act, 2013 and decide:

Whether the contention of the members shall be tenable and whether both the appointment of Directors and the 'single resolution' passed at the Company's Annual General Meeting shall be void.

Answer

The **matter of appointment of directors in place of those retiring at the annual general meeting has been correctly stated in the agenda as the ordinary business to be transacted at the general**

meeting. But in accordance with the provisions of **section 162(1)** of the Companies Act, 2013, at a general meeting of a company, a motion for the appointment of two or more persons as directors of the company by a single resolution shall not be moved unless a proposal to move such a motion has first been agreed to at the meeting without any vote being cast against it. **Section 162 (2)** further provides that a resolution moved in contravention of sub-section (1) shall be void, whether or not any objection was taken when it was moved. **Taking into account of the above, the contention of the members shall be tenable. Each director has to be appointed by way of a separate resolution**.

Question 43

XYZ Company Ltd. in its annual general meeting appointed all its directors by passing one single resolution. No objection was made to the resolution. Examine the validity of appointment of directors explaining the relevant provisions of the Companies Act, 2013. Will it make any difference, if XYZ Company was a private company?

Answer

Under **section 162(1)** of the Companies Act, 2013, at a **general meeting of a company, a motion for the appointment of two or more persons as directors of the company by a single resolution shall not be moved unless a proposal to move such a motion has first been agreed to at the meeting without any vote being cast against it.**

From the above provision of law, **it is mandatory for the company to first get a unanimous approval of the company on the appointment of more than one director by a single resolution.** In the given case, no such motion was put to vote at the meeting and passed unanimously. Merely not raising any objection is not the same as active unanimous approval.

Further, according to **section 162(2)**, a resolution moved in contravention of sub-section (1) shall be void, whether or not any objection was taken when it was moved. **Hence, in the given case the appointment of all the directors made by a single resolution at the AGM is void**.

The Ministry of Corporate Affairs has clarified via Notifications No. 464(E) dated 5th June, 2015, that section 162 of the Companies Act, 2013, **shall not apply to a private company.** Thus, if XYZ would have been a private company, then provisions of section 162 shall not be attracted.

Question 44 ***(May 18)***

Mr. Bond and Mr. James were appointed as Directors of Jamesbond Ltd. at the AGM held on 30th September, 2017 by a single resolution. State the relevant provisions of the Companies Act, 2013 and identify is it possible to appoint the above Directors by a single resolution?

Answer

According to **Section 162** of the Companies Act, 2013, at a general meeting of a Company**, a motion for the appointment of two or more persons as Directors of the Company by a single resolution shall not be moved unless a proposal to move such a motion has first been agreed to at the meeting without any vote being cast against it.**

A resolution moved in contravention of above shall be void, whether or not any objection was taken when it was moved.

A motion for approving a person for appointment, or for nominating a person for appointment as a director, shall be treated as a motion for his appointment.

In the instant case, **it is not possible to appoint Mr. Bond and Mr. James as Directors of James Bond**

Ltd. by a single resolution.

Option to Adopt Principle of Proportional Representation for Appointment of Directors (Section 163)

Question 45

A company has in its Articles of Association provided for appointment of not less than two- thirds of the total number of its directors according to the principle of proportional representation. Can the directors so appointed be removed by the company in general meeting as per the provisions of the Companies Act, 2013?

Answer

Under **section 163** of the Companies Act, 2013, the articles of a company may provide for the appointment of **not less than two-thirds of the total number of the directors** of a company in accordance with the principle of proportional representation, **whether by the single transferable vote or by a system of cumulative voting** or otherwise and such appointments may be made once in every 3 years and casual vacancies of such directors shall be filled as provided in sub-section (4) of section 161 i.e. by the board of directors at a duly convened board meeting.

Section 169 (1) of the Companies Act, 2013 provides for the removal of a director by ordinary resolution of members (except a director appointed by the Tribunal) before the expiry of his term of office. However, according to the proviso to **section 169(1) this is not applicable where the company has availed itself of the option given to it under section 163 to appoint not less than two thirds of the total number of directors according to the principle of proportional representation.**

Hence, according to proviso to section 169(1), the directors elected by the principle of proportional representation under section 163 of the Companies Act, 2013 **cannot be removed by the shareholders in general meeting.**

Disqualifications for Appointment of Director (Section 164)

Question 46

Mr. Kishore is a Director of AB Limited and PQ Limited. AB Limited did not file financial statements for the years ended 31st March, 2010, 2011 and 2012. AB Limited did not pay interest on loans taken from a public financial institution from 1st April, 2012 and also failed to repay matured deposits taken from public on due dates from 1st April, 2013 onwards.

Answer the following in the light of relevant provisions of the Companies Act, 2013:-

i) Whether Mr. Kishore is disqualified under the Companies Act, 2013 and if so; whether he can continue as a Director in AB Limited and can he also seek reappointment when he retires by rotation at the Annual General Meeting of PQ Limited to be held in September, 2014?

ii) Mr. Kishore is proposed to be appointed as Additional Director of XY Limited in June, 2014. Is he eligible to be appointed as Additional Director in XY Limited?

Answer

According to **section 164(2)** of the Companies Act, 2013, a person who is or has been a director of a company which:

A) has not filed the financial statements or annual returns for any **continuous 3 financial years**; or

B) has **failed to repay the deposits accepted by it or pay interest thereon on due date or redeem its debentures on due date or pay interest due thereon or pay any dividends declared and such failure continues for one year or more**.

shall not be eligible to be re-appointed as a director of that company or appointed in other company for a period of five years from the date on which the said company fails to do so.

In the given case, the irregularities committed by AB Ltd. are

a) Non filing of financial statements for year ended 31st March 2010 to 2012 (3 Yrs);
b) Non payment of interest on loans taken from financial institution; and
c) Non repayment of matured deposits taken from the public from 1st April 2013.

i) Here, Mr. Kishore is a director of AB Ltd. and PQ Ltd. AB Ltd. did not file financial statements for three years ended 31st March 2010, 2011 and 2012. Further, AB Ltd failed to repay matured deposits taken from public from 1st April, 2013 onwards. Both these failures constitute a disqualification under section 164 (2) and consequently, Mr. Kishore will not be eligible for reappointment in AB Ltd.

It may be noted that the failure to pay interest on loans taken from a public financial institution is not covered under section 164 (2) and hence does not constitute a disqualification.

As per **section 167(1)(a)** of the Companies Act, 2013, the office of a director shall become vacant in case he incurs any of the disqualifications specified under section 164(2) of the Companies Act, 2013. Since, Mr. Kishore has attracted disqualification under section 164(2) of the Companies Act, 2013, he has to vacate office of a director in AB Ltd.

Mr. Kishore cannot seek reappointment in PQ Ltd. when he retires by rotation at the Annual General Meeting to be held in September, 2014.

ii) In view of his disqualification under section 164 (2), Mr. **Kishore is not eligible to be appointed as additional director in XY Ltd. in June 2014.**

Question 47

State with reference to the relevant provisions of the Companies Act, 2013 whether the following persons can be appointed as a Director of a company:

i) Mr. A, who has huge personal liabilities far in excess of his Assets and Properties, has applied to the court for adjudicating him as an insolvent and such application is pending.

ii) Mr. B, who was caught red-handed in a shop lifting case two years ago, was convicted by a court and sentenced to imprisonment for a period of eight weeks.

iii) Mr. C, a Former Bank Executive, was convicted by a court eight years ago for embezzlement of funds and sentenced to imprisonment for a period of one year.

iv) Mr. D is a Director of DLT Limited, which has not filed its Annual Returns pertaining to the Annual General Meetings held in the years 2011, 2012 and 2013.

Answer

The first 3 cases stated in the question are based on the provisions of Section 164 (1) of the Companies Act, 2013 and the fourth case is dealt with in section 164 (2) of the said Act. Based on the provisions of the said sections, each case can be discussed as follows:

i) **Section 164 (1) (c)** states that a person shall **not be eligible for appointment as a director of a**

company if he has applied to be adjudicated as an insolvent and his application is pending. Therefore, in the present case, Mr. A cannot be appointed as a Director of a Company – whether public or private.

ii) **Section 164 (1) (d)** states that a person **shall not be eligible for appointment as a director of a company if he has been convicted by a court for any offence involving moral turpitude** or otherwise and sentenced in respect thereof to imprisonment for **not less than six months,** and a period of five years has not elapsed from the date of expiry of the sentence. In the present case, although the sentence was only two years ago, but the period of sentence was only eight weeks, i.e., less than six months. **Hence, Mr. B does not come under the purview of this disqualification and can be appointed as a director of a company.**

iii) The third case also falls within the provisions of section 164 (1) (d). In this case the imprisonment was for a period of one year, i.e., for six or more months, but since more than five years have elapsed from the expiry of the sentence, **Mr. C is no longer disqualified and can be appointed as a director of a company.**

iv) **Section 164 (2)** states that a person who is or has been a director of a company which has not filed the financial statements or annual returns for any continuous period of three financial years, then such a person shall not be eligible either to be appointed as a director of other company or reappointed as a director in the same company. In the present case, DLT Limited has failed to file annual returns. Hence, **the disqualification for Mr. D is attracted and he cannot be appointed as a director in other company nor can he be reappointed in the same company.**

Question 48

Mr. John is a director of MNC Ltd., which had accepted deposits from public. The Financial position of MNC Ltd. turned very bad and it failed to repay the deposits which fell due for payment on 10th April, 2014 and such repayment has not been made till 5th May, 2015. Another company JKL Ltd. wants to appoint the said Mr. John as its director at its annual general meeting to be held on 6th May, 2015. You are required to state with reference to the provisions of the Companies Act, 2013 whether Mr. John can be appointed as a director of JKL Ltd.

Answer

Section 164 (2) (b) of the Companies Act, 2013 states that where a person is or has been a director of a company which has **failed to repay its deposit on due date and such failure continues for one year or more, then such person shall not be eligible to be appointed as a director of any other company for a period of five years** from the date on which such company, in which he is a director, failed to repay its deposit.

In the instant case, MNC Ltd., has failed to repay its deposit on due dates and the default continues for more than one year. Hence, **Mr. John will not be eligible to be appointed as a director of JKL Ltd.**

Question 49

Mr. Ramanathan is a Director of Fraudulent Ltd., Honest Ltd. and Regular Ltd. for the financial year ended on 31st March, 2014. Two irregularities were discovered against fraudulent Ltd. Fraudulent Ltd. did not file its financial statements for the year ended 31.3.2014 and failed to pay interest on loans taken from a financial institution for the last three years.

On 1st June, 2015 Mr. Ramnathan is proposed to be appointed as additional director of Goodwill

Ltd, which company has sought a declaration from Mr. Ramnathan and he also submitted the declaration stating that the disqualification specified in Section 164 of the Companies Act, 2013 is not attracted in his case. Decide under the provisions of the Companies Act:

i) Whether the declaration submitted by Mr. Ramanthan to Goodwill Ltd. is in order?
ii) Whether Mr. Ramnathan can continue as a Director in Honest Ltd. and Regular Ltd.?

Answer

i) The declaration of Mr. Ramanthan is in order. According to section 164 (2) of the Companies Act, 2013 a person who is or has been a director of a company which:

a) has not filed the financial statements or annual returns for any **continuous 3 financial years;** or

b) has **failed to repay the deposits accepted by it or interest thereon on due date or redeem its debentures on due date or pay dividends declared and such failure continues for one year or more**.

shall not be eligible to be re-appointed as a director of that company or appointed in other company for a period of five years from the date on which the said company fails to do so.

As the financial statements were not filed only for one year, no disqualification attaches to him. Further, the non -payment of interest to the financial institution is no ground for disqualification under section 164 (2) of the Act.

ii) Mr. **Ramanthan can continue his directorship in all companies as no disqualification attaches to him under section 164 (2) of the Companies Act, 2013.**

Question 50 ***(Nov 17)***

Mr. Vikram, a director of M/s Tubelight Limited has made default in filing of annual accounts and annual returns with Registrar of Companies for a continuous period of 3 financial years ending on 31st March 2016. Examine the validity of the following under the Companies Act, 2013:

i) Whether Mr. Vikram can continue to be a director of M/s Tubelight Limited (defaulting company) and also M/s Green Light Limited, where he is also a director? Also state whether he can be re-appointed as director in these two companies.
ii) What would your answer be in case Mr. Vikram is a nominee director of a Public Financial Institution?
iii) What would be your answer in case the defaulting company (i.e. M/s. Tubelight Limited) is a private limited company?

Answer

Disqualifications for Appointment of Director: According to **Section 164(2)** of the Companies Act, 2013, a person who is or has been a director of a company which:

A) has not filed the financial statements or annual returns for any continuous three financial years; or

B) has failed to repay the deposits accepted by it or pay interest thereon on due date or redeem its debentures on due date or pay interest due thereon or pay any dividends declared and such failure continues for one year or more.

shall not be eligible to be re-appointed as a director of that company or appointed in other company for a period of five years from the date on which the said company fails to do so.

Further, pursuant to **Section 167(1)(a)** of the Companies Act,2013, the office of a director shall

become vacant in case he incurs any of the disqualification specified in Section 164.The co joint reading of both the sections i.e 164(2) and 167(1)(a), we may decide the case as under :

Proviso to sec. 167(1)

i) In the **first case, Mr. Vikram cannot continue to be director of the defaulting company namely M/s Tubelight Limited.** Whereas in Green Light Limited, he can continue as a director because that company is not the defaulting company.

   Further, Mr Vikram is a director of Tubelight Limited and Green Light Limited. Tubelight Limited did not file financial statements for a continuous period of three financial years ending 31st March, 2016. This failure constitute a disqualification under section 164 (2) and consequently, Mr. Vikram will not be eligible for reappointment in Tubelight Limited and Green Light Limited for a period of five years from the date on which the said company incurs the default.

ii) In Case Mr. Vikram is a **nominee director of a Public Financial Institution, then in such case, section 164 is not applicable.**

iii) **In case Tubelight Limited is a Private Limited Company:** According to **section 164(3)**, a private company may by its articles provide for any disqualifications for appointment as a director in addition to those specified in sub-sections (1) and (2) of section 164.

Thus, in this case the answer would be same as above i.e. Mr. Vikram has to vacate his office of directorship from Tubelight Limited and Green Light Limited and cannot be reappointed in both the companies for a period of five years from the date on which the said company incurs the default.

Question 51 ***(Nov 16)***

State with reference to the provisions of the Companies Act, 2013, whether the following persons can be appointed as a Director of a company.

i) Mr. L, who has not paid any calls in respect of any shares of the company held by him and five months have passed from the last day fixed for the payment of calls.
ii) Mr. G is Director of LDT Limited, who has not filed the company's annual return pertaining to the annual general meeting held in the calendar years 2014, 2015 and 2016.

Answer

i) According to **section 164(1)(f)** of the Companies Act, 2013, a person **shall not be eligible for appointment as a director of company, if he has not paid any calls in respect of any shares** of the company held by him, whether alone or jointly with others, and **six months have elapsed from the last day fixed for the payment of the call.**

In the present case, Mr. L who has not paid any calls in respect of any shares of the company held by him and five months have passed from the last day fixed for the payment of calls. So, Mr. L can be appointed as a Director of a company as only five months have passed from the last day fixed for the payment of calls.

ii) According to **section 164(2)(a)** of the Companies Act, 2013, **no person who is or has been a director of a company which has not filed financial statements or annual returns for any continuous period of three financial years.** Further, he **cannot be appointed in other company for a period of 5 years from the date on which the said company (LDT Ltd.) fails to do so.**

In the present case, Mr. G is director of LDT Limited, who has not filed the company's annual return pertaining to the annual general meeting held in the calendar years 2014, 2015 and 2016. It means that the LDT Limited has not filed the annual return for the continuous period of three financial years i.e. 2013-14, 2014-15 and 2015-16. Hence, Mr. G who is a director of LDT Limited

cannot be appointed as a Director of a company.

Number of Directorship (Section 165)

Question 52

Mr. Influential is already a director of 19 companies out of which 10 are public limited companies and 9 are private companies. He is being appointed as a director of another company named Expensive Remedies Ltd. Advise Mr. Influential in regard to the following:

i) Restrictions on the number of directorships to be held by an individual and whether he can accept the new appointment in view thereof.

ii) What are the companies to be excluded for the purpose of calculating the ceiling on the appointment of directors in a public company?

Answer

i) Under **section 165 (1)** of the Companies Act, 2013, no person, after the commencement of this Act, shall hold office as a director including any alternate directorship, in more than twenty companies at the same time.

Provided that the maximum number of public companies in which a person can be appointed as a director **shall not exceed ten**.

Explanation to section 165 (1) clarifies that for reckoning the limit of public companies in which a person can be appointed as director, directorship in private companies that are either holding or subsidiary company of a public company shall be included.

Further, In the said question, Mr. Influential is already a director in 10 public companies and as Expensive Remedies Ltd is a public company, he cannot be appointed as a director therein, even though his total directorships are less than 20.

ii) For calculating the limit of 10 public companies, **a private company which is neither a subsidiary nor a holding company of a public company will be excluded in terms of the explanation to section 165 (1)** of the Companies Act, 2013.

Question 53 ***(RTP May 18)***

Excel limited is a listed company with a turnover of Rs. 60 crores in the FY 2016-2017. The company appoints Ms. R as the women director on 1st March 2017. Ms. R is already a director in twelve companies including ten public companies. Also, Ms. R is chartered accountant in practice.

Further, also, Ms. R, is a director in Supreme Ltd. where he is acting in a professional capacity. Since lots of proposal for the holding of directorship in various companies are lined up before the Ms. R, so in order to retain him, Remuneration and nomination committee proposed to enhance the remuneration of Ms. R from 4 Lac per month to 6 Lac per month. However, Supreme Limited was running in losses for last 2 years.

Evaluate in the light of the given facts, the following situations with reference to the provisions of the Companies Act, 2013-

Answer

1) **Number of directorships:** As per **section 165(1)** of the Companies Act, 2013, no person shall hold office as director, including any alternate directorship, in more than 20 companies at the same time.

Out of the limit of 20, the maximum number of public companies in which a person can be appointed as a director shall not exceed 10. [Proviso to section 165(1)]

Private companies that is either holding or subsidiary company of a public company shall be included in reckoning the limit of public companies in which a person can be appointed as a director.

In the instant case, Ms. R was appointed as a women director on 1st March, 2017 in Excel Limited. **She was already holding directorship in twelve companies including ten public companies.**

As Ms. R was already a director in ten public companies, her appointment in Excel Limited is not valid as it will lead to her directorship in 11 public companies.

In this case, either she can choose between the companies in which she wishes to continue to hold the office of director or resign her office as director in the other remaining companies to maintain the limit of holding of directorship.

2) Remuneration : In the given case, since, the company has suffered losses in the last two years, the company will pay remuneration to its directors in accordance with the provisions of Schedule V to the Companies Act, 2013.

In case of a **managerial person who is functioning in a professional capacity, no approval of Central Government is required, if such managerial person is not having any interest in the capital of the company or its holding company or any of its subsidiaries directly or indirectly or through any other statutory structures and not having any, direct or indirect interest** or related to the directors or promoters of the company or its holding company or any of its subsidiaries at any time during the last two years before or on or after the date of appointment and possesses graduate level qualification with expertise and specialised knowledge in the field in which the company operates. [Item B of Section II of Schedule V]

The total remuneration that supreme Limited is intending to pay to Ms. R is 72 lakhs per annum, from the current remuneration of 48 lakhs per annum. **Since Ms. R is working in professional capacity and the remuneration has been proposed by the remuneration Committee, no approval of Central Government is required**. Also, the case shall be in compliant of Schedule V, Central Government approval will not be required even when there is increase in remuneration payable.

Question 54 ***(Nov 17)***

Referring to the provisions of the Companies Act, 2013, examine the validity of the following appointment of Directors:

(A) Brown Limited, having a turnover of Rs. 60 crore in the financial year 2016-17 appoints Ms. Rose as the women director on 1st March 2017. Ms. Rose already holds directorship in twelve companies including ten public companies. She is whole time Cost Accountant in practice.

(B) Ms. Jasmine holds directorship in eight public companies including managing directorship in two companies and directorship in six companies. In addition, she also holds alternate directorship in three companies and independent directorship in three subsidiary companies of Brown Limited.

Answer

Number of Directorships: As per **section 165(1)** of the Companies Act, 2013, **no person shall hold office as director, including any alternate directorship, in more than 20 companies at the same**

time. Out of the limit of 20, the maximum number of public companies in which a person can be appointed as a director shall not exceed 10. [Proviso to section 165(1)]

Private companies that is either holding or subsidiary company of a public company shall be included in reckoning the limit of public companies in which a person can be appointed as a director.

(A) In the instant case, Ms. Rose was appointed as a women director on 1st March, 2017 in Brown Limited. She was already holding directorship in twelve companies including ten public companies. She is whole time Cost Accountant in practice.

As Ms. **Rose was already a director in ten public companies, her appointment in Brown Limited is not valid as it will lead to her directorship in 11 public companies**.

In this case, either she can choose between the companies in which she wishes to continue to hold the office of director or resign her office as director in the other remaining companies.

(B) In the instant case, **Ms. Jasmine holds directorship in eight public companies including managing directorship in two companies and directorship in six companies**. In addition, she also holds alternate directorship in three companies and independent directorship in three subsidiary companies of Brown Limited.

Ms. Jasmine was already holding directorship in eight public companies and alternate directorship in three companies (assuming these companies as private) and independent directorship in three subsidiary companies of Brown Limited. Directorship in three subsidiary companies of Brown Limited will be considered as directorship in three more public companies.

Hence, total holding of directorship by Ms. Jasmine in public companies amounts to 11 (8+3) which is invalid.

In this case, either she can choose between the companies in which she wishes to continue to hold the office of director or resign her office as director in the other remaining companies.

Assumption: As nothing is mentioned that whether three companies in which Ms. Jasmine is holding alternate directorship are private or public, we are assuming that these companies are private in nature. Even if the student writes the answer based on assumption that Ms. Jasmine is holding alternate directorship of a public company, conclusion will not change.

Vacation of Office of Directors (Section 167)

Question 55 ***(Nov 17)***

Mr. Vikram, a director of M/s Tubelight Limited has made default in filing of annual accounts and annual returns with Registrar of Companies for a continuous period of 3 financial years ending on 31st March 2016. Examine the validity of the following under the Companies Act, 2013:

i) Whether Mr. Vikram can continue to be a director of M/s Tubelight Limited (defaulting company) and also M/s Green Light Limited, where he is also a director? Also state whether he can be re-appointed as director in these two companies.

ii) What would your answer be in case Mr. Vikram is a nominee director of a Public Financial Institution?

iii) What would be your answer in case the defaulting company (i.e. M/s. Tubelight Limited) is a private limited company?

Answer

Disqualifications for Appointment of Director: According to **section 164(2)** of the Companies Act, 2013, a person who is or has been a director of a company which:

A) has not filed the financial statements or annual returns for any continuous three financial years; or

B) has failed to repay the deposits accepted by it or pay interest thereon on due date or redeem its debentures on due date or pay interest due thereon or pay any dividends declared and such failure continues for one year or more.

shall not be eligible to be re-appointed as a director of that company or appointed in other company for a period of five years from the date on which the said company fails to do so. Further, pursuant to **Section 167(1)(a)** of the Companies Act,2013, the office of a director **shall become vacant in case he incurs any of the disqualification specified in Section 164**. The co joint reading of both the sections i.e 164(2) and 167(1)(a), we may decide the case as under :

i) **In the first case, Mr. Vikram cannot continue to be director of the defaulting company namely M/s Tubelight Limited. Whereas in Green Light Limited, he can continue as a director because that company is not the defaulting company.**

Further, Mr. Vikram is a director of Tubelight Limited and Green Light Limited. Tubelight Limited did not file financial statements for a continuous period of three financial years ending 31st March, 2016. This failure constitute a disqualification under section 164 (2) and consequently, Mr. Vikram will not be eligible for reappointment in Tubelight Limited and Green Light Limited for a period of five years from the date on which the said company incurs the default.

ii) **In Case Mr. Vikram is a nominee director of a Public Financial Institution, then in such case, section 164 is not applicable.**

iii) **In case Tubelight Limited is a Private Limited Company:** According to section 164(3), a private company may by its articles provide for any disqualifications for appointment as a director in addition to those specified in sub-sections (1) and (2) of section 164.

Thus, in this case the answer would be same as above i.e. Mr. Vikram has to vacate his office of directorship from Tubelight Limited and Green Light Limited and cannot be reappointed in both the companies for a period of five years from the date on which the said company incurs the default.

Resignation of Directors (Section 168)

Question 56

Due to internal problems in the working of Infighting Detergents Ltd., Mr. Satyam and Mr. Shivam, a Director, have submitted their resignations and decided to disassociate themselves with the working of the company. Mr. Sundram, the Managing Director, decides to refuse their resignations. Examine whether the Managing Director can compel Mr. Satyam and Mr. Shivam to continue as per the provisions of the Companies Act, 2013.

Answer

Section 168(1) of the Companies Act, 2013 provides that a director may resign from his office by giving a notice in writing to the company and the Board shall on receipt of such notice take note of the same and company shall intimate the Registrar in Form DIR-12 as prescribed in Companies (Appointment & Qualification of Directors) Rules, 2014 and shall also place the fact of such

resignation in the report of directors laid in the immediately following general meeting by the company.

The proviso to section 168(1) states that a **director shall also forward a copy of his resignation along with detailed reasons for the resignation to the Registrar within thirty days** of resignation in such manner as may be prescribed. Under the Companies (Appointment & Qualification of Directors) Rules, 2014 the director shall within 30 days of resignation forward to the Registrar a copy of his resignation alongwith the reasons for his resignation in Form **DIR-11** along with the prescribed fee.

Further, **section 168(2)** states that the resignation of a director shall take effect from the **date on which the notice is received by the company or the date, if any, specified by the director in the notice, whichever is later.**

The law does not give an option to the Managing Director or the Company or the Board to reject the resignation of a director and force him to continue.

Therefore, in the given case, the **Managing Director cannot compel Mr. Satyam and Mr. Shivam to continue as directors in view of the above provisions**.

Question 66

Mr. Raj, a director of POL Ltd., submitted his resignation from the post of director to the Board of Directors on 30th June, 2014 and obtained a receipt therefore on the same day. The Board of Directors of POL Ltd. neither accepted the resignation nor did it file the required form with the Registrar of Companies. You are required to state whether Mr. Raj ceases to be the Director of POL Ltd. and if yes, since when?

Answer

Section 168(2) of the Companies Act, 2013 states that the **resignation of a director shall take effect from the date on which the notice is received by the company or the date, if any, specified by the director in the notice, whichever is later**. The effectiveness of the resignation of the director is not in any way connected to its acceptance by the Company or the Board nor is it linked to the filing of required form with the Registrar.

However, under the Proviso to section 168 (1), the resigning director is also required to file with the Registrar a copy of his resignation and the reasons of his resignation in form **DIR 11 within 30 days of the date of his resignation.**

Hence, if the company has failed to file the form **DIR 12** as required by the Companies (Appointment & Qualifications of Directors) Rules, 2014, the effectiveness of his resignation will not be impacted.

Therefore, in the given case, the resignation of Mr. Raj is valid and he will cease to be a director of POL Ltd with effect from the date of notice i.e. 30th June 2014 as he has obtained the receipt of the notice on the same day.

Removal of Directors (Section 169)

Question 67

Mr. Stubborn is a director of Doubtful Industries Ltd. He along with other two directors has been running the Company for the past twenty years without declaring any dividends or giving any

benefit to the shareholders. Frustrated by this, some shareholders are desirous of giving notice to pass a resolution with the support of other shareholders for his removal as a director in the Annual General Meeting of the Company to be held in the month of December of 2014. State the procedure to be followed for the removal of Mr. Stubborn as a director.

Answer

Mr. Stubborn a director of Doubtful Industries Ltd., can be removed by following the provisions laid down in **section 169** of the Companies Act, 2013 which provide for the removal of any director (excluding a director appointed by the tribunal under section 242) **by passing of an ordinary resolution** at a duly convened meeting of the members of the company after giving special notice under section 115.

According to **section 115** where, by virtue of any provision contained in the Companies Act, 2013 or in the articles of a company, **special notice is required of any resolution**, such notice of the intention to move such resolution shall be given to the company by such number of **members holding not less than one percent**. of total voting power or holding shares on which the sum prescribed in the **aggregate not exceeding five lakh rupees has been paid up**, and the company shall give its members notice of the resolution in such manner as may be prescribed.

Therefore, the first thing that the shareholders must do is to ensure that the required number of members as mentioned in section 115 are lined up for giving the special notice of the resolution proposed for the removal of the directors.

Having achieved the required numbers and keeping the various provisions as mentioned above, the procedure for the removal of Mr. Stubborn will be as under:

i) **An ordinary resolution** is required to be passed at the proposed annual general meeting of the company [Section 169 (1)].

ii) **A special notice** shall be required of any resolution, to remove a director under this section [Section 169 (2)].

iii) On receipt of the notice of a resolution to remove a director under section 169, the company shall forthwith send a copy thereof to Mr. Stubborn and he is entitled to be heard on the resolution at the meeting [Section 169 (3)]

iv) **On serving of notice of a resolution to remove director**: Where notice has been given of a resolution to remove a director under this section and the director concerned makes with respect thereto representation in writing to the company and requests its notification to members of the company, the company shall, if the time permits it to do so,—

   a) in any notice of the resolution given to members of the company, **state the fact of the representation having been made;** and

   b) **send a copy of the representation to every member of the company to whom notice of the meeting is sent** (whether before or after receipt of the representation by the company), and if a copy of the representation is not sent as aforesaid due to insufficient time or for the company's default, the director may without prejudice to his right to be heard orally require that the representation shall be read out at the meeting:

Provided that copy of the representation need not be sent out and the representation need not be read out at the meeting if, on the application either of the company or of any other person who claims to be aggrieved, the Tribunal is satisfied that the rights conferred by this sub-section are being **abused to secure needless publicity for defamatory matter**; and the Tribunal may order the company's costs on the application to be paid in whole or in part by the director notwithstanding that he is not a party to it [section 169(4)].

Ch 2 - Appointment & Remuneration of Managerial Personnel

Appointment of Managing Director, Whole time Director or Manger (Section 196)

Question 1 ***(Nov 2011)***

A complaint was received by the Central Government from some shareholders of a public company that a person had been appointed as the Managing Director of the company without seeking the approval of the Central Government when such approval was required. State as to what action can be taken by the Central Government under the Companies Act, 2013. Also examine the validity of the acts of the Managing Director, if the complaint is found true.

Answer

In terms of **section 196 (4)** of the Companies Act, 2013, the appointment of a **managing director or whole-time director or manager** and the terms and conditions of such appointment and remuneration payable thereon must be **first approved by the Board of directors at a meeting and then by an ordinary resolution passed at a general meeting of the company**.

However, in case such appointment is at variance to the conditions **specified in Schedule V, the appointment and the remuneration shall be approved by the Central Government also**. It is to be noted that the approval of the Central Government is necessary only if the appointment is not made in accordance with the conditions specified in Schedule V to the Act.

In the given case, the approval of the Central Government is necessary. It means that the terms and conditions are at variance with Schedule V of the Act. In such a situation the appointment of the managing director is void. The central government may on receipt of the notice refer the matter to the Registrar to take necessary action against the company.

However, **section 196(5)** provides that subject to the provisions of this Act, where an appointment of a managing director, whole-time director or manager is not approved by the company at a general meeting, any act done by him before such approval **shall not be deemed to be invalid**. The interpretation of this sub section can be drawn **even in case the approval of the central government is not taken and the acts done by the managing director will be deemed to be valid.**

Question 2

Advise Super Specialties Ltd. in respect of the following proposals under consideration of its Board of directors:

i) Appointment of Managing Director who is more than 70 years of age;
ii) Payment of commission of 4% of the net profits per annum to the directors of the company;
iii) Payment of remuneration of ₹ 40,000 per month to the whole time director of the company running in loss and having an effective capital of Rs. 95.00 lacs.

Answer

i) Under the proviso to **section 196 (3)** of the Companies Act, 2013, a person who has attained the **age of seventy years** may be employed as managing director, whole-time director or manager by the approval of the members by a special resolution passed by the company in the general meeting and the explanatory statement annexed to the notice for such motion shall indicate the justification for appointing such person.

It is also provided that where no such special resolution is passed but votes cast in favour of the motion exceeds the votes, if any, cast against the motion and the C.G. is satisfied, on an application made by the board, that such appointment is most beneficial to the company, the appointment of the person who has attained the age of 70 years may be made.

ii) Under **section 197 (7)** of the Companies Act, 2013, independent directors may be paid profit related commission as may be approved by the members. However, under section 197 (1) the limit of total managerial remuneration payable by a public company, to its directors, including managing director and whole-time director, and its manager in respect of any financial year **shall not exceed eleven per cent of the net profits of that company for that financial year** computed in the manner laid down in section 198. Further, the third proviso to section 197 (1) provides that except with the approval of the company in general meeting, the **remuneration payable to directors who are neither managing directors or whole-time directors shall not exceed one per cent**. of the net profits of the company, if there is a managing or whole-time director or manager; or three per cent of the net profits in any other case.

Therefore, in the given case, **the commission of 4% is beyond the limit specified, and the same should be approved by the members by ordinary resolution**.

iii) If, in any financial year, a **company has no profits or its profits are inadequate, the company shall not pay to its directors,** including managing or whole time director or manager, any remuneration exclusive of any fees payable to directors except in accordance with the provisions of Schedule V. Section II of Part II of schedule V provides that where in any financial year during the currency of tenure of a managerial person, a company has no profits or its profits are inadequate, it may, without **Central Government approval, pay remuneration to the managerial person not exceeding Rs 60 Lakhs for the year if the effective capital of the company is negative or upto Rs 5 Crores.** In the present case, the proposed remuneration can be paid without the **approval of Central Government**.

Question 3

'X' was appointed as Managing Director for life by the Articles of Association of a private company incorporated on 1st June, 2014. Examine in this connection

a) Can 'X' be appointed for life as Managing Director?
b) Is it possible for the company in general meeting to remove 'X' from his office of directorship during his life time?

Answer

a) Under **section 196(2)** of the Companies Act, 2013 lays down that **no company shall appoint or re-appoint any person as its managing director, whole-time director or manager for a term exceeding five years at a time**. No concession or exception is allowed by the Act to private companies.

Hence, '**X' cannot be appointed as Managing Director for life in a private company**.

b) **Section 169(1)** of the Companies Act, 2013 empowers the company to remove a director, by ordinary resolution before the expiry of his period of office after giving him an opportunity of being heard. This section **applies to both public and private companies**. It applies to all directors except a director appointed by the Tribunal under **section 242** of the Act. The above provision applies to the Managing Director also as he is a director of the company and the member of its Board of Directors. Hence, **it is possible for the company in general meeting to remove 'X' before the expiry of his term of office by an ordinary resolution.**

Question 4 ***(RTP May 18)***

There are four directors in Shine Paper Limited. Mr. Madhav, being the director in station, has been authorized to draw and endorse cheque or oth er negotiable instruments on account of the company and also to direct registration of transfer of shares and signing the share certificates etc. Whether as per provisions of the Companies Act, 2013, he will be treated as managing director of the company? Also narrate the procedure of appointment of a managing director in a company.

Answer

Managing Director [Section 2(54)]: Section 2(54) of the Companies Act, 2013 defines a "Managing Director" as a director who is entrusted with substantial powers of management of the affairs of the company by:

(i) **virtue of articles of a company** or

(ii) **an agreement with the company** or

(iii) a **resolution passed in its general meeting**, or by its Board of Directors, and includes a director occupying the position of the managing director, by whatever name called.

Explanation to Section 2 (54) clarifies that substantial powers of the management shall not be deemed to include the power to do such administrative acts of a routine nature when so authorised by the Board such as:

(i) the power to affix the **common seal** of the company to any document or

(ii) to **draw and endorse any cheque** on the account of the company in any bank or

(iii) to **draw and endorse any negotiable instrument** or

(iv) to **sign any certificate of share** or

(v) to **direct registration of transfer** of any share.

In the instant case, Mr. Madhav, a director in Shine Paper Limited has been authorized to draw and endorse cheque or other negotiable instruments on account of the company and also to direct registration of transfer of shares and signing the share certificates etc.

Hence, according to explanation to section 2(54), Mr. Madhav will not be treated as Managing Director of the company as he is authorized to do administrative acts of a routine nature.

Procedure of appointment of a Managing Director [Section 196(4)]

(1) Subject to the provisions of **section 197 and Schedule V**, a managing director shall be appointed, and the terms and conditions of such appointment and remuneration payable be **approved by the Board of Directors at a meeting**.

(2) The terms and conditions and remuneration approved by Board of Directors as above shall be subject to the **approval of shareholders by a resolution at the next general meeting of the company.**

(3) In case such appointment is at variance to the conditions specified in the Schedule V of the Companies Act, 2013, the **appointment shall be approved by the Central Government**.

(4) The notice convening Board or general meeting for considering such appointment shall include the **terms and conditions of such appointment, remuneration payable and such other matters including interest**, of a director or directors in such appointments, if any.

A return in the prescribed form (Form No. MR.1) along with the prescribed fee shall be filed with the Registrar within sixty days of such appointment.

Overall maximum managerial remuneration and managerial remuneration in case of absence of or inadequacy of profits (Section 197) + Schedule V, Part II

Question 5

Star Health Specialties Ltd. owns a Multi-specialty Hospital in Chennai. Dr. Hamilton, a practising Heart Surgeon, has been appointed by the company as its director and it wants to pay him fee, on case to case basis, for surgery performed on the patients at the hospital. A question has arisen whether payment of such fee to him would amount to payment of managerial remuneration to a director subject to any restriction under the Companies Act, 2013.

Advise the company, which seeks to ensure that the same does not contravene any provision of the Companies Act, 2013.

Answer

In the given case, Dr. Hamilton has been appointed as a director. He has to be paid a fee for surgeries performed by him; it shall be fully possible under **section 197(4)** which states that the remuneration payable to the directors including managing or whole-time director or manager shall be inclusive of the remuneration payable for the services rendered by him in any other capacity except the following:

a) The services rendered are of a **professional nature**; and
b) In the opinion of the Nomination and Remuneration Committee (if applicable) or the Board of Directors in other cases, the **director possesses the requisite qualification for the practice of the profession.**

The company can therefore, pay a remuneration to **Dr. Hamilton a fee for surgeries performed by him as a professional fee which shall not be construed as a Managerial Remuneration under the Act.**

Question 6 ***(RTP Nov 2018)***

The Article of Association of a listed company have fixed payment of sitting fee for each Meeting of Directors subject to maximum of Rs. 30,000. In view of increased responsibilities of independent directors of listed companies, the company proposes to increase the sitting fee to Rs. 45,000 per meeting. Advise the company about the requirement under the Companies Act, 2013 to give effect to the proposal.

Answer

Section 197(5) of the Companies Act, 2013 provides that a director may receive remuneration by way of fee for attending the Board/Committee meetings or for any other purpose as may be decided by the Board, provided that the amount of such fees shall not exceed the amount as may be prescribed. The Central Government through rules prescribed that the amount of sitting fees payable to a director for attending meetings of the Board or committees thereof may be such as may be decided by the Board of directors or the Remuneration Committee thereof which **shall not exceed the sum of rupees 1 lakh per meeting of the Board or committee thereof**. Further, the Board may decide different sitting fee payable to independent and non-independent directors other than whole-time directors.

From the above, it is clear that fee to independent directors can be increased from ₹ 30,000 to ₹ 45,000 per meeting **by passing a resolution in the Board Meeting and alternating the Articles of**

Association by passing Special Resolution.

Question 7

A company wants to include the following clause in its Articles of Association:

"Each director shall be entitled to be paid out of the funds of the company for attending meetings of the Board or a Committee thereof including adjourned meeting such sum as sitting fees as shall be determined from time to time by the Directors but not exceeding a sum of Rs. 30,000 for each such meeting to be attended by the Director."

You are required to advise the company as to the validity of such a clause and the correct legal position under the provisions of the Companies Act, 2013.

Answer

The Companies Act, 2013 vide **section 197 (5)** provides that the sitting fee payable to directors for attending meetings of the Board or committees thereof will be decided by the Board subject to limits prescribed by the Central Government in rules framed in this behalf. **The limit prescribed by the Central Government is Rs. 1 Lakh per meeting and may be different for independent and non-independent directors.**

Hence, the clause in the Articles proposed in the case given, does not make any sense under the Companies Act, 2013.

Question 8 ***(Nov 2010, Nov 18)***

Mr. X, a Director of MJV Ltd., was appointed on 1st April, 2012, one of the terms of appointment was that in the absence of adequacy of profits or if the company had no profits in a particular year, he will be paid remuneration in accordance with Schedule V. For the financial year ended 31st March, 2016, the company suffered heavy losses. The company was not in a position to pay any remuneration but he was paid Rs. 50 lacs for the year, as paid to other directors. The effective capital of the company is Rs. 150 crores. Referring to the provisions of Companies Act, 2013, as contained in Schedule V, examine the validity of the above payment of remuneration to Mr. X.

Answer

Under **Section II of Part II of Schedule V** to the Companies Act, 2013, the remuneration payable to a managerial personnel is linked to the effective capital of the company. Where in any financial year during the currency of tenure of a managerial person, a **company has no profits or its profits are inadequate, it may, without Central Government approval, pay remuneration to the managerial person not exceeding Rs. 120 Lakhs in the year in case the effective capital of the company is between Rs. 100 crores to Rs. 250 crores.** The limit will be **doubled if approved by the members by special resolution** and further if the appointment is for a part of the financial year the remuneration will be pro-rated.

From the foregoing provisions contained in schedule V to the Companies Act, 2013 the payment of Rs. 50 Lacs in the year as remuneration to Mr. X is valid in case he accepts it, as under the said schedule he is entitled to a remuneration of ₹ 120 Lakhs in the year and his terms of appointment provide for payment of the remuneration as per schedule V.

Note: As per the amendment in Schedule V by the Ministry of Corporate Affairs vide Notification S.O. 2922(E) dated 12th September 2016, part II, for Section II of Schedule V has been revised. For detail, please refer the Supplementary Study Paper containing amendments from 1st November 2015 to 31st October 2016.

Question 9

A and B were appointed as first directors on 4th April, 2014 in Sun Glass Ltd. Thereafter, C, D International Technologies Limited, a listed company, being managed by a Managing Director proposes to pay the following managerial remuneration:

i) **Commission at the rate of five percent of the net profits to its Managing Director**, Mr. Kamal.

ii) The directors other than the **Managing Director are proposed to be paid monthly remuneration of Rs. 50,000 and also commission at the rate of one percent of net profits** of the company subject to the condition that overall remuneration payable to ordinary directors including monthly remuneration payable to each of them shall not exceed two percent of the net profits of the company. The commission is to be distributed equally among all the directors.

iii) The company also proposes to **pay suitable additional remuneration to Mr. Bhatt, a director, for professional services rendered as software engineer, whenever such services are utilized.**

You are required to examine with reference to the provisions of the Companies Act, 2013 the validity of the above proposals.

Answer

International Technologies Limited, a listed company, being managed by a Managing Director proposes to pay the following managerial remuneration:

i) Commission at the rate of 5% of the net profits to its Managing Director, Mr. Kamal: Part (i) of the second proviso to section 197(1), provides that except with the approval of the company in general meeting, the remuneration payable to any one managing director; or whole time director or manager **shall not exceed 5 % of the net profits of the company** and if there is more than one such director then **remuneration shall not exceed 10 % of the net profits to all such directors and manager taken together.**

In the present case, since the International Technologies Limited is being managed by a Managing Director, the commission at the rate of 5% of the net profit to Mr. Kamal, the **Managing Director is allowed and no approval of company in general meeting is required.**

ii) The directors other than the Managing Director are proposed to be paid monthly remuneration of Rs. 50,000 and also commission at the rate of **1 % of net profits** of the company subject to the condition that overall remuneration payable to ordinary directors including monthly remuneration payable to each of them **shall not exceed 2 % of the net profits of the company**: Part (ii) of the second proviso to section 197(1) provides that except with the approval of the company in general meeting, the remuneration payable to directors who are neither managing directors nor whole time directors shall not exceed-

a) 1% of the net profits of the company, if there is a managing or whole time director or manager;

b) 3% of the net profits in any other case.

In the present case, the maximum remuneration allowed for directors other than managing or whole time director is 1% of the net profits of the company because the company is having a managing director also. Hence, if the company wants to fix their remuneration at not more than 2% of the net profits of the company, the approval of the company in general meeting is required.

iii) The company also proposes to pay suitable additional remuneration to Mr. Bhatt, a director, for professional services rendered as software engineer, whenever such services are utilized:

a) According to **section 197(4)**, the remuneration payable to the directors of a company, including any managing or whole-time director or manager, shall be determined, in accordance with and subject to the provisions of this section, either

I) by the **articles of the company**, or

II) by a **resolution** or,

III) if the articles so require, by a special resolution, passed by the company in general meeting, and

b) The remuneration payable to a director determined aforesaid **shall be inclusive of the remuneration payable to him for the services rendered by him in any other capacity**.

c) Any remuneration for services rendered by any such director in other capacity shall not be so included if—

I) the services rendered are of a professional nature; and

II) in the opinion of the Nomination and Remuneration Committee, if the company is covered under sub-section (1) of section 178, or the Board of Directors in other cases, the director possesses the requisite qualification for the practice of the profession.

Hence, in the present case, the additional remuneration to Mr. Bhatt, a director for professional services rendered as software engineer will not be included in the maximum managerial remuneration and is allowed but **opinion of Nomination and Remuneration Committee is to be obtained.**

Also, the International Technologies Limited (a listed company) shall disclose in the Board's report, the ratio of the remuneration of each director to the median employee's remuneration and such other details as may be prescribed under the Companies (Appointment and Remuneration of Managerial personnel) Rules, 2014.

Question 10 ***(Nov 17)***

Venus Limited is a widely held, listed company having two executive directors who are technocrats. The company has suffered losses in the last four years. The company wants to enhance the remuneration of the executive directors to ₹ 6,00,000 per month from existing remuneration of ₹ 4,00,000. The audited balance sheet as on 31st March 2016 reveals that the paid up capital of the company is ₹ 15 crores, accumulated losses ₹ 11 crores and secured long term borrowings ₹ 5 crores. Besides, the company has long term investments of ₹ 11 crores. The company's remuneration committee has recommended the proposal and the company is regular in repayment of its debts. Analyse the proposition with reference to the provisions of the Companies Act 2013.

Answer

According to **Section 197** of the Companies Act, 2013,

1. If, in any financial year, a **company has no profits or its profits are inadequate**, the **company shall not pay to its directors, including any managing or whole- time director or manager,** by way of remuneration any sum exclusive of any fees payable to directors except in accordance with the provisions of Schedule V and if it is not able to comply with such provisions, with the **previous approval of the Central Government**. [Sub- section 3]

2. In cases where **Schedule V is applicable on grounds of no profits or inadequate profits**, any provision relating to the remuneration of any director which purports to increase or has the effect of increasing the amount thereof, whether the provision be contained in the company's memorandum or articles, or in an agreement entered into by it, or in any resolution passed by

the company in general meeting or its Board, shall not have any effect unless such increase is in accordance with the conditions specified Schedule V and if such conditions are not being complied, the **approval of the Central Government had been obtained**. [Sub section 11]

However, in case of a **managerial person who is functioning in a professional capacity, no approval of Central Government is required**, if such managerial person is **not having any interest in the capital of the company or its holding company or any of its subsidiaries directly or indirectly or through any other statutory structures and not having any, direct or indirect interest or related to the directors or promoters of the company or its holding company or any of its subsidiaries at any time during the last two years before or on or after the date of appointment** and possesses graduate level qualification with expertise and specialised knowledge in the field in which the company operates. [Item B of Section II of Schedule V]

Further the limits specified under Section II of Schedule V shall apply, if-

(i) payment of remuneration is approved by a resolution passed by the Board and, in the case of a company covered under **sub-section (1) of section 178 also by the Nomination and Remuneration Committee.**

(ii) the company has not committed any default in repayment of any of its debts (including public deposits) or debentures or interest payable thereon for a continuous period of 30 days in the preceding financial year before the date of appointment of such managerial person and in case of a default, the company obtains prior approval from secured creditors for the proposed remuneration and the fact of such prior approval having been obtained is mentioned in the explanatory statement to the notice convening the general meeting.

Since, the **company has suffered losses in the last four years**, the company will pay remuneration to its directors in accordance with the provisions of Schedule V to the Companies Act, 2013.

The total remuneration that Venus Limited is intending to pay to two technocrats is 144 lakhs per annum, from the current remuneration of 96 lakhs per annum. However, since the two executive directors are technocrats (working in professional capacity) and the remuneration has been proposed by the remuneration committee and the company is regular in payment of debts, no approval of Central Government is required. Also, since the given situation is compliant of Schedule V, **Central Government approval will not be required even when there is increase in remuneration payable**.

Assumption: The term technocrat used for the directors has been interpreted as that the directors are 'functioning in a professional capacity'.

Question 11 ***(Nov 2016)***

Mr. Smart, a technocrat aged 71 years and reputed to be a specialist in reviewing sick companies is being considered to be appointed as Managing Director of Downhill Industries Limited. The company has been incurring losses for the past several years and its "effective capital" is ₹ 500 crores. Referring to the provisions of the Companies Act, 2013, discuss:

i) Can Mr. Smart be appointed as Managing Director of the company despite being over 70 years of age? If so, what is the process to be followed to enable this?

ii) What is "effective capital" as per Schedule V of the Act?

iii) What is the maximum permissible remuneration under the Companies Act, 2013?

Answer

i) **Appointment of Managing Director:** According to section 196(3) of the Companies Act, 2013, no company shall appoint or continue the employment of any person as managing director, whole-time director or manager who is below the age of 21 years or has attained the age of 70 years.

However, a person who has attained the age of seventy years may be appointed to such office by passing of a special resolution in which case the explanatory statement annexed to the notice for such motion shall indicate the justification for appointing such person.

It is also provided that where no such special resolution is passed but votes cast in favour of the motion exceed the votes, if any, cast against the motion and the C.G. is satisfied, on an application made by the board, that such appointment is most beneficial to the company, the appointment of the person who has attained the age of 70 years may be made.

Conclusion – Downhill industries limited can appoint Mr. Smart aged 71 years as managing director by passing special resolution and justifying his appointment in the explanatory statement annexed to the notice for such motion.

ii) **Effective Capital as per Schedule V of the Act:** "Effective Capital" means the **aggregate of the paid-up share capital (excluding share application money or advances against shares); amount, if any, for the time being standing to the credit of share premium account; reserves and surplus (excluding revaluation reserve); long- term loans and deposits repayable after one year** (excluding working capital loans, over drafts, interest due on loans unless funded, bank guarantee, etc., and other short-term arrangements) as reduced by the aggregate of any investments (except in case of investment by an investment company whose principal business is acquisition of shares, stock, debentures or other securities), accumulated losses and preliminary expenses not written off.

iii) **Maximum permissible remuneration:** According to **Section II of Part II of Schedule V,** where in any financial year during the currency of tenure of a managerial person, a company has no profits or its profits are inadequate, it may, without Central Government approval pay remuneration to the managerial person not exceeding 60 lakhs plus 0.01% of the effective capital in excess of ₹ 250 crores in case where the effective capital is 250 crores and above.

Hence, the maximum permissible remuneration shall be 60 lakhs plus 0.01% of 250 crore [500 crore - 250 crore]: ₹ 60 Lakhs + 2.5 lakhs is ₹ 62.5 Lakhs.

[Assumption: Mr. Smart reputed to be a specialist in reviewing sick companies is being considered to be appointed as Managing Director of Downhill Industries Limited and the company has been incurring losses for the past several years, it may also be assumed that Downhill Industries Limited is a sick company. So, in that case, the company may pay remuneration upto two times the amount permissible under section II (provided under section III of part II of schedule V)].

Question 12 ***(RTP May 2018)***

Excel limited is a listed company with a turnover of ₹ 60 crores in the FY 2016-2017. The company appoints Ms. R as the women director on 1st March 2017. Ms. R is already a director in twelve companies including ten public companies. Also, Ms. R is chartered accountant in practice.

Further, also, Ms. R, is a director in Supreme Ltd. where he is acting in a professional capacity. Since lots of proposal for the holding of directorship in various companies are lined up before the Ms. R, so in order to retain him, Remuneration and nomination committee proposed to enhance the remuneration of Ms. R from 4 Lac per month to 6 Lac per month. However, Supreme Limited was

running in losses for last 2 years.

Evaluate in the light of the given facts, the following situations with reference to the provisions of the Companies Act, 2013-

a) The validity of an appointment of Ms. R in Excel Limited.
b) Analysis the proposition of enhancement of the remuneration of Ms. R in Supreme Ltd.

Answer

a) Number of directorships: As per **section 165(1)** of the Companies Act, 2013, **no person shall hold office as director, including any alternate directorship, in more than 20 companies at the same time.**

Out of the limit of 20, the maximum number of public companies in which a person can be appointed as a director shall not exceed 10. [Proviso to section 165(1)]
Private companies that is either holding or subsidiary company of a public company shall be included in reckoning the limit of public companies in which a person can be appointed as a director.

In the instant case, **Ms. R was appointed as a women director** on 1st March, 2017 in Excel Limited. **She was already holding directorship in twelve companies including ten public companies.**

As Ms. R was already a director in ten public companies, her appointment in Excel Limited is not valid as it will lead to her directorship in 11 public companies.
In this case, either **she can choose between the companies in which she wishes to continue to hold the office of director or resign her office as director in the other remaining companies to maintain the limit of holding of directorship**.

b) Remuneration : In the given case, since, the **company has suffered losses in the last two years, the company will pay remuneration to its directors in accordance with the provisions of Schedule V** to the Companies Act, 2013.

In case of a managerial person **who is functioning in a professional capacity, no approval of Central Government is required, if such managerial person is not having any interest in the capital of the company or its holding company or any of its subsidiaries directly or indirectly or through any other statutory structures and not having any, direct or indirect interest or related to the directors or promoters of the company or its holding company or any of its subsidiaries at any time during the last two years before or on or after the date of appointment** and possesses graduate level qualification with expertise and specialised knowledge in the field in which the company operates. [Item B of Section II of Schedule V]

The total remuneration that supreme Limited is intending to pay to Ms. R is 72 lakhs per annum, from the current remuneration of 48 lakhs per annum. Since Ms. R is working in professional capacity and the remuneration has been proposed by the remuneration Committee, no approval of Central Government is required. Also, the case shall be in compliant of Schedule V, Central Government approval will not be required even when there is increase in remuneration payable.

Compensation for loss of office of managing or whole time director (Section 202)

Question 13

Can a company pay compensation to its directors for loss of office? Explain briefly the relevant provisions of the Companies Act, 2013 in this regard?

Answer

A company can pay compensation to its directors for loss of office as provided in **sections 202** of the Companies Act, 2013. Under section 202, such compensation can be paid only to managing director, director holding the office of the manager and to a whole time director but not to others. **The compensation payable shall be on the basis of average remuneration actually earned by such director for three years, or such shorter period as the case may be, immediately preceding the ceasing of holding of such office and shall be for the unexpired portion of his term or for three years whichever is shorter**. No such payment can be made, if **winding up of the company is commenced before or commences within 12** months after he ceases to hold office if the assets of the company on the winding up, after deducting expenses thereof, are not sufficient to repay to the shareholders the share capital (including the premium, if any) contributed by them. However, no payment of compensation can be made in the following cases:

a) Where a **director resigns on the ground of amalgamation or reconstruction** and is appointed the office of managing director or manager or other officer of such reconstructed or amalgamated company,

b) Where the **director resigns his office otherwise than on the reconstruction of the company** or its amalgamation as aforesaid,

c) Where the director **vacates office under section 167** of the Companies Act, 2013,

d) Where the winding up of the company is **due to the negligence** of the director concerned,

e) Where the **director has been guilty of any fraud or breach of trust**,

f) Where the director has **instigated or has taken part directly or indirectly in bringing about, the termination of his office**.

Question 14

Mr. Doubtful was appointed as Managing Director of Carefree Industries Ltd. for a period of five years with effect from 1.4.2011 on a salary of Rs. 12 lakhs per annum with other perquisites. The Board of directors of the company on coming to know of certain questionable transactions, terminated the services of the Managing Director from 1.3.2014. Mr. Doubtful termed his removal as illegal and claimed compensation from the company. Meanwhile the company paid a sum of Rs. 5 lakhs on ad hoc basis to Mr. Doubtful pending settlement of his dues. Discuss whether:

i) The company is bound to pay compensation to Mr. Doubtful and, if so, how much.

ii) The company can recover the amount of Rs. 5 lakhs paid on the ground that Mr. Doubtful is not entitled to any compensation, because he is guiding of corrupt practice.

Answer

According to **Section 202** of the Companies Act, 2013, compensation can be paid only to a Managing, Whole-time Director or Manager. Amount of compensation cannot exceed the remuneration which he would have earned if he would have been in the office for the unexpired term of his office or for 3 years whichever is shorter. **No compensation shall be paid, if the director**

has been found guilty of fraud or breach of trust or gross negligence in the conduct of the affairs of the company.

In light of the above provisions of law, the company is not liable to pay any compensation to Mr. Doubtful, if he has been found guilty of fraud or breach of trust or gross negligence in the conduct of affairs of the company. But, it is not proper on the part of the company to withhold the payment of compensation on the basic of mere allegations. **The compensation payable by the company to Mr. Doubtful would be Rs. 25 Lacs calculated at the rate of Rs. 12 Lacs per annum for unexpired term of 25 months.**

Regarding adhoc payment of Rs. 5 Lacs, **it will not be possible for the company to recover the amount from Mr. Doubtful in view of the decision in case of Bell vs. Lever Bros. (1932) AC 161 where it was observed that a director was not legally bound to disclose any breach of his fiduciary obligations so as to give the company an opportunity to dismiss him**. In that case the Managing Director was initially removed by paying him compensation and later on it was discovered that he had been guilty of breaches of duty and corrupt practices and that he could have been removed without compensation.

Question 15

A Managing Director was removed during the tenure of office and certain compensation was paid to him. It was later on found that during the tenure of his office that he was guilty of corrupt practices and the company felt that no compensation should have paid to him and therefore wants to recover the compensation so paid to him. Can the company succeed?

Answer

The Companies Act, 2013 **does not provide for the refund of any compensation paid by the company to its Managing Director, whole time director or manager**. It only lays down the situations under which no compensation is payable for loss of office and one such situation is the commitment of fraud or breach of trust by the director.

Moreover, in Bell vs. Lever Brothers, (1932), Lever Brothers removed their managing director of a subsidiary by paying him compensation. It was afterwards discovered that during his tenure of office he had been guilty of so many breaches of duty and corrupt practices that he could have been removed without compensation. An action was then commenced to recover back the compensation money. **It was held that Bell was not bound to refund the compensation money and to disclose any breach of his fiduciary obligation so as to give the company an opportunity to dismiss him**. Thus, the **Managing Director is not bound to refund the compensation. Hence, the company cannot succeed.**

Appointment of Key Managerial Personnel (Section 203)

Question 16 ***(May 15)***

Explain the concept of KMP (Key Managerial Personnel) as introduced by the Companies Act, 2013. Explain the classes of companies which are required to appoint whole time Key Managerial Person under the provisions of the said Act.

Answer

As per the provisions of **Section 203(1)** of the Companies Act, 2013, every company belonging to such class or classes of companies as may be prescribed, shall have the following whole time Key Managerial Personnel.

a) **Managing Director or Chief Executive Officer or Manager and in their absence, a Whole- time Director**;

b) **Company Secretary**; and

c) Chief Financial Officer

According to Rule 8 of the Companies (appointment and Remuneration of Managerial Personnel) Rules, 2014, every listed company and every other **public company having a paid up share capital of Rs. 10 crore or more shall have a whole-time key managerial personnel**.

Further, as per the Companies (Appointment and Remuneration of Managerial Personnel) Amendment Rules, 2014, a company other than a company covered under Rule 8 above, which has a **paid up share capital of Rs. 5 crore or more shall have a whole-time company secretary**.

With the insertion of Rule 8A to the above rules, it is now mandatory for every other company to have a whole-time company secretary, if its paid up share capital is Rs. 5 Crore or more.

Question 17 ***(RTP Nov 18 & May 18)***

Mr. AMIT is the Managing Director of ANJ Limited, which is a non-government public company. The directors of CHH Limited decided to appoint Mr. AMIT as the Managing Director of the company, even though Mr. AMIT decided not to vacate his place of office of Managing Director of ANJ Limited. A notice for a Board meeting specifying a resolution containing the proposal of appointment of Mr. AMIT was served to all the eligible directors of CHH Limited.

Out of eight directors of the company, six directors attended the meeting and out of them four directors gave consent to the resolution, one director voted against the said appointment and another director abstained from voting. The Board of Directors seek your opinion whether Mr. AMIT can be appointed as the Managing Director, of the company in this situation. Referring to the applicable provisions of the Companies Act, 2013, advise them.

Answer

As per **Section 203(3)** of the Companies Act, 2013, a **whole -time key managerial personnel shall not hold office in more than one company except in its subsidiary company at the same time**.

However, the above sub-Section (3), shall **not disentitle a key managerial personnel from being a director of any company with the permission of the Board**.

Provided also that a company may appoint or employ a person as its managing director, if he is the managing director or manager of one, and of not more than one, other company and such appointment or employment is made or approved by a resolution passed at a meeting of the Board with the consent of all the directors present at the meeting and of which meeting, and of the resolution to be moved thereat, specific notice has been given to all the directors then in India.

In the given case, **unanimous consensus of all the directors present at the meeting was lacking. Hence, Mr. Amit cannot be appointed as a Managing Director of C HH Limited.**

Question 18 ***(May 18)***

ABC Limited, an unlisted company having a paid up share capital of Ten crores of Rupees during the preceding financial year has appointed Shri X, a Fellow member of the Institute of Chartered Accountant of India as Chief Financial Officer of the company who is appointed as Key Managerial Personnel under section 203 of the Companies Act, 2013. Shri X is also a Fellow member of the Institute of Company Secretaries of India. The Company Secretary post has become vacant. In order to reduce the administrative expenses, the Company proposes to appoint Shri X as Company

Secretary in addition to Chief Financial Officer post. Whether the proposal is legally valid under the provisions of the Companies Act, 2013?

Answer

According to **Section 203(1)** of the Companies Act, 2013, every company belonging to such class or classes of companies as may be prescribed, shall have the following whole time key managerial personnel:-

a) **Managing Director, or Chief Executive Officer or Manager and in their absence, a Whole-time Director;**

b) **Company Secretary; and**

c) **Chief Financial Officer.**

According to Rule 8 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 **every listed company and every other public company having a paid-up share capital of ₹ 10 crore or more shall have whole-time key managerial personnel**.

In the instant case, ABC Limited is having paid up share capital of ₹ 10 crore, so it is covered under the above Rule and it is mandatory for it to appoint a whole time KMP. As the term used is 'whole time', therefore, three different individuals are required to hold these three key positions.

In view of the above, the company cannot appoint Mr. X as the Company Secretary of the company in addition to his CFO post. Further, Section 203 of the Act specifically prescribes the word "and" between Company Secretary and CFO. Thus, both the positions are to be held by separate persons.

Hence, the proposal of the company to appoint Mr. X as the Company Secretary is not valid.

Question 19 ***(May 19)***

Mr. Mania is the Managing Director of S Limited (and nowhere else), which is a subsidiary of H Limited. Seeing the success mot S Limited, the directors of H Limited (which is listed company) decided and approached Mr. Mania to act as the managing Director of H Limited. Mr. Mania agreed with directors of H Limited subject to a condition that he will continue to act as the Managing Direct of S Limited also. In this direction, the directors of H Limited propose to appoint him by means of resolution (containing the terms and conditions of appointment excluding remuneration) by circulation. Referring of and analyzing the relevant provisions of the Companies Act, 2013, decide whether the decision of appointing and the proposed mode or appointment of Mr. Mania as the Managing Director of H Limited is valid.

Will your answer differ in case S Limited is not a subsidiary of H Limited?

Answer

Appointment of Key Managerial Personnel:

As per sec. 203(2) of the Companies Act, 2013, every whole-time KMP of a company shall be appointed by means of a Board Resolution containing the terms and conditions of the appointment including the remuneration.

As per sec. 203(3), a whole-time KMP shall not hold office in more than one company except in its subsidiary company at the same time.

A company may appoint or employ a person as its managing director, if he is the managing director or manager of one, and of not more than one, other company. Such appointment or employment is made or approved by a resolution passed at a meeting of the Board with the consent of all the directors present at the meeting. Specific notice of such meeting and of the resolution to be moved

thereat, has been given to all the directors then in India.

Conclusion: Appointment of KMP can be made in duly convened meeting of Board. Proposed mode of appointment i.e. resolution by circulation is not a valid mode. Further Board Resolution must contain the terms and conditions of the appointment including the remuneration.

In case S Ltd. is not a subsidiary of H Ltd. Mr. Mania cannot be appointed as managing director (considering as whole time KMP) of two companies at the same time.

Ch 3 - Meetings of Board and its Powers

Meeting of Board (Section 173)

Question 1

The Board of directors of ABC Ltd. met thrice in the year 2014 and the 4th Meeting, though called, could not be held for want of quorum.

Examine with reference to the relevant provisions of the Companies Act, 2013, whether any provisions of the Companies Act, 2013 have been contravened?

Answer

In terms of **section 173(1)** of the Companies Act, 2013, a company must hold a minimum number of four meetings every year of its Board of directors in such a manner that **not more than 120 days shall intervene between two consecutive meetings of the Board.**

Further, the proviso to this sub-section provides that the Central Government may by notification, direct that these provisions will not apply in relation to any class or description of companies or may apply subject to such exceptions, modifications or conditions as may be specified in the notification.

Under **section 174 (4)** of the Companies Act, 2013, where a meeting of the Board could not be held for want of quorum, then, unless the articles of the company otherwise provide, the **meeting shall automatically stand adjourned to the same day at the same time and place in the next week or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place**.

From the above provisions in case a meeting is adjourned, the violation under section 173(1) does not arise as the meeting was started well in time but **could not close due to want of quorum.** The holding of the adjourned meeting though in the next year will be treated as continuation of the 4th meeting of the previous year and **will therefore not count in the meetings held in the next year but in the previous year.**

Therefore, the provisions of the Companies Act, 2013 have not been violated or contravened.

Question 2

Mr. P and Mr. Q who are the directors of the Company informed the Company their inability to attend the meeting because the notice of the meeting was not served on them. Discuss whether there is any default on the part of the Company and the consequences thereof.

Answer

Under **section 173(3)** of the Companies Act, 2013 a meeting of the Board shall be called by giving **not less than seven days'** notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means.

Section 173(4) further provides that every officer of the company whose duty is to give notice under this section and who fails to do so shall be liable to a penalty of Rs. 25,000.

In the given case as no notice, was served on Mr. P and Mr. Q who are the directors of the company, thus, under section 173(4) **every officer of the company responsible for the default shall be punishable with fine of Rs. 25,000.**

Neither the Companies Act, 2013 nor the Companies (Meetings of the Board and its Powers) Rules, 2014 lay down any specific provision regarding the validity of a resolution passed by the Board of Directors in case notice was not served to all the directors as stipulated in the Act. We shall have to go by the provisions of the Act which clearly provide for the notice to be sent to every director failing which the resolutions passed will be invalid. The Supreme Court, in case of Parmeshwari Prasad vs. Union of India (1974) has held that the resolutions passed in the board meeting shall not be valid, since notice to all the Directors was not given in writing. **Notice must be given to each director in writing.** Hence, **even though the directors concerned knew about the meeting, the meeting shall not be valid and resolutions passed at the meeting also shall not be valid.**

Question 3 ***(RTP May 19)***

The Board of Directors of Infotech Consultants Limited, registered in Kolkata, proposes to hold the next board meeting in the month of May, 2014.They seek, your advice in respect of the following matters:

i) Can the board meeting be held in Chennai, when all the directors of the company reside at Kolkata?
ii) Is it necessary that the notice of the board meeting should specify the nature of business to be transacted?

Advise with reference to the relevant provisions of the Companies Act, 2013.

Answer

i) There is no provision in the Companies Act, 2013 under which the board meetings must be held at any particular place. The Companies Act lays down the provisions for holding meetings by video conferencing, sending notices, procedures at the meeting etc. Therefore, there is **no difficulty in holding the board meeting at Chennai even if all the directors of the company reside at Kolkata and the registered office is situated at Kolkata provided that the requirements regarding the holding of a valid board meeting and the other provisions relating to the signing of register of contracts, taking roll calls, etc. are complied with.**

ii) **Section 173 (3)** of the Companies Act, 2013 provides for the giving of notice of every board meeting of not less than seven days to every director of the company. There is no provision in the Act laying down the contents of the notice. Hence, **it may be construed that notice may be interpreted as intimation of the meeting and does not necessarily include the sending of the Agenda of the meeting**. However, considering the importance of Board Meetings and the responsibilities placed on the directors for decisions taken at the meetings, it is inevitable for them to be properly prepared and informed about the items to be discussed at the Board Meetings. As a **matter of good secretarial practice, the notice should include full details and particulars of the business to be transacted at the Board Meetings.**

The articles of association of the company may make it mandatory to do so in almost all cases.

Question 4

XYZ Ltd. is a foreign collaborator in ABC Ltd. incorporated in India under the Companies Act, 2013. The foreign collaborator holds 49% of the shareholding. The Board meetings of ABC Ltd are usually held in India and sometimes meetings of the Board are called at a very short notice for which there is a provision in the Articles of Association that during such situations notices of the meetings of the Board can be sent by e-mail. State in this connection whether such a provision in the Articles of Association of a foreign collaborated company is valid within the purview of the provisions of the Companies Act, 2013 .

Answer

In terms of the proviso to **section 173(3)** of the Companies Act, 2013 a meeting of the Board **may be called at shorter notice to transact urgent business subject to the condition that at least one independent director**, if any, shall be present at the meeting. No exception is made for any class or classes of companies.

Further, under section 173(3) a meeting of the Board shall be called by giving not less than seven days' notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means.

If we examine the above provision, **it is clear that the notice shall be sent by hand delivery or by post or by electronic means.**

Hence, the sending of notice by e-mail is an ordinary mode of sending notice of a board meeting under the Companies Act, 2013.

Therefore, in the given case the **shorter notice is legally permitted with the only condition being the presence of the quorum and at least one independent director**. The provision of the Articles in this regard is not relevant as the position is amply clear in the Act itself.

Question 5

Examine with reference to the provisions of the Companies Act, 2013 whether notice of a Board Meeting is required to be sent to the following persons:

i) An interested Director;

ii) A Director who has expressed his inability to attend a particular Board Meeting;

iii) A Director who has gone abroad (for less than 3 months).

Answer

Notice of Board meeting

i) **Interested director**: Section 173(3) of the Companies Act, 2013 makes it mandatory for every director to be given proper notice of every board meeting. It is immaterial whether a director is interested or not. In case of an Interested Director, **notice must be given to him** even though he is precluded from voting at the meeting on the business to be transacted.

ii) **A Director who has expressed his inability to attend a particular Board Meeting**: In terms of section 173(3) even if a director states that he will not be able to attend the next Board meeting; **notice must be given to that director.**

iii) **A director who has gone abroad**: A director who has gone abroad is still a director. Therefore, he is entitled to receive notice of board meetings during his stay abroad. The Companies Act, 2013, allows delivery of notice of meeting by electronic means also. This is important because the Companies Act, 2013 **permits a director to participate in a meeting by video conferencing or any other audio visual means.**

Question 6

What are the conditions to be fulfilled for calling meetings at shorter notice than as prescribed by Companies Act, 2013.

One of the directors, a senior professional, objected to receiving the notice by e-mail. Advise him.

Answer

Notice of The Board Meeting & Condition to Call Meeting at Shorter Notice - In terms of the

proviso to **Section 173(3)** of the Companies Act, 2013 a meeting of the Board may be called at shorter notice to transact urgent business subject to the condition that **at least one independent director, if any, shall be present at the meeting**. No exception is made for any class or classes of companies.

Under Section 173 (3) a meeting of the **Board shall be called by giving not less than 7 days notice in writing to every director** at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means.

Hence the senior Director's objections to receiving the notice by email is not sustainable.

Question 7 ***(RTP May 18)***

Examine the following aspect related to convening of board meeting with reference to the provisions of the Companies Act, 2013:

i) The Chairman of Greenhouse Limited convened a board meeting and two weeks' notice was served on all directors of the company. Two of the independent directors on the board objected on the grounds that no proper agenda for the meeting was circulated.

ii) Purple Florence Limited proposes to hold its board meeting at a shorter notice through video conferencing.

Answer

i) According to section 173 (3) of the Companies Act, 2013, **a meeting of the Board shall be called by giving not less than 7 days' notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means.**

According to the question, two of the independent directors on the Board has objected on the grounds that no proper agenda for the meeting was circulated.

The Companies Act, 2013 does not specifically provide for sending agenda along with the notice of the meeting. However, generally as a good secretarial practice, the notice is accompanied with the agenda of the meeting. Thus, the contention of the independent directors objecting on the grounds that no agenda for the meeting was circulated, does not hold good.

Further, the Chairman of Greenhouse Limited has convened the Board meeting by serving a two weeks' notice (i.e. more than 7 days). Hence, the meeting shall be valid.

ii) According to **section 173** of the Companies Act, 2013,

a) The **directors can participate in a meeting of the Board either in person or through video conferencing or other audio visual means, as may be prescribed**, which are capable of recording and recognising the participation of the directors and of recording and storing the proceedings of such meetings along with date and time. **Further, Central Government may provide for matters which cannot be dealt in a meeting through video conferencing or other audio visual means.**

b) A meeting of the Board shall be called by **giving not less than 7 days' notice** in writing to every director at his address registered with the company.

Provided that a meeting of the Board **may be called at shorter notice to transact urgent business subject to the condition that at least one independent director**, if any, shall be present at the meeting. Further, in case the independent directors are not present at such a

meeting of the Board, decisions taken at such a meeting shall be circulated to all the directors and shall be final only on ratification thereof by at least one independent director, if any.

Hence, Purple Florence Limited can hold a board meeting at a shorter notice through video conferencing, for transacting urgent business subject to the condition that **at least one independent director, if any, shall be present at the meeting.** Further, if the independent directors are absent from the meeting of the Board, decision taken at such a **meeting shall be circulated to all the directors and shall be final only on ratification thereof by at least one independent director, if any.**

Question 8

A director goes abroad for a period of more than 3 months and an alternate director has been appointed in his place under section 161(2). During the period of absence of the original director, a board meeting was called. In this connection, with reference to the provisions of the Companies Act, 2013, advise whom should the notice of Board meeting be given to the "original director" or to the "alternate director"?

Answer

According to **Section 161(2)** of the Companies Act, 2013, the Board of Directors of a company may, if so authorised by its articles or by a resolution passed by the company in general meeting, appoint a person, not being a person holding any alternate directorship for any other director in the company, to act as an alternate director for a director during his absence for a period of **not less than three months from India.**

According to **section 173(3),** a meeting of the Board may be called by giving **atleast a 7 days'** notice in writing to every director to his registered address with the company and such notice shall be sent by hand delivery or by post or by electronic means.

There is no legal precedence whether the **notice of the meeting is to be sent to the original director or the alternate director**. But as matter of prudence the notice of the meeting may be served to both the alternate director as well as the original director who is for the time being outside India.

Question 9 ***(Nov 2016)***

Seafood Limited, a public limited company was incorporated on 1st April, 2015. The company has conducted four Board meetings during the financial year 2015-16 i.e. on 6th April, 2015, 28th August, 2015, 30th September, 2015 and 30th March, 2016.

i) Has the company contravened the provisions of the Companies Act, 2013 in respect of the conduct of the meetings?

ii) Will your answer differ if the company was incorporated under Section 8 of the Companies Act, 2013?

Answer

Board Meeting: Section 173(1) of the Companies Act, 2013 provides for the holding of the Board meetings. According to the section, **every company shall hold the first meeting of the Board of Directors within 30 days of the date of its Incorporation and with respect to the subsequent board meetings, every company shall hold minimum of 4 meetings every year provided that the gap between two consecutive board meetings shall not be more than 120 days.**

However, the Central Government vide its Notification G.S.R. 466(E) dated 5th June 2015, notified that **section 173(1) shall apply to the company formed under section 8 of the Companies Act, 2013 only to the extent that the Board of Directors, of such companies shall hold at least one meeting within every six calendar months.**

As per the given facts, Seafood Ltd. was incorporated on 1st April, 2015 and conducted four Board meetings during the financial year 2015-16 on 6th April, 2015, 28th August, 2015, 30th September 2015 and 30th March 2016.

Considering the above provisions in the given situations-

i) Company has contravened the above provisions of the Companies Act, 2013 in respect of the conduct of the subsequent board meetings. The gap between two consecutive board meetings i.e. the meeting held on 6th April, 2015 and 28th August, 2015 is 143 days which is more than 120 days and similarly the gap between the meeting held on 30th September 2015 and 30th March 2016 is 181 days which is again more than 120 days.

ii) In the case of company incorporated under section 8 of the Companies Act, 2013, since the board meetings have been conducted within 6 calendar months, so there is no contravention of the provision related to holding of board meetings.

Question 10

Moonlight Limited, held its Board meeting through video conferencing. Due to technical problems, the video recording which was done, could not be retrieved. The Company seeks your advice for the preparation and recording of the minutes of the Board meeting in the above situation, under the provisions of the Companies Act, 2013 and Rules made thereunder.

Answer

According to Sub- Rule 11 of Rule 3 of the Companies (Meetings of Board and its Powers) Rules, 2014, at the end of discussion on each agenda item, the **Chairperson of the meeting shall announce the summary of the decision taken on such item along with names of the directors, if any, who dissented from the decision taken by majority and the draft minutes so recorded shall be preserved by the company till the confirmation of the draft minutes in accordance with sub-rule (12).**

According to Sub- Rule 12 of Rule 3 of the Companies (Meetings of Board and its Powers) Rules, 2014,

i) The **draft minutes of the meeting shall be circulated among all the directors within 15 days of the meeting either in writing or in electronic mode as may be decided by the Board**.

ii) Every director who attended the meeting, whether personally or through video conferencing or other audio visual means, **shall confirm or give his comments in writing, about the accuracy of recording of the proceedings of that particular meeting in the draft minutes, within seven days or some reasonable time as decided by the Board, after receipt of the draft minutes failing which his approval shall be presumed.**

As per the facts of the question, due to technical problems, the video recordings of a Board meeting of Moonlight Limited, could not be retrieved.

However, the secretary of Moonlight Limited in consultation with the Chairman of the meeting can use the draft minutes that would have been recorded during the meeting to prepare the minutes. Further, when the same minutes will be circulated to the directors, they can give comments in

writing, about the accuracy of recording of the proceedings of that particular meeting in the minutes, within seven days or some reasonable time as decided by the Board, after receipt of the draft minutes. Moonlight Limited may, thus follow the above procedure.

Quorum for meetings of Board (Section 174)

Question 11

Examine with reference to the relevant provisions of the Companies Act, 2013, the validity/legality of the following:

A meeting of the Board of directors of OPQ Ltd. due to be held on 30.9.2014 did not take place for want of quorum. As a result, the Company did not hold any Board meeting for the quarter ended 30.9.2014 and there is a complaint that the Company has violated the provisions of the Act in this regard.

Answer

Section 173(1) of the Companies Act, 2013 requires a company to hold at least 4 board meetings in a year in such a manner that **not more than 120 days shall elapse between two board meetings.**

Moreover, under section 174 (4) in case a meeting is held but could not be continued due to want of quorum, the meeting gets adjourned to the same time and place next week and if such date is a national holiday to the next working day.

From the above therefore, there is no violation as the meeting was not held on 30th Sept 2014 and the meeting will automatically be adjourned to the same day at the same time and place in the next week or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place.

Moreover, **it is not necessary under the Companies Act, 2013 for a company to hold board meetings on quarterly basis as long as 4 meetings are held in a year.**

So considering the dates when other meetings were held, it may emerge that the company has not violated the provisions of the Companies Act, 2013.

Thus, the **allegation that the company has contravened the provisions of section 173(1) in the matter of holding the Board meeting is not correct**.

Question 12

A meeting of the Board of 'No Holiday Ltd' was held on a national holiday. However due to lack of quorum, the proceedings of the meeting could not be held and therefore the Chairman of the meeting decided with the consent of the majority that the Board meeting be adjourned to next Monday. However, the date fixed for the adjourned meeting happened to be a 'national holiday'. Advise and draw your analogy with reference to the provisions of the Companies Act, 2013, whether the adjourned meeting of the Board can be held on a day which is a national holiday.

Answer

The Companies Act 2013 vide **section 173(3)** merely states that a meeting of the Board shall be called by giving **not less than seven days' notice in writing to every director** at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means. It further provides for the board meeting to be held on shorter notice to transact urgent business subject to the condition that at least one independent director, if any, shall be

present at the meeting.

Therefore, as far as the holding of a board meeting is concerned, it may be held at any place on any day including a national holiday if agreed by the directors.

However, when a board meeting is adjourned due to lack of quorum, then under **section 174(4)** the adjourned meeting can be held on the same day at the same time and place in the next week or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place, unless the Articles provide otherwise.

Therefore, the **adjourned meeting cannot be held on a national holiday unless the Articles of the company provide that it can.** The meeting will have to be held on the next working day to the national holiday.

Question 13

PQR Limited held three board meetings till 31st October, 2014 during the financial year 2014. The next board meeting was due to be held on 27th December, 2014 but for want of quorum the meeting could not be held. A group of shareholders complained that the Company has violated the provisions of section 173 of the Companies Act, 2013 in not holding the required number of board meetings. State whether PQR limited has violated the provision given in section 173 of the Act.

Answer

In terms of **section 173(1)** of the Companies Act, 2013, a company must hold a minimum number of four meetings of its Board of directors in such a manner that **not more than 120 days** shall intervene between two consecutive meetings of the Board.

Further, the proviso to this sub-section **provides that the Central Government may by notification, direct that these provisions will not apply in relation to any class or description of companies or may apply subject to such exceptions, modifications or conditions as may be specified in the notification.**

Further, as per **section 174(4)** of the Act, if a meeting of the Board could not be held for want of quorum, then, unless the articles otherwise provide, the meeting shall automatically stand adjourned till the same day in the next week, at the same time and place, or if that day is a national holiday, till the next succeeding day which is not a national holiday, at the same time and place.

It may be noted that on adjournment of a meeting, **the meeting having started and not ended will not constitute a contravention of section 173(1)** under which a company is required to hold four board meetings in a year and **not more than 120 days shall elapse between two board meetings**. In case of adjournment of the meeting, it shall be deemed to have been held on the date on which it was started and not on the date when the adjourned meeting was held.

Therefore, the provisions of **section 173** shall not be deemed to have been contravened merely by reason of the fact that a meeting of the Board which had been called in compliance with the terms of that Section could not be held for want of a quorum.

As the **meeting could not be held for want of quorum, it cannot be said that PQR Ltd. has violated the provisions of section 173 of the Act**.

Question 14

What is the procedure to be followed, when a board meeting is adjourned for want of quorum?

Answer

Section 174(4) of the Companies Act, 2013 provides that, if a **Board meeting could not be held for**

want of quorum, then, unless the articles otherwise provide, the meeting shall automatically stand adjourned to the same day in the next week, at the same time and place, or if that day is a national holiday, till the next succeeding day which is not a national holiday, at the same time and place.

Question 15

Analyse and Advise with reference to the provisions of the Companies Act, 2013, the following situations.

a) There are 9 directors in a company and out of which 2 offices of the directors have fallen vacant. What will be the quorum for the Board Meeting?

b) There are 15 directors in a company and during discussion of a particular item, 13 of the directors are said to be 'interested' within the meaning of section 184(2) of the Companies Act, 2013. What shall be quorum of the meeting?

Answer

a) According to **section 174(1)** of the Companies Act, 2013, **quorum is one third of the total strength of Board** (any fraction contained in the said one third being rounded of as one) or two directors whichever is higher. **The total strength is to be derived after deducting the number of directors whose offices are vacant**. Therefore, where total number of directors is 9 and 2 offices of the directors have fallen vacant, we find: 1/3 of (9-2) = 1/3 of 7 = 21/3 directors which will be rounded off as 3. Being higher than 2, therefore 3 directors would constitute the quorum for the Board meetings.

b) Under **section 174(3)** of the Companies Act, 2013 **if at any time the number of the interested directors exceeds or is equal to two thirds of the total strength of the Board of Directors, the number of the directors who are non-interested but present at the meeting, not being less than two shall constitute the quorum.** Accordingly in the given problem, there are in all 15 directors and the Board meeting commences with all the 15 directors. During the meeting, an item comes up for discussion in respect of which 13 happen to be "interested" directors. In this case, in spite of the excess of the interested directors being more than two-thirds, the prescribed minimum number of non-interested directors constituting the quorum, namely, 2 are present at the meeting and can transact the particular item of business.

Passing of Resolution by Circulation (Section 175)

Question 16

How is a resolution by circulation passed by the Board or its Committee.

Answer

The Companies Act, 2013 permits a decision of the Board of Directors to be taken by means of a resolution by circulation. Board approvals can be taken in one of the two ways, one by a resolution passed at a Board Meeting and the other, by means of a resolution passed by circulation.

In terms of **section 175(1)** of the Companies Act, 2013 no resolution shall be deemed to have been duly passed by the Board or by a committee thereof by circulation, unless the following have been complied with:

a) The **resolution has been circulated in draft, together with the necessary papers**, if any,

b) The **draft resolution has been circulated to all the directors, or members of the committee**, as

the case may be;

c) The Draft resolution **has been sent at their addresses registered with the company in India;**

d) Such **delivery has been made by hand or by post or by courier, or through prescribed electronic means;**

The Companies (Meetings of Board and its Powers) Rules, 2014 provides that a resolution in draft form may be circulated to the directors together with the necessary papers for seeking their approval, by electronic means which may include E-mail or fax.

e) such **resolution has been approved by a majority of the directors or members, who are entitled to vote on the resolution**;

However, if **at least 1/3rd of the total number of directors of the company for the time being require that any resolution under circulation must be decided at a meeting**, the chairperson shall put the resolution to be decided at a meeting of the Board (instead of being decided by circulation).

A resolution that has been passed by circulation shall have to be necessarily be noted in the next meeting of board or the committee, as the case may be, and made part of the minutes of such meeting.

Question 17

Some urgent items are left over in the agenda of Board meeting which concluded and decision cannot be deferred till its next meeting. Advice the company about how the resolution shall be passed now.

Answer

Resolutions may be passed in respect of Board approvals in one of the two ways, **either at the board meetings or by circulation.** The items which could not be concluded and decided at the board meeting, if cannot be deferred till the next meeting may be passed by circulation, provided they do not include such items as are required to be passed only at the meeting of the directors under section 179(3) of the Companies Act, 2013.

In order to pass any resolution of the Board by circulation the following steps must be taken and completed as laid down in **section 175(1):**

a) The **draft of the proposed resolution must be circulated along with all relevant and necessary papers**;

b) The **above documents must be delivered to all the directors**, members or the committee, as the case may be, at their addresses registered with the company in India;

c) The **documents must be delivered by hand delivery or by post or by courier, or through such electronic means as may be prescribed;**

d) The **resolution must be approved by a majority of the directors or members**, who are entitled to vote on the resolution.

e) There **must not be any objection from not less than one-third of the total number of directors of the company** for the time being, requiring that such resolution under circulation must be decided at a meeting.

Further, the resolution so passed shall be noted at a subsequent meeting of the Board or the committee thereof, and be made part of minutes of such meeting.

Defects in appointment of directors not to invalidate action taken (Section 176)

Question 18

Mr. MTP was appointed as a director at the Annual General Meeting of a limited company held on 30th September, 2013 and he carried on his duties and functions as a director. In the month of August, 2014, it was found out that there were certain irregularities in his appointment and on 31st August, 2014, his appointment was declared invalid. But Mr. MTP continued to act as director even after 31st August, 2014. You are required to state, with reference to the provisions of the Companies Act, 2013, whether the acts done by Mr. MTP are valid and binding upon the company ?

Answer

In accordance with **section 176** of the Companies Act, 2013 acts done by a person as a director shall be deemed to be valid, notwithstanding that it may afterwards be discovered that his **appointment was invalid by reason of any defect or disqualification or had terminated by virtue of any provision contained in this Act or in the articles of the company**.

The Proviso to section 176 further provide that nothing in this section shall be deemed to give validity to acts done by a director after his appointment has been noticed by the company to be invalid or to have terminated.

In view of the above provisions of **section 176** of the Companies Act, 2013, the acts done by Mr. MTP upto the date of the irregularity in his appointment coming to the notice of the company will be deemed as valid and binding on the Company.

Any act done by him after the date on which the irregularity or defect in his appointment was noticed by the company will be deemed invalid. The acts done by Mr. MTP after 31st August, 2014 shall be deemed to be invalid and not binding upon the Company.

Audit Committee (Section 177)

Question 19

An Audit Committee of a Public Limited Company constituted under section 177 of the Companies Act, 2013 submitted its report of its recommendation to the Board. The Board, however, did not accept the recommendations. In the light of the situation, analyze whether:

a) The Board is empowered not to accept the recommendations of the Audit Committee.
b) If so, what alternative course of action, would be Board resort to?

Answer

a) As per **Section 177(2) and (3)** of the Companies Act, 2013 an audit committee must be formed within a year of the commencement of the Act or within a year of the incorporation of a company as the case may be, and will consist of at least 3 directors out of which the independent directors shall constitute the majority.

   Under section 177(8) the Board's Report which is laid before a general meeting of the company under section 134 (3) where the financial statements of the company are placed before the members, must disclose the composition of the audit committee and also where the Board has not accepted any recommendations of the audit Committee the same shall be disclosed along

with the reasons therefor. Therefore, the **Board is empowered not to accept the recommendations of the Audit Committee but only under genuine circumstances and with legitimate reasons.**

b) If the **Board does not accept the recommendations of the Audit Committee, it shall disclose the same in its report under section 134 (3)** placed before a general meeting of the company.

Question 20

MNC Ltd., a company, whose paid up capital was Rs. 4.00 Crores, has issued rights shares in the ratio of 1:1. The said company is listed with Mumbai Stock Exchange. Whether the company is required to appoint any Audit Committee and if yes, draft a suitable Board Resolution to appoint an Audit committee covering the aspects as provided in the Companies Act, 2013.

Answer

Under **section 177(1)** of the Companies Act, 2013 the Board of Directors of every listed company and such other class or classes of companies, as may be prescribed, shall constitute an Audit Committee. Therefore, MNC Ltd being a listed company will be bound to constitute an audit committee under the Act.

Further under section 177(2) the **Audit Committee shall consist of a minimum of three directors with independent directors forming a majority**.

Further, the majority of members of Audit Committee including its Chairperson shall be persons with ability to read and understand the financial statement.

The draft Board Resolution for the constitution of an Audit Committee may be as follows:

"Resolved that pursuant to the provision contained in section 177 of the Companies Act 2013 and the applicable clause of Listing Agreement with the Mumbai Stock Exchange, an Audit Committee of the Company be and is hereby constituted with effect from the conclusion of this meeting, with members as under:

1. Mr. A - An Independent Director.
2. Mr. B - An Independent Director
3. Mr. C - An Independent Director
4. Mr. D - An Independent Director
5. Mr. FE - Financial Executive
6. Mr. MD - Managing Director

Further resolved that the Chairman of the Committee, who shall be an Independent Director, be elected by the committee members from amongst themselves.

Further resolved that the quorum for a meeting of the Audit Committee shall be the chairman of the Audit Committee and 2 other members (other than the Managing Director),.

Further resolved that the terms of reference of the Audit Committee shall be in accordance with the provisions of section 177(4) of the Companies Act, 2013.

Further resolved that the Audit committee shall conduct discussions with the auditors periodically about internal control system, the scope of audit including the observations of the auditors.

Further resolved that the Audit Committee shall review the quarterly and annual financial statements and submit the same to the Board with its recommendations, if any.

Further resolved that the recommendations made by the Audit Committee on any matter relating to financial management including the audit report shall be binding on the Board. However, where

such recommendations are not accepted by the Board, the reasons for the same shall be recorded in the minutes of the Board meeting and communicated to the shareholders.

Further resolved that the Company Secretary of the Company shall be the Secretary to the Audit Committee.

Further resolved that the Chairman of the Audit Committee shall attend the annual general meeting of the Company to provide any clarifications on matters relating to audit as may be required by the members of the company.

Further resolved that the Board's Report/Annual Report to the members of the Company shall include the particulars of the constitution of the Audit Committee and the details of the non-acceptance of any recommendations of the Audit Committee with reasons therefor."

Question 21

Explain how the provisions of the Companies Act, 2013 relating to Audit Committee will help in achieving some of the objectives of Corporate Governance.

Answer

Companies, particularly public listed companies raise huge amounts of monies from the members of the public and public financial institutions. They owe it to all the vast number of persons and institutions who have reposed their faith in them and have invested in them, that their faith is rewarded both in terms of annual return and in terms of wealth appreciation in real terms. In order to achieve this it is vital to have the highest quality of corporate governance in the conduct of affairs of such companies. Thus, the role of audit committees have been enhanced, their responsibilities made more objective and the accountability has increased substantially.

In this context the provisions of the Companies Act, 2013 have been framed to improve corporate governance standards and protect the interests of the public and the financial institutions who have invested in companies. These provisions may be highlighted as under:

1. The constitution of Audit Committees under section 177(2) requires the **majority representation from independent directors**. In other words, persons from within the management cannot form a majority in the Committee, thereby making the functioning of these committees more transparent;
2. The proviso to **section 177(2)** further requires the majority of members and the chairperson of the **Audit Committees to be persons who can understand financial statements.** This enables a meaningful exercise of the committee's functions by knowledgeable persons thereby increasing the effectiveness of such committees.
3. Now the terms of reference or the minimum scope of work of an Audit Committee has been laid down in the act itself under section 177(4). **By doing this the vagueness and doubt in the role and functions of such committees has been removed**.
4. The **Audit Committee shall have authority to investigate into any matter in relation to the areas of its scope of functioning or referred to it by the Board** and for this shall have power to obtain professional advice from external sources and have full access to information contained in the records of the company. This provides the Audit Committee to function with a high degree of effectiveness by accessing external professional advice and the records of the company.
5. The **recommendations of the Audit Committee are binding on the Board** to take appropriate corrective actions. In case the **Board of Director refuses to accept the recommendations of the**

Audit Committee, it **bound to disclose the same with the reasons** for non acceptance, in its report to the members of the company under section 134 (3) which relates to the Directors Report on Financial Statements to the members of the company.

It will be seen from the above provisions of the Companies Act, 2013 that efforts have been made to make such committees more impartial, effective and accountable which will enable the company to improve the quality of its corporate governance thereby improving accountability and avoiding financial impropriety.

Question 22

i) R Ltd. wants to constitute an Audit Committee. Draft a board resolution covering the following matters [compliance with Companies Act, 2013 to be ensured].
   1) Member of the Audit Committee
   2) Chairman of the Audit Committee
   3) Any 2 functions of the said Committee

ii) What would be the minimum likely turnover or capital of this company?

iii) What is the role of the Audit Committee vis a vis the statutory auditor when the company wishes to engage them to perform certain engagements not restricted under Section 144?

Answer

i) **Audit Committee – Board's Resolution**:

"Resolved that pursuant to **Section 177** of the Companies Act, 2013 an Audit Committee consisting of the following Directors be and is hereby constituted.

1. Mr. ---- Independent Director
2. Mr. ---- Independent Director
3. Mr. ---- Independent Director
4. Mr. ---- Independent Director
5. Mr. ---- Managing Director.
6. Mr. ---- Chief Financial Officer"

"Further resolved that the Chairman of the Audit Committee shall be elected by its members from amongst themselves and shall be an independent director'.

"Further resolved that the quorum for a meeting of the Audit committee shall be three directors (other than the Managing Director), out of which at least two must be independent directors".

"Resolved further that the Audit Committee shall perform all the functions as laid down in section 177(4) of the Companies Act, 2013 including but not limited to:

a. make the recommendation for appointment, remuneration and terms of appointment of the auditors of the company;

b. review and monitor the independence and performance of auditors of the company and the effectiveness of the audit process".

Further resolved that the Audit Committee shall review the quarterly and annual financial statements and submit the same to the Board with its recommendations if any".

ii) Rule 6 of the Companies (Meetings of Board and its Powers) Rules, 2014 have prescribed that the following classes of companies shall constitute Audit Committee:

a) all **public companies with a paid up capital of 10 crore rupees** or more;

b) all **public companies having turnover of 100 crore rupees** or more;

c) all **public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding 50 crore rupees** or more.

Hence, in the present question, the likely turnover shall be Rs. 100 crore or more or capital shall be Rs. 10 crore or more.

iii) According to **section 177(5),** the Audit Committee is empowered to:

1) **Call for the comments of the auditors about:**
   a) **internal control systems,**
   b) **the scope of audit, including the observations of the auditors,**
   c) **review of financial statement before their submission to the Board**,
2) **Discuss any related issues with the internal and statutory auditors and the management** of the company.

Question 23 ***(Nov 16)***

Referring to the provisions of the Companies Act, 2013, examine the following: XYZ Limited, a listed company has constituted an audit committee consisting of five members out of whom two are independent directors. Subsequently, the company increased the composition of audit committee to six members with three independent directors.

Answer

Composition of Audit Committee: As per **Section 177(2)** of the Companies Act, 2013, the audit committee **shall consist of a minimum of three directors with independent directors forming a majority.** In the given instance, XYZ Ltd. a listed company constituted an Audit committee consisting of 5 members out of which 2 are independent directors. Subsequently company increased the composition of audit committee to 6 members with three Independent directors. Thus, according to the above provision the compliance with respect to the composition of audit committee with an independent directors forming a majority is not valid.

Question 24

M/s Dreamworks Limited (an unlisted company) without any public deposits as per the audited financial statements of the company as at March, 31st 2018 gives you the following information:

Paid up Share Capital	₹ 20 crores
Gross Turnover	₹ 500 crores
Bank Borrowings	₹ 40 crores (from a National Bank)
Other Borrowings	₹40 crores (from a Public Financial Institution)

Mr. Gupta, a Chartered Accountant employed in the finance and audit department of the company wants to form a Vigil Mechanism for directors and employees of the company.

1) Advise whether it is mandatory for M/s Dreamworks Limited to formulate a Vigil Mechanism under the provisions of the Companies Act, 2013 and rules framed there under.
2) Are there any penalties that could be imposed on the company for not formulating the Vigil Mechanism?

Answer

Formation of vigil mechanism: According to **Section 177(9)** of the Companies Act, 2013, a Vigil mechanism shall be formed in:

a) **Every listed company, and**

b) **Such other prescribed classes of companies.**

Rule 7 of the Companies (Meetings of Board and its Powers) Rules, 2014 has prescribed the following class or classes of companies that shall constitute Vigil mechanism:

1) the Companies which accept deposits from the public;
2) the Companies which have borrowed money from banks and public financial institutions in excess of 50 crore rupees.

In the instant case, Dreamworks Limited does not have any public deposits. They have borrowings from banks and public financial institutions of ₹ 80 crores which is in excess of ₹ 50 crores. Since, the Company had borrowed from banks and Public Financial Institutions in excess of ₹ 50 crores as prescribed in Rule 7(2), the company is mandatorily required to form a Vigil Mechanism for directors and employees of the company.

Penalty: According to Section 178(8), in case of contravention of provisions of Section 177, the company shall be punishable with fine which shall not be less than 1 lakh rupees but which may extend to 5 lakh rupees, and, every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 1 year or with fine which shall not be less than 25,000 rupees but which may extend to 1 lakh rupees, or with both

Nomination & Remuneration Committee & Stakeholders Relationship Committee (Section 178)

Question 25 ***(May 2015)***

Referring to the provisions of the Companies Act, 2013, answer the following:

A) Which companies are required to constitute a 'Nomination & Remuneration Committee'?

B) What is the composition of the above committee?

Answer

A) **Formation of Nomination and Remuneration Committee:** As per the provisions of **Section 178** of the Companies Act, 2013, a Nomination and Remuneration Committee shall be constituted by the Board of Directors of:

   a) Every **listed public company** and

   b) Such other class or classes of companies as may be provided.

   The Companies (Meetings of Board and its powers) Rules, 2014, has prescribed the following classes of companies that shall constitute Nomination and Remuneration Committee of the Board:

   1) All **public companies** with a **paid up capital of 10 crore rupees** or more;
   2) All **public companies** having a **turnover of one hundred crore rupees** or more;
   3) All **public companies**, having in aggregate, **outstanding loans or borrowings or debentures or deposits exceeding fifty crore rupees or more**.

Explanation – The paid up share capital or turnover or outstanding loans, or borrowings or debentures or deposits, as the case may be, as existing on the date of last audited Financial Statements shall be taken into account for the purposes of this rule.

Provided further that public companies covered under this rule shall constitute their Nomination

and Remuneration Committee within one year from the commencement of these rules or appointment of independent directors by them, whichever is earlier.

B) Composition of Nomination and Remuneration Committee:

a) This committee shall consist of **3 or more non-executive directors out of which not less than one-half shall be independent directors.**

b) The **Chairman** (whether executive or non-executive) of the company shall not chair such a committee. However, he may be appointed as a member to the committee.

c) The **chairperson or in his absence, any other member of the committee authorized by him in this behalf shall attend the general meetings of the company**.

Power of Board (Section 179)

Question 26 ***(RTP Nov 18)***

M/s. Multiplex Builders Limited is contemplating to enter into a joint venture agreement with another construction company for the development of landed properties located at Delhi. Since it is not possible to convene the Board Meeting immediately, as the directors are at different place in connection with various works, the Managing Director seeks your advice on the following matters:

(a) Whether the resolution pertaining to the joint venture agreement is required to be passed at the Board Meeting convened for this purpose or whether it can be passed by means of a circular resolution?

(b) What are the resolutions that are required to be passed only at the meetings of the Board of Directors?

(c) The steps that are required to be taken to pass the Board resolution by circulation.

Advise the Managing Director in the light of the provisions of the Companies Act, 2013.

Answer

The **directors of the company act together as a body and generally at the meeting of the Board duly convened, unless special powers are delegated to an individual director or the managing director**. Where it is not possible to hold board meetings because the directors are busy elsewhere or the time for convening such a meeting is short, it is possible that the required resolution can be passed by way of circular resolution as provided in section 175 of the Companies Act 2013.

However, under **section 179** of the Companies Act 2013, certain powers can be exercised by the Board of directors by means of a resolution passed at meeting convened for this purpose.

They are:

(i) **to make calls on shareholders in respect of money unpaid on their shares**

(ii) to authorize **buy back of securities** under section 68

(iii) to **issue securities, including debentures, whether in or outside India**

(iv) to **borrow monies**

(v) to **invest the funds** of the company and

(vi) to **grant loans or give guarantee or provide security** in respect of loans

(vii) to **approve financial statements and the Board's report**

(viii) to **diversify the business of the company**

(ix) to **approve amalgamation, merger or reconstruction**

(x) to **take over a company or acquire a controlling or substantial stake in another company**.

(xi) Any other matter as prescribed in Rule 8 of the Companies (Meetings of the Board and its Powers) Rules, 2014.

In view of the above, the **Managing Director can go ahead and complete the joint venture agreement after obtaining the approval of the board by passing a circular resolution.**

For this purpose, the proposed resolution has to be circulated in draft along with the other necessary papers, if any, to all the directors in India at their usual residential addresses.

The resolution will become valid if the same is approved by majority of the directors and who are entitled to vote on the resolution. There after the resolution as passed by way of circulation will be entered in the minutes book of the Board of Directors and is enough compliance of the provisions of Companies Act, 2013 in this regard.

Question 27

Out of the powers exercisable by the Board under section 179, the board wants to delegate to the Managing Director of the company the power to borrow monies otherwise than on debentures. Advise whether such a delegation is possible? Would your answer be different, if the delegation is given to the manager or any other principal officer including a branch officer of the company?

Answer

Under **section 179(3)** of the Companies Act, 2013 the Board of Directors of a company shall exercise the following powers on behalf of the company by means of resolutions passed at meetings of the Board:

a) To **make calls** on shareholders in respect of money unpaid on their shares;
b) To authorise **buy-back of securities** under section 68;
c) To **issue securities**, including debentures, whether in or outside India;
d) To **borrow monies**
e) To **invest the funds** of the company
f) To **grant loans** or give guarantee or provide security in respect of loans;
g) To **approve financial statement** and the Board's report;
h) To **diversify the business of the company**;
i) To approve **amalgamation, merger or reconstruction**;
j) To **take over a company** or acquire a controlling or substantial stake in another company;
k) Any **other matter** which may be prescribed:

Provided that the Board may, by a resolution passed at a meeting, delegate to any committee of directors, the managing director, the manager or any other principal officer of the company or in the case of a branch office of the company, the principal officer of the branch office, the powers specified in clauses (d) to (f) on such conditions as it may specify.

Matters referred to in clauses (d), (e), and (f) above, may be decided by the board by circulation instead of at a meeting in respect to the companies covered under section 8 of the Companies Act, 2013 vide Notification dated 5thJune 2015.

From the above provisions it is clear that the power to **borrow monies under (d) above, may be delegated to the Managing Director** or to the manager or any other principal officer of the company.

Question 28 ***(May 2010)***

Advise the Board of Director of Spectra Papers Ltd. regarding validity and extent of their powers, under the provisions of the Companies Act, 2013 in relation to the following matters:

i) Buy-back of the shares of the Company, for the first time, upto 10% of the paid up equity share capital without passing a special resolution.

ii) Delegation of Power to the Managing Director of the company to invest surplus funds of the company in the shares of some companies.

Answer

i) According to clause (b) of **section 179(3),** The Board of Directors of a company shall exercise the power to authorise buy-back of securities under section 68, on behalf of the company by means of resolutions passed at meetings of the Board.

According to section 68(2), No company shall purchase its own shares or other specified securities, unless—

a) the **buy-back is authorised by its articles**;

b) a **special resolution has been passed at a general meeting of the company authorising the buy-back**:

However, nothing contained in this clause shall apply to a case where—

1) the buy-back is, **10% or less of the total paid-up equity capital and free reserves of the company**; and

2) such **buy-back has been authorised by the Board by means of a resolution passed at its meeting,**

Thus, we can say that in the case of buy-back of shares of the Company, for the first time, upto 10% of the paid up share capital, a special resolution will not be required if such buy-back has been authorised by the Board by means of a resolution passed at its meeting.

ii) According to clause (e) of section 179(3), the **Board of Directors of a company shall exercise the power to invest the funds of the company, on behalf of the company by means of resolutions passed at meetings of the Board**.

The board may under the proviso to section 179(3) of the Companies Act, 2013 delegate the power to invest the funds of the company by a Board Resolution passed at a duly convened Board Meeting. However, the investment in shares of other companies will be governed by the applicable provisions of the Companies Act, 2013 (i.e. section 186 of the Companies Act, 2013). Since the investment of funds is governed by section of the Companies Act, 2013, thus, specific provisions of section 186 will be applicable for such investment.

According to **section 186(5),** No investment shall be made or loan or guarantee or security given by the company unless the resolution sanctioning it is passed at a meeting of the Board with the consent of all the directors present at the meeting and the **prior approval of the public financial institution** concerned where any term loan is subsisting, is obtained. Thus, a **unanimous resolution of the Board is required**.

Section 186 does not provide for delegation. Hence, the proposed delegation of power to the Managing Director to invest surplus funds of the company in the shares of some other companies is not in order.

Restrictions on Powers of Board (Section 180)

Question 29 ***(May 2015)***

One of the Objects Clauses of the Memorandum of Association of Info Company Limited conferred upon the company power to sell its undertaking to another company with identical objects. Company's Articles also conferred upon the directors whereby power was conferred upon them to sell or otherwise deal with the property of the company. At an Extraordinary General Meeting of the company, members passed an ordinary resolution for the sale of its assets on certain terms and authorized the directors to carry out the sale. Directors refused to comply with the wishes of the members where upon it was contended on behalf of the members that they were the principals and directors being their agents, were bound to give effect to their (members') decisions.

Examining the provisions of the Companies Act, 2013, answer the following:

a) Whether the contention of members against the non-compliance of members' decision by the directors is tenable?

b) Whether it is possible for the members usurp the powers which by the Articles are vested in the directors by passing a resolution in the general meeting?

Answer

Powers of Board: In accordance with the provisions of the Companies Act, 2013, as contained under **Section 179(1),** the Board of Directors of a company shall be entitled to exercise all such powers and to do all such acts and things, as the company is authorized to exercise and do:

Provided that in exercising such power or doing such act or thing, the Board shall be subject to the provisions contained in that behalf in this Act, or in the memorandum or articles, or in any regulations not inconsistent therewith and duly made there under including regulations made by the company in general meeting.

Provided further that the **Board shall not exercise any power or do any act or thing which is directed or required, whether under this Act or by the members or articles of the company or otherwise to be exercised or done by the company in general meeting**.

Section 180 (1) of the Companies Act, 2013, provides that the powers of the Board of Directors of a company which can be exercised only with the consent of the company by a special resolution. Clause (a) of Section 180 (1) defines one such power as the power to sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company or where the company owns more than one undertaking of the whole or substantially the whole or any of such undertakings.

Therefore, **the sale of the undertaking of a company can be made by the Board of Directors only with the consent of members of the company accorded vide a special resolution**.

Even if the power is given to the Board by the memorandum and articles of the company, **the sale of the undertaking must be approved by the shareholders in general meeting by passing a special resolution.**

Therefore, the correct procedure to be followed is for the Board to approve the sale of the undertaking clearly specifying the terms of such sale and then convene a general meeting of members to have the proposal approved by a special resolution.

In the given case, the procedure followed is completely incorrect and violative of the provisions of the Act. The shareholders cannot on their own make out a proposal of sale and pass an ordinary resolution to implement it through the directors.

The **contention of the shareholders is incorrect in the first place as it is not within their authority to approve a proposal independently of the Board of Directors**. It is for the Board to approve a proposal of sale of the undertaking and then get the members to approve it by a special resolution. **Accordingly the contention of the members that they were the principals and directors being their agents were bound to give effect to the decisions of the members is not correct.**

Further, in exercising their powers the directors do not act as agent for the majority of members or even all the members. The members therefore, cannot by resolution passed by a majority or even unanimously supersede the powers of directors or instruct them how they shall exercise their powers. **The shareholders have, however, the power to alter the Articles of Association of the company in the manner they like subject to the provisions of the Companies Act, 2013.**

Question 30

The Board of Directors of Stepping Stones Publications Ltd. at a meeting held on 15.1.2014 resolved to borrow a sum of Rs. 15 crores from a nationalized bank. Subsequently the said amount was received by the company. One of the Directors, who opposed the said borrowing as not in the interest of the company has raised an issue that the said borrowing is outside the powers of the Board of Directors. The Company seeks your advice and the following data is given for your information:

i) Share Capital Rs. 5 crores
ii) Reserves and Surplus Rs. 5 crores
iii) Secured Loans Rs. 15 crores
iv) Unsecured Loans Rs. 5 crores

Advice the management of the company.

Answer

According to the provisions of **Section 180(1)(c)** of the Companies Act, 2013, there are restrictions on the borrowing powers to be exercised by the Board of directors. According to the said section, the **borrowings should not exceed the aggregate of the paid up capital and free reserves**. While calculating the limit, the temporary loans obtained by the company from its bankers in the ordinary course of business will be excluded. However, from the figures available in the present case the proposed borrowing of Rs. 15 crores will exceed the limit mentioned. Thus, the borrowing will be beyond the powers of the Board of directors.

Thus, the management of Stepping Stone Publications Ltd., should take steps to convene the general meeting and pass a special resolution by the members in the meeting as stated in Section 180(1)(c) of the Companies Act, 2013. Then the borrowing will be valid and binding on the company and its members.

Question 31

The last three years' Balance Sheet of PTL Ltd., contains the following information and figures:

	As at 31.03.2012	As at 31.03.2013	As at 31.03.2014
Paid up capital	50,00,000	50,00,000	75,00,000
General Reserve	40,00,000	42,50,000	50,00,000
Credit Balance in P&L A/c	5,00,000	7,50,000	10,00,000
Debenture Redemption Reserve	15,00,000	20,00,000	25,00,000
Secured Loans	10,00,000	15,00,000	30,00,000

Net Profit for the year (as calculated in accordance with the provisions of the Companies Act, 2013)	12,50,000	19,00,000	34,50,000

On going through other records of the Company, the following is also determined:

In the ensuing Board Meeting scheduled to be held on 5th November, 2014, among other items of agenda, following items are also appearing:

i) To decide about borrowing from financial institutions on long-term basis.

ii) To decide about contributions to be made to Charitable funds.

Based on above information, you are required to find out as per the provisions of the Companies Act, 2013, the amount upto which the Board can borrow from Financial institution and the amount upto which the Board of Directors can contribute to Charitable funds during the financial year 2014-15 without seeking the approval in general meeting.

Answer

i) **Borrowing from Financial Institutions:** As per **Section 180(1)(c)** of the Companies Act, 2013, the Board of Directors of a company, without obtaining the approval of shareholders in a general meeting, can borrow **money including moneys already borrowed upto an amount which does not exceed the aggregate of paid up capital** of the company and its free reserves. Such **borrowing shall not include temporary loans obtained from the company's bankers in ordinary course of business.** Here, free reserves do not include the reserves set apart for specific purpose.

Since the decision to borrow is to be taken in a meeting to be held on 5th November, 2014, the figures relevant for this purpose are the figures as per the Balance Sheet as at 31.03.2014. According to the above provisions, the Board of Directors of PTL Ltd. Can borrow, without obtaining approval of the shareholders in a general meeting, upto an amount calculated as follows:

	`
Paid up Capital	7,500,000
General Reserve (being free reserve)	5,000,000
Credit Balance in Profit & Loss Account (to be treated as free reserve)	1,000,000
Debenture Redemption Reserve (This reserve is not to be considered since it is kept apart for specific purpose of debenture redemption)	----
Aggregate of paid up capital and free reserve	13,500,000
Total borrowing power of the Board of Directors of the company, i.e,	
100% of the aggregate of paid up capital and free reserves	13,500,000
Less: Amount already borrowed as secured loans	3,000,000
Amount upto which the Board of Directors can further borrow without the approval of shareholders in a general meeting.	10,500,000

ii) **Contribution to Charitable Funds:** As per **Section 181** of the Companies Act, 2013, the Board of Directors of a company without obtaining the approval of shareholders in a general meeting,

can make contributions to genuine charitable and other funds upto an amount which, in a financial year, **does not exceed five per cent of its average net profits during the three financial years immediately preceding, the financial year**.

According to the above provisions, the Board of Directors of the PTL Ltd. can make contributions to charitable funds, without obtaining approval of the shareholders in a general meeting, upto an amount calculated as follows:

Net Profit for the year (as calculated in accordance with the provisions of the Companies Act, 2013):

	Amount
For the financial year ended 31.3.2012	12,50,000
For the financial year ended 31.3.2013	19,00,000
For the financial year ended 31.3.2014	34,50,000
TOTAL	66,00,000
Average of net profits during three preceding financial years	22,00,000
Five per cent thereof	1,10,000

Hence, the maximum amount that can be donated by the Board of Directors to a genuine charitable fund by PTL Ltd during the financial year 2014 -15 will be Rs. 1,10,000 without seeking the approval of the shareholders in a general meeting.

Question 32 ***(Nov 2014)***

Following is data relating to Prince Company Limited:

Authorised Capital (Equity Shares)	Rs. 100 crores
Paid – up Share Capital	Rs. 40 crores
General Reserves	Rs. 20 crores
Debenture Redemption Reserve	Rs. 10 crores
Provision for Taxation	Rs. 5 crores
Loan (Long Term)	Rs. 10 crores
Short Term Creditors	Rs. 3 crores

Board of Directors of the company by a resolution passed at its meeting decided to borrow an additional sum of Rs. 90 crores from the company's Bankers. You being the company's financial advisor, advise the Board of Directors the procedure to be followed as required under the Companies Act, 2013.

Answer

Borrowing by the Company (**Section 180** of the Companies Act, 2013) As per Section 180(1)(c) of the Companies Act, 2013, the Board of Directors of a company, **without obtaining the approval of shareholders in a general meeting through a special resolution, can borrow the funds including funds already borrowed upto an amount which does not exceed the aggregate of paid up capital of the company and its free reserves.** Such borrowing shall not include temporary loans obtained from the company's bankers in ordinary course of business.

Free reserves do not include the reserves set apart for specific purpose.

According to the above provisions, the Board of Directors of Prince Company Limited can borrow, without obtaining approval of the shareholders in a general meeting, upto an amount calculated as follows:

Particulars	Amount
Paid up Share Capital	40 Crore
General Reserve (being free reserve)	20 Crore
Debenture Redemption Reserve (This reserve is not to be considered since it is kept apart for specific purpose of debenture redemption)	----
Aggregate of paid up capital and free reserve.	60 Crore
Total borrowing power of the Board of Directors of the company, i.e, 100% of the aggregate of paid up capital and free reserves	60 Crore
Less: Amount already borrowed as Long term loan Amount upto which the Board of Directors can further borrow without the approval of shareholders in a general meeting.	10 Crore 50 Crore

In the present case, the directors of Prince Company Limited by a resolution passed at its meeting decide to borrow an additional sum of Rs. 90 Crore from the company bankers. Thus, the borrowing will be beyond the powers of the Board of directors.

Thus**, the management of Prince Company Limited., should take steps to convene the general meeting and pass a special resolution by the members in the meeting as stated in Section 180(1)(c) of the Companies Act, 2013. Then, the borrowing will be valid and binding on the company and its members.**

[Note: In case of private companies section 180 shall not apply vide Notification no. G.S.R. 464(E), dated 5th June 2015]

Question 33 ***(May 18)***

Queen Construction Company Ltd. acquired 60 % of the equity paid up share capital of ABC Ltd. Queen Construction Ltd. has planned to expand its operation for which additional fund is required. The Board of Directors decided to avail additional exposure of ₹ 10 crore from the Bank.

The following data is furnished as on 30th June, 2017.

	₹ In crores
Authorised Equity Share Capital	25
Issued and Subscribed Equity Share Capital	22
Paid up Equity Share Capital	20
Capital Reserve	2
Revaluation Reserve	1
General Reserve	3
Open cash credit Limit (for working Capital requirement) with the Bank repayable in 3 months	5
Loan obtained under the Hire Purchase agreement for acquiring vehicles.	1
Long term Borrowing from Banks and other parties	15

ABC Ltd. approached Queen Construction Ltd. to grant a loan of ₹ 25 Lakhs and stand as guarantor for repayment of loan ₹ 10 Lakhs to be sanctioned by a Bank.

The two loans (25 Lakhs plus 10 Lakhs) will be utilized by ABC Ltd. for its principal business activities.

You being the Financial Advisor of the company, advise the Board of Directors about the procedure to be followed to avail additional exposure of ₹ 10 Crore from the Bank. Also evaluate whether the loan guarantee given by Queen Construction Ltd. to ABC Ltd. is valid according to Section 185 of the Companies Act, 2013.

Answer

Borrowing by the Company (Section 180 of the Companies Act, 2013)

As per Section 180(1)(c) of the Companies Act, 2013, the **Board of Directors of a Company, without obtaining the approval of shareholders in a general meeting through a special resolution, can borrow the funds including funds already borrowed upto an amount which does not exceed the aggregate of paid up capital of the company and its free reserves**. Such borrowing shall not include temporary loans obtained from the company's bankers in the ordinary course of business.

According to the above provisions, the Board of Directors of Queen Construction Ltd. can borrow, without obtaining approval of the shareholders in a general meeting, upto an amount calculated as follows:

Particulars	₹ In Crores
Paid up Equity Share Capital **(A)**	20
General Reserve (being free reserve) **(B)**	3
Capital Reserve (Not a free reserve)	-
Revaluation Reserve (Not a free reserve)	-
Aggregate of paid up capital and free reserve **(A)+(B)**	23
Total borrowing power of the Board of Directors of the company, i.e ., 10 the aggregate of paid up capital and free reserves **(C)**	23
Less: Amount already borrowed as Long term loan **(D)**	16
Amount upto which the Board of Directors can further borrow without t approval of shareholders in a general meeting. (C) – (D)	7

In the present case, the Directors of Queen Construction Limited by a resolution passed at its meeting decide to borrow an additional sum of ₹ 10 Crores from the bank. Hence, the borrowing will be beyond the powers of the Board of directors.

Thus, the Management of Queen Construction Limited., should take steps to convene the general meeting and pass a special resolution by the members in the meeting as stated in Section 180(1)(c) of the Companies Act, 2013. Then, the borrowing will be valid and binding on the company and its members.

According to Section 185 of the Companies Act, 2013, no Company shall, directly or indirectly, advance any loan, including any loan represented by a book debt, to any of its directors or to any other person in whom the director is interested or give any guarantee or provide any security in connection with any loan taken by him or such other person.

However, the above sub-section shall not apply to any guarantee given or security provided by a holding company in respect of loan made by any bank or financial institution to its subsidiary Company. [Section 185(1)(c)]. It is also provided that the loans made under this clause are utilized by the subsidiary company for its principal business activities.

In the instant case, Queen Construction Ltd. acquired 60% of the equity paid up share capital of ABC Ltd. Hence, ABC Ltd. is a subsidiary company of Queen Construction Ltd. [as per Section 2(87)]

Hence, as per Section 185(1)(c), granting of loan of ₹ 25 Lakhs by Queen Construction Ltd to ABC

Ltd is not valid but providing of guarantee for repayment of loan of ₹ 10 lakhs to be sanctioned by bank is valid.

Question 34 ***(May 2019)***

The following information is provided in respect of M/s Fortune Limited under three different case scenarios on the borrowing powers of the Board of Directors of the company. Mr. Murli, the CFO seeks your advice with explanations as to the nature of resolution which needs to be passed under each of the case scenarios as per the provisions of section 180(1)(c) of the Companies Act, 2013. Detailed workings should form part of your answer.

Particulars	Case I (₹ in Crores)	Case II (₹ in Crores)	Case III (₹ in Crores)
Equity Share Capital (Paid- up)	150	150	150
Preference Share Capital (Paid-up)	50	50	50
Securities Premium Account	50	50	50
Free Reserves	20	20	20
Total:	270	270	270
Working Capital Loan (repayable on demand-Existing) from Sigma Capital Limited	50	50	50
Cash Credit Limit from a scheduled bank (repayable on demand-Existing)	120	120	120
6 months loan for purchase of Plant & Machinery from scheduled bank (proposed)	30	40	130
24 months loan for purchase of Plant & Machinery from scheduled bank (proposed)	10	20	150
Total	210	230	450

Answer

According to section 180(1)(c) of the Companies Act, 2013, the Board of Directors of a company shall exercise the following powers only with the consent of the company by a special resolution, namely:—(c) to borrow money, where the money to be borrowed, together with the money already borrowed by the company will exceed aggregate of its paid-up share capital, free reserves and securities premium, apart from temporary loans obtained from the company's bankers in the ordinary course of business:

Explanation—For the purposes of this clause, the expression "temporary loans" means loans repayable on demand or within six months from the date of the loan such as short- term, cash credit arrangements, the discounting of bills and the issue of other short-term loans of a seasonal character, but does not include loans raised for the purpose of financial expenditure of a capital nature.

Particulars	**Case I (₹ In crores)**	**Case II (₹ In crores)**	**Case III (₹ In crores)**
Total amount of Paid up share capital, free reserves and securities premium	**270**	**270**	**270**
Hence, Total amount that the company can borrow without passing Special Resolution **Amount (A)**	**270**	**270**	**270**

(a) Existing Working Capital Loan (Repayable on demand) from Sigma Capital Limited since it is not a banker	50	50	50
(b) Total amount of Loan that Company needs is:	30	40	130
(i) 6 months loan for purchase of Plant & Machinery	10	20	150
(ii) 24 months loan for purchase if Plant & Machinery	**40**	**60**	**280**
Amount (B)	**90**	**110**	**330**
Is **Amount (A)> Amount (B),** then **SR need not be passed**	SR not to be passed	SR not to be passed	SR to be passed

Working Notes:

1. Paid up share capital includes both equity share capital and Preference share capital
2. 'Cash credit limit from scheduled bank' are temporary loans as they are repayable on demand.
3. '6 months loan for purchase of Plant & Machinery' is not treated as a temporary loan as temporary loans does not include loans raised for the purpose of financial expenditure of a capital nature.

Company to contribute to bona fide and charitable funds etc. (Section 181)

Question 35

The Board of directors of Very Well Ltd., are contributing every year to a charitable organization a sum of Rs. 60, 000/-. In a particular year, the company suffered losses and the directors are contemplating to contribute the said amount in spite of the losses. In this connection, state whether the directors can do so?

Answer

Under **section 181** of the Companies Act, 2013 the Board of Directors of a company is authorized to contribute to bonafide charitable and other funds. However, in case the **aggregate amount of such contribution in any financial year exceeds five per cent**. of its average net profits for the three immediately preceding financial years, prior permission of the company in general meeting shall be required.

The section **does not make it mandatory for the company to have a profit for making a charitable contribution in a financial year**. As the amount of donation is restricted to the average of previous 3 years' profits, it is possible for a company suffering a loss to make a contribution provided it is to a bonafide charitable fund.

In the present case, even though the company has incurred a loss it can contribute to the charitable fund only if it is a bonafied charitable fund and the amount is upto 5% of the average of the preceeding three years' profits. **In case the contribution exceeds the limit, the prior approval of the members must be taken at a general meeting of the company**.

Question 36 ***(Nov 17)***

M/s Jai Industries Limited earned net profit for the last three years as under:

Financial Year	Net Profit (Rs. in Crores)
2013-14	30
2014-15	40
2015-16	50

During the financial year 2016-17, the Board of Directors of the company contributed to a Charitable Fund ₹ 1.25 crores in July, 2016. Again in January 2017, the Board of Directors passed resolution to contribute to another Charitable Fund ₹ 1.00 crore.

Decide the validity of the decision of the Board of Directors regarding the contribution on both the occasions with reference to the provisions of the Companies Act, 2013.

Answer

According to **Section 181** of the Companies Act, 2013, the Board of Directors of a company may contribute to bona fide charitable and other funds.

Prior permission of the company in general meeting shall be required for such contribution in case any amount the aggregate of which, in any financial year, exceeds five per cent of its average net profits for the three immediately preceding financial years.

In the instant case, the average Net Profit of M/s Jai Industries Limited in the three immediately preceding financial years (2013-14, 2014-15 and 2015-16) is 40 Crores [30+40+50/3].

Thus, if M/s Jai Industries Limited wants to contribute more than ₹ 2 crores [40 crores * 5%] in Charitable fund, it has to take the prior permission of the company in general meeting.

In July 2016, the Board of Directors of M/s Jai Industries Limited contributed to a Charitable Fund ₹ 1.25 crores. This contribution is within the limit of ₹ 2 crore, thus no prior permission of the company in general meeting shall be required.

In January 2017, the Board of Directors passed resolution to contribute to another Charitable Fund ₹ 1.00 crore. For this contribution, prior permission of the company in general meeting shall be required as the aggregate contribution in Charitable Fund in the year 2017 is ₹ 2.25 crores which is exceeding ₹ 2 Crore. [₹ 1.25 crores + ₹ 1 Crore].

Disclosure of Interest by Director (Section 184)

Question 37

Mr. Bond and Mr. James were appointed as Directors of Jamesbond Ltd. at the AGM held on 30th September, 2017 by a single resolution. State the relevant provisions of the Companies Act, 2013 and identify is it possible to appoint the above Directors by a single resolution?

OR

When does a Director required to disclose his / her interest to the Company as per Section 184 of the Companies Act, 2013? What are the consequences of non- disclosure?

Answer

According to **Section 162** of the Companies Act, 2013, **at a general meeting of a Company, a motion for the appointment of two or more persons as Directors of the Company by a single resolution shall not be moved unless a proposal to move such a motion has first been agreed to at the meeting without any vote being cast against it.**

A resolution moved in contravention of above shall be void, whether or not any objection was taken when it was moved.

A motion for approving a person for appointment, or for nominating a person for appointment as a director, shall be treated as a motion for his appointment.

In the instant case, **it is not possible to appoint Mr. Bond and Mr. James as Directors of James Bond Ltd. by a single resolution.**

Or

According to **Section 184(1)** of the Companies Act, 2013 every Director shall disclose his concern or interest in any Company or companies or bodies corporate, firms, or other association of individuals which shall include the shareholding, in such manner as may be prescribed:

a) **At the First meeting of the Board in which he participates as a director**, and
b) Thereafter, **at the first meeting of the Board in every financial year,** or
c) Whenever **there is any change in the disclosures already made, then at the first Board meeting held after such change.**

Consequences of non-disclosure [Section 184(3) and 184(4)]:

a) Voidable at the option of company: A contract or arrangement entered into by the company without disclosing or with participation by a director who is concerned or interested in any way, directly or indirectly, in the contract or arrangement, shall be voidable at the option of the company.

b) Penalty: If a director of the company contravenes the provisions of section 184, such director shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than fifty thousand rupees but which may extend to one lakh rupees, or with both.

Question 38

Company Y entered into a contract with company Z with a paid-up capital of Rs. 50 lakhs. The director of Y company is holding equity shares of the nominal value of Rs. 50,000 in Z company. The director of Y company did not disclose his interest at the Board meeting under section 184 of the Companies Act, 2013. Is the director liable for his act?

Answer

As per **section 184 (2)** of the Companies Act, 2013 the disclosure of interest by directors do not apply to any contract or arrangement within two companies where any of the directors of one company or two or more of them **together holds or hold not more than 2% of the paid up share capital in the other company.** In the present case, the holding of the director of Y company in company Z is less than 2% [(50,000/50,00,000)*100% = 1%], so the director of Y company is not liable.

Note: **In case of private companies section 184(2) shall apply with the exception that the interested director may participate in such meeting after disclosure of his interest**, issued by the Central Government vide Notification No.G.S.R. 464(E), dated 5th June 2015.

Whereas with respect to the companies covered under **section 8** of the Companies Act, 2013, vide Notification G.S.R. 466(E), dated 5th June 2015, the Section 184(2) **shall apply only if the transaction with reference to section 188 on the basis of terms and conditions of the contract or arrangement exceeds one lakh rupees.**

Question 39 ***(May 2016)***

State the circumstances in which a director of a company is required under the Companies Act, 2013 to disclose his interest in a contract or arrangement to be entered into by the company. Examine whether the validity of the contract is affected by non- disclosure of interest by the director.

Answer

Circumstances in which disclosure of Interest by director is necessary - **Section 184** of the Companies Act, 2013 provides for disclosure of interest by director. According to this section whenever any director of a company who is in any way, whether directly or indirectly, concerned or interested in a contract or arrangement or proposed contract or arrangement entered into or to be entered into shall disclose the nature of his concern or interest at the meeting of the Board in which the contract or arrangement is discussed and **shall not participate in such meeting.**

Following are the circumstances where disclosure is necessary:

Whenever any director of the company, who is in any way, whether directly or indirectly, concerned or interested in a contract or arrangement or proposed contract or arrangement entered into or to be entered into —

a) With a body corporate in which such director or such director in association with any other director, **holds more than two per cent shareholding of that body corporate, or is a promoter, manager, Chief Executive Officer of that body corporate**; or

b) With a **firm or other entity in which, such director is a partner, owner or member, as the case may be.**

However, where any director who is not so concerned or interested at the time of entering into such contract or arrangement, he shall, if he becomes concerned or interested after the contract or arrangement is entered into, disclose his concern or interest forthwith when he becomes concerned or interested or at the first meeting of the Board held after he becomes so concerned or interested.

Validity of the contract on non-disclosure of interest: A contract or arrangement entered into by the company without disclosing or with participation by a director who is concerned or interested in any way, directly or indirectly, in the **contract or arrangement, shall be voidable at the option of the company.**

Loan to Directors (Section 185)

Question 40

Mr. X is a director of ABC Ltd. He has approached Housing Finance Co. Ltd. for the purpose of obtaining a loan of Rs. 50 lacs to be used for construction of building his residential house. The loan was sanctioned subject to the condition that ABC Ltd. should provide the guarantee for repayment of loan installments by Mr. X. Advise Mr. X .

Answer

According to **section 185** of the Companies Act, 2013, **No company shall**, directly or indirectly, **advance any loan, including any loan represented by a book debt to, or give any guarantee or provide any security** in connection with any loan taken by,—

a) any director of company, or of a company which is its holding company or any partner or

relative of any such director; or

b) any firm in which any such director or relative is a partner.

Thus, **Mr. X is not allowed for loan of Rs. 50 Lacs against guarantee by the company ABC Ltd.**

Question 41

Mr. KMP is director of XLS Ltd. He intends to construct a residential building for his own use. The cost of construction is estimated at Rs. 1.50 Crores, which Mr. KMP proposes to finance partly from his own sources to the tune of Rs. 60 lacs and the balance Rs. 90 lacs from housing loan to be obtained from a housing finance company. For the purpose of obtaining the loan, he has approached the housing finance company which has in principle agreed to grant the loan, but has put a condition. The condition put by the housing finance company is that the Company XLS Ltd. of which Mr. KMP is a director should provide the guarantee for repayment of the loan and interest as per the terms of the proposed agreement for granting the loan to Mr. KMP. You are required to advise Mr. KMP on the matter with reference to the provisions of the Companies Act, 2013.

Answer

According to **section 185** of the Companies Act, 2013, **No company shall**, directly or indirectly, **advance any loan, including any loan represented by a book debt to, or give any guarantee or provide any security** in connection with any loan taken by,—

a) any director of company, or of a company which is its holding company or any partner or relative of any such director; or

b) any firm in which any such director or relative is a partner.

Thus, guarantee by Company XLS Ltd. of which Mr. KMP is a director, for repayment of the loan and interest as per the terms of the proposed agreement is not allowed.

Further, If any loan is advanced or a guarantee or security is given or provided in contravention of the above provisions, the **company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees**, and the director or the other person to whom any loan is advanced or guarantee or security is given or provided in connection with any loan taken by him or the other person, shall be punishable with **imprisonment which may extend to 6 months** or with **fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees, or with both**.

Question 42 ***(May 2012)***

Mr. DRT is a director of PCS Ltd. The said company is having sufficient liquid funds and Mr. DRT is in dire need of funds. In order to mitigate the hardship of Mr. DRT the board of directors of PCS Ltd. wants to lend Rs. 5 lakhs to him and Rs. 2 lakhs to his wife. State whether such loans can be given and if so under what conditions.

Answer

Loan to Director and his relative:

As per Sec. 185 of the Companies Act, 2013, no company shall, directly or indirectly advance any loan, including any loan represented by a book debt to, or give any guarantee or provide any security in connection with any loan taken by,

a) any director of company, or of a company which is its holding company or an which is its holding company or any partner or relative of any such director; or

b) any firm in which any such director or relative is a partner

In the instant case, board of directors of PCS Ltd. wants to lend 5 lakhs to Mr. DRT, the director of the company and 2 lakhs to his wife.

Conclusion: Granting loan to director or any other person in whom the director is interested is in violation of section 185 of the Companies Act, 2013.

If PCS Ltd. would have been PCS Private Ltd. than provisions of sec. 185 of the Companies Act, 2013 shall not apply over it subject to following conditions:

a) no other body corporate has invested any money in share capital of such company,

b) borrowings of such company from banks or financial institutions or any body corporate is less than twice of its paid-up share capital or 50 crore, whichever is lower; and

c) no default in repayment of such borrowings subsist at the time of making transactions u/s 185.

d) company has not committed a default in filing of its financial statements u/s 137 or annualreturn u/s 92 with the Registrar

Loan and Investment by Company (Section 186)

Question 43 ***(May 2018 & RTP Nov 18)***

ASK Housing Finance Limited are prepared to give housing loans to the employees of M/s NEWS Pharmacy Limited subject to the condition that the loans are guaranteed by M/s. NEWS Pharmacy Limited. M/s NEWS Pharmacy Limited is not a listed company and the company will be exceeding the limits prescribed under the Companies Act, 2013 by providing the guarantees. Advise the company about this legal requirement under the Companies Act, 2013 to give effect to the above proposal. What would be your advice if the company was required to provide security instead of guarantee?

Answer

Loans and Investment by the company:

As per Section 186(2) of the Companies Act, 2013, no company shall directly or indirectly

a) give any loan to any person or other body corporate;
b) give any guarantee or provide security in connection with a loan to any other body corporate or person, and
c) acquire by way of subscription, purchase or otherwise, the securities of any other body corporate, exceeding 60% of its paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account, whichever is more.

Explanation provided in Section 186(2) of the Companies Act, 2013 states that for the purposes of this sub-section, the word "person" does not include any individual who is in the employment of the Company.

In the instant case, the loans are to be guaranteed by M/s. News Pharmacy Limited for its employees which falls within the purview of the explanations which includes guarantee for the employees.

Conclusion: Sec. 186(2) shall not be applicable in the situation as cited in the question. M/s NEWS Pharmacy Limited can give the guarantee without any condition on the limits imposed in the Section 186(2). Hence, there are no legal requirements to be fulfilled under the Companies Act, 2013 to give effect to the above proposal.

Question 44 ***(May 2012)***

Amar Textiles Ltd. is a company engaged in the manufacture of fabrics. The company has investments in shares of other bodies corporate including 70% shares in Amar Cotton Company Ltd. and it has also advanced loans to other bodies corporate.

The aggregate of all the investments made and loans granted by Amar Textiles Ltd. exceeds 60% of its paid up share capital and free reserves and also exceeds 100% of its free reserves. In course of its business requirements, Amar Textiles Ltd. has obtained a term loan from Industrial Development Bank of India which is still subsisting.

Now the company wants to increase its holding from 70% to 80% of the equity share capital in Amar Cotton Company Ltd. by purchase of additional 10% shares from other existing shareholders. State the legal requirements to be complied with by Amar Textiles Ltd. under the provisions of the Companies Act, 2013 to give effect to the above proposal.

Answer

Legal provisions as to making Loan and Investments by the company:

Section 186 of Companies Act, 2013 provides the provisions relating to giving loans and making investment in other companies. Accordingly, Amar Textiles Ltd. need to comply with the below mentioned legal requirements:

a) Special Resolution:

As per Sec. 186(2) of the Companies Act, 2013, no company shall directly or indirectly, give any into any person or other body corporate; give any guarantee or provide security in connection with a loan to any other body corporate or person; and acquire by way of subscription, purchase or otherwise, the securities of any other body corporate, exceeding 60% of its paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account, whichever is more.

Sec. 186(3) provides that where the aggregate of the loans and investment so far made, the amount for which guarantee or security so far provided to or in all other bodies corporate along with the investment, loan, guarantee or security proposed to be made or given by the Board, exceed the limits specified under sub-section (2), no investment or loan shall be Made or guarantee shall be given or security shall be provided unless previously authorized by a special resolution passed in a general meeting.

In the present case, aggregate of the investments in shares and loans granted to other bodies corporate exceeds 60% of the paid-up share capital and free reserves and also 100% of the free reserves, it is therefore, necessary for the Amar Textiles Ltd., to pass a special resolution before increasing its holding from 70% to 80%.

Special resolution shall specify the total amount up to which the Board of Directors are authorised to make such acquisition.

b) Disclosures in financial statements:

As per Sec. 186(4), the company shall disclose to the members in the financial statement the full particulars of the loans given, investment made or guarantee given or security provided and the purpose for which the loan or guarantee or security is proposed to be utilised by the recipient of the loan or guarantee or security.

c) Unanimous resolution of Board and Prior Approval of Public Financial Institution:

As per Sec. 186(5), no investment shall be made or loan or guarantee or security given he the company unless the resolution sanctioning it is passed at a meeting of the Board with the consent

of all the directors present at the meeting and the prior approval of the public financial institution concerned where any term loan is subsisting, is obtained.

However, prior approval of a public financial institution shall not be required where the aggregate of the loans and investments so far made, the amount for which guarantee or security so far provided to or in all other bodies corporate, along with the investments loans, guarantee or security proposed to be made or given does not exceed the limit as specified in section 186(2), and there is no default in repayment of loan installments or payment of interest thereon as per the terms and conditions of such loan to the public financial institution.

In the present case, Amar Textiles Ltd., had obtained a term loan from IDBI which is not a public financial institution and therefore the provisions of Section 186(5) are not attracted even if such loan is still subsisting. The company is not required to obtain prior approval of IDBI for making any further investment.

So, as per Sec. 186(5), investment proposal must be passed at the Board meeting by a unanimous decision of all the director's present at the meeting.

d) Maintenance of register:

As per Sec. 186(9) every company giving loan or giving a guarantee or providing security or making an acquisition under this section shall keep a register which shall contain such particulars and shall be maintained in manner as prescribed by Rule 12.

Question 45 ***(Nov 17)***

Star Limited proposes to acquire 15% equity shares of Gain Investments (P) Limited for 45 lakhs which has a face value of Rs. 35 lakhs. Star Limited has an outstanding loan of Rs. 15 lakhs to a public financial institution and had not defaulted in the repayment of loan installments stipulated in the loan agreements. Based on the following financial data. Advise Star Limited about the legal position regarding the allow ability of the proposed investment under the provisions of the Companies Act, 2013.

	(Rs. In Crores)	
	Star Ltd.	**Gain Investment (P) Ltd.**
Authorized Capital	1.00	3.00
Paid up Share Capital	0.50	2.00
Free Reserves	0.20	1.50

As on the date of proposition, Star Ltd. does not hold any shares of any company.

Answer

According to **Section 186(2),** no company shall directly or indirectly acquire by way of subscription, purchase or otherwise, the **securities of any other body corporate, exceeding 60% of its paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account, whichever is more.**

Where the giving of any loan or guarantee or providing any security or the acquisition exceeds the limits specified in Section 186(2), prior approval by means of a special resolution passed at a general meeting shall be necessary. [Sub- section (3)]

According to **Section, 186(5), no investment shall be made or loan or guarantee or security given by the company unless the resolution sanctioning it is passed at a meeting of the Board with the consent of all the directors present at the meeting and the prior approval of the public financial institution concerned where any term loan is subsisting, is obtained.**

However, prior approval of a public financial institution shall not be required where the aggregate of the loans and investments so far made, the amount for which guarantee or security so far provided to or in all other bodies corporate, along with the investments, loans, guarantee or security proposed to be made or given does not exceed the limit as specified in sub-section (2), and there is no default in repayment of loan installments or payment of interest thereon as per the terms and conditions of such loan to the public financial institution.

In the given question, Star Limited has proposed to acquire 15% equity shares of Gain Investments (P) Limited for Rs. 45 lakhs.

Star Limited can make a maximum investment of Rs. 42 lakhs [(0.5+.2)*60% or (.2)*100%, whichever is more]. Since, the investment proposed by Star Limited in Gain Investment (P) Limited is 45 lakhs, prior approval by means of a special resolution passed at a general meeting shall be necessary.

Further, though **Star Limited has not defaulted in the repayment of loan installments of the loan taken from public financial institutions, but the amount of investment proposed exceeds the limit calculated in accordance with the provision specified in section 186(2), it will have to take prior approval of the public financial institution also.**

Question 46 ***(Nov 2016)***

Soft and Secure Lenders Limited, has convened a Board Meeting on 25th October, 2016. One of the items of the agenda is to approve the grant of loan of ₹ 20 crore to Easy Going Industries Limited, for expansion of its business activities. At the Board Meeting, out of the total of six Directors of the lending company, five directors were present and except one director, the remaining four directors approved the grant of loan of ₹ 20 crores to Easy Going Industries Limited. The borrowing company has taken loans from a public financial institution and also deposits from public. Examine the loan proposal with reference to the provisions of the Companies Act, 2013.

Answer

Loan by company: The given problem is based on the Section 186 of the Companies Act, 2013. According to section 186 (2) of the Companies Act, 2013, no company shall directly or indirectly —

i) **give any loan to any person or other body corporate;**

ii) **give any guarantee or provide security in connection with a loan to any other body corporate or person; and**

iii) **acquire by way of subscription, purchase or otherwise, the securities of any other body corporate,**

exceeding 60% of its paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account, whichever is more.

Further, Section 186 (5) of the Companies Act, 2013 provides of unanimous resolution that is required for grant of loan to the borrowing company. Any investment shall be made or loan or guarantee or security given by the company only after when the resolution sanctioning it is passed at a meeting of the Board with the consent of all the directors present at the meeting.

Facts in the given problem states that Soft and Secure Lenders Limited convened a board meeting and was to approve grant of loan of ₹ 20 Crore to Easy Going Industries Limited. However, at the Board meeting, out of the total of six directors of the Soft and Secure Lenders Ltd., five directors were present and except one director, the remaining four directors approved the grant of the loan of ₹ 20 Crore. Considering the above mentioned provisions, **since the approval for the grant of loan has not been sanctioned by passing of resolution at a meeting of the Board with the consent of all**

the directors present at the meeting, so loan proposal is not in compliance with the Companies Act, 2013.

Question 47 ***(May 19)***

Vogue Limited has an Authorised Capital of 250 lakhs and paid up capital of 200 lakhs. The free reserves are there to the tune of ₹ 150 Lakhs. The company has advanced a loan of ₹ 160 Lakhs to other companies as on 30th November, 2018. Now the company proposes to advance an interest free loan of ₹ 60 Lakhs to its wholly owned subsidiary Fashion Limited.

Discuss the validity of the proposed transaction with reference to the restrictions imposed by the applicable provisions of the Companies Act, 2013 and relevant Rules made thereunder.

Answer

According to **Section 186(2)** of the Companies Act, 2013, no Company shall directly or indirectly give any loan, guarantee or provide security to other body corporate, exceeding 60% of its paid-up share capital, free reserves and securities premium account or one hundred per cent. of its free reserves and securities premium account, whichever is more.

Sub section (3) of Section 186 provides that where the aggregate of the loans and investment so far made, the amount for which guarantee or security so far provided to or in all other bodies corporate along with the investment, loan, guarantee or security proposed to be made or given by the Board, exceed the limits specified under sub-section (2), no investment or loan shall be made or guarantee shall be given or security shall be provided unless previously authorised by a special resolution passed in a general meeting:

However, where a loan or guarantee is given or where a security has been provided by a company to its wholly owned subsidiary company or a joint venture company, or acquisition is made by a holding company, by way of subscription, purchase or otherwise of, the securities of its wholly owned subsidiary company, the requirement of this sub-section shall not apply.

Further, sub- section (7) provides that no loan shall be given under Section 186 at a rate of interest lower than the prevailing yield of one year, three year, five year or ten year Government Security closest to the tenor of the loan.

In the given question, Vogue Limited has to provide interest free loan to its wholly owned subsidiary Fashion Limited. The maximum amount of loan that Vogue Limited can provide to other body corporate is ₹ 210 lakhs [Higher of {60% of (200+150)} or {100% of 150}]. But, Vogue Limited has already provided loans of ₹ 160 lakhs to other companies. Thus, if Vogue Limited proposes to provide loan beyond of ₹ 50 lakhs (₹ 210-160 lakhs) it requires shareholders' approval.

However, since Fashion Limited is a wholly owned subsidiary of Vogue Limited, it can give loan to Fashion Limited without approval of shareholders.

However, the Companies Act, 2013, prohibits giving interest free loan, Vogue Limited cannot provide an interest free loan even to its wholly owned subsidiary.

Related Party Transaction (Section 188)

Question 48 ***(May 18)***

Discuss "Related Party Transactions" under the Companies Act, 2013, with specific reference to the nature of transactions which fall under the purview of the Companies Act, 2013.

Answer

Related party transactions: **Section 188** of the Companies Act, 2013 provides for related party transactions. According to this section, following are the nature of transactions covered under the purview of the Companies Act, 2013 -

On the consent of the Board of Directors given by a resolution at a meeting of the Board and subject to such conditions prescribed in the Companies (Meetings of Board and its Powers) Rules, 2014, company shall enter into any contract or arrangement with a related party with respect to —

a) **sale, purchase or supply of any goods or materials;**
b) **selling or otherwise disposing of, or buying, property of any kind;**
c) **leasing of property of any kind;**
d) **availing or rendering of any services;**
e) **appointment of any agent for purchase or sale of goods, materials, services or property;**
f) **such related party's appointment to any office or place of profit in the company, its subsidiary company or associate company; and**
g) **underwriting the subscription of any securities or derivatives thereof, of the company:**

However, where in above transactions, limits as prescribed in Companies (Meetings of Board and its Powers) Rules, 2014 is exceeding, there in such case a company shall enter into a transaction/transactions only on the **prior approval of the company by a resolution**. [First proviso to section 188(1)]

Explanation.— It is hereby clarified that the limits specified in Companies (Meetings of Board and its Powers) Rules, 2014 shall apply for transaction or transactions to be entered into either individually or taken together with the previous transactions during a financial year.

Question 49 ***(May 19)***

M/s Tristar Ltd. (an unlisted public limited company) with the annual turnover of ₹ 700 crores entered into a contract of purchasing of raw material from M/s. PTC Pvt. Ltd. during the year 2018. M/s Tristar Ltd. appointed Mr. Sudhir, a Director of the Company, to act in this deal of transaction on behalf of the company. Mr. Sudhir is also one of the member of M/s PTC Pvt. Ltd. Mr. Sudhir settled the said transaction of purchase for ₹ 85 crores and entered into the contract. After a few transactions executed under the contract, the Board of M/s Tristar Ltd. finds degradation in the quality of the raw material supplied. Further, in a board meeting this contract was challenged considering it as a related party transaction and in contravention to section 188 (1) of the Companies Act, 2013 read with rules framed thereunder. During the period Mr. Sudhir was appointed as director in a newly incorporated company M/s Raaga Limited.

In the light of the given facts, examine the following situations as per the Companies Act, 2013.

i) What is the legal position of the contract entered between M/s Tristar Ltd. through its director Mr. Sudhir, and M/s. PTC Pvt. Ltd.?
ii) Is there any contravention of section 188 (1)? If yes, then state the liability of the wrongdoer.
iii) Comment upon the appointment of Mr. Sudhir as a Director in M/s Raaga Limited.

Answer

As per the given facts, Mr. Sudhir, a director of M/s Tristar Ltd., was also a member of M/s PTC private Ltd. with which he entered into contract for the purchase of the raw material. In terms of section 2(76) of the Companies Act, 2013, M/s Tristar Ltd. is a related party to M/s PTC private Ltd.

Also, as per section 188(1) of the Act, no company shall enter into any contract or arrangement with a related party with respect to the transaction related to the sale, purchase or supply of any goods or

materials or made through an appointment of any agent for purchase or sale of goods, materials, services or property, except with the consent of the Board of Directors given by a resolution at a meeting of the Board and subject to such conditions as given in rule 15 of the Companies (Meetings of Board and its Powers) Rules, 2014 .

However, no contract or arrangement, in the case of a company having a paid-up share capital of not less than such amount, or transactions not exceeding such sums, as prescribed in Rule 15(3) of the Companies (Meetings of Board and its Powers) Rules, 2014, shall be entered into except with the prior approval of the company by a resolution. [First proviso to section 188(1)]

A company shall not enter into transaction/s related to sale, purchase or supply of any goods or materials, directly or through appointment of agent, where the transaction or transactions to be entered into is amounting to 10% or more of the turnover of the company or rupees 100 crore, whichever is lower, except with the prior approval of the company by a resolution.

Since in the given case, M/s Tristar Ltd. has turnover of ₹ 700 crore. The transaction of purchase settled by Mr. Sudhir, is ₹ 85 crore which is more than 10% of the turnover (i.e., 700 crore x10/100= 70 crore). Neither M/sTristar Ltd. had taken prior approval of the company by a resolution, nor it was ratified by the shareholders at a meeting within three months from the date on which such contract or arrangement was entered into. [Section 188(3)]

i) So, in terms of the above provision, this contract is of voidable nature at the option of the shareholders according to section 188(3) of the Companies Act, 2013.

ii) **Contravention of Section 188(1):** Yes, as per the answer given under Part (i), there is a contravention of section 188(1).

Following is the liability of the Sudhir, Director of M/s Tristar Ltd: Section 188(3) specifies, if the contract or arrangement is with a related party to any director, or is authorised by any other director, the directors concerned shall indemnify the company against any loss incurred by it.

Therefore, M/s Tristar Ltd. may proceed to recover loss**.** Section 188 (4) provides that it shall be open to the company to proceed against a director or any other employee who had entered into such contract or arrangement in contravention of the provisions of this section for recovery of any loss sustained by it as a result of such contract or arrangement.

Penalty: Any director or any other employee of a company, who had entered into or authorised the contract or arrangement in violation of the provisions of this section shall be punishable with fine which shall not be less than 25,000 rupees but which may extend to 5 lakh rupees.

iii) **Appointment of Director in M/s Raaga Ltd.:** As per section 164(1)(g) of the Companies Act,2013, a **person** shall not be eligible for appointment as a director of a company, where he has been convicted of the offence of dealing with related party transactions under section 188 at any time during the last preceding 5 years;

In the given instance, Mr. Sudhir was not convicted rather only the contract was challenged in the board meeting considering it as a related party transaction which is in contravention to section 188(1) and may attract penalty in terms of Section 188(5) against the offence dealt with related party transaction hence Mr. Sudhir remains eligible to be appointed as a director of M/s Raaga Ltd.

Payment to directors for loss of office, Etc. in connection with transfer of undertaking, property or shares (Section 191)

Question 50 ***(May 18)***

The register of contracts or arrangement under Section 189 of the Companies Act, 2013 is maintained at the Registered office of Fortune Ltd. under the custody of the Company Secretary. The AGM was held in different place but in the same town where the registered office is situated. Mr. Semar, a shareholder of the company and Mr. Raj, proxy of a shareholder insisted for producing the said register at the commencement of the AGM for inspection. The Company Secretary refused to produce the register stating that being the statutory register it has to be maintained at the registered office only. Examine whether Mr. Semar and Mr. Raj will succeed in their attempt under the provisions of the Companies Act, 2013?

Also identify the particulars to be disclosed to the members of a company to pass a resolution approving any payment by way of compensation for loss of office of a director as per the provisions of Section 191 of the Companies Act, 2013 read with Rule 17 of the Companies (Meetings of Board and its Powers) Rules, 2014.

Answer

Place of maintenance of Register of Contracts or Arrangements:

As per **Section 189** of the Companies Act, 2013, every Company shall keep one or more registers giving separately the particulars of all contracts or arrangements related to disclosure of interest by director as per Section 184(2) or related party transactions given under Section 188.

The register shall be kept at the registered office of the Company and it shall be-

- **open for inspection at such office during business hours and extracts may be taken therefrom, and**
- **copies thereof as may be required by any member of the company shall be furnished by the company**

The register to be kept under this Section shall also be produced at the commencement of every annual general meeting of the Company and shall remain open and accessible during the continuance of the meeting to any person having the right to attend the meeting.

As per law, register shall be produced at the commencement of every annual general meeting of the Company and shall remain open and accessible during the meeting to any person having the right to attend the meeting.

Hence, Mr. Semar and Mr. Raj, being a shareholder and proxy of a shareholder, have a right to inspect the register of contract and arrangements during the meeting.

Payment by way of compensation for loss of office to Director

As per the Rule 17 of the *Companies (Meetings of Board and its Powers) Rules, 2014*, no director of a company shall receive any payment by way of compensation in connection with any event mentioned in 191(1) unless the following particulars are disclosed to the members of the company and they pass a resolution at a general meeting approving the payment of such amount -

(a) name of the director;

(b) amount proposed to be paid;

(c) event due to which compensation become payable;
(d) date of Board meeting recommending such payment;
(e) basis for the amount determined;
(f) reason or justification for the payment;
(g) manner of payment - whether payable in cash or otherwise and how;
(h) sources of payment; and
(i) any other relevant particulars as the Board may think fit.

Restriction on Non – Cash Transactions involving Directors (Section 192)

Question 51

In what way does the Companies Act, 2013 restricts the non-cash transactions involving directors of public limited company? Explain.

Answer

Restrictions on non-cash transactions involving Directors: Section 192 of the Companies Act, 2013 provides for restrictions on non-cash transactions involving directors. According to the provision,

i) No company shall enter into an arrangement by which—
   a) a director of the company or its holding, subsidiary or associate company or a person connected with him **acquires or is to acquire assets for consideration other than cash, from the company**; or
   b) the company acquires or is to acquire assets for consideration other than cash, from such director or person so connected, unless prior approval for such arrangement is accorded by a resolution of the company in general meeting and if the director or connected person is a director of its holding company, approval shall also be **required to be obtained by passing a resolution in general meeting of the holding company**.

ii) The notice for approval of the resolution by the company or holding company in general meeting **shall include the particulars of the arrangement along with the value of the assets involved in such arrangement duly calculated by a registered valuer**.

iii) Any arrangement entered into by a company or its holding company in contravention of the provisions of this section **shall be voidable at the instance of the company unless** -
   a) the restitution of any money or other consideration which is the subject-matter of the arrangement is no longer possible and the company has been indemnified by any other person for any loss or damage caused to it; or
   b) any rights are acquired bona fide for value and without notice of the contravention of the provisions of this section by any other person.

Ch 4 - Inspection, Inquiry and Investigation

Power to call for Information, Inspect books and Conduct inquiries (Section 206)

Question 1 ***(RTP May 2016)***

A notice was sent to Mr. Left by the registrar to furnish the information related to a business transacted during his tenure in the X company. Mr. Left ignored the notice considering that he is no more an employee of X company. Registrar issued the summon against Mr. Left. Explain in the light of the Companies Act, 2013 about the liability of the Mr. Left in the given case.

Answer

Power of the Registrar to call for information, explanation or documents: According to **section 206(1)** of the Companies Act, 2013, where on a scrutiny of any document filed by a company or on any information received by him, the Registrar is of the opinion that any further information or explanation or any further documents relating to the company is necessary, he may by a written notice require the company—

a) to **furnish in writing** such information or explanation; or
b) to **produce such documents**,

within such **reasonable time**, as may be specified in the notice.

Further, proviso to sub-section (2) of section 206 provides that where such information or **explanation relates to any past period,** the **officers who had been in the employment of the company for such period, if so called upon by the Registrar** through a notice served on them in writing, shall also furnish such information or explanation to the best of their knowledge.

In the given instance, Mr. Left is a past member of the company. Registrar by serving notice asked Mr. Left to furnish the information related to the business transaction made during his tenure. So as per the above provision, where such information or explanation relates to any past period, the officers who had been in the employment of the company for such period, if so called upon by the Registrar through a notice served on him, he has a duty to give such information/Explanation to the best of his knowledge. Mr. Left is liable to provide such information.

Search and Seizure (Section 209)

Question 2 ***(May 2016)***

A group of creditors of Mac Trading Limited makes a complaint to the Registrar of Companies, Hyderabad alleging that the management of the company is indulging in destruction and falsification of the accounting records of the company. The complainants request the Registrar to take immediate steps to seize the records of the company so that the management may not be allowed to tamper with the records. The complaint was received at 10 A.M. on 1st July 2015 and the ROC entered the premises at 10.30 A.M. for the search. Examine the powers of the Registrar to seize the books of the company.

Or

A group of creditors of MBIND Bronze Limited makes a complaint to the Registrar of Companies, Himachal Pradesh alleging that the management of the company is indulging in destruction and falsification of the accounting records of the company. The complainants request the Registrar to take immediate steps to seize the records of the company so that the management may not be allowed to tamper with the records. The complaint was received at 11 am on 6 January, 2018 and

the registrar has attempted to enter the premise of the company but has been denied by the company, due to not having order from the special court.
Is the contention of company being valid in terms of Companies Act, 2013? Discuss.

Answer

Search and seizure - **Section 209** of the Companies Act, 2013 provides that where upon information in his possession or otherwise, the Registrar or inspector has reasonable ground to believe that the books and papers of -

i) a **company**, or

ii) **relating to the key managerial personnel**, or

iii) **any director**, or

iv) **auditor**, or

v) **company secretary in practice** if the company has not appointed a company secretary,

are **likely to be destroyed, mutilated, altered, falsified or secreted, he may, after obtaining an order from the Special Court for the seizure of such books and papers—**

1) enter, with such assistance as may be required, and search, the place or places where such books or papers are kept; and

2) seize such books and papers as he considers necessary after allowing the company to take copies of, or extracts from, such books or papers at its cost.

According to the above provisions, Registrar may enter and search the place where such books or papers are kept and seize them only after obtaining an order from the Special Court.

Since in the given question, **Registrar entered the premises for the search and seizure of books of the company without obtaining an order from the Special Court, he is not authorised to seize the books of the Mac Trading Limited**.

Investigation into Affairs of Company (Section 210)

Question 3

A majority of the Board of directors of M/s High Value Infotech Ltd. have realised that some of the business activities carried out in the name of the company are not in the interest of either the company or its members. They want that the company should make an application to the Central Government to appoint an Inspector to carry out investigation and find out the whole truth. Explain the steps that should be taken to achieve the purpose and draft the application under the Companies Act, 2013.

Answer

1. According to **section 210 (1)** of the Companies Act, 2013 the Central Government may order an investigation into the affairs of the company, if it of the opinion that it is necessary to do so:
   - **a)** **On the receipt of a report of the Registrar or inspector under section 208**;
   - **b)** On **intimation of a special resolution passed by a company that the affairs of the company ought to be investigated**;
   - **c)** In **public interest**.
2. According to **section 210 (3)** of the Companies Act, 2013, the Central Government may appoint one or more persons as inspectors to investigate into the affairs of the company and to report thereon in such manner as the Central Government may direct.

In the given case, the majority of directors are already of the view that the affairs of the company are not conducted in a manner beneficial either to the company or to the members and want to make an application to the Central Government to appoint an inspector. Therefore, the steps to be carried out for the purpose will be as under:

i) **Convene an Extraordinary General Meeting of members for passing the required special resolution**. The provisions for convening the meeting should be complied with and the explanatory statement with the notice of the meeting must provide full details of the proposed special resolution.

ii) Once the **special resolution is passed, a copy of it along with the copy of the notice should be filed with the Registrar**;

iii) An **application should be made under section 210 (1) to the Central Government** requesting it to appoint an inspector to investigate the affairs of the company.

iv) The Central Government on receipt of such notice will ask for information**, documents and other supporting evidence and may order an investigation only if it is of the opinion that an investigation is warranted**. It may appoint one or more inspectors to investigate into the affairs of the company and to report thereon in such manner as it may direct.

Draft Application:

High Value InfoTech Ltd. (Address) Date:

The Secretary,

Ministry of Corporate Affairs, New Delhi

Sir,

At a meeting of the shareholders of the company held on_____at_____,the members have passed the following resolution as a Special Resolution:

"Resolved that the Central Government be approached to appoint one or more Inspector to carry out an investigation into the affairs of the company to determine whether the activities in the name of the Company are being carried on in a manner which is against the interest of either the company or its members.

Resolved further that the Board of Directors be and is hereby authorized to make necessary application to the Central Government for this purpose and submit the necessary documents and informations as may be required by the Central Government in this regard".

The above referred special resolution was passed at an extraordinary general meeting of the company held on…….

It is, therefore, prayed that the Central Government be pleased to appoint as per section 210 of the Companies Act, 2013, an inspector to investigate the affairs of the company regarding the matters mentioned in the above resolution and communicate its decision to the company.

Yours faithfully,
For and on behalf of High Value InfoTech Ltd. Secretary.

Question 4 ***(Nov 2015)***

Shareholders of Hide and Seek Ltd. are not satisfied about performance of the company. It is suspected that some activities being run in the name of the company are not in the interest of the company or its members. 101 out of total 500 shareholders of the company have made an

application to the Central Government to appoint an inspector to carry out investigation and find out the true picture.

With reference to the provisions of the Companies Act, 2013, mention whether the shareholders' application will be accepted? Elaborate.

Or

Shareholders of Akash Ltd. not satisfied with the performance of the company inferred that some activities conducted by the company are against the interest of the members of the company. Group of shareholders of the company filed an application to the Central Government to appoint an inspector to carry out investigation to look into the matter.

With reference to the provisions of the Companies Act, 2013, mention whether the shareholders application is tenable? Elaborate.

Answer

According to the Companies Act, 2013, the Central Government under **section 210 (1)** may order an investigation into the affairs of the company, if it is of the opinion that it is necessary to do so:

a) on the **receipt of a report of the Registrar or Inspector under section 208;**
b) on **intimation of a special resolution passed by a company** that the affairs of the company ought to be investigated;
c) in **public interest**.

According to **section 210 (3)** of the Companies Act, 2013, the Central Government may appoint one or more persons as **inspectors to investigate into the affairs of the company and to report thereon in such manner as the Central Government may direct**.

The shareholders' application will not be accepted as **under 210** of the Companies Act, 2013, Central Government may order an investigation into affairs of the company on the intimation of a special resolution passed by a company that the affairs of the company ought to be investigated and then may appoint the inspectors. Here, 101 out of total 500 shareholders of the company have made an application to the Central Government to appoint an inspector to carry out investigation but it is not sufficient as the company has not passed the special resolution.

Question 5

Greater DINA Investors Association made a complaint by an informal letter to the Central Government that Management of Secret Limited has been indulging in fraudulent activities causing loss to the shareholders and that an investigation should be carried out to find out the whole truth. On receipt of the letter, the Central Government directed the Association to approach them formally after complying with the provisions of the Companies Act, 2013. Advise the Association.

Answer

Section 210 of the Companies Act, 2013 provides for Investigation into affairs of company. According to sub-section (1), where the Central Government is of the opinion, that it is necessary to investigate into the affairs of a company,—

(a) **on the receipt of a report of the Registrar or inspector under section 208**;
(b) on **intimation of a special resolution** passed by a company that the affairs of the company ought to be investigated; or
(c) in **public interest,**

It may order an investigation into the affairs of the company. According to section 214,

(i) The Central Government may before appointing an inspector under Section 210, require the applicant to give a security **not exceeding ₹25,000 rupees for payment of the costs and expenses of investigation as per the criteria given in the Companies** (Inspection, investigation and inquiry) Rules, 2014.

(ii) Further, the above referred security shall be refunded to the applicant if the investigation results in prosecution.

As stated in the question that Central Government directing the association to approach them formally after complying with the provision of the Companies Act, 2013 is not required in view of the above stated provisions because Central Government can act in Public interest.

Question 6

i) The shareholders of Kumar Ltd. passed a special resolution that the affairs of the Company ought to be investigated. The Company submitted the special resolution to the Central Government. Examine, explaining the relevant provision of the Companies Act, 2013, whether the power of the Central Government to order an investigation is mandatory or discretionary?

ii) Enumerate the procedures to be followed by the Serious Fraud Investigation Office to arrest a person who has been found guilty of an offence committed under Section 447 of the Companies Act, 2013.

Answer

i) **Investigation in the opinion of Central Government [Section 210(1) of the Companies Act, 2013]:** Where the Central Government is of the opinion, that it is necessary to investigate into the affairs of a company,—

a) on the receipt of a report of the Registrar or inspector under section 208;

b) on intimation of a special resolution passed by a company that the affairs of the company ought to be investigated; or

c) in public interest,

it may order an investigation into the affairs of the company.

Hence, the power of the Central Government to order an investigation is discretionary.

ii) As per section 212(6) of the Companies Act, 2013, offences covered under section 447 of this Act shall be cognizable as well as non-bailable. So, the person found guilty for commission of an offence under the said section, shall be liable to be arrested, by SFIO.

The Central Government by general or special order authorize the Director, Additional Director or Assistant Director of SFIO in this behalf, on the basis of material in his possession reason to believe (the reason for such belief to be recorded in writing) that any person has been guilty of any offence punishable under sections referred to in sub-section (6) i.e. Section 447,to arrest such person and shall, as soon as may be, inform him of the grounds for such arrest. [Section 212(8)].

Immediately after arrest, they shall forward a copy of the order, along with the material in his possession, to the SFIO in a sealed envelope, in such manner as may be prescribed and the SFIO shall keep such order and material for such period as may be prescribed. [Sub section (9)] and present the person so arrested before the Judicial Magistrate or a Metropolitan Magistrate having jurisdiction within twenty-four hours. The period twenty four hours shall exclude the time necessary for the journey from the place of arrest to the Magistrate's court. [Sub section (10)]. An Interim report is submitted, if so directed, to the Central Government, till the completion of the investigation. [Sub section (11)&(12)].

Investigation into affairs of company by Serious Fraud Investigation office (Section 212)

Question 7 ***(Nov 17)***

Mrs. Preeti, a lady aged about 32 years and Managing Director of M/s Growmore plantations Ltd., has been arrested for an offence covered under section 447 of the Companies Act, 2013 on a complaint made by the Director, Serious Fraud Investigation Officer. Mrs. Preeti seeks your legal advise as to the conditions under which she can be released on bail and the role of Special Court in this regard.

Answer

According to **Section 212(6)** of the Companies Act, 2013, notwithstanding anything contained in the Code of Criminal Procedure, 1973, offence covered under section 447 shall be cognizable and no person accused of any offence under those sections shall be released on bail or on his own bond unless—

(i) the Public Prosecutor has been given an opportunity to oppose the application for such release; and

(ii) where the Public Prosecutor opposes the application, the court is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while on bail.

A person, who, is under the age of sixteen years or is a woman or is sick or infirm, may be released on bail, if the Special Court so directs.

The Special Court shall not take cognizance of any offence referred to this sub- section except upon a complaint in writing made by—

a) the **Director, Serious Fraud Investigation Office;** or

b) **any officer of the Central Government authorised, by a general or special order in writing in this behalf by that Government.**

Hence, in the instant case, Mrs. Preeti has been arrested for an offence covered under section 447 of the Act on a complaint made by the Director, SFIO.

As Mrs.Preeti is a woman, she may be released on bail if the Special Court so directs.

Investigation into company's affairs in other cases (Section 213)

Question 8 ***(RTP Nov 18)***

Some creditors of NTY Limited approached you to guide them to apply to the Tribunal for seeking an order for conducting an investigation into the affairs of the company due to the fact that the business of the company is being conducted with intention to defraud its creditors. Referring to the provisions of the Companies Act, 2013, guide them regarding the circumstances under which and how a person, not being a member of the company can apply to the Tribunal to seek an order for conducting an investigation into the affairs of a company.

Answer

According to **Section 213(b)(i)** of the Companies Act, 2013, the Tribunal may, on filling of an application by any other person (not being a member of company) or otherwise, if the **Tribunal is satisfied that there are circumstances suggesting that the business of the company is being**

conducted with intent to defraud its creditors, members or any other person or otherwise for a fraudulent or unlawful purpose, or in a manner oppressive to any of its members or that the company was formed for any fraudulent or unlawful purpose, may order after giving a reasonable opportunity of being heard to the parties concerned, that the affairs of the company ought to be investigated by an inspector or inspectors appointed by the Central Government and where such an order is passed, the **Central Government shall appoint one or more competent persons as inspectors to investigate into the affairs of the company in respect of such matters and to report thereupon to it in such manner as the Central Government may direct.**

The creditors of NTY Ltd should be guided in terms of the provisions stated above.

Security for Payment of Costs and Expenses of Investigation (Section 214)

Question 9 ***(May 18)***

The business of Weak Fabrication Limited is conducted fraudulently and the management activities are not in the interests of the Company. The paid up capital of the company is One crore rupees. A group of shareholders numbering 110 members representing 1/9 of total voting power decided to approach Tribunal (NCL T) to carryout investigation into the Company's affairs under the provisions of the Companies Act, 2013. They seek your advice in the following matters, stating the relevant provisions of the Companies Act, 2013.

(1) Whether the group can make valid application?

(2) Other than member, can any other person make application?

(3) Are the applicants required to furnish security for payment of cost and expenses of Investigation?

Answer

(1) Whether the Group can make a valid application?

According to **Section 213(a)(i)** of the Companies Act, 2013, the Tribunal may **on an application made by not less than one hundred members or members holding not less than one-tenth of the total voting power**, in the case of a Company having a share capital, order, after giving a reasonable opportunity of being heard to the parties concerned, that the affairs of the company ought to be investigated by an inspector or inspectors appointed by the Central Government.

In the instant case, the **application by 110 members representing 1/9 of total voting power of Weak Fabrication Limited to carryout investigation into the company's affairs is valid.**

(2) Other than member, can any other member make an application?

According to **Section 213(b)(i)** of the Companies Act, 2013, the Tribunal may, **on filling of an application by other person** (not being a member of Company), if satisfied, that there are circumstances suggesting that the business of the Company is being conducted with **intent to defraud its creditors, members or any other person or otherwise for a fraudulent or unlawful purpose, or in a manner oppressive** to any of its members or that the Company was formed for any fraudulent or unlawful purpose, may order after giving a reasonable opportunity of being heard to the parties concerned, that the affairs of the Company ought to be investigated by an Inspector or Inspectors appointed by the Central Government and where such an Order is passed, the Central Government shall appoint one or more competent persons as Inspectors to investigate into the affairs of the Company in respect of such matters and to report thereupon to it in such manner as the Central Government may direct.

Thus, any other person (other than a member) can also make an application.

(3) Section 214 of the Companies Act, 2013 provides for security for payment of costs and expenses of investigation:

Where an investigation is ordered by the Central Government in pursuance of an order made by the Tribunal under Section 213, the Central Government may before appointing an Inspector under clause (b) of Section 213, **require the applicant to give such security not exceeding 25,000 rupees as may be prescribed, as it may think fit, for payment of the costs and expenses of the investigation.** Such security shall be refunded to the applicant if the investigation results in prosecution.

Protection of Employees during Investigation (Section 218)

Question 10 ***(May 17)***

Damage Ltd, the Company wanted to suspend Mr. Z, the CFO of the Company during the pendency of an investigation being conducted under the provisions of the Companies Act, 2013 on the order of Tribunal. The Company approached the Tribunal on 3rd January, 2017 for the proposed action. The Company on 15th February, 2017 passed an order of suspension without waiting for the orders from Tribunal. Comment upon the action taken by the Company with reference to the relevant provisions of the Act.

Answer

Section 218 of the Act deals with the Protection of Employees during Investigation and relevant provisions are as under:

(1) **Approval of tribunal to take action against the employee:** Notwithstanding anything contained in any other law for the time being in force, if –

(a) **during the course of any investigation of the affairs** and other matters of or relating to a company, other body corporate or person under **section 210, section 212, section 213 or section 219** or of the membership and other matters of or relating to a company, or the ownership of shares in or debentures of a company or body corporate, or the affairs and other matters of or relating to a company, other body corporate or person, under section 216; or

(b) **during the pendency of any proceeding** against any person concerned in the conduct and management of the affairs of a company under Chapter XVI, such company, other body corporate or person proposes –

- **to discharge or suspend any employee; or**
- **to punish him whether by dismissal, removal, reduction in rank or otherwise; or**
- **to change the terms of employment to his disadvantage the company,** other body corporate or person, as the case may be shall obtain approval of the Tribunal of the action proposed against the employee and if the Tribunal has any objection to the action proposed, it shall send by post notice thereof in writing to the company, other body corporate or person concerned.

(2) **Action against employee:** if the company, other body corporate or person concerned **does not receive within thirty days of making of application** under sub-section (1), the approval of the Tribunal, then the only then, the company, other body corporate or person concerned may proceed to take against the employee, the action proposed.

In the instant case, the action taken by Damage Ltd. to suspend Mr. Z, the CFO of the company is valid as the company approached the Tribunal on 3rd January, 2017 for the proposed action

and on 15th February, 2017 passed an order of suspension without waiting the orders from Tribunal (after 30 days of making the application)

Question 11 ***(Nov 17)***

Pursuant to Section 210 of the Companies Act, 2013 an Inspector was appointed to investigate the affairs of Sterling Trading Limited. Mr. Ahmed the General Manager (Operations) who is aware of certain misdeeds of the management, desires to know whether he is entitled to any protection against dismissal by the company if he discloses the misdeeds during the course of examination by the Inspector. Advise him explaining the relevant provisions of the Companies Act, 2013.

Answer

According to **Section 218** of the Companies Act, 2013, if during the course of any investigation of the affairs and other matters of or relating to a company under section 210, or during the pendency of any proceeding against any person concerned in the conduct and management of the affairs of a company under Chapter XVI, such company, other body corporate or person proposes—

(i) to discharge or suspend any employee; or

(ii) to punish him, whether by dismissal, removal, reduction in rank or otherwise; or

(iii) to change the terms of employment to his disadvantage,

the company, other body corporate or person, as the case may be, shall obtain approval of the Tribunal of the action proposed against the employee and if the Tribunal has any objection to the action proposed, it shall send by post notice thereof in writing to the company, other body corporate or person concerned.

Action against Employee: If the company, other body corporate or person concerned does not receive within thirty days of making of application under sub- section (1), the approval of the Tribunal, then and only then, the company, other body corporate or person concerned may proceed to take against the employee, the action proposed.

In the instant case, the above **mentioned protection is available to Mr. Ahmed, the General Manager of Sterling Trading Limited.**

Power of Inspector to conduct Investigation into affairs of related companies, etc. (Section 219)

Question 12

What are the circumstances in which an inspector appointed under section 210 of the Companies Act, 2013, can investigate into affairs of related companies also?

Answer

Investigation into affairs of related companies: According to **section 219** of the Companies Act, 2013, **if an inspector appointed under section 210 or section 212 or section 213 to investigate into the affairs of a company** considers it necessary for the purposes of the investigation, can also investigate the affairs of—

a) Any other body corporate which is, or has at any relevant time been the company's subsidiary company or holding company, or a subsidiary company of its holding company;

b) Any other body corporate which is, or has at any relevant time been managed by any person as managing director or as manager, who is, or was, at the relevant time, the managing director or the manager of the company;

c) Any other body corporate whose Board of Directors comprises nominees of the company or is accustomed to act in accordance with the directions or instructions of the company or any of its directors; or

d) Any person who is or has at any relevant time been the company's managing director or manager or employee.

Question 13 ***(RTP May 18)***

During investigations conducted on the affairs of a company in the public interest, the inspector observed that the Directors of the company had been acting on the instructions of the holding company and he proceeded to investigate the holding company. Is Inspector permitted to do under the provisions of the Companies Act, 2013?

Answer

i) **Investigation into affairs of related companies: Section 219** of the Companies Act, 2013, provides for power of Inspector to conduct investigation into the affairs of related companies etc., if an inspector appointed under section 210 or section 212 or section 213 to investigate into the affairs of a company considers it necessary for the purposes of the investigation, **to investigate also the affairs of: -**

a) any other body corporate which is, or has at any relevant time been the company's **subsidiary company or holding company, or a subsidiary company of its holding company**;

b) any other body corporate which is, or has at any relevant time been **managed by any person as managing director or as manager,** who is, or was, at the relevant time, the managing director or the manager of the company;

c) any other body corporate whose Board of Directors **comprises nominees of the company or is accustomed to act in accordance with the directions or instructions of the company or any of its directors; or**

d) any person who is or has at any relevant time been the **company's managing director or manager of employee, he shall, subject to the prior approval of the Central Government**, investigate into and report on the affairs of the other body corporate or of the managing director or manager, in so far as he considers that the results of his investigation are relevant to the investigation of the affairs of the company for which he is appointed.

Therefore, the inspector shall subject to the prior approval of the Central Government, investigate into and report on the affairs of the other body corporate or of the Managing Director or Manager, in so far as he considers that the results of his investigation are relevant to the investigation of the affairs of the Company for which he is appointed. In view of above, the Inspector is permitted to investigate the holding company.

Imposition of Restrictions upon Securities (Section 222)

Question 14 ***(Nov 17)***

Remedial Pharma Limited, over the years, enjoys a high reputation in the market and its general reserves are ten times more than the paid up capital of the company. There is a serious apprehension of cornering the share of the company by a group of unscrupulous persons likely to result in change in the Board of directors which may be prejudicial to the public interest. The company seeks your advice as to how it can block the transfer of shares of the company under the provisions of the Companies Act, 2013.

Answer

Where it appears to the NCLT, in connection with any investigation under **Section 216** of the Companies Act, 2013 or on a c**omplaint made by any person in this behalf that there is good reason to find out the relevant facts any securities issued or to be issued by the company and the Tribunal** is of the opinion that such facts cannot be found out unless certain restrictions as it may deem fit are imposed, the Tribunal may, by order, direct that the securities shall be subject to such restrictions as it may deem fit for such period not exceeding 3 years as be specified in the order.

Where securities in any company are issued or transferred or acted upon in contravention of an order of the Tribunal under sub section (1), the **company** shall be punishable with fine which shall **not less than one lakh rupees** but which **may extend to 25 lakh rupees** and every **officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 6 months or with fine which shall not be less than twenty five thousand rupees but which may extend to 5 lakh rupees or with both**. **[Section 222(2)]**

The facts given in the question squarely fall within the provision of Section 222 of the Companies Act, 2013. The management of Remedial Pharma Limited may make a complaint to the NCLT and convince that the transfer of shares in favour of the group of unscrupulous persons would change the composition of the Board of directors of the company which shall be prejudicial to the public interest and if the NCLT is convinced with the pleas of the company, it may pass an order as stated above which would block the transfer of shares as stated in the question.

Question 15 ***(Nov 18)***

The Central Government ordered an investigation under Section 216 of the Companies Act, 2013 against M/s Green Wood Limited for determining the true membership of the company. In connection with this investigation a reference was made to the Tribunal. It appears to the Tribunal that there is a good reason to find out the relevant facts about the equity shares with Differential Voting Rights (DVRs) issued by the company and the Tribunal is of the opinion that unless restrictions are imposed on further issue of such equity shares for two years, the purpose cannot be solved. Referring to the provisions of the Companies Act, 2013 and Rules framed in this regard, answer:

i) Can the Tribunal put such a restriction on further issue of shares?
ii) Period for which such a restriction can be imposed by the Tribunal?

Answer

Imposition of Restrictions upon Securities

Section 222 of the Companies Act, 2013, deals with the Imposition of Restrictions upon Securities. According to this section:

Where it appears to the Tribunal, in connection with any investigation under section 216 or on a complaint made by any person in this behalf, that there is good reason to find out the relevant facts about any securities issued or to be issued by a company and the Tribunal is of the opinion that such facts cannot be found out unless certain restrictions, as it may deem fit, are imposed, the Tribunal may, by order, direct that the securities shall be subject to such restrictions as it may deem fit for such period not exceeding three years as may be specified in the order.

In the light of the above provisions:

i) The Tribunal can put restriction on further issue of shares, in order to determine the true membership of the company.

ii) The Tribunal may impose such restrictions for such period as it may deem fit. However, such period shall not exceed three years.

Inspector's Report (Section 223)

Question 16

What are the duties of the inspector as enumerated in section 223 of the Companies Act, 2013, in relation to his report.

Answer

Section 223 of the Companies Act, 2013 deals with Inspector's report. The following provisions are applicable in respect of the Inspector's report on investigation:

i) **Submission of interim report and final report [Sub section (1)]:** An inspector appointed under this Chapter (Chapter XIV- Inspection, Inquiry and Investigation) may, and if so directed by the Central Government shall, submit interim reports to that Government, and on the conclusion of the investigation, shall submit a final report to the Central Government.

ii) **Report to be writing or printed [Sub section (2)]:** Every report made under sub section (1) above, shall be in writing or printed as the Central Government may direct.

iii) **Obtaining copy or report [Sub section (3)]:** A copy of the above report may be obtained by making an application in this regard to the Central Government.

iv) **Authentication of report [Sub section (4)]:** The report of any inspector appointed under this Chapter shall be authenticated either—

a) by the seal, if any, of the company whose affairs have been investigated; or

b) by a certificate of a public officer having the custody of the report, as provided under section 76 of the Indian Evidence Act, 1872, and such report shall be admissible in any legal proceeding as evidence in relation to any matter contained in the report.

v) **Exceptions:** Nothing in this section shall apply to the report referred to in section 212 of the Companies Act, 2013.

Voluntary Winding up of company, Etc. not to stop Investigation proceedings (Section 226)

Question 17

Decent Marbles Limited has been incurring business losses for past couple of years. The company, therefore, passed a special resolution for voluntary winding up. Meanwhile, complaints were made to the Tribunal and to the Central Government about foul play of the directors of the company, which adversely affected the interests of shareholders of the company as well as the public. In this situation advise whether investigation may be initiated against the company under the provisions of the Companies Act, 2013.

Answer

According to section 226 of the Companies Act, 2013, an investigation may be initiated notwithstanding, and no such investigation shall be stopped or suspended by reason only of, the fact that—

a) an application has been made under section 241;

b) the company has passed a special resolution for voluntary winding up; or

c) any other proceeding for the winding up of the company is pending before the Tribunal.

In the instant case, Decent Marbles Limited has been incurring business losses for past couple of years. The company passed a special resolution for voluntary winding up. Meanwhile complaints were made to the Tribunal and to the Central Government about foul play of the directors of the company, which adversely affected the interests of shareholders of the company as well as the public.

As, the company has passed a special resolution for voluntary winding up of the company, then also the investigation may be initiated against the company under section 226 of the Companies Act, 2013

Question 18 ***(RTP May 18)***

Origin paper Ltd. has been incurring business losses for past couple of years. The company therefore, passes a special resolution for voluntary winding up. Meanwhile, complaints were made to the tribunal and to the Central Government about foul play of the directors of the company, which adversely affected the interests of shareholders of the company as well as public. In this situation **advise** whether investigation may be initiated against the company under the provision of the Companies Act, 2013. Further **decide** whether application can be made to Tribunal for Relief in the above affairs of the company once the investigation is initiated against the company.

Answer

According to **section 226** of the Companies Act, 2013, an investigation may be initiated notwithstanding, and no such investigation shall be stopped or suspended by reason only of, the fact that—

i) an **application has been made under section 241;**

ii) the company has passed a **special resolution for voluntary winding up**; or

iii) any other **proceeding for the winding up of the company is pending before the Tribunal.**

In the instant case Origin Paper Ltd. has been incurring business losses for past couple of years. The company passed a special resolution for voluntary winding up. Meanwhile complaints were made to the Tribunal and to the Central Government about foul play of the directors of the company, which adversely affected the interests of shareholders of the company as well as the public.

As the company has passed a special resolution for voluntary winding up of the company, then also the investigation may be initiated against the company under section 226 of the Companies Act, 2013.

Yes as per the above provision, though investigation was initiated against the company, it shall not bar members to file an application to Tribunal for Relief under section 241 of the companies Act, 2013.

According to the said section, any member of a company may apply to the Tribunal for an order on the complains that—

i) the **affairs of the company have been or are being conducted in a manner prejudicial to public interest** or in a manner prejudicial or oppressive to him or any other member or members or in a manner prejudicial to the interests of the company; or

ii) the **material change taken place in the management or control of the company, whether by an alteration in the Board of Directors, or manager, or in the ownership of the company's shares**, or if it has no share capital, in its membership, or in any other manner whatsoever, and that by reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to its interests or its members or any class of members,

The Central Government, if it is of the opinion that the affairs of the company are being conducted

in a manner prejudicial to public interest, it may itself apply to the Tribunal for an order.

Where any members of a company are entitled to make an application, any one or more of them having obtained the consent in writing of the rest, may make the application on behalf and for the benefit of all of them.

Question 19 ***(Nov 17)***

M/s Genesis Paper Ltd. has been incurring business losses for past couple of years. The company, therefore, passed a special resolution for voluntary winding up. Meanwhile, complaints were made to the Tribunal and to the Central Government about foul play of the directors of the company, which adversely affected the interests of shareholders of the company as well as the public. In this situation advise whether investigation may be initiated against the company under the provisions of the Companies Act, 2013.

Answer

According to **section 226** of the Companies Act, 2013, an investigation may be initiated notwithstanding, and no such investigation shall be stopped or suspended by reason only of, the fact that—

(a) **an application has been made under section 241;**

(b) **the company has passed a special resolution for voluntary winding up;**

(c) **or any other proceeding for the winding up of the company is pending before the Tribunal.**

In the instant case, M/s Genesis Paper Ltd. has been incurring business losses for past couple of years. The company passed a special resolution for voluntary winding up. Meanwhile complaints were made to the Tribunal and to the Central Government about foul play of the directors of the company, which adversely affected the interests of shareholders of the company as well as the public.

As, the **company has passed a special resolution for voluntary winding up of the company, then also the investigation may be initiated against the company under section 226 of the Companies Act, 2013.**

Penalty for furnishing false statement, mutilation, destruction of documents (Section 226)

Question 20 ***(RTP May 19)***

Decide the liability of the person for commission of the act during the course of inspection, inquiry or investigation under the Companies Act, 2013:

i) A person who is required to make statement during the course of investigation pending against its company, is a party to the manipulation of documents related to the transfer of securities and naming of holders in the register of members by the company.

ii) An employee of the company publicized among his social networking of sound financial position of his organization in order to incite the public to purchase the shares of its company. In actuality, the company was running in loss.

Answer

Section 229 of the Companies Act, 2013 states that where a person who is required to provide an explanation or make a statement during the course of inspec tion, inquiry or investigation, or an officer or other employee of a company or other body corporate which is also under investigation,-

a) destroys, mutilates or falsifies, or conceals or tampers or unauthorisedly removes, or is a party to the destruction, mutilation or falsification or concealment or tampering or unauthorised removal

of, documents relating to the property, assets or affairs of the company or the body corporate;

b) makes, or is a party to the making of, a false entry in any document concerning the company or body corporate; or

c) provides an explanation which is false or which he knows to be false, -he shall be punishable for fraud in the manner as provided in section 447.

As per the above provision:

i) With respect to this part of the question, the person shall be liable for fraud. Since, in the given case, he is a party in the manipulation of documents relating to the transfer of securities and in the register of members of the company which is under investigation.

ii) Employee shall not be liable here, as the said company in which he is an employee, is not undergoing investigation. Secondly, the person purchasing the shares can act with due diligence before purchasing shares rather fully relying on the publicity made on social networking.

Ch 5 – Compromises, Arrangements & Amalgamations

Power to Compromise or make arrangements with creditors and Members (Section 230)

Question 1

A meeting of members of ABC Limited was convened under the orders of the Court to consider a scheme of compromise and arrangement. Notice of the meeting was sent in the prescribed manner to all the 600 members holding in the aggregate 25,00,000 shares. The meeting was attended by 450 members holding 15,00,000 shares. 210 members holding 11,00,000 shares voted in favor of the scheme. 180 members holding 3,00,000 shares voted against the scheme. The remaining members abstained from voting.

Examine with reference to the relevant provisions of the Companies Act, 2013 whether the scheme is approved by the requisite majority.

Answer

As per section 230 (6), of the Companies Act, 2013 where majority of persons at a meeting held **representing 3/4th in value,** voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and if such compromise or arrangement is sanctioned by the Tribunal by an order.

The majority of person representing 3/4th Value shall be counted of the following:

a) **The creditors, or**
b) **Class of creditors or**
c) **Members or**
d) **Class of members, as the case may be,**

The majority is dual, in number and in value. A simple majority of those voting is sufficient. **Whereas the 'three-fourths' requirement relates to value**. The three-fourths value is to be computed with reference to paid-up capital held by members present and voting at the meeting.

In this case out of 600 members, 450 members attended the meeting, but only 390 members voted at the meeting. As 210 members voted in favor of the scheme the requirement relating to majority in number (i.e. 196) is satisfied. 390 members who participated in the meeting held 14,00,000, three-fourth of which works out to 10,50,000 while 210 members who voted for the scheme held 11,00,000 shares. As both the requirements are fulfilled, the scheme is approved by the requisite majority.

Question 2

A meeting of members of DEF Limited was convened under the orders of the Court for the purpose of considering a scheme of compromise and arrangement. The meeting was attended by 300 members holding 9,00,000 shares. 120 members holding 7,00,000 shares in the aggregate voted for the scheme. 140 members holding 2,00,000 shares in aggregate voted against the scheme. 40 members holding 1,00,000 shares abstained from voting. Examine with reference to the relevant provisions of the Companies Act, 2013 whether the scheme was approved by the requisite majority?

Answer

As per **section 230 (6),**of the Companies Act, 2013 where majority of persons at a meeting held representing 3/4th in value, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and if such compromise or arrangement is sanctioned by the Tribunal by an order. The majority of person representing 3/4th Value shall be counted of the following:

a) **The creditors, or**
b) **Class of creditors or**
c) **Members or**
d) **Class of members, as the case may be,**

The majority is dual, in number and in value. A simple majority of those voting is sufficient. Whereas the **'three-fourths' requirement relates to value.** The three-fourths value is to be computed with reference to paid-up capital held by members present and voting at the meeting.

In this case 300 members attended the meeting, but only 260 members voted at the meeting. As 120 members voted in favor of the scheme the requirement relating to majority in number (i.e. 131) is not satisfied.

260 members who participated in the meeting held 9,00,000 shares, three-fourth of which works out to 6,75,000 while 120 members who voted for the scheme held 7,00,000 shares. The majority representing three-fourths in value is satisfied.

Thus, in the instant case, the scheme of compromise and arrangement of DEF Limited is not approved as though the value of shares voting in favor is significantly more, the number of members voting in favor do not exceed the number of members voting against.

Question 3

M/s Eternal Health Limited was facing acute financial difficulty as operations were continuously disrupted due to (a) non-availability of raw material (b) successive drought in its marketing areas and loss of demand and (c) frequent breakdown due to non- replacement of old plant and machinery. On the verge of liquidation, the Management proposes one last ARRANGEMENT between creditors and the company, whereby the creditors have to forego 50 % of their dues to the company. This has evoked strong protest from some of the creditors who may block the arrangement. You are requested to examine the arrangement in the light of the Companies Act, 1956 and advise the course of action/procedure to be adopted by the company to implement the same.

Answer

The Given problem relates to **section 230** of Companies Act, 2013, Section 230 contains the provisions with respect to the power of a company to compromise or to make arrangement with creditors and members.

The Steps to be taken by the directors / company for giving effect to the proposal scheme of compromise or arrangements are as under:

1. An application proposing a compromise or arrangement shall be made to the tribunal. Such application may be made by –
   a) **The Company or**
   b) **Any creditor of the company or**
   c) **Any member of the company or**
   d) **The liquidator**

2. All **Material facts** relating to the company shall be disclosed to the tribunal by way of an affidavit.
3. On receipt of an application proposing a compromise or arrangements, the **tribunal may order a meeting of the creditors and members.** The tribunal may dispense with calling of a meeting of creditors, if the **creditors having at least 90% in value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement.**
4. The notice of the meeting called by the tribunal shall be sent to all the creditor and members. The notice shall be accompanied by –
   a) **A statement disclosing the details of the compromise or arrangement**
   b) **A copy of the valuation report, if any**
   c) **A statement explaining the effect of the compromise or arrangement on the creditors, key managerial personnel, promoters and non – promoters members, debenture holders, directors, debenture trustees and**
   d) **A statement containing such other matters as may be prescribed.**
5. The notice of the meeting shall also be **issued by way of an advertisement.**
6. The notice of the meeting and other **documents shall be placed on the website** of the company, if any.
7. The notice of the meeting shall be **sent to the Securities and Exchange Board and Stock exchange,** in case of a listed company. Such notice shall be placed on the website of the Securities and Exchange Board of India and stock exchange.
8. The notice of the meeting shall disclose that the members and creditors may vote on the compromise or arrangement –
   a) **Either themselves or**
   b) **Through proxies or**
   c) **By postal ballot, within 1 month of receipt of such notice.**
9. Any objection to the compromise or arrangement may be made only by-
   a) **Persons holding not less than 10% of the shareholding** or
   b) **Person having outstanding debt amounting to not less than 5%** of the total outstanding debt as per the latest audited financial statement.
10. The notice of the meeting along with all the documents shall be sent to –
    a) **The central Government**
    b) **The Income tax authorities**
    c) **The Reserve Bank of India**
    d) **The Securities and Exchange board**
    e) **The Registrar**
    f) **The Respective Stock Exchanges**
    g) **The official Liquidator**
    h) **The competition commission of India, if necessary**
    i) **Such other sectoral regulators or authorities which are likely to be affected by the compromise or arrangement.**
11. All the above authorities shall have right to make their representations within a period of 30 days from the date of the receipt of such notice.
12. Where any representation made by any of the above authorities, the tribunal shall consider such

representation, but the **tribunal shall not be bound to accept such representation**.

13. The meeting shall be held and conducted as per the directions of the tribunal. If, at a meeting held in pursuance of order of the tribunal, m**ajority of persons representing 3/4th in value** of the creditors, or class of creditors or members or class of members, as the case may be, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement, the tribunal may, by an order, sanction the compromise or arrangement.
14. If a compromise or arrangement is **sanctioned by the tribunal, the same shall be binding on the company, all the creditors and members**.
15. The order made by the tribunal shall contain provisions with respect to variation of shareholders rights.
16. The order of the tribunal shall be filed with registrar by the **company within 30 days of the receipt of order.**

Question 4

A meeting of members of ABC Limited was convened as per the orders of the Court to consider a scheme of compromise and arrangement. Notice of the meeting was sent to 1000 members holding in aggregate 500000 equity shares. The meeting was attended by 800 members holding 350000 shares. 450 members holding 240000 shares voted in favour of the scheme; 200 members holding 60000 shares voted against the scheme. The remaining 150 members abstained from voting. Explain with reference to the provisions of the Companies Act, 2013, whether the scheme is approved by the requisite majority.

Answer

As per section 230 (6), of the Companies Act, 2013 where majority of persons at a meeting held representing 3/4th in value, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and if such compromise or arrangement is sanctioned by the Tribunal by an order. The majority of person representing 3/4th Value shall be counted of the following:

- the creditors, or
- class of creditors or
- members or
- class of members, as the case may be,

Usage of word "majority" in the provision is dual in nature i.e., may be taken into account in number & in value. A simple majority of those voting is sufficient. Whereas the 'three-fourths' requirement relates to value. The three-fourths value is to be computed with reference to paid-up capital held by members present and voting at the meeting.

In this case, out of 1000 members, 800 members attended the meeting and 450 members voted in favor of the scheme, thus, the requirement relating to majority in number (i.e. more than 325) is satisfied.

Further, as per the facts, total 650 members participated in the meeting holding 3,00,000 shares. According to the provision, three-fourth of which works out to 2,25,000, while 450 members who voted for the scheme held 2, 40,000 shares.

Hence, the requirements as to the holding of 3/4th values of shares as a majority is also met.
Therefore, the scheme is approved by the requisite majority.

Merger and Amalgamation of Companies (Section 232)

Question 5

Pioneer Textiles Limited desired to amalgamate its enterprise with Latex Textiles Limited. A scheme of amalgamation for this purpose was approved by an overwhelming majority of shareholders and all creditors of both companies at meetings held under the provisions of Section 232 of the Companies Act, 2013. Thereupon it was presented to the Company Law Tribunal for its sanction. While the scheme was pending in the Tribunal, some of the dissentient shareholders of Pioneer Textiles Limited requisitioned an extraordinary general meeting to negotiate with Latex Textiles Limited as according to the requisitionists the exchange ratio was not fair and reasonable.

Examine whether the directors may refuse to call the extraordinary general meeting. Also discuss the powers of the Tribunal in this respect.

Answer

According to **Section 235** of the Companies Act, 2013,

(1) Where a **scheme or contract involving the transfer of shares or any class of shares in a Company** (the "Transferor Company") **to another company** (the "Transferee Company") has, **within four months after making of an offer** in that behalf by the transferee company, been approved by the holders of not less than nine-tenths in value of the shares whose transfer is involved, other than shares already held at the date of the offer by, or by a nominee of the transferee company or its subsidiary Companies, the transferee Company may, at any time within two months after the expiry of the said four months, give notice in the prescribed manner to any dissenting shareholder that it desires to acquire his shares.

(2) Where a notice under sub-section (1) is given, the transferee Company shall, unless on an application made by the dissenting shareholder to the Tribunal, within one month from the date on which the notice was given and the Tribunal thinks fit to order otherwise, be entitled to and bound to acquire those shares on the terms on which, under the scheme or contract, the shares of the approving shareholders are to be transferred to the transferee Company.

According to Section 232(3) of the Companies Act, 2013, the Tribunal, after satisfying itself that the procedure specified in 232(1) and (2) has been complied with, may, by order, sanction the compromise or arrangement or by a subsequent order, make provision to be made for any persons who, within such time and in such manner as the Tribunal directs, dissent from the compromise or arrangement.

In the light of the above stated provisions,

a) **Once the scheme of amalgamation has been approved by an overwhelming majority**, transferee Company gets the right to give notice to any dissenting shareholder that it desires to acquire his shares. Further, as per the facts of the question, the **dissenting shareholders has not applied to the Tribunal against the scheme of amalgamation.**

   Hence, it is not mandatory for the directors to call the extraordinary general meeting.

b) According to Section 232(3) of the Companies Act, 2013, the Tribunal may make provision to be made for any persons who, within such time and in such manner as the Tribunal directs, dissent from the compromise or arrangement.

   [Note: It is assumed that overwhelming majority as specified in the question signifies approval by the holders of not less than nine-tenths in value of the shares (which is a pre- requisite to apply the provisions of section 235 of the Companies Act, 2013)].

Merger or Amalgamation of certain Companies (Section 233)

Question 6

ABC Limited is a wholly owned subsidiary company of XYZ Limited. The Company wants to make application for merger of Holding and Subsidiary Companies under Section 232. The Company Secretary of the XYZ Limited is of the opinion that company cannot apply for merger as per section 232. The company shall have to apply for merger as per section 233 i.e. Fast Track Merger. Is the contention of Company Secretary being valid as per law?

Answer

As per **section 233 (1),** notwithstanding the provisions of section 230 and section 232, a scheme of merger or amalgamation may be entered between,

a) **2 or more small companies**
b) **A holding company and its wholly-owned subsidiary company**. If 100% of its share capital is held by the holding company, except the shares held by the nominee or nominees to ensure that the number of members of subsidiary company is not reduced below the statutory limit as provided in section 187
c) **Such other class or classes of companies as may be prescribed.**

The provisions given for fast track merger in the **section 233** are in the optional nature and not a compulsion to the company. If a company wants to make application for merger as per section 232, it can do so.

Hence, here the **Company Secretary of the XYZ limited has erred in the law and his contention is not valid as per law**. The company shall have an option to choose between normal process of merger and fast track merger.

Merger or Amalgamation of company with foreign Company (Section 234)

Question 7

A Scheme provides amalgamation of PQL International Limited, a foreign company, with DHP limited, an Indian company registered under the companies Act, 2013. Referring to the provisions of the above Act, decide whether the scheme providing amalgamation of a foreign company as a transferor company can be sanctioned by the tribunal.

Answer

Section 234 of the Companies Act, 2013 is a specific provision with respect to merger or amalgamation of an Indian company and a foreign company may be effected by –

a) Complying with the provision of sections 230 to 232
b) Obtaining prior approval of Reserve Bank of India, and
c) Complying with the rules prescribed by the central government in this behalf

However, a merger of an Indian company and a foreign company may be effected only if the foreign company has been incorporated in the jurisdictions of any such country as has been notified by the Central Government in this behalf.

Also, the transferee company shall –

a) Ensure that **valuation is conducted by valuers** who are members of a recognized professional

body in the jurisdiction of the transferee company.

b) Ensure that **such valuation is in accordance with internationally accepted principles an accounting and valuation and**

c) File a declaration along with the application made to RBI for obtaining approval.

The Application for obtaining the approval of the tribunal as per the provisions of sections 230 to section 232 shall be filed after obtaining approval of RBI

For the purpose of Section 234, the term 'foreign company' means any company incorporated outside India, whether having place of business in India or not. Thus, where a company has not established any place of business in India and does not conducted any business activity in India, it is not a foreign company within the meaning of section 2(42), but it shall be regarded as a foreign company for the purpose of section 234. Thus, a merger or amalgamation between an Indian company and a company incorporated outside India is possible as per the provisions of section 234 read with sections 230 and 232, whether or not the company incorporated outside India has a place of Business in India, provided the legal requirements as discussed above are complied with.

Conclusion – The companies being amalgamated may or may not be companies registered in India.

Question 8

M/s. Unicorn Rubber Sheets Limited was incorporated and registered in the United Kingdom. M/s Artha Rubber Sheets Manufacturing and Trading Limited is an Indian Company incorporated and registered under the provisions of the Companies Act, 2013. A scheme of compromise between the above two companies provided for an amalgamation of the English Company with the Indian company. The CFO of the Indian Company is of the opinion that the companies being amalgamated must be companies registered in India and therefore an amalgamation with a company registered outside India is not possible. Explaining the relevant provisions of the Companies Act, 2013, examine the correctness or otherwise of the following with reference to a scheme of amalgamation of Companies:

i) Whether the contention of the CFO is correct that the companies being amalgamated must be Companies registered in India?

ii) What is the majority required for approving the scheme of amalgamation in a meeting of members of a company called as per the directions of the Tribunal? Is the scheme required to be approved by the preference shareholders?

Answer

i) As per **Section 234(3) of the Companies Act, 2013**, a foreign company, may with the prior approval of the Reserve Bank of India, merge into a Company registered under this Act or vice versa as per the scheme to be drawn up for the purpose.

Therefore, the **contention of CFO** of the M/s Artha Rubber Sheets Manufacturing and Trading Ltd. (Indian Company) is incorrect.

ii) According to **Section 230(3) of the Companies Act, 2013**, where a meeting is proposed to be called in pursuance of an order of the Tribunal, a notice of such meeting shall be sent to all the creditors / class of creditors and to all the members / class of members and the debenture-holders of the company.

Where, at a meeting, majority of persons representing three-fourths in value of the creditors, or class of creditors or members or class of members, as the case may be, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and if such compromise or arrangement is sanctioned by the Tribunal by an Order, the same shall be binding on the

Company, all the creditors, or class of creditors or members or class of members, as the case may be, or, in case of a Company being wound up, on the liquidator, and the contributories of the Company.

As the expression used is 'members', not only holders of equity shares but also preference shareholders will have to be taken into account or, if the meeting of holders of preference shares and equity shares are ordered by the tribunal to be held separately, the three-fourths majority of each class will have to be ascertained separately. Where the compromise or arrangement provides for conversion of preference shares into equity shares, such preference shareholders shall be given an option to either obtain arrears of dividend in cash or accept equity shares equal to the value of the dividend payable.

Power of Central Government to provide for Amalgamation of Companies in Public Interest (Section 237)

Question 9 ***(RTP Nov 18)***

Cotton On Yarn Ltd., and Country Cotton Blossom Ltd., are two listed companies engaged in the Business of Textiles. The companies are not making profits and as such their share's market price have gone down. A substantial portion of their share capital is held by Central Government as well as some Public Financial Corporations. In order to increase the share value, the Central Government wants to amalgamate the aforesaid two companies into a single company. Examine the powers of Central Government to amalgamate the two companies in public interest as per the provisions of the Companies Act, 2013

Answer

Central Government may by order provide for amalgamation in public interest.

According to Section 237 of the Companies Act, 2013, where the Central Government is satisfied that it is essential in the public interest that two or more companies should amalgamate, the Central Government, may, by order notified in the official gazette, provide for the amalgamation of those companies into a single company with such constitution, with such property, powers, rights, interests, authorities and privileges and with such liabilities, duties and obligations, as may be specified in the order.

Continuation by or against the transferee company of any legal proceedings

The order may also provide for the continuation by or against the transferee company of any legal proceedings pending by or against any transferor company and such consequential, incidental and supplemental provisions as may, in the opinion of the Central Government, be necessary to give effect to amalgamation.

Same interest rights or compensation

Every member or creditor including a debenture holder of each of the transferor companies before the amalgamation shall have, as nearly as may be, the same in terest in or rights against the transferee company as he had in the company of which he was originally a member or creditor and in case the interest or rights of such member or creditor in or against the transferee company are less than the interest in or rights against the original company, he shall be entitled to compensation to that extent, which shall be assessed by such authority as may be prescribed and every such assessment shall be published in the official gazette and the compensation so assessed shall be paid to the member or creditor concerned by the transferee company.

Preservation of books and papers of Amalgamated companies (Section 239)

Question 10 ***(May 18)***

CPR Ltd. and TJC Ltd. are wholly owned by Government of Tamil Nadu. As a policy matter, the Government issued administrative orders for merging TJC Ltd. with CPR Ltd. in the public interest. State the authority with whom the application for merger is required to be filed under the provisions of the Companies Act" 2013. Also state the provisions governing the preservation of Books and Records of TJC Ltd. after merger under the said Act.

Answer

Authority to whom the application for merger is to be made

According to Section 237 of the Companies Act, 2013, where the Central Government is satisfied that it is essential in the public interest that two or more companies should amalgamate, the Central Government may, by order notified in the Official Gazette, provide for the amalgamation of those companies into a single company.

Thus, In the given situation of merger between two wholly owned Government companies in public interest, there is no specific authority with whom the application for merger is required as the Central Government shall by notification in the Official Gazette, will provide for the amalgamation of the two said companies into a single company.

Preservation of books and records of amalgamated companies

According to Section 239 of the Companies Act, 2013, the books and papers of a Company which has been amalgamated with, or whose shares have been acquired by, another Company shall not be disposed of without the prior permission of the Central Government and before granting such permission, that Government may appoint a person to examine the books and papers or any of them for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion or formation, or the management of the affairs, of the transferor company or its amalgamation or the acquisition of its shares.

Ch 6 – Prevention of Oppression and Mismanagement

Application to Tribunal for Relief in cases of Oppression, Etc. (Section 241)

Question 1 ***(May 2017)***

A group of shareholders holding 20% of the issued share capital of DEF Limited have filed a petition before the Tribunal alleging the following:

i) Various acts of illegal, invalid and irregular transactions entered into the name of the company.

ii) Losses incurred due to mismanagement by the board of directors.

iii) Non-declaration of dividend despite having sufficient profits in the past years.

Examine the merits of the above petitions made under Section 241 of the Companies Act, 2013 in the light of the judicial pronouncements made in this regard.

Answer

According to **Sections 244** of the Companies Act, 2013, a group of shareholders of DEF Limited **must hold atleast 10% of the issued share capital of the Company or satisfy other requirements under section 244 of the Companies Act, 2013**. Since the group holds 20% of the issued share capital they are entitled to file a petition beforethe Tribunal under Section 241 of the Companies Act, 2013 by alleging that the affairs of the Company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members of the Company. However, on the basis of Sheth Mohanlal Ganpatram vs. Shri Sayaji Jubilee Cotton and Jute Mills Company Ltd., mere illegal, invalid or irregular transactions entered into in the name of the company do not constitute a ground for invoking the provisions of section 241 unless it is proved that they are oppressive to any shareholder or prejudicial to the interest of the company or to the public interest.

Similarly, **losses incurred due to mismanagement by the board of directors, cannot, by itself, be regarded as oppression** (Ashok Betelnut Co. P. Ltd. vs. M.L. Chandrakanth).

Also, **failure to declare dividends or payment of low dividends also does not amount to oppression.** (Thomas Veddon V.J. vs. Kuttanad Robber Co. Ltd.).

Thus, in the present case, the **petition filed by the group of shareholders will fail unless they can prove to the satisfaction of the Tribunal that the acts complained of in the petition are oppressive and prejudicial to the interest of the company and the public interest.**

Powers of Tribunal (Section 242)

Question 2

ABC limited used the business resources of the company in favour of the majority shareholders and completely excluded the minorities from the affairs of the company. As of consequences, minority members filed an application to Tribunal to look into the matter on the regulation of conduct of affairs of the company in future. State in the light of the Companies Act, 2013,the action to be taken by the Tribunal in the given situation.

Answer

The given problem is based on the section 242 of the Companies Act, 2013 which deals with the powers of the Tribunal. According to the given provision if, on any application made under section

241, the Tribunal is of the opinion that the company's affairs have been or are being conducted in a manner prejudicial or oppressive to any member or members or prejudicial to public interest or in a manner prejudicial to the interests of the company, with a view to bringing to an end the matters **complained of the Tribunal may, on the application of any party to the proceeding, make any interim order which it thinks fit for regulating the conduct of the company's affairs upon such terms and conditions as appear to it to be just and equitable as per the section 241(4) of the Companies Act, 2013.**

Tribunal may on application of the minorities make any interim order of appointment of administrator/officer for overseeing the affairs of the company made on the application that established prima facie the fact that business resources of the company were being used only for the **benefit of the majority shareholders and the minority shareholder was totally excluded from the affairs of the company.**

Right to apply under section 241 (Section 244)

Question 3

What is meant by oppression'? State whether the aggrieved party would succeed in obtaining relief from Tribunal on the ground of oppression in the following cases:

i) The majority of the Board of directors override the minority directors and the minority directors apply to Tribunal complaining oppression by majority directors.

ii) A petition by majority shareholders complaining oppression by minority shareholders. Give your answer according to the provisions of the Companies Act, 2013.

Answer

Oppression: Oppression, according to the Dictionary meaning of the word, is any act exercised in a manner burdensome, harsh and wrongful. The meaning of the term 'oppression' was explained by Lord Cooper in the Scottish case of Elder v. Elder and Watson Ltd, as given below:

"**The conduct complained of should be at the lowest involve a feasible departure from the standards of fair dealing and the violation of the conditions of fair play on which every shareholder entrusting his money to the company is entitled to rely**.

i) **Oppression of a member as a director**: The oppression dealt with by **section 241** of the Companies Act, 2013, is only oppresinvolve section 241. The harsh treatment, for instance, of a member who is a director or other officer or employee, by the Board of directors or management does not come within section 241. It has been held in Re. Bellador Silk Ltd. that if the majority of the Board of directors override the minority directors the lattersion of members in their character as such; and it is only in that character they can cannot resort to section 241 and **hence the minority directors will not succeed in getting relief from Tribunal on the ground of oppression**.

ii) **Right not confined to minority**: According to **section 244**, the right to apply for relief under section 241/242 is given to **100 members or 1/10th of the total number of members** or any member or members holding **not less than 1/10th of the issued share capital** of the company. There is nothing in this section which suggests even indirectly that unless the application is made by minority shareholders it is not maintainable. The right to apply is, therefore, not confined to oppressed minority of the shareholders alone. It was held by Calcutta High Court in

Re. Sindhri Iron Foundry (P) Ltd. that the oppressed majority also might apply for relief under section 241. **Therefore, the petitioners are likely to succeed in getting relief provided the other condition laid down in section 242** (i.e. that to wind up the company would unfairly prejudice such members, but that otherwise the facts would justify the making of a winding-up order on just and equitable ground) is satisfied, even though the Delhi High Court held a contrary view in Suresh Kumar Sanghi v. Supreme Motors Ltd.

Question 4

ABC Private Limited is a company in which there are eight shareholders. Can a member holding less than one-tenth of the share capital of the company apply to the Tribunal for relief against oppression and mismanagement? Give your answer according to the provisions of the Companies Act, 2013.

Answer

Under **section 244** of the Companies Act, 2013, in the case of a company having share capital, the following member(s) have the right to apply to the Tribunal under section 241:

a) **Not less than 100 members of the company** or **not less than one-tenth of the total number of members, whichever is less**; or

b) Any **member or members holding not less than one-tenth of the issued share capital of the company** provided the applicant(s) have paid all the calls and other sums due on the shares.

In the given case, since there are eight shareholders. As per the condition (a) above, 10% of 8 i.e. 1 satisfies the condition. Therefore, a single member can present a petition to the Tribunal, regardless of the fact that he holds less then one-tenth of the company's share capital.

Question 5 ***(RTP May 2018)***

The issued and paid up capital of MNC Limited is ₹ 5 crores consisting of 5,00,000 equity shares of Rs. 100 each. The said company has 500 members. A petition was submitted before the Tribunal signed by 80 members holding 10,000 equity shares of the company for the purpose of relief against oppression and mismanagement by the majority shareholders. Examining the provisions of the Companies Act, 2013, decide whether the said petition is maintainable. Also explain the impact on the maintainability of the above petition, if subsequently 40 members, who had signed the petition, withdrew their consent.

Answer

Right to apply for oppression and mismanagement: As per the provisions of Section 244 of the Companies Act, 2013, in the case of a company having share capital, members eligible to apply for oppression and mismanagement shall be lowest of the following:

100 members; or

1/10th of the total number of members; or

Members holding not less than 1/10th of the issued share capital of the company.

The share holding pattern of MNC Limited is given as follows:

₹ 5,00,00,000 equity share capital held by 500 members.

The petition alleging oppression and mismanagement has been made by some members as follows:

i) No. of members making the petition – 80

ii) Amount of share capital held by members making the petition – ₹ 10,00,000 The petition shall be

valid if it has been made by the lowest of the following :

100 members; or

50 members (being 1/10th of 500); or

Members holding ₹ 50,00,000 share capital (being 1/10th of ₹ 5,00,00,000)

As it is evident, the petition made by 80 members meets the eligibility criteria specified under section 244 of the Companies Act, 2013 as it exceeds the minimum requirement of 50 members in this case. Therefore, the petition is maintainable.

The consent to be given by a shareholder is reckoned at the beginning of the proceedings. The withdrawal of consent by any shareholder during the course of proceedings shall not affect the maintainability of the petition [Rajamundhry Electric Corporation Vs. V. Nageswar Rao A.I.R. (1956) Sc. 2013.]

Question 6

A group of members of XYZ Limited has filed a petition before the Tribunal alleging various acts of oppression and mismanagement by the majority shareholders of the company. The Petitioner group holds 12% of the issued share capital of the company. During the pendancy of the petition, some of the petitioner group holding about 5% of the issued share capital of the company wish to disassociate themselves from the petition and they along with the other majority shareholders have submitted before the Tribunal that the petition may be dismissed on the ground of non-maintainability. Examine their contention having regard to the provisions of the Companies Act, 2013.

Answer

The argument of the majority shareholders that the petition may be dismissed on the ground of non-maintability is not correct. The proceedings shall continue irrespective of withdrawl of consent by some petitioners. It has been held by the Supreme Court in Rajmundhry Electric Corporation vs. V. Nageswar Rao, AIR (1956) SC 213 that if some of the consenting members have subsequent to the presentation of the petition withdraw their consent, it would not affect the right of the applicant to proceed with the petition. **Thus, the validity of the petition must be judged on the facts as they were at the time of presentation**. Neither the right of the applicants to proceed with the petition nor the jurisdiction of Tribunal to dispose it of on its merits can be affected by events happening subsequent to the presentation of the petition.

Question 7

A group of shareholders consisting of 25 members decide to file a petition before the Tribunal for relief against oppression and mismanagement by the Board of Directors of M/s Fly By Night Operators Ltd. The company has a total of 300 members and the group of 25 members holds one – tenth of the total paid –up share capital accounting for one-fifteenth of the issued share capital. The main grievance of the group is the due to mismanagement by the board of directors, the company is incurring losses and the company has not declared any dividends even when profits were available in the past years for declaration of dividend. In the light of the provisions of the Companies Act, 2013, advise the group of shareholders regarding the success of (i) getting the petition admitted and (ii) obtaining relief from the Tribunal.

Answer

Section 244 of the Companies Act, 2013 provides the right to apply to the Tribunal for relief against

oppression and mis-management. This right is available only when the petitioners hold the prescribed limit of shares as indicated below:

i) In the case of company having a share capital, **not less than 100 members of the Company or not less than one tenth of the total number of its members whichever is less** or any member or members holding not less than one tenth of the issued share capital of the company, provided that the applicant(s) have paid all calls and other dues on the shares.

ii) In the case of company not having share capital, **not less than one-fifth of the total number of its members.**

Since the group of shareholders do not number 100 or hold $1/10^{th}$ of the issued share capital or constitute $1/10^{th}$ of the total number of members, they have no right to approach the Tribunal for relief.

However, the Tribunal may, on an application made to it waive all or any of the requirements specified in (i) or (ii) so as to enable the members to apply under section 241.

As regards obtaining relief from Tribunal, continuous losses cannot, by itself, be regarded as oppression (Ashok Betelnut Co. P. Ltd. vs. M.K. Chandrakanth).

Similarly, failure to declare dividends or payment of low dividends also does not amount to oppression. (Thomas Veddon V.J. (v) Kuttanad Robber Co. Ltd).

Thus the shareholders may not succeed in getting any relief from Tribunal.

Question 8

Examine the merits of the following petitions made under Sections 241 of the Companies Act, 2013 in the light of judicial pronouncements made in this regard:

A group of shareholders holding 12% of the issued share capital of Unique Products Limited have filed a petition before the Tribunal alleging various acts of illegal, invalid and irregular transactions entered into in the name of the Company.

Answer

According to Sections 244 of the Companies Act, 2013, a group of shareholders of Unique Products Limited **must hold atleast 10% of the issued share capital of the Company** or satisfy other requirements under section 244 of the Companies Act, 2013. Since the group holds 12% of the issue capital they are entitled to file a petition before the Tribunal under 241 of the Companies Act, 2013 by alleging that the affairs of the Company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members of the Company. However, on the basis of Sheth Mohanlal Ganpatram V. Shri Sayaji Jubilee Colton and Jute Mills Company Ltd., **mere illegal, invalid or irregular transactions entered into in the name of the company do not constitute a ground for invoking the provisions of section 241 unless it is proved that they are oppressive to any shareholder or prejudicial to the interest of the company or to the public interest.**

Thus, in the present case, the **petition filed by the group of shareholders will fail unless they can prove to the satisfaction of the Tribunal that the acts complained of in the petition are oppressive and prejudicial to the interest of the company and the public interest**. And that to wind up the company would unfairly prejudice such member or members, but that otherwise those facts would justify the making of a winding up order on the ground that it was just and equitable that the Company should be wound up.

Class Action (Section 245)

Question 9 ***(RTP Nov 18)***

A group of depositors in M/s. Bright Limited, a listed company, appointed Mr. Fair, an advocate as a representative to file an application in the National Company Law Tribunal (NCLT) on the behalf of the depositors to bring a Class Action suit against the management of the company as they are of the opinion that the management and conduct of affairs of the company are being conducted in a manner which is prejudicial to the interest of the depositors being oppressive.

Examine in the given situation, whether the appointment of Mr. Fair is valid as regards to the filling of the application before the Tribunal in the light to the provisions of the Companies Act, 2013?

Answer

In the given instance, an appointment of Mr. Fair was made by a group of depositors of M/s. Bright Limited (listed company), as their representative to bring a Class Action Suit against the management of the Company.

The given problem will be dealt with **Section 432** read with the **245(10)** of the Companies Act, 2013. Section 432 states that a **party to any proceeding or appeal before the Tribunal or Appellate Tribunal as the case may be, may appear in person or authorize one or more Chartered Accountant or Company Secretaries or Cost Accountants or legal practioners or any other person to present his case before the Tribunal or Appellate Tribunal as the case may be.**

Whereas, **Section 245(10)** of the Companies Act, 2013, provides that an application may be filed or any other action may be taken under this section by any person, group of persons or any association of persons representing the persons affected by any ac t or omission, specified in section 245(1) subject to the compliances of this section .

In view of the above, the appointment of Mr . Fair is valid and an application of Mr. Fair who is a **representative of depositors, will be admitted by the Hon'ble Tribunal, provided, the requirement of minimum number of members filing the application under Section 245(3)(ii) is fulfilled.**

Question 10 ***(May 18)***

M/s Sunshine Oils Limited, a listed company as at 31st March, 2018 as per the audited financial statements is having 200 depositors with ₹ 50 Crores of deposit in the company. Out of the total 200 depositors 20 depositors of the company have formed a group and have appointed Mr. Ram (a practicing advocate who is not one of the depositor) as their representative to file an application in the National Company Law Tribunal (NCLT) to bring a Class Action suit against the management of the company as they are of the opinion that the management and conduct of affairs of the company are being conducted in a manner which is prejudicial to the interest of the depositors being oppressive. Will the application of Mr. Ram be admitted by the Honourable Tribunal. Discuss with reference to the provisions of the Companies Act, 2013?

Answer

M/s. Sunshine Oils Limited, a listed company as at 31st March, 2018, as per the audited financial statements is having 200 depositors with ₹ 50 crores of deposit in the company. Out of total 200 depositors, 20 depositors of the company have formed a group and have appointed Mr. Ram (a practising Advocate who is not one of the depositors) as their representative. To bring a class action suit against the management of the Company.

Section 245(3)(ii) of the Companies Act, 2013 prescribes that the **requisite number of depositors to file an application shall not be less than 100 depositors or not less than such percentage of the**

total number of depositors as may be prescribed, whichever is less. However, Section 245(3)(ii) of the Companies Act, 2013 is silent regarding the minimum percentage of the depositors and no Rules have been prescribed till date.

Further, as per Section 432, a party to any proceeding or appeal before the Tribunal or Appellate Tribunal as the case may be, **may appear in person or authorize one or more Chartered Accountant or Company Secretaries or Cost Accountants or legal practioners or any other person to present his case before the Tribunal or Appellate Tribunal as the case may be**.

Section 245(10) states that subject to the compliances of this section, an application may be filed or any other action may be taken under this section by any person, group of persons or any association of persons representing the persons affected by any act or omission, specified in sub-section(1). In view of the above, the application of **Mr. Ram who is a representative of depositors will be admitted by the Hon'ble Tribunal, provided, the requirement of minimum number of members filing the application under Section 245(3)(ii) is fulfilled.**

Question 11 ***(Nov 2018)***

M/s DJ Limited, a listed company, as per the audited financial statements as at March 31, 2018 is having issued and paid-up equity share capital comprising of ₹ 10 Lakhs shares of ₹ 10 each and issued and paid-up preference share capital of ₹ 5 Lakhs shares of ₹ 10 each respectively. The members of the company after complying with the provisions of Section 169 of the Companies Act, 2013 removed one Mr. Satish from the directorship of the company on 1st August 2018 before the completion of his term of office. Mr. Satish is also one of the members of the company holding 110000 fully paid- up equity shares. Mr. Satish has alleged oppression on his removal and has moved the jurisdictional Honourable National Company Law Tribunal (NCLT) under Section 241 read with Section 244 of the Companies Act, 2013. The Board of Directors of the company is of the opinion that the application is not maintainable as per the provisions of Section 244 of the Companies Act, 2013. Decide.

Also, state if any other recourse that is available with Mr. Satish under the provisions of the Companies Act, 2013.

Answer

According to section 244(1)(a) of the Companies Act, 2013, the following members of a company shall have the right to apply under section 241, namely:—

in the case of a company having a share capital, not less than one hundred members of the company or not less than one-tenth of the total number of its members, whichever is less, or any member or members holding not less than one-tenth of the issued share capital of the company, subject to the condition that the applicant or applicants has or have paid all calls and other sums due on his or their shares.

However, the Tribunal may, on an application made to it in this behalf, waive all or any of the requirements specified above so as to enable the members to apply under section 241.

In the instant case, the equity share capital of the company is ₹ 1 crore (10 lakh shares of ₹ 10 each) and preference share capital is ₹ 50 Lakh (5 lakh shares of ₹ 10 each). The total issued and paid up share capital is ₹ 1.50 crore comprising of 15 lakh shares.

Mr. Satish is holding 110000 fully paid up equity shares. His holding is less than one- tenth of the issued share capital of the company [1/10th of 15 Lakhs i.e. 150000 shares].

Hence, his application is not maintainable as per provisions of section 244 of the Companies Act, 2013 and therefore the opinion of Board of directors is correct.

However, as per proviso to section 244(1), Mr. Satish may make an application to the Tribunal in this behalf for the waiver of the above condition so that he may apply under section 241.

Question 12 ***(Nov 2018)***

MNC Private Ltd. is a Company in which there are six shareholders. Mr. Srinath, who is a director and also the legal representative of a deceased shareholder holding less than one tenth of the share capital the Company made a petition to the Tribunal for relief against oppression and mismanagement. Examine under the provisions of the Companies Act, 2013 whether the petition made by Mr. Srinath valid and maintainable?

Answer

i) According to section 244 of the Companies Act, 2013, in the case of a company having share capital, the following member(s) have the right to apply to the Tribunal under section 241:

   a) Not less than 100 members of the company or not less than one-tenth of the total number of members, whichever is less; or
   b) Any member or members holding not less than one-tenth of the issued share capital of the company provided the applicant(s) have paid all the calls and other sums due on the shares.

ii) Legal heir of the deceased shareholder with minority status is entitled to file the petition.

In the given case, there are six shareholders. As per the condition (a) above, 10% of 6 i.e. 1 (round off 0.6) satisfies the condition. Therefore, in the light of the provisions of the Act, a single member (even the legal representative of a deceased shareholder) can present a petition to the Tribunal, regardless of the fact that he holds less than one-tenth of the company's share capital.

Thus, the petition made by Mr. Srinath is valid and maintainable.

Ch 7 – Winding Up

Circumstances in which company may be wound up (Section 271)

Question 1

Under what circumstances shall it be deemed that the substratum of a company has gone? A company has ceased to carry on two of the ten business stated as the main objects of the company. Examine whether the company can be wound up on the ground that substratum of the company is gone.

Answer

Circumstances in which loss of substratum is deemed

Substratum is the purpose or the main object, for which the company was formed. If the company has abandoned all of its main objects and not merely some of them, or if it cannot achieve any of its main objects, its substratum has gone and will be wound up by the tribunal.

The substratum of a company is deemed to have disappeared or gone, if the main objects for which the company was formed has become impracticable, i.e. permanently impracticable. Usual tests for determining whether the substratum of the company has disappeared are whether:

a) **The subject matter of the company is gone or**
b) **The object for which it was formed has substantially failed or**
c) **It is impossible to carry on the business of the company except at a loss, which means there is no reasonable hope that the object of trading at a profit can be attained, or**
d) **The existing and probable assets are insufficient to meet the existing liabilities.**

Powers of Tribunal (Section 273)

Question 2

LED Bulb Ltd., has made default in filing financial statements and annual returns for a continuous period of 4 financial years ending on 31st March, 2017. The Registrar of Companies having jurisdiction approached the Central Government to accord sanction to present a petition to Tribunal (NCLT) for the winding up of the company on the above ground under Section 272 of the Companies Act, 2013

Examine the validity of the ROC move, explaining the relevant provisions of the Companies Act, 2013. State the time limit for passing an order by the Tribunal under Section ·273 of the Companies Act, 2013?

Answer

Validity of ROC's action

According to **Section 271(d)** of the Companies Act, 2013, a Company may, on a petition under Section 272, be wound up by the Tribunal, 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.**

In the instant case, the move by ROC to present a petition to Tribunal for the winding up of LED Bulb Ltd. is not valid as the Company has made default in filing financial statements and annual returns for a continuous period of 4 financial years ending on 31st March, 2017.

Time limit for passing of an Order under section 273: An order under section 273 of the Act shall be

made within ninety days from the date of presentation of the petition.

Powers of Tribunal (Section 285)

Question 3

Define "contributory" in a winding up. Explain the liabilities of contributories as present and past member.

Answer

Meaning of Contributory:

Clause 26 of section 2 of the Companies Act, 2013 defines **contributory as a person liable to contribute towards the assets of the company in the event of its being wound up.**

A person holding fully paid – up shares in a company shall be considered as a contributory but shall have no liabilities of a contributory under the Act whilst retaining rights of such a contributory.

Liabilities of contributories as present and past member:

As per section 285 of Companies Act, 2013, While settling the list of contributories, the Tribunal shall include every person, who is or has been a member, who shall be liable to contribute to the assets of the company an amount sufficient for payment of the debts and liabilities and the costs, charges and expenses of winding up, and for the adjustment of the rights of the contributories among themselves, subject to the following conditions, namely:—

a) a person who has been a member shall not be liable to contribute if he has ceased to be a member for the **preceding one year or more before the commencement of the winding up**;

b) a person who has been a member shall **not be liable to contribute in respect of any debt or liability of the company contracted after he ceased to be a member;**

c) no person who has been a member shall be liable to contribute unless it appears to the Tribunal that the present members are unable to **satisfy the contributions required to be made by them in pursuance of this Act;**

d) in the case of a company limited by shares, **no contribution shall be required from any person, who is or has been a member exceeding the amount, if any, unpaid on the shares in respect of which he is liable as such member;**

e) in the case of a company limited by guarantee, **no contribution shall be required from any person, who is or has been a member exceeding the amount undertaken to be contributed by him to the assets of the company in the event of its being wound up but if the company has a share capital,** such member shall be liable to contribute to the extent of any sum unpaid on any shares held by him as if the company were a company limited by shares.

Question 4 ***(Nov 18, RTP May 19)***

M/s, IJK Limited was wound up with effect from 15th March 2018 by an order of the Court. Mr. A, who ceased to be a member of the company from 1st June 2017, has received a notice from the liquidator that he should deposit a sum of ₹ 5,000 as his contribution towards the liability on the shares previously held by him. In this context explain whether Mr. A can be called as a contributory, whether he can be made liable and whether there is any limitation on his liability.

Answer

Contributory: According to section 285 of the Companies Act, 2013, as soon as may be after the passing of a winding up order by the Tribunal, the Tribunal shall settle a list of contributories.

While settling the list of contributories, the Tribunal shall include every person, who is or has been a member, who shall be liable to contribute to the assets of the company an amount sufficient for payment of the debts and liabilities and the costs, charges and expenses of winding up, and for the adjustment of the rights of the contributories among themselves.

Liability of the contributory: A person who has been a member shall not be liable to contribute if he has ceased to be a member for the preceding one year or more before the commencement of the winding up. In the given case, M/s, IJK Ltd. was wound up on 15th March 2018. Whereas Mr. A ceased to be a member of the company from 1st June, 2017. So, according to the above provision, Mr. A will be a contributory and be liable to contribute as the time period of one year from the commencement of winding up has not elapsed. So, Mr. A is liable to deposit ₹ 5000 (if any unpaid on the shares in respect of which he is liable as member [Section 285 (3) (d)] as his contribution towards the liability on the shares previously held by him.

Arrest of Person trying to leave India or Abscond (Section 301)

Question 5

Info-tech Overtrading Ltd. was ordered to be compulsory wound up by an order dated 10th March, 2019 by the Tribunal. The official liquidator who has taken control of the assets and other records of the company has noticed that:

i) One of the contributory whose calls are pending to be paid is about to leave India for evading payment of calls and;

ii) A person having books of accounts of the company his possession may abscond to avoid examination of books of accounts in respect of the affairs of the company.

Apprehending such possibilities, Tribunal detained such contributory for next 6 month disallowing him to leave India as well as arrest & seized books of accounts from the person which may possibly abscond to avoid examination of the affairs of the company.
Referring to the provisions of Companies Act, 2013, answer the following in current scenario:

i) What is the validity of Tribunal's order for detention of contributory disallowing him to leave India?

ii) Is it correct from Tribunal's part to arrest and seize books of accounts from the person planning to abscond to avoid examination of books of accounts in respect of the affairs of the company?

Answer

According to section 301 of the Companies Act, 2013, at any time either before or after passing a winding up order, if the Tribunal is satisfied that

- a contributory or
- a person having property, accounts or papers of the company in his possession

is about to leave India or otherwise to abscond, or is about to remove or conceal any of his property, for the purpose of evading payment of calls or of avoiding examination respecting the affairs of the company, the Tribunal may cause—

a) the contributory to be detained until such time as the Tribunal may order; and
b) his books and papers and movable property to be seized and safely kept until such time as the Tribunal may order.

In the instant case, by taking into account the above provisions:

i) The Tribunal's order for detention of contributory for next 6 months disallowing him to leave

India, is valid.

ii) It is correct from Tribunal's part to arrest and seize books of accounts from the person planning to abscond to avoid examination of books of accounts in respect of the affairs of the company.

Overriding Preferential Payment (Section 326)

Question 6

M/s Raman Ltd. was wound up by the Tribunal. The company liquidator invited claims from its creditors which stood as under:

	₹
Income Tax dues	11 Lakh
Sales tax dues	5 Lakh
Dues of workers	25 Lakh
Unsecured loans payable to directors	25 Lakh
Trade creditors who supplied raw material	15 Lakh
Secured creditor being the bankers of the company	75 Lakh
	156 Lakh

Company liquidator could realize only ₹ 80 Lakhs by sale of assets and realization made from the company's debtors, which is not sufficient to pay to all the creditors. Please decide the order of priority for payment to creditors explaining the relevant provisions of the Companies Act, 2013.

Answer

Computation of amount likely to get by creditors

As the amount available for distribution falls short of dues of workmen and secured creditors, and workmen.

Proviso to section 325 provides that the security of every secured creditor shall be deemed to be subject to a pari passu charge in favour of the workmen to the extent of the workmen's portion therein.

Workmen's portion, in relation to the security of any secured creditor of a company, means the amount which bears to the value of the security the same proportion as the amount of the debts due to the secured creditors.

Workman's Share to Secured assets = Amount Realized * Workman's Dues / Workman's Dues + Secured Loan

Workman's Share to Secured Asset = $\frac{80,00,000 * 25,00,000}{25,00,000 + 75,00,000}$

Workman's Share to Secured Assets = 20,00,000

Amount available to secured creditor is ₹ 80 Lakhs – ₹ 20 Lakhs = ₹ 60 Lakhs
Hence, no amount is available for payment of government dues and unsecured creditors.

Question 7

XYZ Limited is being would up by the tribunal. All the assets of the company have been charged to the company's bankers to whom the company owes ₹ 5 crores. The company owes following amounts to others:

- Dues to workers – ₹ 1,25,00,000
- Taxes Payable to Government – ₹ 30,00,000
- Unsecured Creditors – ₹ 60,00,000

You are required to compute with the reference to the provision of the Companies Act, 2013 the amount each kind of creditors is likely to get if the amount realized by the official liquidator from the secured assets and available for distribution among creditors is only ₹ 4,00,00,000/-

Answer

Section 326 of the Companies Act, 2013 is talks about the overriding preferential payments to be made from the amount realized from the assets to be distributed to various kind of creditors. According to the proviso given in the section 326 the security of every secured creditor shall be deemed to be subject to a pari passu change in favor of the workman to the extent of their portion.

$$\textbf{Workman's Share to Secured} = \frac{\textbf{Amount Realied} * \textbf{Workman's Dues}}{\textbf{Workman's Dues + Secured Loan}}$$

$$\text{Workman's Share to Secured Asset} = \frac{4,00,00,000 * 1,25,00,000}{1,25,00,000 + 5,00,00,000}$$

Workman's Share to Secured Assets = 80,00,000

Amount available to secured creditor is ₹ 400 Lakhs – 80 Lakhs = 320 Lakhs
Hence, no amount is available for payment of government dues and unsecured creditors.

Preferential Payment (Section 327)

Question 8

In relation to winding up of a company, explain clearly the meaning of the term 'overriding preferential payments'. Examine the provisions of the Companies Act and decide whether the following debts of a company under the winding up shall be 'Preferential Payments' and shall be paid in priority to the claim of unsecured creditors:

a) Wages amounting to ₹ 30,000 only of an employee for services rendered for a period of 8 months within the preceding 12 months next before the relevant date.
b) ₹ 1 Lac due to an employee from provident fund and ₹ 50,000 towards gratuity.
c) ₹ 20,000/- payable by the company on account of expenses incurred in respect of investigation held u/s 213 of the Companies Act, 2013.

Answer

Section 326 of Companies Act, 2013 deals with the **overriding Preferential Payments**. Accordingly, notwithstanding anything contained in this Act or any other law for the time being in force, in the winding up of a company, (a) Workmen's dues and (b) debts due to secured creditors to the extent such debts rank pari passu with such dues, shall be paid in priority to all other debts.

As per **section 327** of Companies Act, 2013, in a winding up, subject to the provisions of section 326, there shall be paid in priority to all other debts:

(a) all **revenues, taxes, cesses and rates due from the company to the Central Government** or a

State Government or to a local authority at the relevant date, and having become due and payable within the **twelve months immediately before thatdate;**

(b) all **wages or salary including wages payable for time or piece work and salary earned wholly or in part by way of commission of any employee in respect of services rendered to the company and due for a period not exceeding four months within the twelve months** immediately before the relevant date, subject to the condition that the amount payable under this clause to any workman shall not exceed such amount as may be notified;

(c) all **accrued holiday remuneration becoming payable to any employee**, or in the case of his death, to any other person claiming under him, on the termination of his employment before, or by the winding up order, or, as the case may be, the dissolution of the company;

(d) unless the company is being wound up **voluntarily merely for the purposes of reconstruction or amalgamation** with another company, all amount due in respect of contributions payable during the period of twelve months immediately before the relevant date by the company as the employer of persons under the **Employees' State Insurance Act, 1948** or any other law for the time being in force;

(e) unless the company has, at the commencement of winding up, under such a contract with any insurer as is mentioned in section 14 of the Workmen's Compensation Act, 1923, **rights capable of being transferred to and vested in the workmen, all amount due in respect of any compensation or liability for compensation** under the said Act in respect of the death or disablement of any employee of the company:

Provided that where any compensation under the said Act is a weekly payment, the amount payable under this clause shall be taken to be the amount of the lump sum for which such weekly payment could, if redeemable, be redeemed, if the employer has made an application under that Act;

(f) all **sums due to any employee from the provident fund, the pension fund, the gratuity fund or any other fund for the welfare of the employees, maintained by the company**; and

(g) the **expenses of any investigation held in pursuance of sections 213 and 216, in so far as they are payable by the company.**

Fraudulent Preference (Section 328)

Question 9

Modern Textiles Limited incurred huge losses during the last three financial years and its financial position was bad. The Company created a legal mortgage on some of its immovable properties in favour of a bank on 1st September, 2012 in the hope that by keeping good faith with the bank it could get further advances from the bank and the same could be utilized to revive the Company. Some creditors filed winding up petition in the court on 15th January, 2013. The court passed an order of winding up on 1st August, 2013. Answer the following with reference to the provisions of the Companies Act, 1956:

i) What is meant by 'Fraudulent Preference'? State the effect of 'Fraudulent Preference'.

ii) Whether the creation of legal mortgage by the Company in favour of the bank would amount to fraudulent preference?

Answer

a) Fraudulent Preference:

Section 328 of Companies Act, 2013 deals with the fraudulent preference. Accordingly,

i) Where a company has given **preference to a person who is one of the creditors of the company or a surety or guarantor for any of the debts or other liabilities of the company**, and the company does anything or suffers anything done which has the effect of putting that person into a position which, in the event of the company going into liquidation, will be better than the position he would have been in if that thing had not been done prior to six months of making winding up application, the Tribunal, if satisfied that, such **transaction is a fraudulent preference may order as it may think fit for restoring the position to what it would have been if the company had not given that preference.**

ii) If the Tribunal is satisfied that there is a preference **transfer of property, movable or immovable, or any delivery of goods, payment, execution made, taken or done by or against a company within six months** before making winding up application, the Tribunal may order as it may think fit and may declare such transaction invalid and restore the position.

b) Pledge of movable properties with a nationalized bank, whether amount to fraudulent preference:

For the purpose of providing a fraudulent preference, two things need be shown, viz:

i) That in the case of a winding up, the **transaction took place within 6 months before the presentation of the petition**; and

ii) That the **main motive in the the mind of the company, acting through its directors, was to to prefer one creditor to the other**.

Thus, pledging certain movable properties or mortgaging immovable properties with a bank is not a fraudulent preference because it has been done in the good faith so that their loan limits would be increased. It is a transaction in good faith. Answer would remain same if the charge was created in favour of an NBFC.

Question 10

Info-tech Overtrading Ltd. was ordered to be wound up compulsory by an order dated 10th March, 2017 by the Tribunal. The official liquidator who has taken control for the assets and other records of the company has noticed the following:

The Managing Director of the company has sold certain properties belonging to the company to a private company in which his son was interested causing loss to the company to the extent of INR 50 lakhs. The sale took place on 15th October, 2016.

Examine what action the official liquidator can take in this matter. Having regard to the provisions of the Companies Act, 2013.

Answer

The official liquidator can invoke the provisions contained in **Section 328** of the Companies Act, 2013 to recover the sale of assets of the company. According to Section 328, **If the Tribunal is satisfied that there is a preference transfer of property, movable or immovable, or any delivery of goods, payment, execution made, taken or done by or against a company within six months before making winding up application, the Tribunal may order as it may think fit and may declare such transaction invalid and restore the position.**

Since in the present case, the sale of immovable property took place on 15th October, 2016 and the company went into liquidation on 10th March, 2017 i.e., within 6 months before the winding up of the company and since the sale has resulted in a loss of INR 50 lakhs to the company.

The official liquidator will be able to succeed in proving the case under Section 328 by way of fraudulent preference as the property was sold to a private company in which the son of the ex-managing was interested.

Hence, **the transaction made will be regarded as invalid and restore the position of the company as if no transfer of immovable property has been made**.

Liabilities and Rights of certain persons fraudulently preferred (Section 331)

Question 11

Skyline Ltd. Was ordered to be wound up compulsory on a petition filed on 10th February, 2018 before Tribunal. The official liquidator who has taken control for the assets and other records of the company has noticed that the managing Director of the company has transferred certain properties belonging to the company to one of its creditor "Vansh (Pvt.) Ltd.", in which his son was interested. This was causing huge monetary loss to the company. The sale took place on the 15th September 2017.

Determine the rights and liabilities of fraudulently preferred persons by mortgage of charge of property to him to secure the company's debt.

Answer

Determination of rights and liabilities of fraudulently preferred persons:

As per **section 331** of the Companies Act, 2013, Where a company is being wound up and anything made, taken or done after the commencement of this Act is invalid under section 328 as a fraudulent preference of a person interested in property mortgaged or charged to secure the company's debt, then, without prejudice to any rights or liabilities arising, apart from this provision, the person preferred shall be subject to the same liabilities, and shall have the same rights, as if he had undertaken to be personally liable as a surety for the debt,

i) **to the extent of the mortgage or charge on the property or**

ii) **the value of his interest, whichever is less.**

not liable for any penal action under the Act.

Ch 9 – Companies Incorporated Outside India

Definitions

Question 1

Examine with reference to the provisions of the Companies Act, 2013 whether the following companies can be treated as foreign companies:

i) A company incorporated outside India having a share registration office at Mumbai.

ii) Indian citizens incorporated a company in Singapore for the purpose of carrying on business there.

Answer

Section 2(42) of the Companies Act, 2013 defines a "foreign company" as any company or body corporate incorporated outside India which:

a) **Has a place of business in India whether by itself or through an agent, physically or through electronic mode;** and

b) **Conducts any business activity in India in any other manner**.

According section 386 of the Companies Act, 2013, for the puproses of Chapter XXII of the Companies Act, 2013 (Companies incorporated outside India), expression "Place of business" includes a share transfer or registration office.

Accordingly, to qualify as 'foreign company' a company must have the following features:

a) It **must be incorporated outside India**; and

b) It **should have a place of business in India**.

c) That place of business may be **either in its own name or through an agent or may even be through the electronic mode**; and

d) It must conduct a **business activity of any nature in India**.

i) Therefore, a company incorporated outside India having a share registration office at Mumbai will be treated as a foreign company provided it conducts any business activity in India.

ii) In the case of a company incorporated in Singapore for the purpose of carrying on business in Singapore will not fall within the definition of a foreign company. Its incorporation by Indian citizen is immaterial. In order to be a foreign company it has to have a place of business in India and must conduct a business activity in India.

Question 2

Robertson Ltd. is a company registered in Thailand. Although, it has no place of business established in India, yet it is doing online business through telemarketing in India. Whether it will be treated as a Foreign Company under the Companies Act, 2013? Explain.

Answer

According to section 2(42) of the Companies Act, 2013, "foreign company" means any company or body corporate incorporated outside India which –

(a) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and

(b) conducts any business activity in India in any other manner.

According to the Companies (Registration of Foreign Companies) Rules, 2014, "electronic mode" means carrying out electronically based, whether main server is installed in India or not, including, but not limited to –

(a) **business to business and business to consumer transactions**, data interchange and other digital supply transactions;

(b) offering to **accept deposits or inviting deposits or accepting deposits** or subscriptions in securities in India or from citizens of India;

(c) **financial settlements, web based marketing, advisory and transactional services, data base services and products, supply chain management**;

(d) **online services such as telemarketing, telecommuting, telemedicine, education & information research**; and

(e) **all related data communication services whether conducted by e-mail, mobile devices, social media, cloud computing, document management**, voice or data transmission or otherwise.

Looking to the above description, it can be said that being involved in business activity through telemarketing, Robertson Ltd., will be treated as foreign company.

Question 3 ***(RTP Nov 18)***

Examine and state whether the following Companies can be considered as 'Foreign Company' under the Companies Act, 2013:

(i) A company which is incorporated outside India employs agents in India but has no place of business in India.

(ii) A company incorporated outside India having shareholders who are all Indian citizens.

(iii) A company incorporated in India but all the shares are held by foreigners.

(iv) A company which has no place of business established in India, yet, is doing online business through telemarketing in India.

Answer

As per Section 2(42) of the Companies Act, 2013, a foreign company means any company or body corporate incorporated outside India which-

(a) has a place of business in India whether by itself or through an **agent, physically or through electronic mode; and**

(b) conducts any business activity in India in any other manner.

(i) **A company incorporated outside India and have not established a place of business in India, is not deemed to be a Foreign Company**. Thus establishing a place of business is an essential ingredient in the definition. In the given case, the company has not established a place of business in India though employs agents in India. It will not be deemed to be a foreign company.

(ii) A company **incorporated outside India, will not be deemed to be a Foreign Company even though all the shareholders are Indian citizens, unless it has a place of business in India**.

(iii) A company incorporated In India but having all foreign shareholders will be deemed to be an Indian Company as it is **not incorporated outside India though it has a place of business in India.**

(iv) According to the Companies (Registration of Foreign Companies) Rules, 2014, "electronic mode" means carrying out electronically based, whether main server is installed in India or not, including, but not limited to:

(a) **Business to business and business to consumer transactions**, data inter-change and other digital supply transactions

(b) **Offering to accept deposits or inviting deposits or accepting deposits or subscriptions in India or from citizens of India**

(c) **Financial settlements, web-based marketing, advisory and transactional services, data based services and products and supply chain management,**

(d) **Online services such as telemarketing, telecommuting, telelmedicine, education and information research.**

(e) All related data communication services whether conducted by e -mail, mobile devices, social media, cloud computing, data management, voice or data transmission or otherwise.

Therefore, looking to the above description, a company which has no place of business established in India, yet doing online business through telemarketing in India will be treated as a foreign company.

Question 4

Joel Ltd. was incorporated in London with a paid up capital of 10 million pounds. Mr. Y an Indian citizen holds 25% of the paid up capital. X Ltd. a company registered in India holds 30% of the paid up capital of Joel Ltd. Joel Ltd. has recently established a share transfer office at New Delhi.

i) The company seeks your advice as to what formalities it should observe as a foreign company under Companies Act, 2013.

ii) State briefly the requirements relating to filing of accounts with the Registrar of Companies by the foreign company in respect of its global business as well as Indian business.

Answer

In terms of the definition of a foreign company under **section 2 (42)** of the Companies Act, 2013 a "foreign company" means any company or body corporate incorporated outside India which:

a. **Has a place of business in India whether by itself or through an agent, physically or through electronic mode; and**

b. **Conducts any business activity in India in any other manner**.

According section 386 of the Companies Act, 2013, for the puproses of Chapter XXII of the Companies Act, 2013 (Companies incorporated outside India), "Place of business" includes a share transfer or registration office.

Further, **section 379** states that where not less than 50% of the paid-up share capital, whether equity or preference or partly equity and partly preference, of a foreign company is held by one or more citizens of India or by one or more companies or bodies corporate incorporated in India, or by one or more citizens of India and one or more companies or bodies corporate incorporated in India, whether singly or in the aggregate, such company shall comply with the provisions of this Chapter and such other provisions of this Act as may be prescribed with regard to the business carried on by it in India as if it were a company incorporated in India.

In the case given in the question, the following facts are given:

a. Joel Ltd. was incorporated in London and has a place of business (share transfer office) in India, hence, it is a foreign company.

b. Its shareholding comprises of 25% held by Y who is a citizen of India and 30% by X Ltd. which is a company registered in India. Together the two Indian shareholders hold 55% of the share capital of Joel Ltd.

Therefore, although Joel Ltd. is a foreign company, due to the holding of more than 50% of its share capital by two Indian entities, it will be covered under section 379 and will be treated as a company incorporated in India or as an Indian Company.

However, it may be noted that under section 379, the application of the Companies Act, 2013 on Joel Ltd. will be only in respect of business carried by it in India and not in relation to its business anywhere outside India.

The Companies Act, 2013 under Chapter XXII does not require a foreign company to file any documents in relation to its global business.

1) Under **section 380** of the Act, a foreign company is required to file for registration within 30 days of the establishment of a place of business in India the following documents with the Registrar:

   a) a **certified copy of the charter, statutes or memorandum and articles, of the company or other instrument constituting or defining the constitution of the company**. If the instruments are not in the English language, a **certified translation thereof in the English language;**

   b) the **full address of the registered or principal office of the company**;

   c) a **list of the directors and secretary of the company containing such particulars as may be prescribed**;

In relation to the nature of particulars to be provided as above, the Companies (Registration of Foreign Companies) Rules, 2014, provide that the list of directors and secretary or equivalent (by whatever name called) of the foreign company shall contain the following particulars, for each of the persons included in such list, namely:

i) personal name and surname in full;
ii) any former name or names and surname or surnames in full;
iii) father's name or mother's name and spouse's name;
iv) date of birth;
v) residential address;
vi) nationality;
vii) if the present nationality is not the nationality of origin, his nationality of origin;
viii) passport Number, date of issue and country of issue; (if a person holds more than one passport then details of all passports to be given)
ix) income-tax permanent account number (PAN), if applicable;
x) occupation, if any;
xi) whether directorship in any other Indian company, (Director Identification Number(DIN), Name and Corporate Identity Number (CIN) of the company in case of holding directorship);
xii) other directorship or directorships held by him;
xiii) Membership Number (for Secretary only); and
xiv) e-mail ID.

d) the **name and address or the names and addresses of one or more persons resident in India authorised to accept** on behalf of the company service of process and any notices or other documents required to be served on the company;

e) the **full address of the office of the company in India which is deemed to be its principal place of business in India**;

f) particulars of **opening and closing of a place of business in India on earlier occasion or occasions;**

g) declaration that none of the directors of the company or the authorized representative in India has ever been convicted or debarred from formation of companies and management in India or abroad; and

h) any other information as may be prescribed.

2) According to **section 381** of the Companies Act, 2013:
Every foreign company shall, **in every calendar year**,—

a) make out a balance sheet and profit and loss account in such form, containing such particulars and including or having attached or annexed thereto such documents as may be prescribed under Rules 4 & 5 of the Companies(Registration of Foreign Companies)Rules, 2014, and

b) deliver a copy of those documents to the Registrar.

Question 5 ***(Nov 17)***

Mr. Ziyan an Indian citizen holds 25% of the paid up capital of Laurel Steven Limited, a company which was incorporated in Singapore with a paid up capital of 10 million Singapore Dollars. Swaraj Limited a company registered in India holds 30% of the paid up capital of Laurel Steven Limited. Laurel Steven Limited has recently established a share transfer office at New Delhi. The Company seeks your advise as to what formalities it should observe as a foreign company under the Companies Act, 20l3.

Answer

In terms of the definition of a foreign company under **section 2 (42)** of the Companies Act, 2013 a "foreign company" means any company or body corporate incorporated outside India which:

(i) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and

(ii) conducts any business activity in India in any other manner.

According to **Section 386** of the Companies Act, 2013, "Place of business" includes a share transfer or registration office.

Further, **Section 379** states that where not less than 50% of the paid-up share capital, whether equity or preference or partly equity and partly preference, of a foreign company is held by one or more citizens of India or by one or more companies or bodies corporate incorporated in India, or by one or more citizens of India and one or more companies or bodies corporate incorporated in India, whether singly or in the aggregate, such company shall comply with the provisions of this Chapter and such other provisions of this Act as may be prescribed with regard to the business carried on by it in India as if it were a company incorporated in India.

In the case given in the question, the following facts are given:

a. Laurel Steven Ltd. was incorporated in Singapore and has a place of business (share transfer

office) in New Delhi, hence, it is a foreign company.

b. Its shareholding comprises of 25% held by Mr. Ziyan who is a citizen of India and 30% by Swaraj Limited which is a company registered in India. Together the two Indian shareholders hold 55% of the share capital of Laurel Steven Ltd.

Therefore, although Laurel Steven Ltd. is a foreign company, due to the holding of more than 50% of its share capital by two Indian entities, it will be covered under section 379 and will be treated as a company incorporated in India or as an Indian Company.

However, it may be noted that under section 379, the application of the Companies Act, 2013 on Laurel Steven Ltd. will be only in respect of business carried by it in India and not in relation to its business anywhere outside India.

Under **Section 380** of the Act, a foreign company is required to file for registration within 30 days of the establishment of a place of business in India the following documents with the Registrar:

(a) a **certified copy of the instrument constituting or defining the constitution of the company.**

(b) the **full address of the registered or principal office of the company;**

(c) a **list of the directors and secretary of the company** containing such particulars as prescribed under Companies (Registration of Foreign Companies) Rules, 2014;

(d) the **name and address or the names and addresses of one or more persons resident in India who is authorized for correspondence on behalf of the company**.;

(e) the **full address of the office of the company in India which is deemed to be its principal place of business in India**;

(f) particulars of **opening and closing of a place of business in India on earlier occasion or occasions;**

(g) **declaration that none of the directors of the company or the authorized representative in India has ever been convicted or debarred from formation of companies and management in India or abroad;** and

(h) any other information as may be prescribed.

Question 6 ***(May 18)***

Qinghai Huading Industrial Company Ltd., incorporated in China established a place of business at Mumbai. The Charter / Documents constituting the Company is in Mandarian Chinese (Chinese local language). It is required inter alia to file a certified translation of above documents with the Registrar of Companies in India. Who can authenticate the translated charter/ documents as per the provisions of the Companies Act, 2013 and Rules made there under governing foreign companies in case such translation is made at Mumbai?

Answer

According to Rule 10 of the Companies (Registration of Foreign Companies) Rules, 2014,

(i) **All the documents required to be filed with the Registrar by the foreign companies shall be in English language** and where any such document is not in English language, there shall be attached a **translation thereof in English language duly certified to be correct in the manner given in these rules.**

(ii) **Where** such translation is made within India, it shall be authenticated by-

(a) **an advocate, attorney or pleader entitled to appear before any High Court; or**

(b) **an affidavit, of a competent person having, in the opinion of the Registrar, an adequate knowledge of the language of the original and of English.**

In the instant case, Qinghai Huading Industrial company Ltd. can translate the related documents within India and they shall be authenticated by the persons mentioned under the above Rules.

Application of Act foreign companies (Section 379)

Question 7 ***(Nov 2018)***

Trans Asia Limited is registered as a public company u/s 4 (7) of the erstwhile Companies Act, 1956 which is a subsidiary of Galilio Limited, a foreign company. Trans Asia Limited carries on business in India describing itself as a foreign company. Can it do so? State the actions that can be taken against the company for improper use or description as foreign company under the provisions of the Companies Act, 2013.

Answer

Foreign Company [Section 2(42)]: "Foreign company" means any company or body corporate incorporated outside India which-

a) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and
b) conducts any business activity in India in any other manner.

In the instant case, Trans Asia Limited is registered as a public company u/s 4(7) of the erstwhile Companies Act, 1956 which is a subsidiary of Galilio Limited, a foreign company. Though Trans Asia Limited is a subsidiary of a foreign company but since it is registered in India, it is not a foreign company. Hence, it cannot describe itself as a foreign company.

Action against the improper use/description as foreign co.: As per Rule 12 of the Companies (Registration of Foreign Co.) Rules, 2014*, i*f any person or persons trade or carry on business in any manner under any name or title or description as a foreign company registered under the Act or the rules made thereunder, that person or each of those persons shall, unless duly registered as foreign company under the Act and rules made thereunder, shall be liable for investigation under section 210 of the Act and action consequent upon that investigation shall be taken against that person.

Accounts of foreign companies (Section 381)

Question 8 ***(May 2016)***

Galilio Ltd. is a foreign company in Germany and it established a place of business in Mumbai. Explain the relevant provisions of the Companies Act, 2013 and rules made thereunder relating to preparation and filing of financial statements, as also the documents to be attached alongwith the financial statements by the foreign company.

Answer

(a) Preparation and filing of financial statements by a foreign company:

According to **section 381** of the Companies Act, 2013:

(i) Every foreign company shall, in every calendar year,—

(a) **make out a balance sheet and profit and loss account** in such form, containing such particulars and including or having attached or annexed thereto such documents as may be

prescribed, and

(b) **deliver a copy of those documents to the Registrar.**

According to the Companies (Registration of Foreign Companies) Rules, 2014, every foreign company shall prepare financial statement of its Indian business operations in accordance with Schedule III or as near thereto as possible for each financial year including:

(1) **documents that are required to be annexed should be in accordance with Chapter IX i.e. Accounts of Companies.**

(2) The **documents relating to copies of latest consolidated financial statements of the parent foreign company, as submitted by it to the prescribed authority in the country of its incorporation under the applicable laws there**.

(ii) The Central Government is empowered to direct that, in the case of any foreign company or class of foreign companies, the requirements of clause (a) of section 381(1) shall **not apply, or shall apply subject to such exceptions and modifications as may be specified in notification in that behalf.**

(iii) If any of the **specified documents are not in the English language, a certified translation thereof in the English language shall be annexed**. [Section 381 (2)]

(iv) Every foreign company **shall send to the Registrar along with the documents required to be delivered to him, a copy of a list in the prescribed form, of all places of business established by the company in India as at the date with reference to which the balance sheet referred to in section 381(1) is made**.

According to the Companies (Registration of Foreign Companies) Rules, 2014, every foreign company shall file with the Registrar, along with the financial statement, in Form FC3 with such fee as provided under Companies (Registration Offices and Fees) Rules, 2014 a list of all the places of business established by the foreign company in India as on the date of balance sheet.

According to the Companies (Registration of Foreign Companies) Rules, 2014, if any foreign company ceases to have a place of business in India, it shall forthwith give notice of the fact to the Registrar, and as from the date on which notice is so given, the obligation of the company to deliver any document to the Registrar shall cease, if it does not have other place of business in India.

(v) According to the *Companies (Registration of Foreign Companies) Rules, 2014*,

(a) Further, every foreign company shall, along with the financial statement required to be filed with the Registrar, attach thereto the following documents; namely:-

(1) **Statement of related party transaction**

(2) **Statement of repatriation of profits**

(3) **Statement of transfer of funds (including dividends, if any)**

The above statements shall include such other particulars as are prescribed in the Companies (Registration of Foreign Companies) Rules, 2014.

(b) All these documents shall be delivered to the Registrar within a period of 6 months of the close of the financial year of he foreign company to which the documents relate.

Display of Name Etc. of Foreign Company (Section 382)

Question 9

The liability of members of Style Limited, a company incorporated in Singapore, is limited. The company plans to start a place of business in Mumbai from 1st Dec., 2016. It has taken an office space in Andheri (West), Mumbai for that purpose. The person who is to take charge of Mumbai Office seeks your advice regarding the provisions of the Companies Act, 2013, in respect of displaying of the company's name etc., at its Mumbai office as well as in its business letters and other documents. Advise him with reference to the provisions of the Companies Act, 2013 governing foreign companies**.**

Answer

Display of names etc. of foreign company: Section 382 of the Companies Act, 2013 provides that every foreign company shall—

(a) **conspicuously exhibit on the outside of every office or place where it carries on business in India**, the name of the company and the country in which it is incorporated, in letters easily legible in English characters, and also in the characters of the language or one of the languages in general use in the locality in which the office or place is situate;

(b) cause the name of the company and of the country in which the company is incorporated, to be **stated in legible English characters in all business letters, bill- heads and letter paper, and in all notices, and other official publications of the company; and**

(c) if the liability of the members of the company is limited, cause notice of that fact—

(i) to be stated in every such prospectus issued and in all business letters, bill- heads, letter paper, notices, advertisements and other official publications of the company, in legible English characters; and

(ii) to be conspicuously exhibited on the outside of every office or place where it carries on business in India, in legible English characters and also in legible characters of the language or one of the languages in general use in the locality in which the office or place is situate.

Hence, the person who is to take charge of Mumbai Office of Style Limited may follow the above provisions in respect of displaying of the company's name etc. at its Mumbai office as well as in its business letters and other documents

Other Provisions

Question 10

Aster Ltd., is a company incorporated outside India. 50% of its preference share capital and 20% of its equity share capital is held by companies incorporated in India. It issued prospectus inviting subscriptions in India for its shares but did not state the country in which it is incorporated.
Examine

i) Is the prospectus of the company valid?

ii) What other disclosures in the prospectus are required to be made by a foreign company?

Answer

i) Under **Section 379** of the Companies Act, 2013 where

a) **Not less than 50%** of the **paid-up share capital**,

b) whether **equity or preference** or partly equity and partly preference, of a foreign company

c) is held either **singly or in the aggregate** by one or more citizens of India or by one or more companies or bodies corporate incorporated in India,

d) such company shall **comply with this Chapter (XXII)** and

e) such **other provisions** of this Act as may be prescribed

f) with regard to the **business carried on by it in India**

g) as if it were a **company incorporated in India**.

It may further be added that the chapter XXII which governs the foreign companies is spread from Section 379 to Section 393.

From the above provisions, it is clear that Aster Ltd. will fall within the purview of section 379 as more than 50% (50% preference share capital + 20% equity share capital = 70%) is held by companies incorporated in India.

Further, section 387 (1) (a) (iv) requires for the prospectus of a foreign company to include the date on which and the country in which the company would be or was incorporated.

ii) In view of the above provisions, the prospectus issued by Aster Ltd. is a **non-compliant prospectus**. Thus, **according to Section 387** the **prospectus is not valid.**

Further, according to **Section 393** which states that any failure by a company to comply with the provisions of this Chapter shall **not affect the validity of any contract, dealing or transaction** entered into by the company or its liability to be sued in respect thereof, but the company shall not be entitled to bring any suit, claim any set-off, make any counter-claim or institute any legal proceeding in respect of any such contract, dealing or transaction, until the company has complied with the provisions of this Act applicable to it. Therefore, it may be concluded that the non- disclosure of the country in which it was incorporated will not invalidate the validity of any contract, dealing or transaction entered into by Aster Ltd.

Under **Section 387 (1)** of the Companies Act, 2013 **no person shall issue, circulate or distribute in India any prospectus** offering to subscribe for securities of a company incorporated or to be incorporated outside India, **unless the prospectus is dated and signed, and contains the following particulars**:

a) the **instrument constituting or defining the constitution** of the company;

b) the **enactments or provisions** by or under which the incorporation of the company was effected;

c) the **address in India** where the said instrument, enactments or provisions, or copies thereof can be inspected. If the same are not in the English language, a certified translation thereof in the English language should be available for inspection;

d) the **date on which and the country** in which the company would be or was incorporated; and

e) **whether the company has established a place of business in India** and , if so, the address of its principal office in India, and the matters specified under section 26 (so far as they are applicable) which lays down the matters to be included in a prospectus issued by an Indian Company.

Question 11

i) As per provisions of the Companies Act, 2013, what is the status of XYZ Ltd., a Company incorporated in London, U.K., which has a share transfer office at Mumbai?

ii) ABC Ltd., a foreign company having its Indian principal place of business at Kolkata, West Bengal is required to deliver various documents to Registrar of Companies under the provisions

of the Companies Act, 2013. You are required to state, where the said company should deliver such documents.

iii) In case, a foreign company does not deliver its documents to the Registrar of Companies as required under section 380 of the Companies Act, 2013, state the penalty prescribed under the said Act, which can be levied.

Answer

i) In terms of the definition of a foreign company under section 2(42) of the Companies Act, 2013 a "foreign company" means any company or body corporate incorporated outside India which:

a) Has a place of business in India whether by itself or through an agent, physically or through electronic mode; and

b) Conducts any business activity in India in any other manner

According section 386 of the Companies Act, 2013, for the puproses of Chapter XXII of the Companies Act, 2013 (Companies incorporated outside India), "**Place of business" includes a share transfer or registration office.**

From the above definition, the status of XYZ Ltd. will be that of a foreign company as it is incorporated outside India, has a place of business in India and it may be presumed that it carries on a business activity in India.

ii) The Companies Act, 2013 vide **section 380** requires every foreign company is required to deliver to the Registrar for registration, **within 30 days of the establishment of office in India**, documents which have been specified therein. According to the Companies (Registration of Foreign Companies) Rules, 2014, any document which any foreign company is required to deliver to the Registrar shall be delivered to the Registrar having jurisdiction over New Delhi.

iii) The Companies Act, 2013 lays down the governing provisions for foreign companies in Chapter XXII which is comprised of sections 379 to 393. The penalties for non filing or for contravention of any provision for this chapter including for non filing of documents with the Registrar as required by section 380 and other sections in this chapter are laid down in section 392 of the Act which provides that if a foreign company contravenes the provisions of this Chapter, the foreign company shall be punishable with a fine which **shall not be less than Rs. 1,00,000 but which may extend to Rs. 3,00,000** and in the case of a continuing offence, with an **additional fine which may extend to Rs. 50,000 for every day** after the first during which the contravention continues and every officer of the foreign company who is in default shall be punishable with imprisonment for a term which may extend to **six months or with fine which shall not be less than Rs. 25,000 but which may extend to Rs. 5,00,000, or with both**.

Question 12

Blue Berry Ltd. is a Company incorporated outside India. 50% of its preference share capital and 20% of its equity share capital are held by Companies incorporated in India. It issued prospectus inviting subscriptions in India for its shares but did not state the Country in which it is incorporated. Examine in the light of the provisions of the Companies Act, 2013 whether the issue of prospectus by the Company is valid.

Answer

According to **Section 387(1)(a)(iv)** of the Companies Act, 2013, no person shall issue, circulate or

distribute in India any prospectus offering to subscribe for securities of a company incorporated or to be incorporated outside India, whether the company has or has not established, or when formed will or will not establish, a place of business in India, unless the prospectus is dated and signed, and contains particulars with respect to the date on which and the country in which the company would be or was incorporated.

Hence, in the instant case, issue of prospectus by Blue Berry Limited is not valid as it did not state the Country in which it is incorporated.

Question 13

Ronnie Coleman Ltd., a foreign Company failed to deliver some documents to the Registrar of Companies as required under Section 380 of the Companies Act, 2013. State the provisions of penalty prescribed under the Act, which can be levied on Ronnie Coleman Ltd. for its failure to deliver the documents.

Answer

The Companies Act, 2013 lays down the governing provisions for foreign companies in Chapter XXII which is comprised of sections 379 to 393. The penalties for non-filing or for contravention of any provision for this chapter including for non-filing of documents with the Registrar as required by section 380 and other sections in this chapter are laid down in section 392 of the Act which provides that if a foreign company contravenes the provisions of this Chapter, the foreign company shall be punishable with a fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 3,00,000 and in the case of a continuing offence, with an additional fine which may extend to ₹ 50,000 for every day after the first during which the contravention continues and every officer of the foreign company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than ` 25,000 but which may extend to ₹ 5,00,000, or with both.

Ch 10 – Miscellaneous Provisions

Removal of names of companies from the register of companies (Section 248 – 252)

Question 1 ***(May 18)***

Kojol Research Development Ltd. was registered to innovate unique business idea emerging from research and development in a new area. It is a future project and the Company has no significant accounting transactions and business activities. Therefore the company made an application to RoC for obtaining the status of a Dormant Company. The application is under process. In the meantime, the Company without extinguishing all its liabilities filed an application to RoC for removing the name of the Company, after passing a special resolution giving effect to this.

In the light of the provisions of the Companies Act, 2013, analyse the following:

(1) Whether the application is tenable under the Act?

(2) What are the restrictions imposed under the Act for making application by a Company to remove the name of the Company from the register of ROC?

(3) What are the penal consequences III case of violation of restrictions?

Answer

According to Section 248 (1) of the Companies Act, 2013, where the Registrar has reasonable cause to believe that—

(a) a Company has failed to commence its business within one year of its incorporation, or;

(b) a Company is not carrying on any business or operation for a period of two immediately preceding financial years and has not made any application within such period for obtaining the status of a dormant Company under section 455,

-he shall send a notice to the Company and all the Directors of the Company, of his intention to remove the name of the Company from the register of Companies and requesting them to send their representations along with copies of the relevant documents, if any, within a period of thirty days from the date of the notice.

According to Section 248 (2) of the Companies Act, 2013, a Company may, after extinguishing all its liabilities, by-

- a special resolution, or
- consent of seventy-five per cent. members in terms of paid-up share capital,

-file an application in the prescribed manner to the Registrar for removing the name of the Company from the register of Companies on all or any of the grounds specified in sub-section (1) and the Registrar shall, on receipt of such application, cause a public notice to be issued in the prescribed manner:

(1) **Whether the application is tenable under the Act?**

In the light of the above provisions, since the Company has applied for the status of dormant Company and also without extinguishing its liabilities applied for the removal of the name of the Company from Register of members, such an application shall not be tenable.

(2) **Restrictions**

According to Section 249(1) of the Companies Act, 2013,

An application under Section 248 of the Companies Act, 2013, on behalf of a Company shall not be made if, at any time in the previous three months, the Company -

(a) has changed its name or shifted its registered office from one State to another;

(b) has made a disposal for value of property or rights held by it, immediately before ceases of trade or otherwise carrying on of business, for the purpose of disposal for gain in the normal course of trading or otherwise carrying on of business;

(c) has engaged in any other activity except the one which is necessary or expedient for the purpose of making an application under that section, or deciding whether to do so or concluding the affairs of the company, or complying with any statutory requirement;

(d) has made an application to the Tribunal for the sanctioning of a compromise or arrangement and the matter has not been finally concluded; or

(e) is being wound up under Chapter XX of this Act or under the Insolvency and Bankruptcy Code, 2016.

(3) **Penal Consequences**

According to section 249(2) of the Companies Act, 2013, if a Company files an application in violation of restriction as given in sub-section (1) as given above, it shall be punishable with fine which may extend to one lakh rupees.

Question 2 ***(May 2017 & RTP – May 2018)***

Buina Limited has discontinued its business since 2015 and has not been filing annual returns. The Registrar of companies issued a notice for striking off the company. Since no reply was received within the time specified in the notice, the name of the company was struck off from the register of companies. There were tax arrears and a notice was sent to the company by the tax recovery officer. The Directors contended that since the company's name has been struck off, the company does not exist and not liable to pay the tax. Referring to and analysing the relevant provisions of the Companies Act, 2013 examine the validity of the Company's claim.

Answer

According to **Section 248(6)** of the Companies Act, 2013, the Registrar, before passing an order for removal of name of the Company, shall satisfy himself that sufficient provision has been made for the realisation of all amount due to the Company and for the payment or discharge of its liabilities and obligations by the Company within a reasonable time and, if necessary, obtain necessary undertakings from the Managing Director, Director or other persons in charge of the Management of the Company.

Provided that, notwithstanding the undertakings referred to in this sub-section, the assets of the Company shall be made available for the payment or discharge of all its liabilities and obligations even after the date of the order removing the name of the company from the Register of Companies.

Also, as per **sub-section (7),** the liability, if any, of every Director, Manager or other Officer who was exercising any power of Management, and of every Member of the Company dissolved under **sub-section (5),** shall continue and may be enforced as if the Company had not been dissolved.

Hence, in the instant case, Bunia Limited's claim not to pay the tax is not valid.

Government Companies (Section 394 – 395)

Question 3

i) Central Government and Government of Maharashtra together hold 40% of the paid-up share capital of MN Limited. A government company also holds 20% of the paid-up share capital in MN Limited.

ii) PQ Limited is a subsidiary but not a wholly owned subsidiary of a government company.

Examine with reference to the provisions of the Companies Act, 2013 whether MN Limited and PQ Limited can be considered as Government Company.

Answer

According to **section 2(45)** of the Companies Act, 2013, "**Government company**" means any company in which **not less than fifty-one per cent of the paid-up share capital is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, and includes a company which is a subsidiary company of such a Government company.**

i) The Central Government and Government of Maharashtra together hold 40% of the paid-up share capital of MN Limited. A government company also holds 20% of the paid-up share capital in MN Limited.

In this case, MN Limited is not a Government company because the holding of the Central Government and Government of Maharashtra is 40% which is less than the 51% prescribed under the definition of Government Company. The holding of the government company in MN Limited of 20% cannot be taken into account while counting the prescribed limit of 51%.

ii) PQ Limited is a subsidiary but not a wholly owned subsidiary of a government company.

In this case, PQ Limited is a government company as the definition of Government Company clearly specifies that a Government Company includes a company which is a subsidiary company of a Government company. Whether the subsidiary should be a wholly owned subsidiary or not is not clearly mentioned under the definition of the Government company under section 2(45).

Registration Office & fees (Section 396 – 404)

Question 4

M/s Kashi Mutual Benefits Nidhi Ltd. is incorporated as a Nidhi Company under the Companies Act, 2013. The Board of Directors of the company seeks your advice on the following issues as per the provisions of the Companies Act, 2013 read with rules. Advise.

i) The Board of Directors is planning to issue preference shares.

ii) The Board of Directors have decided to provide Locker Facilities on rent to its members and have estimated that rental income from such letting will be around 30 of the gross income of the company.

iii) The Board of Directors of the company is planning to declare dividend for the current year at 45%.

iv) The Board of Directors of the company have decided to appoint Mr. Prince (a minor) as a member of the company.

Answer

i) According to Rule 4(2) and 6(b) of the Nidhi Rules, 2014, no Nidhi shall issue preference shares.

So, the boards of Directors of M/s Kashi Mutual Benefits Nidhi Ltd. cannot issue preference shares.

ii) According to Rule 6(e) of the Nidhi Rules, 2014, Nidhis which have adhered to all the provisions of these rules may provide locker facilities on rent to its members subject to the rental income from such facilities not exceeding twenty per cent of the gross income of the Nidhi at any point of time during a financial year. So, the board of directors cannot provide locker facilities on rent to its members on which the rental income will be around 30% of the gross income of the company.

iii) According to Rule 18 of the Nidhi Rules, 2014, a Nidhi shall not declare dividend exceeding 25% or such higher amount as may be specifically approved by the Regional Director for reasons to be recorded in writing and further subject to the following conditions, namely:—

a) an equal amount is transferred to General Reserve;

b) there has been no default in repayment of matured deposits and interest; and

c) it has complied with all the rules as applicable to Nidhis.

In the instant case, the Board of Directors cannot declare dividend at the rate of 45%.

iv) According to Rule 8(3) of the Nidhi Rules, 2014, a minor shall not be admitted as a member of Nidhi. However, deposits may be accepted in the name of a minor, if they are made by the natural or legal guardian who is a member of Nidhi.

Hence, the Board of directors of the company cannot appoint Mr. Prince (a minor) as a member of the company.

Question 5

Akri Nidhi Limited proposes:

i) To reappoint Mr. X, a Director who has completed a term of 10 consecutive year as a Director of the Nidhi.

ii) To pay dividend at the rate of 45%.

Examine and analyse the validity of the above proposals with reference to Nidhi Rules 2014 formulated under Companies Act, 2013

Answer

i) According to **Rule – 17** of the Nidhi Rules, 2014, the Director of a Nidhi shall hold office for a term up to ten consecutive years on the Board of Nidhi and he shall be eligible for re-appointment only after the expiration of two years of ceasing to be a Director.

Hence, in the instant case, Akri Nidhi Limited cannot reappoint Mr. X as a director for a period of two years after completion of 10 consecutive years.

ii) According to **Rule 18** of the Nidhi Rules, 2014, a Nidhi shall not declare dividend exceeding 25% or such higher amount as may be specifically approved by the Regional Director for reasons to be recorded in writing and further subject to the following conditions, namely:—

a) an equal amount is transferred to General Reserve;

b) there has been no default in repayment of matured deposits and interest; and

c) it has complied with all the rules as applicable to Nidhis.

In the instant case, if the Company wants to pay dividend at the rate of 45%, it has to follow the procedure mentioned under Rule 18.

Penalty for Frauds (Section 447)

Question 6

Explain the meaning of 'Fraud' in relation to the affairs of a company and the punishment provided for the same in Section 447 of the Companies Act, 2013.

Answer

As per the explanation given to **section 447** of the Companies Act, 2013, 'Fraud' in relation to affairs of a company or anybody corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss.

"**Wrongful gain**" means the **gain by unlawful means of property to which the person gaining is not legally entitled.**

"**Wrongful loss**" means, the **loss by unlawful means of property to which the person losing is legally entitled.**

Punishment:

i) without prejudice to any liability including repayment of any debt underthis Act or any other law for the time being inforce, any person who is found to be guilty of fraud involving an amount of atleast **10 lakh rupees or 1% of the turnover of the company, whichever is lower**, shall be punishable with imprisonment for a term which **shall not be less than 6 months but which may extend to 10 years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to 3 times the amount involved in the fraud.**

ii) Provided that here the fraud in question **involves public interest, the term of imprisonment shall not be less than 3years.**

iii) Provided further that where the **fraud involves an amount less than 10 lakh rupees or 1% of the turnover of the company**, **whichever is lower**, and **does not involve public interest**, any person guilty of such fraud shall be punishable with imprisonment for a term which may extend to **5 years or with fine which may extend to 50 lakh rupees or with both.**

Penalty for Frauds (Section 455)

Question 7 ***(RTP Nov 2018)***

JKL Research Development Limited is a registered Public Limited Company. The company has a unique business idea emerging from research and development in a new area. However, it is a future project and the company has no significant accounting transactions and business activities at present. The company desires to obtain the status of a 'Dormant Company'. Advise the company regarding the provisions of the Companies Act, 2013 in this regard and the procedure to be followed in this regard.

Answer

The provisions related to the **Dormant companies** is covered under section 455 of the Companies Act, 2013. According to provisions-

1. a company is formed and registered under this Act for the purpose of a **future project or to**

hold an asset or intellectual property and has no significant accounting transaction.

2. Such company or an **inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company**.
3. The **Registrar shall allow the status of a dormant company to the applicant and issue a certificate after considering of the application**.
4. The **Registrar shall maintain a register of dormant companies in such form as may be prescribed**.

In case of a company which has not filed financial statements or annual returns for two financial years consecutively, the Register shall issue a notice to that company and enter the name of such company in the register maintained for dormant companies.

A dormant company shall have such minimum number of directors, file such documents and pay such annual fee as may be prescribed to the Registrar to retain its dormant status in the register and may become an active company on an application made in this behalf accompanied by such documents and fee as may be prescribed. However, the Registrar shall strike off the name of a dormant company from the register of dormant companies, which has failed to comply with the requirements of this section.

Thus, **JKL Research Development Limited may follow the above procedure to obtain the status of a 'Dormant Company'**.

Question 8 ***(RTP May 2019)***

Rudraksh Ltd. was incorporated for supply of solar panels for the emerging project of government for construction of highways. However, the said project did not turn up for two years due to some legal implications. During the said period, no any significant accounting transaction was made and so the company did not file financial statements and annual returns during the last two financial years. In the meantime, the Board proposed for Mr. Ram & Mr. Rahim to be appointed as an Independent Directors for their independent and expertise knowledge and experience for better working and improvement of financial position of the company.

Evaluate in the light of the given facts, the following legal position:

i) Accountability for non- filing of financial statements and annual returns for last two financial years, of the Rudraksh Ltd.

ii) Nature of the proposal for an appointment of Mr. Ram & Mr. Rahim in the Rudraksh Ltd. for improvement of financial position of the company.

Answer

i) As per the stated facts, Ruraksh Ltd. is an inactive company as per the provision given under the Companies Act, 2013. According to the section 455 of the Companies Act, 2013, where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company (which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years, or has not filed financial statements and annual returns during the last two financial years;) may make an application to the Registrar for obtaining the status of a dormant company. Since in the given case, neither Rudraksh Ltd. filed an application to the Registrar for obtaining the status nor has filed the financial statements or annual returns for 2 financial years consecutively, therefore, the Registrar shall issue a notice to

the company and enter the name of the company in the register maintained for dormant companies.

ii) As per section 149(6) read with Rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014, the public companies of prescribed class shall require to appoint minimum 2 Independent directors. However, vide Notification number G.S.R. 839(E) dated 5th July, 2017 an amendment was issued through the Companies (Appointment and Qualification of Directors) Amendment Rules, 2017. It provided that an unlisted public company which is a joint venture, a wholly owned subsidiary or a dormant company will not be required to appoint Independent Directors. So, the proposal for appointment of Independent Director (Mr. Ram & Mr. Rahim) is not required.

Question 9 ***(May 2019)***

Gulmohar Ltd. is a company registered in India for last 5 years. Since last 2 financial years, it has not been carrying on any business or operations and has not filed financial statements and annual returns saying that it has not made any significant accounting transaction during the last two financial years. Considering the current situation, Directors of the Company is contemplating to apply to Registrar of Companies to obtain status of dormant or inactive company. Advise them on:

i) Whether Gulmohar Ltd. is eligible to apply to Registrar of Companies to obtain dormant status for the company?
ii) Will your answer be different if Gulmohar Ltd is continuing payment of fees to Registrar of Companies and payment of rentals for its office and accounting records for last two financials years?
iii) Is special resolution in general meeting a pre-requisite to make an application to Registrar of Companies for obtaining the status of dormant company?
iv) What will be your answer if it is found after making an application of dormant company to Registrar of Companies that an investigation is pending against the company which was ordered 6 months ago?

Answer

i) According to section 455 of the Companies Act, 2013, an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.

Here, "inactive company" means a company which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years, or has not filed financial statements and annual returns during the last two financial years.

Gulmohar Ltd., since from last two years is not carrying on business or operations and has not filed financial statements and annual returns saying it has not made any significant accounting transaction during the last two financial years. Thus, it falls within the definition of inactive company as stated above and hence is eligible to apply to Registrar of Companies to obtain the status of Dormant company.

ii) According to Explanation to section 455, "significant accounting transaction" means any transaction other than—
   a) payment of fees by a company to the Registrar;
   b) payments made by it to fulfill the requirements of this Act or any other law;
   c) allotment of shares to fulfill the requirements of this Act; and

d) payments for maintenance of its office and records.

Thus, Gulmohar Ltd. is still eligible to apply to the Registrar of Companies to obtain the status of Dormant company even if it has continued 'payment of fees to Registrar of Companies and payment of rentals for its office and accounting records' for last two years, as these transactions have been kept outside the purview of significant accounting transactions.

iii) According to the Rule 3 of the Companies (Miscellaneous) Rules, 2014, a company may make an application in prescribed form to the Registrar for obtaining the status of a Dormant Company in accordance with the provisions of section 455 after passing a special resolution to this effect in the general meeting of the company or after issuing a notice to all the shareholders of the company for this purpose and obtaining consent of at least $3/4^{th}$ shareholders (in value).

Thus, special resolution is a pre- requisite to make an application to Registrar of Companies for obtaining the status of dormant company.

According to the Rule 3 of the Companies (Miscellaneous) Rules, 2014, a company shall be eligible to apply under this rule only, if no inspection, inquiry or investigation has been ordered or taken up or carried out against the company.

iv) According to section 455(6), the Registrar shall strike off the name of a dormant company from the register of dormant companies, which has failed to comply with the requirements of section 455.

In the given case, Gulmohar Ltd. was not eligible to apply for the status of a dormant company as an investigation was pending against the company which was ordered 6 months ago. But since, it has already made an application and then it came to the light about the pending investigation against the company, the Registrar shall not register it as a dormant company and if already registered as a dormant company, strike off the name of a dormant company from the register of dormant companies as the company has contravened the necessary requirements.

Ch 11 – Compounding of Offences & Special Court

Offences to be Non - Cognizable (Section 439)

Question 1

In the annual general meeting of XYZ Ltd., while discussing on the matter of retirement and reappointment of director Mr. X, allegations of fraud and financial irregularities were levelled against him by some members. This resulted into chaos in the meeting. The situation was normal only after the Chairman declared about initiating an inquiry against the director Mr. X, however, could not be re-appointed in the meeting. The matter was published in the newspapers next day. On the basis of such news, whether the court can take cognizance of the matter and take action against the director on its own?

Justify your answer with reference to the provisions of the Companies Act, 2013.

Answer

Section 439 of the Companies Act, 2013 provides that offences under the Act shall be non-cognizable. As per this section:

1. Notwithstanding anything in the Code of Criminal Procedure, 1973, every offence under this Act except the offences referred to in sub section (6) of section 212 shall be deemed to be non-cognizable within the meaning of the said Code.
2. No court shall take cognizance of any offence under this Act which is alleged to have been committed by any company or any officer thereof, except on the complaint in writing of the Registrar, a shareholder of the company, or of a person authorized by the Central Government in that behalf.

Thus, in the given situation, the court shall not initiate any suo moto action against the director Mr. X without receiving any complaint in writing of the Registrar of Companies, a shareholder of the company or of a person authorized by the Central Government in this behalf.

Question 2

Mr. Joseph, a member of Armaments Ltd., is aggrieved due to failure of the company to make payment of dividend declared in the AGM held in August, 2015. He makes a complaint, in writing, before the court of competent jurisdiction within the prescribed period of limitation, but the court refused to take cognizance of the alleged offence. Explain the legal position in this regard under the Companies Act, 2013.

Also state the offences under the Companies Act, 2013 which are cognizable and which are non-cognizable.

Answer

Cognizance of offence: A court shall take cognizance of any offence under this Act which is alleged to have been committed by any company or any officer thereof only on the written complaint of -

(a) The **Registrar,**

(b) **A shareholder or member of the company, or**

(c) **Of a person authorised by the Central Government in that behalf**.

Provided that the court may take cognizance of offences relating to issue and transfer of securities

and non-payment of dividend, on a complaint in writing, by a person authorised by the Securities and Exchange Board of India.

In the present case, Mr. Joseph, a member of Armaments Ltd. is aggrieved due to failure of the company to make payment of dividend declared in the AGM held in August 2015. **He makes a complaint, in writing, before the court of competent jurisdiction within the prescribed period of limitation, but the court refused to take cognizance of the alleged offence.**

Here, the Court shall take cognizance of the offence relating to non payment of dividend as the shareholders have made a complaint in writing before the competent jurisdiction.

Cognizable and non-cognizable offences: Overriding the provisions given under the Code of Criminal Procedure, 1973, every offence under the Companies Act, 2013 except the offences referred to in section 212(6) of the Companies Act, 2013, **which deals with the investigation into affairs of company by serious fraud investigation office, shall be deemed to be non-cognizable within the meaning of the said Code.**

Therefore, the offences as covered under **section 212(6) shall now be deemed to be cognizable where police officer may arrest person without warrant and are non-bailable**. The Companies Act, 2013 establishes the offence covered under section 212(6) as a public wrong which has to be prevented and controlled. This non- bailable nature of the offences deter the offender and the others from committing further and similar offences.

Question 3 ***(May 18)***

All offences under the Companies Act, 2013 are non-cognizable except offences of fraud covered under Section 447 of the Act. Explain the validity of the statement.

Answer

Offences to be Non-cognizable: As per Section 439 (1) of the Companies Act, 2013, every offence under the Companies Act, 2013, except the offences referred to in section 212(6), shall be deemed to be non-cognizable under the Code of Criminal Procedure.

As per Section 212(6), *offence covered under Section 447 of this Act shall be cognizable.

The given statement in the question is valid.

* The offences covered under Section 7(5) & (6), Section 34, Section 36, sub- section 38(1), Section 46(5), Section 56(7), Section 66(10), Section 140(5), Section 206(4),
Section 213, Section 229, Section 251(1), Section 339 (3) and Section 448 attract the punishment for fraud provided in section 447.

Offences to be Non - Cognizable (Section 442)

Question 4

What are provisions related to constitution and working of the Mediation and Conciliation Panel as per Section 442 of the Companies Act, 2013?

Answer

Mediation and Conciliation Panel: In common parlance, **Mediation means intervention of some third party in a dispute with the intention to resolve the dispute**.

Conciliation means the process of adjusting or settling disputes in a friendly manner through extra judicial means. This new provision introduced by the Companies Act, 2013 has come into force with effect from 1st April, 2014 vide notification dated 26th of March, 2014. Section 442 of

the Companies Act, 2013 deals with the constitution and functioning of the mediation and conciliation panel in order to dispose the matter.

Section 442 lays the following law with respect to the constitution and working of the Mediation and Conciliation Panel:

1) **Central Government to maintain the Panel of Mediators:** The Central Government shall maintain a panel of experts to be known as Mediation and conciliation panel for mediation between the parties during the pendency of any proceedings before the Central Government or the Tribunal or the Appellate Tribunal under this Act.

   Hence, it is important that the case should be pending before the Central Government or the Tribunal or the Appellate Tribunal under this Act.

2) **Panel consisting of experts:** The panel shall consist of such number of experts having such qualification as may be prescribed.

3) **Filing of application:** Application for mediation and conciliation can be made by:

   a) any parties to the proceedings. (It shall be accompanied with such fees and in such form as may be prescribed.)

   b) The Central Government or the Tribunal or the Appellate Tribunal before which any proceeding is pending may, suo motu refer any matter pertaining to such proceeding to such number of experts as it may deem fit.

4) **Appointment of expert/s from panel:** The Central Government or the Tribunal or the Appellate Tribunal before which any proceeding is pending may appoint one or more experts from the Panel as may be deemed fit.

5) **Fees, terms and conditions of the experts:** The fee and other terms and conditions of experts of the Mediation and Conciliation Panel shall be such as may be prescribed.

6) **Procedure for the disposal of matter:** In order to dispose the matter, the Mediation and Conciliation Panel shall follow such procedure as may be prescribed.

7) **Period for the disposal of matter:** The Mediation and Conciliation Panel shall dispose of the matter referred to it within a period of three months from the date of such reference and forward its recommendations to the Central Government or the Tribunal or the Appellate Tribunal, as the case may be.

8) **Filing of objection on the recommendation of the panel:** Any party aggreived by the recommendation of the Mediation and Conciliation Panel may file objections to the Central Government or the Tribunal or the Appellate Tribunal, as the case may be.

Question 5

What is the object of Constituting Panel for Mediation and Conciliation under the Companies Act, 2013? Who can file application for mediation and conciliation?

Answer

Under **section 442** of the Companies Act, 2013, it is provided that the Central Government shall maintain a panel of experts for mediation between the parties during pendency of any proceedings before the Central Government or the Tribunal or the Appellate Tribunal under the Act. In common parlance, mediation means intervention of some third party in a dispute with the intention to resolve the dispute. Similarly, **conciliation means the powers of adjusting or settling disputes in a friendly manner through extra judicial means**. The object behind the panel is to dispose the matter pending before the Government / Tribunal as mentioned above.

Filing of application: Application for mediation and conciliation can be made by:

a) any parties to the proceedings (It shall be accompanied with such fees and in such form as may be prescribed)

b) The Central Government or the Tribunal or the Appellate Tribunal before which any proceeding is pending may, suo moto refer any matter pertaining to such proceeding to such number of experts as it may deem fit.

Power of Central Government to Appoint Company Prosecutor (Section 443)

Question 6

What are the powers of the Central Government under the Companies Act, 2013 regarding:

i) To appoint company prosecutors

ii) To Appeal against acquittal

Answer

i) **Power of Central Government to appoint company prosecutors:** This section 443 of the Companies Act, 2013 has come into force with effect from 12th September, 2013. This section lays down the provisions seeking to provide that the Central Government may appoint company prosecutors with the same powers as given under the Cr. PC on Public Prosecutors.

   a) **Appointment of company prosecutors:** The Central Government may appoint (generally, or for any case, or in any case, or for any specified c lass of cases in any local area) one or more persons, as company prosecutors for the conduct of prosecutions arising out of this Act; and

   b) **Powers and Privileges:** The persons so appointed as company prosecutors shall have all the powers and privileges conferred on Public Prosecutors appointed under section 24 of the Cr. PC.

ii) **Appeal against acquittal:** According to section 444 of the Companies Act, 2013, the Central Government may, in any case arising under this Act, direct –

   a) any company prosecutor, or

   b) authorise any other person either by name or by virtue of his office, to present an appeal from an order of acquittal passed by any court, other than a High Court.

   Appeal presented by such prosecutor or other person shall be deemed to have been validly presented to the appellate court.

Question 7 ***(Nov 18)***

The Central Government wants to appoint Mr. Honest as Company Prosecutor. Can it do so? Mention the provisions regarding the power of Central Government to appoint Company Prosecutors along with their powers and privileges under the Companies Act, 2013.

Answer

Power of Central Government to appoint Company Prosecutors [Section 443 of the Companies Act, 2013]: The Central Government may appoint generally, or for any case, or in any case, or for any specified class of cases in any local area one or more persons, as company prosecutors for the conduct of prosecutions arising out of this Act.

The persons so appointed as company prosecutors shall have all the powers and privileges

conferred by the Code of Criminal Procedure, on Public Prosecutors appointed under section 24 of the Code.

Accordingly, the Central Government may appoint Mr. Honest as Company Prosecutor for conducting any prosecution, appeal or other proceeding on behalf of the Central Government in the Tribunal/Court.

Ch 12 – National Company Law Tribunal and Appellate Tribunal

Appeal from orders of Tribunal (Section 421)

Question 1 ***(Nov 18)***

Aggrieved by an Order of NCLT dated 05.05.2018, passed without the consent of the parties, Madhruk Ltd. decided to file an appeal before NCLAT. Meanwhile, the employees and officers of the Company went on a strike from 10.05.2018 demanding higher pay and allowances and as a result of which, the operational and management activities were badly affected. The strike was called-off on 15.06.2018. Thereafter, the appeal was filed on 25.06.2018 before NCLAT with a prayer for condoning the delay in filing the appeal. A single judicial member of NCLT started the hearing. With reference to the provisions of the Companies Act, 2013, examine the following:

i) Whether the appeal is admissible?

ii) Maximum period allowed for condonation

iii) Is the appeal transferable to a Bench consisting of two members?

Answer

Appeal from Orders of Tribunal [Section 421 of the Companies Act, 2013]

(1) **Appeal to AT:** Any person aggrieved by an order of the Tribunal may prefer an appeal to the Appellate Tribunal (AT).

(2) **When order made by consent of parties:** No appeal shall lie to the Appellate Tribunal from an order made by the Tribunal with the consent of parties.

(3) **Period for filing of appeal:** Every appeal under sub-section (1) (i.e. appeal to AT against order of Tribunal) shall be filed within a period of 45 days from the date on which a copy of the order of the Tribunal is made available to the person aggrieved and shall be in such form, and accompanied by such fees, as may be prescribed.

However, the Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days from the date aforesaid, but within a further period not exceeding 45, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within that period.

In the instant case,

i) The appeal is admissible as the order of NCLT was passed without the consent of the parties.

ii) The maximum period allowed for condonation is 45 days if the AT is satisfied that the appellant was prevented by sufficient cause from filing the appeal within that period. In the instant case, the appeal filed on 25.06.2018 before NCLAT is tenable.

iii) As per second proviso to section 419(3) if at any stage of the hearing of any such case or matter, it appears to the Member that the case or matter is of such a nature that it ought to be heard by a Bench consisting of two Members, the case or matter may be transferred by the President, or, as the case may be, referred to him for transfer, to such Bench as the President may deem fit.

Question 2 ***(May 19)***

Aggrieved by an order of Hon'ble NCLT, dated 3rd April, 2018, passed without the consent of parties, Solan Minerals Limited decided to file an appeal before Hon'ble NCLAT. The order was

received by the company on 4th April, 2018. The employees and officers went on a strike for a period of 10 days from 22nd May, 2018 demanding higher bonus and pay. In view of this, the management of the company was forced to a grinding halt during the strike period. Thereafter, the appeal was filed on 6th June, 2018 before the Hon'ble NCLAT and the company prayed for condonation of delay. Referring to and analysing the applicable provisions of the Companies Act, 2013, decide the following:

i) Whether the proposed appeal would be admitted by the Hon'ble NCLAT.

ii) What is the maximum period allowed by the NCLAT for condonation of delay?

Answer

Appeal from Orders of Tribunal [Section 421 of the Companies Act, 2013]

a) **Appeal to Appellate Tribunal:** Any person aggrieved by an order of the Tribunal may prefer an appeal to the Appellate Tribunal (AT).

b) **When order made by consent of parties:** No appeal shall lie to the Appellate Tribunal from an order made by the Tribunal with the consent of parties.

c) **Period for filing of appeal:** Every appeal against order of Tribunal, shall be filed **within a period of 45 days** from the date on which a copy of the order of the Tribunal is made available to the person aggrieved.

d) **Extension of period:** However, the Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days from the date aforesaid, **but within a further period not exceeding 45**, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within that period.

Thus,

i) In the instant case, the appeal was filed on 6th June, 2018 before the NCLAT, and Company prayed for condonation of delay. As per the provisions of the Act, the appeal should have been filed with NCLAT by 19th May, 2018 (i.e. 45 days from 4th April, 2018). Though the appeal could have been admitted on the grounds that the order of NCLT was passed without the consent of the parties. But the appeal was not tendered within the prescribed time. Further, the delay of condonation cannot be given as the strike started in the company from 22nd May, 2018 i.e. after 45 days of receiving the order of the NCLT and thus, the appellant was not prevented by sufficient cause from filing the appeal within the prescribed period. Hence the proposed appeal by Solan Minerals Limited will not be admitted by the NCLAT.

ii) The maximum period allowed for condonation is **45 days** if the AT is satisfied that the appellant was prevented by sufficient cause from filing the appeal within that period.

Appeal to Supreme Court (Section 423)

Question 3 ***(May 18)***

JSK, a shareholder of CRI (Private) Ltd. filed an application before erstwhile Company Law Board, alleging various acts of oppression and mis-management in the affairs of the Company and sought certain relief measures. The petition was transferred to NCLT on its constitution. The NCLT passed an order on 5th October, 2017 without the consent of the parties. Aggrieved by the order, the shareholder decided to prefer an appeal. Nevertheless the shareholder was suffering from low blood pressure. He was medically advised not to move and he did not move. Therefore, he preferred the appeal with NCLAT on 5th December, 2017. Examine whether the appeal is admissible with reference to time limitation?

Identify the provisions governing further appeal on the orders of NCLAT under Section 423 of the Companies Act, 2013.

Answer

Appeal from Orders of Tribunal: According to **Section 421** of the Companies Act, 2013, any **person aggrieved by an Order of the Tribunal may prefer an appeal to the Appellate Tribunal**. However, no appeal shall lie to the Appellate Tribunal from an Order which was made by the Tribunal with consent of parties.

***Time period of appeal:** Every appeal in the above case, shall be filed within a period of **forty-five days** from the date on which a copy of the order of Tribunal is made available to the person aggrieved.

Provided that the Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days, but within a **further period not exceeding forty-five days**, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within that period.

In the given situation, NCLT passed an order on 5th October, 2017 without the consent of the parties on the acts of oppression and mis-management in the affairs of the company and for the obtaining certain relief measures.

JSK, a shareholder, aggrieved by an order of NCLT, can prefer an appeal in the NCLAT within 45 days from the date on which a copy of the order of Tribunal is made available to the person aggrieved. However, on reasonable ground this period may be further extended by 45 days i.e. within 90 days from the date on which a copy of the order of Tribunal is received by JSK.

Further Appeal on the orders of NCLAT: **Section 423** of the Companies Act, 2013 provides that any person aggrieved by any order of the **Appellate Tribunal may file an appeal to the Supreme Court within sixty days** from the date of receipt of the order of the Appellate Tribunal to him on any question of law arising out of such order.

Provided that the Supreme Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be **filed within a further period not exceeding sixty days**

*** Assumption: In the question, date of order of the NCLT may be taken as the date on which a copy of the order of Tribunal is made available to the person aggrieved to answer the question within the provided information**.

Ch 13 – Registered Valuers

Registered Valuers (Section 247)

Question 1 ***(Nov 18, RTP May 19)***

The Board of Directors of M/s APCO Limited a listed company, for carrying out the valuation of the immovable properties standing in the name of the company as required under the provisions of the Companies Act, 2013 proposes to appoint Mr. Mehta, an individual as the valuer. Referring to the provisions of the Companies Act, 2013 read with the Companies (Registered Valuers and Valuation) Rules, 2017, the Audit Committee is of the opinion that the Board of Directors does not have the right to appoint the valuer. Decide.

Answer

Valuation by Registered Valuers (Section 247): According to the provisions of the section 247 of the Companies Act, 2013 read with the Companies (Registered Valuers and Valuation) Rules, 2017, where a valuation is required to be made in respect of any property, stocks, shares, debentures, securities or goodwill or any other assets (herein referred to as the assets) or net worth of a company or its liabilities under the provision of this Act, it shall be valued bya person having such qualifications and experience and registered as a valuer in such manner, on such terms and conditions as may be

i) prescribed and appointed by the audit committee or in its absence by the Board of Directors of that company.

ii) Hence, in the given instance, proposal for appointment of Mr. Mehta as the valuer by the Board of directors of M/s APCL Ltd. is against the said provision. In fact, valuer shall be appointed by the audit committee or in its absence by the Board of Directors of that company.

iii) In view of above, the opinion of the Audit Committee is correct.

Ch 14 – Corporate Secretarial Practice- Drafting of Resolution, Minutes, Notices and Reports

Question 1

Draft a resolution proposed to be passed at a General Meeting of a Public Company giving consent to the Board of Directors for borrowing upto a specified amount in excess of the limits laid down under Section 180(1)(c) of the Companies Act, 2013 and also state the borrowings, which are to be excluded from the said limits.

Answer

Draft of special resolution under Section 180 (1) (c) of the Companies Act, 2013

"Resolved that the company hereby accords the consent of members to the Board of Directors for borrowing money together with the monies already borrowed by the company for an aggregate sum not exceeding `……(Rupees……..) in excess of the aggregate of the paid-up capital of the company and its free reserves, that is to say reserves apart from temporary loans taken by the company from its bankers in the ordinary course of business, as provided in Section 180(1)(c) of the Companies Act, 2013.

Resolved further that the powers given as above shall be exercised by the Board of Directors at a duly convened meeting of the Board and not by passing resolution by circulation".

Borrowings excluded from the said limits under section 180(1)(c)

Section 180(1)(c) excludes from the prescribed limits of borrowing under section 180 (1) (c) those temporary loans taken by the company from its bankers in the ordinary course of business. Therefore, in calculating the limits stipulated in section 180 (1) (c), temporary loans obtained from the company's bankers in the ordinary course of business shall be excluded.

The expression 'temporary loans' means loans repayable and demand or within six months from the date of the loan such as short term cash credit arrangements, the discounting of bills and the issue of other short terms loans of a seasonal character, but does not include loans raised for the purpose of financing expenditure of capital nature [Explanation to Section 180(1)(c)].

Question 2

Answer any **one** of the following:

(i) Board of Directors of DBM Limited held a board meeting on 2nd May, 2014 at its registered office. You are required to state the salient points to be taken into account while drafting the minutes of the said board meeting.

(ii) Draft a board resolution for appointment of Mr. Paul as the managing director for 5 years with effect from 1st June, 2014 of DBM Limited passed in the above stated board meeting.

Answer

i) While drafting the minutes of a board meeting following salient points should be kept in mind:

(a) the minutes may be drafted in a tabular form or they may be drafted in the form of a series of paragraphs, numbered consecutively and with relevant headings.

(b) the place, date and time of the meeting should be stated.

(c) The chairman of the meeting must be mentioned. The general phrase used in the Minutes is

"Mr.---, chairman of the meeting took the chair and called the meeting to order".

(d) the minutes should clearly mention the attendance and the constitution of the meeting, i.e., persons present and the capacity in which present, e.g. name of the person chairing the meeting, names of the directors and secretary, identifying them as director or secretary, names of persons in attendance like auditor, internal auditor etc. The minutes should also contain the subject of leave of absence granted, if any, to any of the board members.

(e) The adoption of the Minutes of the previous Board Meeting must be the first item on the Agenda by the directors giving their approval and the Chariman signing the Minutes as proof of approval of the Minutes.

(f) Conduct of the business at the meeting should be recorded in the chronological sequence as per the Agenda.

(g) In respect of each item of business the names of the directors dissenting or not concurring with any resolution passed at the board meeting should be mentioned.

(h) Reference about interested directors abstaining from voting is also required to be stated in the minutes.

(i) Chairman's signature and date of verification of minutes as correct.

ii) Resolution passed at the meeting of board of directors of DBM Limited held at its registered office situated at …… on 2nd May, 2014 at …… A.M.

"RESOLVED that subject to the approval by the shareholders in a general meeting and pursuant to the provisions of the applicable provisions of the Companies Act, 2013, Mr. Paul be and is hereby appointed as the Managing Director of the Company with effect from 1st June, 2014 for a period of five years on a remuneration approved by the Remuneration Committee as enumerated below:

(1) Salary: ` …… per month

(2) Perquisites, Benefits and Facilities …….

RESOLVED FURTHER that Mr. Paul, so long as he functions as the Managing Director of the Company shall not be entitled to any sitting fee for attending the meeting of the board of directors or any committee thereof and that he shall not be liable to retire by rotation.

RESOLVED FURTHER that the Secretary of the company be and is hereby directed and authorized to file necessary returns with the Registrar of Companies and to do all other necessary things required under the provisions of the Companies Act, 2013."

Question 3

The Board of Directors of XYZ Limited decided to pass a resolution to purchase 35,000 equity shares of Rs. 100 each of PQR Limited at a meeting. Draft a specimen Board Resolution to be passed at the said meeting.

Answer

Specimen Board Resolution: Purchase of Equity Shares Resolution passed at the meeting of the board of directors of XYZ Limited held at its registered office situated at _____ on _____ (day) at _____ A.M.

"Resolved unanimously that pursuant to provisions of Section 186(2) of the Companies Act, 2013, the company be and is hereby authorized to purchase 35,000 equity shares of ₹ 100 each of PQR Limited, the investment in addition to other investments made to date in the aggregate being within

the limits prescribed under the said section."

"Resolved further that Mr. ……., a Director of the company, be and is hereby authorised to sign /execute the necessary documents in this connection."

Sd/-

Board of Directors of XYZ Limited

Question 4

The members of XYZ Limited decided to pass a resolution for appointing Mr. Smith as an Independent director of the company. Draft a specimen resolution to be passed at the said meeting.

Answer

Specimen Board Resolution: Purchase of Equity Shares

Resolution passed at the meeting of the board of directors of XYZ Limited held at its registered office situated at on_____(day) at_A.M.

"Resolved unanimously that pursuant to provisions of Section 186(2) of the Companies Act, 2013, the company be and is hereby authorized to purchase 35,000 equity shares of ₹ 100 each of PQR Limited, the investment in addition to other investments made to date in the aggregate being within the limits prescribed under the said section."

"Resolved further that Mr. ……., a Director of the company, be and is hereby authorised to sign/execute the necessary documents in this connection."

Sd/-

Board of Directors XYZ Limited

Question 5

The members of XYZ Limited decided to pass a resolution for appointing Mr. Smith as an Independent director of the company. Draft a specimen resolution to be passed at the said meeting.

Answer

Appointment of Independent Director – Ordinary Resolution

"RESOLVED that pursuant to the provisions of Sections 149, 150, 152 and any other applicable provisions of the Companies Act, 2013 and the rules made thereunder (including any statutory modification(s) or re- enactment thereof for the time being in force) read with Schedule IV to the Companies Act, 2013, Mr. Smith (holding DIN -------), Director of the Company who retires by rotation at the Annual General Meeting and in respect of whom the Company has received a notice in writing from a member proposing his candidature for the office of Director, be and is hereby appointed as an Independent Director of the Company to hold office for five consecutive years for a term up to ---, 20--."

Question 6

Mr. N is appointed as an additional Director by the Board of Directors of MNR Company Limited at its meeting held on 1st October, 2014 for a period as permitted by law.
Draft a resolution and state the body which appoints N.

Answer

Appointment of Additional Director: Resolution (Section 161 of the Companies Act, 2013) According to **Section 161(1)** of the Companies Act, 2013, the articles of a company may confer on its Board of Directors the power to appoint any person as an additional director at any time.

Board Resolution
"Resolved that pursuant to the Articles of Association of the company and section 161(1) of the Companies Act, 2013, Mr. N is appointed as an Additional Director of the MNR Company Limited with effect from 1st October, 2014 to hold office up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier.

Resolved further that Mr. N will enjoy the same powers and rights as other directors.

Resolved further that Mr._____Secretary of MNR Company Limited be and is hereby authorised to electronically file necessary returns with the Registrar of Companies and to do all other necessary things required under the Act."
Assumption: As the question is silent about the Articles of Association, it is assumed that Articles of Association has conferred the power to appoint the additional director on the Board of Directors of MNR Company Limited.

Question 7

The Board of Directors of RPS Limited decides to pass a resolution by circulation for allotment of 1,000 equity shares to Mr. A. Draft a specimen Board Resolution to be passed by circulation for this purpose.

Answer
Specimen Board Resolution – Passed by circulation RPS Limited (Place)

To,
Mr.X (Director)
(Address in India only)

Dear Sir,

The following resolution which is intended to be passed as a resolution by circulation as provided in Section 175 of the Companies Act, 2013 is circulated herewith as per the provisions of the said section.

If only you are Not Interested in the resolution, you may please indicate by appending your signature in the space provided beneath the resolution appearing herein below as a separate perforated slip, if you are in favour or against the said resolution. The perforated slip may please be returned if and when signed within seven days of this letter.

However, it need not be returned if you are interested in the resolution.

Yours faithfully,
(Secretary) RPS Limited

Question 8

Elaborate the provisions of the Companies Act, 2013 regarding Notice of Board Meeting. Draft a notice for the first meeting of the Board of Directors of India Timber Ltd.

Answer

Notice of Board Meeting: Notice of Board Meeting is required pursuant to Section 173(3) of the Companies Act, 2013. According to this section, **a meeting of the Board shall be called by giving not less than seven days' notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means.**

Further, a meeting of the Board may be called at shorter notice to transact urgent business subject to the condition that at least one independent director, if any, shall be present at the meeting.

In case of absence of independent directors from such a meeting of the Board, decisions taken at such a meeting shall be circulated to all the directors and shall be final only on ratification thereof by at least one independent director, if any.

The Companies (Meetings of Board and its Powers) Rules, 2014, further provides that the notice of the meeting shall inform the directors regarding the option available to them to participate through video conferencing mode or other audio visual means, **and shall provide all the necessary information to enable the directors to participate through video conferencing mode or other audio visual means.**

On receiving such a notice, a director intending to participate through video conferencing or audio visual means shall communicate his intention to the Chairperson or the company secretary of the company. He shall give prior intimation to the effect sufficiently in advance so that the company is able to make suitable arrangements in this behalf.
If the director does not give any intimation of his intention to participate that he wants to participate through the electronic mode, it shall be assumed that the director shall attend the meeting in person.

As per section 173(4) of the Companies Act, 2013, every officer of the company whose duty is to give notice under this section and who fails to do so shall be liable to a penalty of ₹ 25,000.

Draft Notice

India Timber Limited

Address: _____

Dated: _____

To
Mr._____

Address: _____

_____ (each director to be addressed individually)

Dear Sir,

Notice is hereby given that first meeting of the Board of Directors will be held at the registered office of the company at …….(address)……..(place) on…..(day), the.....(date) at……AM/PM.
You are requested to make it convenient to attend the meeting. An option is also available to you to participate in the Board Meeting through video conferencing or audio visual means. Kindly communicate your preference in this regard.
A copy of the agenda of the meeting is enclosed for your perusal.

Yours faithfully,
For India Timber Ltd
(Secretary)

Question 9

R Ltd. wants to constitute an Audit Committee. Draft a board resolution covering the following matters [compliance with Companies Act, 2013 to be ensured].

1) Member of the Audit Committee.
2) Chairman of the Audit Committee
3) Any 2 functions of the said Committee

Answer

Audit Committee – Board's Resolution:

"Resolved that pursuant to Section 177 of the Companies Act, 2013 an Audit Committee consisting of the following Directors be and is hereby constituted.

1. Mr. ---- Independent Director
2. Mr. ---- Independent Director
3. Mr. ---- Independent Director
4. Mr. ---- Independent Director
5. Mr. ---- Managing Director.
6. Mr. ---- Chief Financial Officer"

"Further resolved that the Chairman of the Audit Committee shall be elected by its members from amongst themselves and shall be an independent director'.

"Further resolved that the quorum for a meeting of the Audit committee shall be three directors (other than the Managing Director), out of which at least two must be independent directors".

"Resolved further that the Audit Committee shall perform all the functions as laid down in section 177(4) of the Companies Act, 2013 including but not limited to:

a) make the recommendation for appointment, remuneration and terms of appointment of the auditors of the company;
b) review and monitor the independence and performance of auditors of the company and the effectiveness of the audit process".

Further resolved that the Audit Committee shall review the quarterly and annual financial statements and submit the same to the Board with its recommendations if any"

Question 10

The Board of Directors of Luxury Limited in consistent with the Articles of Association of the company, appointed Mr. More as an additional Director at its meeting held on 1st October, 2016 for a period as permitted by law.

Draft a resolution stating appointment of Mr. More in the said company.

Answer

Board Resolution for appointment of an additional director

"Resolved that pursuant to the Articles of Association of the company and section 161(1) of the Companies Act, 2013, Mr. More is appointed as an Additional Director of the Luxury Limited with effect from 1st October, 2016 to hold office up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier.

Resolved further that Mr. More will enjoy the same powers and rights as other directors.

Resolved further that Mr. Secretary of Luxury Limited be and is hereby authorized to electronically

file necessary returns with the Registrar of Companies and to do all other necessary things required under the Act."

Ch. 1 – Securities Contracts (Regulation) Act, 1956

Definitions (Section 2)

Question 1 ***(RTP May 2018)***

A company Cookies Private Limited has two shareholders, Mr. Rock and Mr. Salt. Mr. Rock decides to sell his part of shares in Cookies Private Limited to another company, Crispy Private Limited for a specified monetary consideration. State how should Mr. Rock proceed to document the transaction so as to make it legally binding on both the parties under the Securities Contract (Regulation) Act, 1956?

Answer

As per the stated facts, Mr. Rock decides to sell his part of the share in other company. So, such an understanding of transfer of the shares of Cookies Private Limited held by Mr. Rock to Crispy Private Limited shall be recorded in Share Purchase Agreement (SPA), which is a legally binding contract, and lists down all the terms and conditions which are relevant to the sale of shares, such as –

i) the exact description of shares, i.e. the number of shares, price per share, premium amount, if any;
ii) the conditions that must be satisfied before the sale takes place;
iii) the date on which the sale will be completed;
iv) the manner in which the transfer will be made;
v) any indemnities or protections available to the parties;
vi) the representations and warranties made by either party; and
vii) the conditions upon which the agreement will terminate.

Question 2 ***(RTP May 2018)***

Mr. Vivaan is having 400 shares of Travel Everywhere Limited and the current price of these shares in the market is ₹ 100. Vivaan's goal is to sell these shares in 6 months' time. However, he is worried that the price of these shares could fall considerably, by then. At the same time, Vivaan doesn't want to sell off these shares today, as he conjectured that the share price might appreciate in the near future. Determine how should Mr. Vivaan protect his security and reduce the risk of loss on the share price under the Securities Contract (Regulation) Act, 1956?

Answer

In this case, Mr. Vivaan may opt for 'Option' derivative contract, which is an agreement to buy or sell a set of assets at a specified time in the future for a specified amount. However, it is not obligatory for him to hold the terms of the agreement, since he has an 'option' to exercise the contract. For example, if the current market price of the share is ₹ 100 and he buy an option to sell the shares to Mr. X at ₹ 200 after three-month, so Vivaan bought a put option.

Now, if after three months, the current price of the shares is ₹ 210, Mr. Vivaan may opt not to sell the shares to Mr. X and instead sell them in the market, thus making a profit of ₹ 110. Had the market price of the shares after three months would have been ₹ 90, Mr. Vivaan would have obliged the option contract and sold those shares to Mr. X, thus making a profit, even though the current market price was below the contracted price. Thus, here, the shares of Travel Everywhere Limited is the underlying asset and the option contract is a form of derivative.

Question 3 ***(May 2017)***

Mr. Veer a newly entered investor in the field of securities business seeks your advice on the investments to be made in securities of large Companies for long term purposes. With this object in view, he wants to know the meaning of the following terms commonly used in any stock exchange.

a) Derivative

b) Option in securities

c) Spot delivery contract. Advise suitably.

Or

Define the term "Derivative" as appearing in the Securities Contracts (Regulation) Act, 1956

(May 2019)

Answer

Mr. Veer, a new investor, desirous of entering investments business in any Stock Exchange, can be advised on different terms commonly used in any Stock Exchange.

a) Derivative: Derivative includes –

i) a security derived from a debt instrument, share, loan whether secured or unsecured risk instrument or contract for differences or any other form of security.

ii) a contract, which derives its value from the prices or index of prices, of underlying securities.

iii) Commodity derivatives

iv) Such other instruments as may be declared by the Central Government to be derivatives

b) Option in Securities:

Option in Securities means a contract for the purchase or sale of a right to buy or sell or a right to buy and sell, securities in future, and includes a teji, a mandi, a tejimandi, a galli, a put, a call or a put and call securities.

c) Spot Delivery Contract

Spot delivery contract means a contract which provides for:

i) Actual delivery of securities and the payment of a price therefore either on the same day as the Chapter date of the contract or on the next day, the actual period taken for the dispatch of the securities or the remittance of money therefore through the post being excluded from the computation of the period aforesaid if the parties to the contract do not reside in the same town or locality.

ii) Transfer of the securities by the depository from the account of a beneficial owner to the account of another beneficial owner when such securities are dealt with by a depository.

Question 4 ***(May 2018)***

Explain the meaning of the term "Demutualization" used under the Securities Contracts (Regulation) Act, 1956.

Answer

Meaning of "Demutualisation"

According to Section 2(ab) of the Securities Contracts (Regulation) Act, 1956, "Demutualisation" means the segregation of ownership and management from the trading rights of the members of a recognised stock exchange in accordance with a scheme approved by the Securities and Exchange Board of India.

In simple words, it is a term used to describe the transition from mutual association of exchange members operating on a not-for-profit basis to a limited liability, for-profit company, accountable to shareholders. Essentially, demutualisation separates ownership (and voting right) from the right of access to trading.

Recognition of Stock Exchange (Section 3-5, Rules 3-7)

Question 5

Rampur Stock Exchange wants to get itself recognized. Explain:

a) Who enjoys the power to recognize stock exchange?
b) What information will have to be provided with the application for recognition?

Answer

a) Power to recognize Stock Exchange vests with Central Government. However, Central Government has delegated the powers to SEBI vide its notification No.F.No.1/57/SE/93 dated 13.9.94. (Section 3 of Securities Contracts (Regulation) Act, 1956).

b) Application for recognition must be accompanied with Bye-Laws, Rules, Regulations which must contain specific details on:

1. **Constitution, powers of management and manner of transacting business** by the Governing Body of the Stock Exchange.
2. **Power's and duties** of the offer bearers of Stock Exchange.
3. **Various classes of Members, qualification of membership and the exclusion, suspension, expulsion and re-admission of members**.
4. The **procedure for registration of Partnerships** as members to stock exchange and rules of nomination of authorized representatives.

   Membership provisions, composition of Board, Powers of Governing Board are defined in the Articles of the Exchange. Rules governing Listing, Trading and Settlement, Penalties and Prohibitions, Disciplinary Actions and Defaults are defined in Bye-Laws of the Exchange.

Question 6

Referring to the provisions of the Securities Contracts (Regulation) Act, 1956:

a) Examine the extent to which the Central Government is empowered to suspend business of a recognized Stock Exchange.
b) The Central Government has granted recognition to a Stock Exchange. To what conditions may such a recognition be subject to?

Answer

a) **Power of the Central Government to suspend business at a Stock Exchange:** Section 12, Securities Contracts (Regulations) Act, 1956.

   If in the opinion of the **Central Government an emergency has arisen and for the purpose of meeting of the emergency the Central Government considers it expedient so to do**, it may, by Notification in the Official Gazette, for reasons to be set out therein, direct a recognized stock exchange to suspend such of its business for such period **not exceeding 7 days** and subject to such conditions as may be specified in the notification, and if in the opinion of the Central Government the:

   i) **interest of the trade** or

ii) **the public interest requires that the period should be extended, may, by like notification extend the said period from time to time.**

Provided that where the period of suspension is to be extended beyond the first period, no notification extending the period of suspension shall be issued unless the Governing Body of the recognized Stock Exchange has been given an opportunity of being head in the matter.

b) **Grant of recognition to stock exchanges** - Conditions: Section 4(2), SCRA, 1956.
The conditions may include, condition relating to:
   i) Qualification for Membership of the Stock Exchange.
   ii) Manner in which contracts shall be entered into and enforced as between members.
   iii) Representation of the Central Government. on the Stock Exchange (not exceeding 3 nominated by the Central Government.)
   iv) Maintenance of Accounts of members and their audit by Chartered Accountants wherever audit is required by the Central Government.

Question 7

Working of City Stock Exchange Association Ltd. is not being carried on by its Governing Board in public interest. On receipt of representations from various Investors and Investors' Association, the Central Government is thinking to withdraw the recognition granted to the said Stock Exchange. You are required to state the circumstances and procedure for withdrawal of such recognition as per the provisions of Securities Contracts (Regulation) Act, 1956 in this regard. Also state the effect of such withdrawal on the contracts outstanding on the date of withdrawal. ***(May 2018)***

Answer

a) The Central Government by virtue of powers as conferred upon it under Section 5 of the Securities Contracts (Regulation) Act, 1956, **may withdraw the recognition after serving due notice on the governing Board of the Stock Exchange.**
b) **Withdrawal however will not affect the validity of contracts enter into before the date of withdrawal of notification** (sub-section 1).
c) Sub-section (2) provides that where the recognized stock exchange has not been corporatized or demutualized or it fails to submit the scheme referred to in sub-section (1) of Section 4B within the specified time therefore or the scheme has been rejected by the Securities Exchange Board of India under sub-section (5) of section 4B, **the recognition granted to such stock exchange** under Section 4, shall, notwithstanding anything to the contrary contained in this Act, **stand withdrawn and the Central Government shall publish by notification in the Official Gazette, such withdrawal of recognition.**
d) Provided **that no such withdrawal shall the affect the validity of any contract entered into or made before the date of the notification**, and the Securities Exchange Board of India may, after consultation with the stock exchange, make such provisions as it deems fit in the order rejecting the scheme published in the Official Gazette under sub-section (5) of Section 4B.

Question 8 ***(Nov 2010)***

A stock exchange desirous of taking over another stock exchange, seeks your advice on corporatization. Examining the provisions of the Securities Contracts (Regulation) Act, 1956 and the meaning of the terms 'corporatization' and 'demutualization.' Advise the stock exchange about the

steps to be taken to give effect to the scheme of corporatization.

Answer

Corporatization & Demutualization of Stock Exchanges:

Corporatization' means the succession of a recognized stock exchange, being a body of individuals or a society registered under the Societies Registration Act, 1860, by another stock exchange, Being a company incorporated for the purpose of **assisting, regulating or controlling the business of buying, selling or dealing in securities** carried on by such individuals or society.

'Demutualization' means the segregation of ownership and management from the trading rights of the members of a recognized stock exchange in accordance with a scheme approved by the SEBI.

Steps for Corporatization and Demutualization [Section 4B - Securities Contracts (Regulations) Act, 1956]

1. In accordance with the provisions of the Securities Contracts (Regulation) Act, 1956, as contained in section 4B:
2. All recognized stock exchanges referred to in section 4A shall, within such time as may be specified by the SEBI submit a scheme for corporatization and demutualization for its approval.
3. On receipt of the scheme, the SEBI may, after making such enquiry as may be necessary in this behalf and obtaining such further information, if any, as it may require and if it is satisfied that it would be in the interest of the trade and also in the public interest, approve the scheme with or without modification.

   No scheme shall be approved by the SEBI if the issue of shares for a lawful consideration or provision of trading rights in lieu of membership card of the members of a recognized stock exchange or payment of dividends to members has been proposed out of any reserves or assets of that stock exchange.
4. **Where the scheme is approved, the** scheme so approved shall be published immediately by-
   a) **The SEBI in the Official Gazette**
   b) **The recognized Stock Exchange in such** two daily newspapers circulating in India**, as may be specified by the SEBI, and upon such publication, notwithstanding anything to the contrary contained in this Act or any other law for the time being in force or any agreement, award, judgment, decree or other instrument for the time being in force, the** scheme shall have effect and be binding on all persons and authorities including all members, creditors, depositors and employees **of the recognized stock exchange and on all persons having any contract, right, power, obligation or liability with, against, over, to, or in connection with, the recognized stock exchange or its members.**
5. **Where the SEBI is satisfied that it would** not be in the interest of the trade and also in the public interest **to approve the scheme, it may, by an order,** reject the scheme **and such order of rejection shall be published by it in the Official Gazette. SEBI shall give a** reasonable opportunity of being heard **to all the persons concerned and the recognized stock exchange concerned before passing an order rejecting the scheme.**
6. **SEBI may, while approving the scheme by an order in writing, restrict -**
   a) The **voting rights of the shareholders** who are stock brokers of the recognized stock exchange.
   b) The **right of shareholders or a stock broker of the recognized stock exchange** to appoint the representatives on the governing board or the stock exchange.
7. The order made by SEBI shall be published in the Official Gazette and on the publication thereof,

the order, notwithstanding anything to the contrary contained in: the Companies Act,1956. Or any other law for the time being in force, have full effect.

8. Every recognized stock exchange, in respect of which the scheme for corporatization or demutualization has been approved shall either by fresh issue of equity shares to the public or in any other manner as may be specified by the regulations made by SEBI, **ensure that at least 51% of its equity share capital is held, within 12 months** from the date of publication of the order by the public other than shareholders having trading rights. The SEBI may, on sufficient cause being shown to it and in the public interest, **extend the said period by another 12 months.**

Question 9

Explain the powers, which can be exercised by the Securities and Exchange Board of India under the Securities Contracts (Regulation) Act, 1956, while approving the schemes for corporatization and demutualization submitted by recognized stock exchanges, so that there is segregation of ownership and management from the trading rights of members of such stock exchanges.

Answer

Corporatization and Demutualization – Power of SEBI under SCRA, 1956

SEBI has been empowered under sub-section (2) of section 4B of Securities Contracts (Regulation) Act, 1956 to approve the scheme of corporatization and demutualization with or without modification. **SEBI can reject the proposed scheme if it is satisfied that it would not be in the interest of the trade and also in the public interest to approve the scheme**. Besides these general powers, **SEBI has got certain specific powers** under section 4B (6). SEBI, while approving the scheme, may, by an order in writing.

Restrict:

a) The **voting rights of the shareholders** who are also stock-brokers of the recognized stock exchange.

b) The **right of shareholders** in a stockbroker of the recognized stock exchange **to appoint the representatives** on the governing board of the stock exchange.

c) The **maximum number of representatives** of the stock-broker of the recognized stock exchange to be appointed on the governing board of the stock exchange shall not exceed **1/4th of the total strength** of the governing body.

On receipt of approval of scheme, stock exchange will issue shares to public within 12 months so that **at least 51% equity shares are with public other than shareholders having trading rights.** SEBI can extend the period up to another 12 months [Section 4B (8)].

Question 10 ***(Nov 2011)***

The Securities and Exchange Board of India, for the purpose of corporatization and demutualization of a recognized stock exchange issued an order that at least fifty one percent of its equity share capital shall be held, within twelve months, by the public other than share holders having trading rights. Decide whether the said order of the Securities and Exchange Board of India is valid und er the provisions of the Securities Contracts (Regulation) Act, 1956 including the time limit of twelve months as stated in the order.

Answer:

Corporatisation and demutualization:

- According to sub section (8) of Section 4B of the Securities Contracts (Regulation) Act, 1956, every

recognised stock exchange, in respect of which the scheme for corporatisation or demutualisation has been approved shall, either by fresh issue of equity shares to the public or in any other manner as may be specified by the regulations made by the Securities and Exchange Board of India, ensure that at least fifty-one per cent of its equity share capital is held, within twelve months from the date of publication of the order under sub-section (7) of the said section by the public other than shareholders having trading rights.

- However the Securities and Exchange Board of India may, on sufficient cause being shown to it and in the public interest, extend the said period by another twelve months.

Power of CG to call for periodical returns or direct enquiries to be made (Sec. 6)

Question 11 ***(May 2013)***

The Securities and Exchange Board of India received serious complaints against Mr. Satyanarayan, a member of Mavli Stock Exchange. State as to what powers can be exercised by the Securities and Exchange Board of India to make enquiries and to take action in this matter, under the provisions of the Securities Contracts (Regulation) Act, 1956?

Answer:

Disciplinary action against members of Stock Exchange: SEBI can exercise the following powers under Securities Contracts (Regulation) Act, 1956 on receipt of serious complaints against the affairs of Mr. Satyanarayan, a member of Mavli Stock Exchange.

i) SEBI may, if it is satisfied that it is in the **interest of the trade** or. in the **public interest**, by order in writing call upon the member of the stock exchange to furnish in writing information or explanation in respect of the matter under inquiry [Section 6(3)(a)].

ii) SEBI **instead of calling for information, may either appoint one or more persons to make an enquiry or direct the governing body of stock exchange to make inquiry and submit its report to SEBI [Section 6(3)(b)].**

In case of adverse findings, SEBI can direct Mavli Stock Exchange to take **disciplinary action against Mr. Satyanarayan,** such as: fine, expulsion from membership, suspension from membership for a specified period and any other penalty of a like nature not involving the payment of money. Bye-laws of the stock exchange usually provide for such punishment [Section 9(3)(b)]. Mavli Stock Exchange is under obligation to take the action as directed.

Question 12 ***(May 2018)***

In Public interest, HEM Stock Exchange Limited was issued an order by the Stock Exchange Board of India to produce certain information and explanation relating to its operation in writing. The management of the Stock exchange were reluctant to part with such information with SEBI and approached you to seek your advice in the following matters:

i) Duty of HEM Stock Exchange Limited to furnish periodic returns to SEBI;

ii) Power of SEBI to ask for the information asked as stated above, over and above the periodic returns;

iii) Period for which Stock Exchange is required to maintain the books of account which may be inspected by SEBI;

iv) Duty of Stock Exchange and persons dealing with the Sock Exchange with regard to the information sought for by SEBI.

Advice them referring to the relevant provisions of the Securities Contracts (Regulation) Act,

1956.

Answer:

Powers of SEBI to call for periodical returns, etc.

i) As per Sec 6(1) of the Securities Contracts (Regulation) Act, 1956, every recognized stock exchange shall furnish to the SEBI such periodical return relating to its affairs as may be prescribed. These Returns contain information on current affairs of the Exchange including Volume and Value of transactions, short deliveries, important decisions taken by Board etc.

ii) As per Sec 6(3) of the Securities Contracts (Regulation) Act, 1956,SEBI may call for information and explanation from member.

iii) As per Sec 6(2) of the Securities Contract (Regulation) Act,1956,every recognized stock exchange and every member thereof shall maintain and preserve for such periods not exceeding 5 years such books of account as prescribed and these books may be inspected by SEBI at any point of time.

iv) As per Sec 6(4) of the Securities contracts(Regulation) Act,1956, every Director, Manager, Secretary or Officer of Exchange; every member of such Stock Exchange; if the member of Stock Exchange is a firm, every partner, manager, secretary or other officer of the firm and every other person or body of persons who has had dealings in the course of business with any of the persons mentioned above whether directly or indirectly, is bound to provide information to Enquiry officer or SEBI representative who are looking into the affairs of the Exchange.

Miscellaneous Powers of Stock exchanges, C.G. and SEBI (Sec 7A – Sec 12A)

Question 13

PQR Ltd. is holding 33% of the paid up equity capital of Koya Stock Exchange. The company appoints MNL Ltd. as its proxy who is not a member of the Koya Stock Exchange, to attend and vote at the meeting of the stock exchange. Examine whether the Koya Stock Exchange can restrict the appointment of MNL ltd. as proxy for PQR Ltd. and further restrict, the voting rights of PQR Ltd. in the Koya Stock Exchange.

Answer:

Provision:

Section 7(a) of the Securities (Contracts) Regulation Act, 1956 provides that a recognized stock exchange is empowered to amend rules to provide for all or any of the following matters:

a) **Restriction of voting right to members only**.

b) **Regulation of voting rights** by specifying that **each member is entitled to one vote only irrespective of number of shares held.**

c) **Restriction on right of members to appoint proxy.**

Conclusion:

i) As such Koya Stock Exchange can restrict the appointment of MNL Ltd., as proxy, if rules of the exchange so provide. If it is not so provided, rules may be amended and after getting approval of the Central Government regarding amendment, it can restrict appointment of proxies.

ii) Koya Stock Exchange can also restrict the voting rights of PQR Ltd. if rules of the exchange so provide. If it is not so provided, rules maybe amended and after getting approval of Central Government regarding amendment, it can restrict the voting rights of PQR Ltd appointment of

proxies.

Question 14

The management of Rampur Stock Exchange desires to transfer its duties and functions to a clearing corporation. Advise the management of the said stock exchange about the extent of control which may be exercised by the clearing corporation under the Securities Contracts (Regulation) Act, 1956.

Answer:

1) A recognized stock exchange may, with the prior approval of the Securities and Exchange Board of India, transfer the duties and functions of a clearing house to a clearing corporation being a company incorporated under the Companies Act, 1956, for the purpose of -
   a) the periodical settlement of contracts and differences there under;
   b) the delivery of, and payment for, securities;
   c) any other matter incidental to, or connected with, such transfer
2) Every clearing corporation shall, for the purpose of transfer of the duties and functions of a clearing house to a clearing corporation referred to in sub-section (1) make by-laws and submit the same to the Securities and Exchange Board of India for its approval.
3) The securities and Exchange Board of India may, on being satisfied that it is in the interest of the trade and also in the public interest to transfer the duties and functions of a clearing house to a clearing corporation, grant approval to the by-laws submitted to it under sub-section (2) and approve transfer of the duties and functions of a clearing house to a clearing corporation referred to in sub-section (1)
4) The provision of section 4, 5, 6, 7, 8, 9, 10, 11 and 12 shall, as far as may be, apply to a clearing corporation referred to in sub-section (1) as they apply in relation to a recognized stock exchange.

Question 15 ***(Nov 2013)***

A recognized stock exchange proposes to make bye-laws for the regulation and control of contracts relating to the purchase and sale of securities. State the legal requirements under the Securities Contracts (Regulation) Act, 1956 to give effect to the proposal. Explain the powers of the Securities and Exchange Board of India to amend the bye-laws of a recognized stock exchange.

Answer:

Power of Stock Exchange to make bye-laws: Any recognized stock exchange may make bye - laws for the regulation and control of contracts relating to the purchase and sale of securities by complying with the requirements under section 9(1) of the Securities Contracts (Regulation) Act, 1956.

The bye-laws made by the stock exchange are subject to the previous approval of the Securities and Exchange Board of India.

The bye-laws made under this section may

Specify the bye-laws, **the contravention of which shall make a contract void** under sub-section of section 14 of the said Act and **Provide that the contravention of any of the bye-laws** shall render the member concerned **liable to**

i) **punishments**, namely, fine or expulsion from membership or

ii) **suspension from membership** or

iii) **any other penalty** of a like nature not involving the payment of money [Sub-section (3)].

Any bye-laws made under this section shall be subject to such conditions in regard to previous

publication as may be prescribed, and, when approved by the SEBI, shall be published in the Gazette of India and also in the Official Gazette of the State in which the principal office of the recognized stock exchange is situated, and shall have effect as from the date of its publication in the Gazette of India [Sub-section (4)].

If the SEBI is satisfied, in any case, that **in the interest of the trade or in the public interest any bye-laws should be made immediately, it may, by order in writing specifying the reasons therefore, dispense with the condition of previous publication**.

Power of SEBI to amend bye-laws:

a) Section 10 of the Securities Contracts (Regulation) Act, 1956 empowers the SEBI to amend bye-laws of a recognized stock exchange.

b) **SEBI may either on a request in writing received by it** in this behalf from the governing body of a recognized stock exchange **or on its own motion amend any bye-laws** made by such stock exchange.

c) SEBI will have to be satisfied, after consultation with the governing body of the stock exchange that it is necessary or expedient to amend the bye-laws and record its reasons also. Amended bye-laws should be published in the Gazette of India and also in the Official Gazette of the State in which the principal office of the stock exchange is situate.

d) **If the stock exchange has any objection to the amendments made by the SEBI, it may, within 2 months apply to the SEBI for revision.**

Question 16

SEBI is of the opinion that in the interest of investors, it is desirable to amend the rules of RSP Stock Exchange prohibiting the appointment of the broker-member as President of the Stock Exchange. Explain briefly with reference to the provisions of Securities Contracts (Regulation) Act, 1956, whether it is possible for SEBI to amend the rules of the Stock Exchange, if the Stock Exchange does not change the rules.

Answer:

a) In accordance with the provisions of section 8 of Securities Contracts (Regulation) Act, 1956, **the Central Government is empowered to issue**:

b) **written order** directing all or any of the recognized stock exchange to make any rules or to amend any rules already made within **2 months** from the date of the order in respect of matters specified in section 3(2) of the said Act.

c) One of the matters specified in the said section 3(2) is the governing body of stock exchange, its constitution and powers of management and the manner in which its business is to be transacted.

d) Hence, the Central Government is empowered to direct the stock exchange in respect of prohibition on broker-member being appointed as **President of the stock exchange.** According to notification issued by Central Government under section 29A of the said Act, this power is also exercisable by SEBI.

e) If any recognized stock exchange **(SE) fails or neglects to comply with any order made by SEBI within 2 months, SEBI may itself make the rules or amend the rules made by stock exchange**

   i) Either in the form proposed in the order or

   ii) With such modification thereof as may be agreed to between SEBI and the stock exchange.

The amended rules are required to be notified in the Gazette of India and in the Gazette of the State

where the principal office of the stock exchange is situated. After such publication, the rules shall be valid as if the same were made or amended by the recognized stock exchange itself.

Accordingly, of the above provisions of Securities Contracts (Regulation) Act, 1956, SEBI can issue directions to RSP Stock Exchange to amend the rules and if the said stock exchange does not comply with the above, SEBI can amend the rules on its own.

Question 17

Describe the provisions of the Securities Contracts (Regulation) Act, 1956 regarding the powers of the Central Government to supersede the Governing Body of a recognized Stock Exchange and the consequences of such supersession.

Answer:

a) According to the provisions of section 11 of the Securities Contracts (Regulation) Act, 1956, where the **Central Government is of opinion that the governing body of any recognized stock exchange should be superseded**, then notwithstanding anything contained in any other law for the time being in force,

b) The **Central Government may serve on the governing body a written notice** that the Central Government is considering the supersession of the governing body for the reasons specified in the notice**.**

c) **After giving an opportunity to the governing body** of such Stock Exchange to be heard in the matter, the Central Government may, **by notification in the Official Gazette**, **declare the governing body of such Stock Exchange to be superseded.**

d) The Central Government **may appoint any person or persons to exercise and perform all the powers and duties** of the governing body.

e) If more than one person is so appointed, one of them may be the Chairman and another as the Vice- Chairman.

f) **Such person or persons shall hold office for such period as may be specified in the Notification** and the Central Government may vary such period by way of another Notification.

On the publication of the notification in the Official Gazette, **following are the consequences:**

i) **The members** of the governing body of such Stock Exchange **cease to hold office** as such members on and from the date of notification.

ii) The **person or persons appointed by the Central Government may exercise and perform all the powers and duties** of the governing body which has been so superseded.

The **property of the Stock Exchange** as deemed necessary and so specified in writing by such person or persons to carry on the business of the Stock Exchange **shall vest in such person or persons**.

Question 18

Complaints of unethical practices have been received against members of the Governing Body of a Recognized Stock Exchange. Examine whether the Government has any power to take action against the Governing Body of the said exchange.

Answer:

Section 11, of the Securities Contracts (Regulation) Act, 1956 deals with the powers of the Central Government to **supersede the Governing body of a recognized Stock Exchange.**

The Central Government may serve on a governing body a written notice **specifying the reasons and after giving an opportunity to the governing body to be heard**, may, by notification in the Official

Gazette, declare the governing body as superseded. The Central Government after superseding the governing body may appoint any person or persons to exercise and perform all the powers and duties of governing body. **It may also appoint one of such nominees as Chairman.**

Question 19 ***(Nov 2014)***

Complaints of unethical practices have been received against members of a recognized Stock Exchange by the Government. Examine whether the government has any power to suspend the business of such a recognized Stock Exchange.

Answer:

Section 12 of the Securities Contracts (Regulation) Act, 1956 deals with the powers of the Central Government to suspend business of recognized Stock Exchange. Central Government, if it deems fit, is vested with power to suspend business for a period not exceeding 7 days by notification in Gazette. Central Government also have power to extend this period by a like notification. However, such power can be exercised by the Central Government, if it is of opinion that an emergency has arisen and it is expedient so to do.

Question 20 ***(Nov 2016)***

RES Stock Exchange Limited, a recognized stock exchange is involved in training of shares of Son Limited. The SEBI on receiving complaint from a group of investors enquired and found that trading of shares of Son Limited is being conducted in manner detrimental to the interest of the general investors. In order to curb the same, the SEBI wants to issue some directions to RSE stock Exchange Limited. Referring to the provisions of the Securities Contract (Regulation), Act, 1956, discuss whether the SEBI has power to issue such directions. Can such directions be given to an individual who made some profit in any transaction in contravention of any provision of the Securities Contracts (Regulation) Act, 1956, or regulations made thereunder?

Answer:

Powers to issue direction

As per Sec.12A of the Securities Contract (Regulation) Act,1956, where the SEBI is satisfied after an enquiry, that it is necessary-

a) in the interest of investors, or orderly development of securities market; or

b) to prevent the affairs of any recognized stock exchange, or, clearing corporation, or such other agency or person, providing trading or clearing or settlement facility in respect of securities, being conducted in a manner detrimental to the interests of investors or securities market; or

c) to secure the proper management of any such stock exchange or clearing corporation or agency or person, referred to in clause (b),

It may issue such directions,-

i) to any stock exchange or clearing corporation or agency or person referred to in clause (b) or any person or class of persons associated with the securities market.

ii) to any company whose securities are listed or proposed to be listed in a recognized stock exchange,

as may be appropriate in the interest of investors in securities and the securities market.

Conclusion: SEBI may issue such direction to RSE Stock Exchange Ltd.

Explanation given in the section clarifies that power to issue directions under Sec.12A shall include and always be deemed to have been included the power to direct any person, who made profit or

averted loss by indulging in any transaction or activity in contravention of the provisions of this Act or regulations made thereunder, to disgorge an amount equivalent to the wrongful gain made or less averted by such contravention.

So, accordingly the direction can be given to an individual who had made some profit in any transaction in contravention of any provision of the Securities Contract (Regulation) Act,1956.

Contracts and Options in Securities (Sec 13 – Sec 20)

Question 21

Delhi Stock Exchange wants to establish additional Trading Floor. Explain briefly the meaning of and procedure for establishing additional Trading Floor.

Answer:

According to **section 13A** of Securities Contracts (Regulation) Act 1956, a Stock Exchange may establish additional trading floor with the **prior approval** of the Securities Exchange Board of India in accordance with the terms and conditions stipulated by the said Board.

For the purpose of this section **'Additional Trading Floor' means a trading ring or trading facility offered by a recognized stock exchange outside its area of operation to enable the investor to buy and sell securities** through such trading floor under the regulatory frame work of that Stock Exchange.

Question 22 ***(May 2011)***

M/s AB & Company, a member of a recognized stock exchange proposes to buy and sell shares of a particular company on behalf of investors as well as on their own account. They seek your advice as to restrictions, if any, under Securities Contracts (Regulation) Act, 1956 for dealing in securities on their own account. Advise.

Answer:

Members not to act as principals in certain circumstances: Members of stock exchange normally carry out transactions on behalf of investors and hence principal agent relationship exists.

A Member can enter into transaction as principal with another member of the Exchange only. **If he desires to enter into contract as principal with a non-member, then he has to get written consent from such person to act as principal.**

Contract note should indicate that he is acting as principal [Section 15, Securities Contract (Regulation) Act, 1956].

Where the member has secured the consent of such person otherwise than in writing he shall secure written confirmation by such person or such consent within 3 days from the date of the contract **[Proviso to Section 15].**

Spot delivery contracts are outside the preview of section 15 (Section 18).
M/s A & Co., stock broker must bear in mind the above restrictions while entering into any transaction as principal with an on-member.

Listing of Securities (Sec 21 – Sec 22F)

Question 23

The shares of MLM Ltd. were listed in Cochin Stock Exchange. The stock exchange delists the shares of the company. The aggrieved company approaches you to know the remedy available to the

company. Give your suggestion to the company keeping in view the provision of the Securities Contracts (Regulation) Act, 1956.

Answer:

Section 21A of Securities Contracts (Regulation) Act, 1956 contains the **provision relating to delisting of securities**. As per this section:

a) A recognized Stock Exchange **(SE) may delist the securities after recording reasons** therefore from any recognized stock exchange **on any ground or grounds** as may be prescribed under this Act.

b) The Securities of a company shall not be delisted unless the company concerned has been given a **reasonable opportunity of being heard.**

c) A listed company may **file an appeal before** the Securities Appellate Tribunal **(SAT)against the decision of the recognized stock exchange** delisting the securities **within 15 days** from the date of the decision of recognized stock exchange delisting the securities.

d) Securities Appellate Tribunal may, if it is satisfied that the company was prevented by sufficient cause from filing the **appeal within the said period, allow it to be filed within a further period of not exceeding 1 month.**

Conclusion:

So here, the company may make an appeal to the **Securities Appellate Tribunal against the delisting within** 15 days **or such** extended period **not exceeding** 1 month **after showing sufficient cause of not filing within 15 days.**

Question 24 ***(May 2012)***

DVJ Ltd., a company incorporated under Companies Act, 1956 applies to Bombay Stock Exchange for listing of its shares. The Stock Exchange refuses to grant listing without assigning any reasons for refusal. Company seeks your advice on the options available to it against the Stock Exchange and wants to move the Court. Examining the provisions of the Securities Contract (Regulation) Act, Advise the company.

Answer:

Right to appeal to Securities Appellate Tribunal (SAT) against refusal of stock exchange to list securities of public companies:

As per Sec.22A of the Securities Contracts (Regulation) Act,1956, where a recognized stock exchange, acting in pursuance of any power given to it by its bye-laws, refuses to list the securities of any company, the company shall been entitled to be furnished with reasons for such refusal, and may:

a) Within 15 days from date on which the reasons for such refusal are furnished to it, or

b) Where the Stock Exchange has omitted or failed to dispose of, within the time specified, the application for permission for the shares or debentures to be dealt with on the Stock Exchange, within 15 days from the date of expiry of the specified time or within such further period, not exceeding 1 month, as the SAT may, on sufficient cause being shown, allow, appeal to SAT having jurisdiction in the matter against such refusal, omission and failure.

Conclusion : DVJ Ltd. May lodged an appeal with Securities Appellate Tribunal within 15 days

Question 25 ***(May 2018)***

Securities of Herbal Products Limited were listed in Madras Stock Exchange, Which is recognized Stock Exchange. The company has incurred losses during the preceding three consecutive years and it

has also negative net worth. On having such information, Madras Stock Exchange decided to delist the Securities of the company.

Decide the validity of the decision and explain the provisions of Securities Contract (Regulation) Act, 1956 along with the grounds made under the Securities Contract (Regulation) Rules regarding delisting of securities.

Answer:

Delisting of securities

- As per Sec 21A of Securities Contracts (Regulation) Act, 1956, a recognized stock exchange may delist the securities, after recording the reasons thereof, on any of the grounds as may be prescribed. However, securities shall not be delisted unless the company concerned has been given a reasonable opportunity of being heard.
- As per Rule 21 of Securities Contracts (Regulation) Rules, 1957, a recognized stock exchange may, delist any securities listed thereon on any of the following grounds.

a) the company has incurred losses during the preceding 3 consecutive years and it has negative net worth

b) trading in the securities of the company has remained suspended for a period of more than 6 months;

c) the securities of the company has remained infrequently traded during the preceding 3 years;

d) the company or any of its promoter or any of its directors has been convicted for failure to comply with any of the provisions of the Act, or SEBI Act, 1992 or the Depositories Act, 1996 or rules, regulations, agreements made thereunder, as the case may be and awarded a penalty of not less than 1 crore or imprisonment of not less than 3 years;

e) the addresses of the company or any of its promoter or any of its directors, are not known or false addresses have been furnished or the company has changed its registered office in contravention of provisions of the Companies Act, or

f) Shareholding of the company held by the public has come below the minimum level applicable to the company as per the listing agreement under the Act and the company has failed to raise public holding to the required level within the time specified by the recognized stock exchange.

- In the present case, Madras Stock Exchange decided to list the securities of Herbal Products Limited on the ground that the company has incurred losses during the preceding three consecutive years and it has also negative net worth.

  Conclusion: Madras Stock Exchange can delist the securities after providing a reasonable opportunity of being heard to the company.

Question 26 ***(Nov 2018)***

Aggrieved by the Order of Securities Appellate Tribunal (SAT), MNO Ltd. decided to prefer an appeal with the Supreme Court. Identify the provisions governing further appeal on the Order by the Company under the provision of Securities Contracts (Regulation) Act, 1956. Also state whether any question of fact arising out of the Order of SAT can be challenged in the appeal?

Answer:

According to section 22F of the Securities Contracts (Regulation) Act, 1956, any person aggrieved by any decision or order of the Securities Appellate Tribunal (SAT) may file an appeal to the Supreme Court within 60 days from the date of communication of the decision or order of the Securities Appellate Tribunal to him on any question of law arising out of such order. However, the Supreme Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal

within the said period, allow it to be filed within a further period not exceeding 60 days.

From the perusal of the section, it is evident that any question of fact arising out of the Order of SAT cannot be challenged in the appeal.

Penalties & Procedures (Sec 23 – Sec 26E)

Question 27 ***(Nov 2015)***

RPS Ltd. got its shares listed with a Stock Exchange. It has been regularly paying the listing fees. Certain information about share holding pattern etc. was asked by the Stock Exchange, which the company could not supply in the prescribed time. It was then given a further opportunity to furnish the desired information along with supporting document, but in vain, as the company did not maintain any record. What are the penalties leviable against the company under the Securities Contracts (Regulation) Act, 1956 for the failure to furnish the information?

Answer:

According to **section 23 A** of the Securities Contracts (Regulation) Act, 1956, any person who is required under this Act or any rules made thereunder;

a) to furnish any information, document, books, returns or report to a recognized stock exchange, fails to furnish the same within the time specified therefore in the listing agreement or conditions or bye-laws of the recognized stock exchange, shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less for each such failure;

b) to maintain books of account or records, as per the listing agreement or conditions, or bye -laws of a recognised stock exchange and if there is failure to maintain the same, shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees whichever is less.

Therefore, in the given case, RPS Ltd. is liable under section 23A of the Securities Contracts (Regulation) Act, 1956 as it could not supply the certain information asked by the stock exchange and also did not maintain any record.

Question 28 ***(May 2016)***

XYZ, a recognized stock exchange fails to comply with certain directions issued by the Securities and Exchange Board of India and the adjudicating officer initiated proceedings for the purpose of imposing penalty. The stock exchange seeks your advice whether it is possible to go for settlement of the proceedings. Advise explaining the relevant provisions of the Securities Contracts (Regulation) Act, 1956?

Answer:

Settlement of administrative and civil proceedings [Section 23JA of the Securities Contracts (Regulation) Act, 1956]-

a) **Filing of application to the Board -** Notwithstanding anything contained in any other law for the time being in force, any person, against whom any proceedings have been initiated or may be initiated under section 12A or section 23-I, may file an application in writing to the Board proposing for settlement of the proceedings initiated or to be initiated for the alleged defaults.

b) **Board may consider for the settlement -** The Board may, after taking into consideration the nature, gravity and impact of defaults, agree to the proposal for settlement, on payment of such sum by the defaulter or on such other terms as may be determined by the Board in accordance

with the regulations made under the Securities and Exchange Board of India Act, 1992.

c) **Procedure to be followed as prescribed under the SEBI Act**- For the purposes of settlement under this section, the procedure as specified by the Board under the Securities and Exchange Board of India Act, 1992 shall apply.

No appeal to an order- No appeal shall lie under section 23L against any order passed by the Board or the adjudicating officer, as the case may be, under this section.

So according to the above provision of the Securities Contracts (Regulation) Act, 956, XYZ, stock exchange may propose for the settlement of the proceedings.

Question 29 ***(Nov 2012)***

The Securities and Exchange Board of India issued an order against a stock broker to redress the grievances of the investors within the stipulated time. The stock broker failed to do so, which is an offence under the provisions of the Securities Contracts (Regulation) Act, 1956. Decide:

a) Whether the offence committed by the stock broker is compoundable? If so, by whom?
b) Whether this offence can be compounded after institution of proceedings against the stock broker?

Answer:

According to Section 23C of the Securities Contracts (Regulation) Act, 1956, if any stock broker or sub-broker or a company whose securities are listed or proposed to be listed in a recognized stock exchange, after having been called upon by the Securities and Exchange Board of India or a recognized stock exchange in writing, to redress the grievances of the investors, fails to redress such grievances within the time stipulated by the Securities and Exchange Board of India or a recognized stock exchange, he or it shall be liable to a penalty:

i) **1 lakh rupees for each day during which such failure continues or**
ii) **1 crore rupees,**
iii) **whichever is less.**

a) Composition of certain offences:

According to Section 23N of the Act, notwithstanding anything contained in the Code of Criminal Procedure, 1973, **any offence punishable under Securities Contracts (Regulation) Act, 1956,**

i) **not being an offence punishable with imprisonment only**, or
ii) **with imprisonment and also with fine,**
iii) **may either before or after the institution of any proceeding,**

b) Yes this offence can be compounded by a Securities Appellate Tribunal (SAT) or a Court before which such proceedings are pending.

Conclusion:

Thus, in the instant case, offence committed by the stock broker is compoundable as he is punishable with fine only as provided under section 23C.

Yes, this offence can be compounded after institution of proceedings against the stockbroker as it is clearly stated under Section 23N.

Question 30 ***(Nov 2018)***

Primex Securities (P) Ltd. is a Company involved in stock broking and is registered with SEBI. The said broking Company failed to:

- Redress the grievances of the investors within the stipulated time.

- Segregate securities or money of clients and used the same for self use or for any other clients.

The Securities and Exchange Board of India issued an Order against the said Company for committing the above offences. The Managing Director of the Company seeks your advice and the following under the provisions of the Securities Contract (Regulation) Act, 1956.

(i) What is the penalty for the above offences?

(ii) Whether the offence committed by the stock broking company is compoundable? If so, by whom?

Whether this offence can be compounded after institution of proceedings against the stock broking Company?

Answer:

The Managing Director of Primex Securities (P) Ltd. is advised that:

(i) Broking company fails to redress the grievances of the investors within the stipulated time [Section 23C of the Securities Contract (Regulation) Act, 1956]: Fine of at least INR 1,00,000 but may extend to INR 1,00,000 per day during which such failure continues, subject to a maximum of INR 1 crore.

Broking company fails to segregate securities or money of client and used the same for self-use or for any other clients [Section 23D of the Securities Contract (Regulation) Act, 1956: Penalty of at least INR 1,00,000 but it may extend to INR 1 crore.

(ii) **Composition of certain offences (Section 23N):** Any offence punishable under this Act, not being an offence punishable 'with imprisonment' only, or 'with imprisonment and also with fine' may either before or after the institution of any proceeding, be compounded by SAT or a court before which such proceedings are pending.

Hence, the offence committed by the stock broking company is compoundable by SAT or a Court.

Yes, this offence can be compounded after institution of proceedings against the stock broking company but only by SAT or a Court before which such proceedings are pending.

Question 31 ***(May 2019)***

What are the factors to be considered by the Adjudicating Officer while adjudging the quantum of penalty under Sec. 23I of the Securities Contract (Regulation) Act, 1956?

Answer:

Factors to be taken into account by Adjudicating Officer [Section 23J of Securities Contract (Regulation) Act, 1956]

While adjudging the quantum of penalty under section 23-I, the adjudicating officer shall have due regard to the following factors –

a) The amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default;

b) The amount of loss caused to an investor or group of investors as a result of the default;

c) The repetitive nature of the default.

The power of the Adjudicating Officer to adjudge the quantum of penalty levied under sections 23A to 23C shall be and shall always be deemed to have exercised under the provisions of this section.

Question 32 ***(Nov 2018)***

State the Special Provisions related to commodity derivatives inserted in the Finance Act, 2015, with effect from 28 09.2015 in the Securities Contracts (Regulation) Act, 1956.

Answer:

Special Provisions related to commodity derivatives [Section 30A of the Securities Contracts (Regulation) Act, 1956]

(1) Nothing contained in this Act shall apply to non-transferable specific delivery contracts: Provided that no person shall organise or assist in organising or be a member of any association in any area to which the provisions of section 13 have been made applicable (other than a stock exchange) which provides facilities for the performance of any non-transferable specific delivery contract by any party thereto without having to make or receive actual delivery to or from the other party to the contract or to or from any other party named in the contract.

(2) Where in respect of any area, the provisions of section 13 have been made applicable in relation to commodity derivatives for the sale or purchase of any goods or class of goods, the Central Government may, by notification, declare that in the said area or any part thereof as may be specified in the notification all or any of the provisions of this Act shall not apply to transferable specific delivery contracts for the sale or purchase of the said goods or class of goods either generally, or to any class of such contracts in particular.

Notwithstanding anything contained in sub-section (1), if the Central Government is of the opinion that in the interest of the trade or in the public interest it is expedient to regulate and control non-transferable specific delivery contracts in any area, it may, by notification in the Official Gazette, declare that all or any of the provisions of this Act shall apply to such class or classes of non-transferable specific delivery contracts in such area in respect of such goods or class of goods as may be specified in the notification, and may also specify the manner in which and the extent to which all or any of the said provisions shall so apply.

Ch. 2A – The Securities and Exchange Board of India Act, 1992

Basics of SEBI Act, 1992

Question 1

Explain briefly the purpose of establishing SEBI.

Answer:

The purpose of the SEBI Act is to provide for the establishment of a Board called Securities and Exchange Board of India (SEBI).

The **Preamble to the Act provides for the establishment of a Board to**:

a) **Protect the interests** of investors in securities,
b) **Promote the development** of the securities market,
c) To **regulate the securities market**, and
d) For matters connected therewith or incidental thereto.

The Securities and Exchange Board of India (SEBI) was **set up to achieve the following objectives**:

i) To **promote fair dealings** by the issuers of securities and ensure a market place where they can raise funds at a relatively low cost.

ii) To **provide a degree of protection** to the investors and safeguard their rights and interests so that there is a steady flow of savings into the market.

To **regulate and develop a code of conduct and fair practices** by intermediaries like brokers, merchant bankers, etc., with a view to making them competitive and professional.

Establishment of SEBI

Question 2

On Completion of 60 years of age as on 31st March 2017, Mr. Jain retired as a professor from a University .From 1st April 2017, he was appointed as chairman of the SEBI for a period of 3 years. Under the provisions of the SEBI Act, 1992. Decide whether he can be re-appointed on the same post after expiry of original tenure? Also state whether it could be possible for him to relinquish the office before expiry of his tenure?

Answer:

Appointment of Chairman

- As per Sec.5 of the SEBI Act, 1992 read with Rule 3 of SEBI (Terms and Condition of Chairman mad Members) Rules, 1992, the Chairman may hold office for period of 3 years subject to the maximum age limit of 65 years and can be re-appointed by the C.G
- In the present case, Mr. Jain retired as professor from university on completion of 60 years of age as on 31st March, 2017 and appointed as Chairman of SEBI from 1st April, 2017 for a period of 3 years.

Conclusion: Mr. Jain can be reappointed after expiry of the original tenure of 3 years, but only upto 65 years of age i.e up to 31st March, 2022 (i.e only for 2 years)

Right to Relinquish the office: The Chairman shall have the right to relinquish office at any time before the expiry of their tenure by giving a notice of 3 months in writing to the C.G

Question 3

A group of complainants have alleged that Mr. Z, a Member of the Securities and Exchange Board of India (SEBI) has pecuniary interest in some of the cases that came up before the Board and that he misused his position and therefore, he should be removed from his office. The complainants seek your advice. Advise.

Answer:

Provision: Removal of Member of the SEBI (Section 6 of the Securities and Exchange Board of India Act, 1992)

According to section 6 of the Securities and Exchange Board of India Act, 1992, the Central Government shall have the power to remove a member appointed to the Board, if he:

a) Is, or at any time has been **adjudicated as insolvent**;
b) Is of **unsound mind** and stands so declared by a competent court;
c) Has been **convicted of an offence** which, in the opinion of the Central Government, **involves a moral turpitude** has, in the opinion of the Central Government so abused his position as to render his continuance in office **detrimental to the public interest.** Before removing a member, he will be given a **reasonable opportunity of being heard** in the matter.

Conclusion:

In the present case, a group of complainants have alleged that Mr. Z, a member of the SEBI has pecuniary interest in some of the cases that came up before the Board and he misused his position and therefore, he **should be removed** from his office.

Here, above **complainants may approach the Central Government** for removal of Mr. Z, a member of the SEBI and if the Central Government is of the opinion that **Mr. Z has so abused his position as to render his continuation in office detrimental to the public interest**, the Central Government may remove Mr. Z from his office after giving him a reasonable opportunity of being heard in the matter.

Powers and Functions of SEBI (Sec 11 – Sec 11D)

Question 4 ***(May 2016, Nov 18, RTP – May 19)***

Securities and Exchange Board of India (SEBI) has undertaken inspection of books of accounts and records of LR Ltd., a listed public company. Specify the measures which may be taken by SEBI under the Securities and Exchange Board of India Act, 1992 to protect the interest of investors and securities market, on completion of such inquiry.

Answer:

As per **section 11 (4)** of the Securities and Exchange Board of India Act, 1992, the Board may, by an order, for reasons to be recorded in writing, in the interest of investors or securities market, take any of the following measures, either pending investigation or inquiry or on completion of such investigation or inquiry, namely:—

a) **Suspend the trading** of any security in a recognised stock exchange;
b) **Restrain persons from accessing the securities market** and prohibit any person associated with securities market to buy, sell or deal in securities;
c) **Suspend any office-bearer of any stock exchange or self-regulatory organization** from holding such position;
d) **Impound and retain the proceeds or securities** in respect of any transaction which is under investigation;

Attach, after passing of an order on an application made for approval by the Judicial Magistrate of the

first class having jurisdiction, for a period not exceeding one month, one or more bank account or accounts of any intermediary or any person associated with the securities market in any manner involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder:

a) However only the bank account or accounts or any transaction entered therein, so far as it relates to the **proceeds actually involved in violation of any of the provisions of this Act, or**
b) **The rules or the regulations made thereunder shall be allowed to be attached;**

direct any intermediary or any person associated with the securities market in any manner not to dispose of or alienate an asset forming part of any transaction which is under investigation.

Question 5 ***(May 2011)***

Point out the circumstances where under the following powers may be exercised by the Securities and Exchange Board of India:

a) Prohibiting a company from issuing or publishing any document or advertisement soliciting money from public for issue of securities.
b) Pass cease and desist order in relation to any listed company.

What remedies are available to the companies against such orders under the SEBI Act, 1992?

Answer:

Orders of SEBI and Remedies: Under sec 11 of the SEBI Act, 1992 the basic duty of the SEBI is to

a) **Protect the interests of investors** in securities
b) **regulate** the securities market.

Section 11A (1)(b) specifically empowers SEBI to **prohibit any company from issuing prospectus, any offer document or advertisement soliciting money from the public** for the issue of securities by general or special order if such prohibition is necessary for the purpose of protection of investors.

According to section 11D, **SEBI can issue, cease and desist order in respect of any listed company only if SEBI has reasonable grounds** to believe that such **company has**

a) **Indulged in insider trading** or
b) **Market manipulation.**

Aggrieved companies may appeal against orders of SEBI made under SEBI Act, 1992, rules or regulations **to** the Securities Appellate Tribunal **(SAT)** under section 15T of the said Act. Such appeal should be filed **within 45 days from the date on which a copy of the order of SEBI** is received by the company.

If the company is **aggrieved by the order of SAT**, **further appeal** against the order of SAT can be made to the **Supreme Court within 60 days** from the date of communication of the order of SAT on **any question of law** arising out of such order.

The appeal lies only on question of law. As far as facts are concerned, **decision of the SAT is final.** Further section 20A of the said Act bars jurisdiction of Civil Court in respect of orders issued by the SEBI.

Penalties and Adjudication (Sec 15A – Sec 15JB)

Question 6

Mr. Raman, an investor is not satisfied with the dealings of his stock broker who is registered with Delhi Stock Exchange. Mr. Raman approaches you to guide him regarding the avenues available to

him for making a complaint against the stock broker under Securities and Exchange Board of India Act, 1992 and also the grounds on which such complaint can be made. You are required to briefly explain the answer to his queries.

Answer:

Securities and Exchange Board of India (SEBI) was established for regulating the various aspects of stock market. One of its functions is to register and regulate the stock brokers. In the light of this, Mr. Raman is advised that the complaint against the erring stock broker may be submitted to SEBI.

The grounds on which or the defaults for which complaints may be made to SEBI are as follows:

a) Any failure on the part of the **stock broker to issue contract notes in the form and manner specified by the stock exchange of which the stock broker is a member.**
b) Any failure to deliver any security or any **failure to make payment of the amount due to the investor in the manner within the period specified in the regulations.**

Any collection of charges by way of brokerage which is in excess of the brokerage specified in the regulations.

Question 7

On the complaint of Mr. Kamlesh Gupta, after enquiry SEBI finds that Mr. P. Mehta a Chief Executive Officer of the Company, on the basis of unpublished price sensitive information, has indulged in the trading of the securities of that company. Explain, on the basis of the said finding, what action SEBI can take against Mr. P. Mehra under the Securities and Exchange Board of India Act, 1992.

Answer:

Section 15G of the Securities and Exchange Board of India (SEBI) Act, 1992 deals with **penalty for Insider Trading**. According to this, if any insider

a) either on his own behalf or on behalf of any other person, **deals in securities of a body corporate** on any stock exchange on the basis of any unpublished price sensitive information; or
b) **communicates any unpublished price sensitive information** to any person, with or without his request for such information except as required in the ordinary cause of business or under any law, or
c) **counsels or procures for, any other person to deal in any securities** of anybody corporate on the basis of unpublished price sensitive information, shall be liable to a **penalty:**
    i) **25 crore rupees**
    ii) **3 times amount of profits made out of insider trading,**
    iii) **whichever is higher**.

As such SEBI can, after following the prescribed procedure, impose a penalty on Mr. P.Mehra.

Question 8

What are the defaults for which a stock-broker may be penalized under the provisions of Securities and Exchange Board of India Act, 1992 in respect of his dealings with the investors? State the factors that must be taken into account by the adjudicating officer while determining the quantum of penalty in such cases.

Answer:

Penalty for default in case of stock brokers: Section 15F of Securities and Exchange Board of India Act, 1992 provides for **penalty for default in case of stock brokers**. If any person who, is registered, as a stock broker under this Act:

a) **fails to issue contract notes** in the form and in the manner specified by the stock exchange of which such broker is a member, he shall be liable to **a penalty not exceeding 5 times the amount for which the contract note was required to be issued by that broker;**

b) **fails to deliver any security or fails to make payment of the amount due to the investor** in the manner or within the period specified in the regulations, he shall be liable to a **penalty:**
   i) **1 lakh rupees for each day during which such failure continues** or
   ii) **1 crore rupees,**
   iii) **whichever is less;**

c) **charges an amount of brokerage which is in excess of the brokerage specified** in the regulations, he shall be **liable to a penalty:**
   i) **1 lakh rupees or**
   ii) **5 times amount of brokerage charged in excess of the specified brokerage,**
   iii) **Whichever is higher.**

Factors for taking into account while action While adjudging quantum of penalty under section 15J, the adjudicating officer shall have **due regard to the following factors:**

i) The **amount of disproportionate gain or unfair advantage**, wherever quantifiable, made as a result of the defaults.
ii) The **amount of loss**to an investor or group of investors as a result of the default.
iii) **The repetitive nature of the default.**

Taking into consideration the above factors, the adjudicating officer may levy a maximum penalty as prescribed in section 15F for default by the concerned stock broker in making the payment to the investor.

Question 9

SEBI received complaints from some investors alleging that ABC Ltd. and some brokers are indulging in price manipulation in the shares of ABC Ltd. Explain the powers that can be exercised by SEBI under the Securities and Exchange Board of India Act, 1992 in case the allegations are found to be correct.

Answer:

Price manipulation in the shares of ABC Ltd. can be considered as fraudulent and unfair trade practices relating to securities market. In this case SEBI may exercise the following powers under section 11(4) of securities and Exchange Board of India Act, 1992.

a) **Suspend the trading** of any security (in this case the securities of ABC Ltd.) in a recognized stock exchange.

b) **Restrain persons** (in this case ABC Ltd.) **from accessing the securities** market.

It can also **prohibit any person associated with securities market** (i.e. **brokers** who have indulged in price manipulation) to buy, sell or deal in securities market.

SEBI may issue the above orders for reasons to be recorded in writing. SEBI shall, either before or after passing such orders **give an opportunity of hearing to company and brokers concerned** (proviso 2 to Section 11(4)) SEBI may also appoint an adjudicating officer who may **levy penalty** under section 15 HA **after holding an enquiry** in the prescribed manner. According to section 15HA if any person indulges in fraudulent and unfair trade practices relating to securities, he shall be leviable to a **penalty of 25 crores or 3 times the amount of profits made out of such practices, whichever is higher.**

Prohibition on manipulation and deceptive practices: Further according to section 12A, no person shall directly or indirectly indulge in following (i.e.)

a) **using in manipulative or deceptive device** in connection with purchase, sale or securities listed
b) **Employ any scheme or device to defraud** in connection with dealing in securities which are listed
c) Engage in an act which would operate as **fraud or deceit upon any person** in connection with dealing in securities which are listed.

Penalty Amount: SEBI may impose **penalty up to 1 crore** on any person who fails to comply with any provisions of SEBI Act (Section 15 HB).

Establishment, Jurisdiction, Authority and Procedure of SAT (Sec 15K – 15Z)

Question 10

Mr. Clever who is registered as an Intermediary fails to enter into an agreement with his client and hence penalized by SEBI under section 15B of the SEBI Act. Advise Mr. Clever as to what remedies are available to him against the order of SEBI.

Answer:

Remedies against SEBI order: Section 15B of the Securities and Exchange Board of India Act, 1992 lays down that if any person, who is registered as an intermediary and is required under this Act or any rules or regulations made there under, to enter into an agreement with his client, fails to enter into such agreement, he shall be liable to a penalty:

a) **1 lakh rupees for each day during which such failure continues or**
b) **1 crore rupees, whichever is less**.

Mr. Clever has been penalized under the above mentioned provision.

Two remedies are available to Mr. Clever in this matter: -

a) **Appeal to the Securities Appellate Tribunal (SAT):**

Section 15T of the SEBI Act, 1992 provides that any person aggrieved by an order of the Board made, on and after the commencement of the Security Laws (Second Amendment) Act, 1999, under this Act or the rules or regulations made there under may prefer an appeal to a Securities Appellate Tribunal having jurisdiction in the matter.

Such appeal shall be filed **within a period of 45 days from the date on which a copy of the order made by the Board is received** and it shall be in such form and be accompanied by such fee as may be prescribed.

What if delay happens?

The Tribunal **may entertain an appeal after the expiry** of the said period if it is satisfied that there was **sufficient cause for not filing** it within the said period.

The Tribunal may, after giving the parties an **opportunity of being heard**, pass such orders as it thinks fit, confirming, modifying or setting aside the order appealed against.

b) **Appeal to the Supreme Court (SC):**

Section 15Z of the SEBI Act, 1992 provides that any person **aggrieved by any decision or order of the Securities Appellate Tribunal** may file an appeal to the Supreme Court **within 60 days from the date of communication of the decision or order to him on any question or fact or law arising out of such order**.

What if delay happens?

The Supreme Court may, if it is satisfied that the appellant was **prevented by sufficient cause** from filing the appeal within the said period, allow it to be filed within a further period not exceeding 60

days.

Question 11

Mr. DB is a member of RPA Ltd. He obtains an order against the company for redressal of his grievances against the company. But the company fails to redress the grievances of DB within the time fixed by the SEBI. The Board thereafter imposed penalty upon the company u/s 15C of the SEBI Act. RPL Ltd. seeks your advice whether it has any remedy against the order of SEBI. Advise

Answer:

Remedy against order of SEBI:

ABC Limited was penalized by the SEBI. The following remedies are available to the Company:

a) Appeal to the Securities Appellate Tribunal: Section 15T of the SEBI Act, 1992 provides that any person aggrieved by an order of the Board may prefer an appeal to the Securities Appellate Tribunal. Such appeal shall be filed within 45 days from the date on which a copy of the order of the Board was received. However, the Tribunal may entertain an appeal after the expiry of the said period if it is satisfied that there was sufficient cause for not filing it within the said period of limitation.

b) Appeal to the Supreme Court: Section 15Z of the SEBI Act, 1992 provides that any person aggrieved by the decision or order of the SAT may file an appeal to the Supreme Court within 60 days from the date of communication of the decision or order on any question of law arising out of such order. The Supreme Court may entertain such appeal even after the expiry of said period of limitation for a future period not exceeding sixty days, if there was reasonable cause for such delay.

Question 12 ***(May 2015)***

What is the required qualification for the appointment of:

a) The Presiding Officer
b) Member of the Securities Appellate Tribunal as per the provisions of the Securities and Exchange Board of India (SEBI) Act, 1992?

Answer:

Qualification for appointment as Presiding Officer or Member of Securities Appellate Tribunal: As per the provisions of Section 15M of the Securities and Exchange Board of India (SEBI) Act, 1992, a person shall not be qualified for appointment as the Presiding Officer or Member of Securities Appellate Tribunal unless he -

a) **is a sitting or retired judge of the Supreme Court or a sitting or retired Chief Justice of a High Court** or
b) **is a sitting or retired judge of a High Court who has completed not less than seven years of service as a Judge in a High Court.**

The Presiding Officer of the Security Appellate Tribunal shall be appointed by the Government in consultation with the Chief Justice of India or his nominee.

A person shall not be qualified for appointment as member of a Securities Appellate Tribunal unless he is a person of **ability, integrity and standing who has shown capacity in dealing with problems relating to securities market and has qualification and experience of corporate law, securities laws, finance, economics or accountancy.** A member of the Board or any person holding a post at senior management level equivalent to Executive Director in the Board shall not be appointed as Presiding Officer or Member of a Securities Appellate Tribunal during his service or tenure as such with the Board or within two years from the date on which he ceases to hold office as such in the Board.

Question 13 ***(Nov 2015)***

Mr. S, a member of MN Ltd., obtained an order from the Securities and Exchange Board of India (SEBI) against the company. But the company failed to redress the grievance of Mr. S within the time fixed. Consequently, SEBI imposed penalty on the company. The company, however, did not pay the penalty also. State how the penalty can be recovered from the company?

Answer:

According to **Section 28A** of the Securities and Exchange Board of India Act, 1992, **if a person fails to pay the penalty imposed by the adjudicating officer or fails to comply with any direction of the Board for refund of monies or fails to comply with a direction of disgorgement order issued under section 11B** or fails to pay any fees due to the Board, the Recovery Officer may draw up under his signature a statement /certificate in the specified form specifying the amount due from the person and shall proceed to recover from such person the amount specified in the certificate by one or more of the following modes, namely:

a) **attachment and sale of the person's movable property;**
b) **attachment of the person's bank accounts;**
c) **attachment and sale of the person's immovable property;**
d) **arrest of the person and his detention in prison;**
e) **appointing a receiver for the management of the person's movable and immovable properties.**

The expression **'Recovery Officer'** means any officer of the Board who may be authorized by general or special order in writing, to exercise the powers of a Recovery Officer. **The Recovery Officer shall be empowered to seek the assistance of the local district administration while exercising the powers.**

Miscellaneous (Sec 16 – 35)

Question 14 ***(Nov 2018)***

Mr. Ravi failed to pay the penalty imposed by the Adjudicating Officer for an offence committed under Securities and Exchange Board of India Act, 1992. After the penalty has become due, Mr. Ravi, otherwise than for adequate consideration, transferred his residential property to his sister and the fixed deposits with Banks in favour of his minor son. The minor son has become major and deposits continue to be held by his son.

With reference to the provisions of SEBI Act, 1992 discuss,

i) Whether the residential property and fixed deposits with Banks can be attached by the Recovery Officer for the purpose of recovering the penalty?
ii) Whether the Recovery Officer can seek assistance of local district administration for attaching the property?

Answer:

As per requirement of section 28A of the Securities and Exchange Board of India Act, 1992, if a person fails to pay the penalty imposed by the adjudicating officer, the Recovery Officer may draw up under his signature a statement in the specified form specifying the amount due from the person and shall proceed to recover from such person the amount specified in the certificate by modes specified in the said section.

As per the explanation, the person's movable or immovable property or monies held in bank accounts shall include any property or monies held in bank accounts which has been transferred directly or indirectly on or after the date when the amount specified in certificate had become due, by the person to his spouse or minor child or son's wife or son's minor child, otherwise than for

adequate consideration, and which is held by, or stands in the name of, any of the persons aforesaid; and so far as the movable or immovable property or monies held in bank accounts so transferred to his minor child or his son's minor child is concerned, it shall, even after the date of attainment of majority by such minor child or son's minor child, as the case may be, continue to be included in the person's movable or immovable property or monies held in bank accounts for recovering any amount due from the person under this Act.

Further, Section 28A states that the Recovery Officer shall be empowered to seek the assistance of the local district administration while exercising his powers.

In the light of the provisions enumerated above and facts of the question,

i) The residential property shall not be attached by the Recovery Officer for the purpose of recovering the penalty, as it has been transferred by Mr. Ravi to his sister and said transfer has not been covered in the section.

   The Fixed deposits with Bank that have transferred by Mr. Ravi in favour his minor son can be attached by the Recovery Officer for the purpose of recovering the penalty. Further, these Fixed deposits can even after the date of attainment of majority by such minor son, continue to be included in Mr. Ravi's monies held in bank accounts for recovering any amount due from him under this Act.

ii) Yes, the Recovery Officer can seek assistance of local district administration for attaching the property.

Ch. 1 – Foreign Exchange Management Act, 1999

Definitions (Sec 2)

Question 1 ***(Nov 2010)***

Mr. Ram, citizen of India, left India for employment in U.S.A. on 1st June, 2002. Mr. Ram purchased a flat at New Delhi for ₹ 15 lakhs in September, 2003. His brother, Mr. Gopal employed in New Delhi, also purchased a flat in the same building in September, 2003 for ₹ 15 lakhs. Mr. Gopal's flat was financed by a loan from a Housing Finance Company and the loan was guaranteed by Mr. Ram.

Examine with reference to the provisions of Foreign Exchange Management Act, 1999 whether purchase of flat and guarantee by Mr. Ram are Capital Account transactions and whether these transactions are permissible.

Answer:

Section 2(e) of Foreign Exchange Management Act, 1999 states that **'capital account transactions' means**

a) **a transaction which alters the assets or liabilities, including contingent liabilities, outside India of person's resident in India**
b) **a transaction which alters assets or liabilities in India of person resident outside India** and includes transactions referred to in section 6(3).

According to the said definition, a transaction which alters the contingent liability will be considered as capital account transaction in the case of person resident in India, but it is not so in the case of person resident outside India.

Purchase of immovable property by Mr. Ram in India is a capital account transaction. It has also been specifically provided in section 6(3)(i) as a capital account transaction.

Guarantee will be considered as a capital account transaction in the following cases:

i) Guarantee in respect of any debt, obligation or other liability incurred by a person resident in India and owed to a person resident outside India.
ii) Guarantee in respect of any liability, debt or other obligation incurred by a person resident outside India.

Conclusion:

In this case, Mr. Ram, a resident outside India gives a guarantee in respect of a debt incurred by a person resident in India and owed to a person resident in India.

Hence, it would appear that guarantee by Mr. Ram cannot be considered as a capital account transaction within the meaning of Section 2(e), particularly because it is a contingent liability.

All capital account transactions are prohibited unless specifically permitted. RBI is empowered to issue regulations in this regard [Section 6(3)]. **Permissible capital account transactions by persons resident outside India are given in Schedule II to Foreign Exchange Management** (Permissible Capital Account Transactions) Regulations, 2000.

According to the said regulations both the purchase of immovable property by Mr. Ram and guarantee by Mr. Ram are permissible.

Question 2

A Company incorporated in United Kingdom established a branch at Chennai. What is the residential

status of the Chennai branch? The Chennai branch proposes the purchase of some immovable property at Chennai for the purpose of its business. Is it a 'Capital Account Transaction' within the meaning of section 2(e) of the Foreign Exchange Management Act, 1999? Are there any restrictions under the Foreign Exchange Management Act, 1999 in respect of such acquisition?

Answer:

According to **section 2(v)(iii)** of the FEMA, 1999, person resident in India inter alia means an office, branch, or agency in India owned or controlled by a person resident outside India. The company incorporated in U.K is a person resident outside India [Section 2(v)(ii) read with section 2(w) of the FEMA] as it is not a body corporate registered or incorporated in India. As the Chennai branch is branch in India is owned and controlled by the U.K Company is resident outside India, the Chennai branch is resident is India under section 2(v) (iii) stated above.

Capital account transaction.

In the case of a resident in India, capital account transaction means a transaction which alters the assets or liabilities including contingent liabilities, outside India. The Chennai branch (is resident in India) acquires immovable properly at Chennai (is in India). Hence this acquisition is not a capital account transaction within the meaning of section (2(e) of FEMA. Section 6(3) empowers RBI to restrict or regulate the acquisition of immovable property in India by a person resident outside India. Hence there is no restriction in acquisition of immovable property in India by Chennai branch.

Question 3

Examine whether the following branches can be considered as a 'Person resident in India' under Foreign Exchange Management Act, 1999:

i) ABC Limited, a company incorporated in India established a branch at London on 1st January, 2003.
ii) M/s XYZ, a foreign company, established a branch at New Delhi on 1st January, 2003. The branch at New Delhi controls a branch at Colombo.

Answer:

Person resident in India (Foreign Exchange Management Act, 1999):

i) Any person or body corporate registered or incorporated in India is a resident in India [section 2(v)(ii)]. 'Person' includes a company [section 2(u)]. An office, branches or agency outside India owned or controlled by a person resident in India is a person resident in India. [Section 2(v)(iv)].

   In view of the above provisions in FEMA, 1999 London branch established by ABC Ltd, a company incorporated in India, is a 'person resident in India' under the Act from the date of establishment i.e. 1st January, 2003.

ii) According to Section 2(v)(iii) of FEMA, 1999 an office, branch or agency in India owned or controlled by a person resident outside India is a person resident in India'. Only a body corporate registered or incorporated in India is a 'person resident in India'. According to section 2(w), 'person resident outside India' means a person who is not resident in India. Hence M/s XYZ, foreign company is a 'resident outside India. But the branch at New Delhi owned by M/s XYZ is a 'resident in India' within the meaning of section 2(v) (iii) from the date of establishment i.e. 1st January, 2003. The branch at Colombo controlled by the branch at New Delhi referred to in the question is a person 'resident in India' within the meaning of section 2(v)(iii) read with section 2(v)(iv).

Question 4

'Printex Computer' is a Singapore based company having several business units all over the world. It has a unit for manufacturing computer printers with its Headquarters in Pune. It has a Branch in

Dubai which is controlled by the Headquarters in Pune. What would be the residential status under FEMA, 1999 of printer units in Pune and that of Dubai branch?

Answer:

a) Printex Computer being a Singapore based company would be person resident outside India [(Section 2(w)] Section 2(u) defines 'person' under clause (viii) thereof, as person would include any agency, office or branch owned or controlled by such person.

b) The term such person appears to refer to a person who is included in clause (i) to (vi). Accordingly printex unit in Pune, being a branch of a company would be a 'person'.

c) Section 2(v) defines a person resident in India. Under clause (iii) thereof person resident in India would include an office, branch or agency in India owned or controlled by a person resident outside India.

d) Printex unit in Pune is owned or controlled by a person resident outside India, and hence it, would be a 'person resident in India.'

e) However, Dubai Branch though not owned is controlled by Print unit in Pune which is a person resident in India. Hence prima facie, it may be possible to hold a view that the Dubai Branch is a person resident in India.

Question 5

How will you determine whether a particular business unit like a factory or office is a 'person resident in India' under Foreign Exchange Management Act, 1999?

Answer:

Person resident in India

Section 2 of FEMA, 1999 defines the term **"person resident in India". According to Section 2 (iii), all business units in India will be "resident in India" even though these units are owned or** controlled by a person resident outside India.

Similarly, all business units outside India will be 'resident in India' provided the business units are either owned or controlled by a person resident in India [Section 2(v) (iv)]. It is necessary to determine the residential status of the person who owns or controls the business unit.

Question 6

Mr. Ram had resided in India during the Financial Year 1999-2000 for less than 183 days. He again came to India on 1st May, 2000 for higher studies and business and stayed upto 15th July, 2001. State under the Foreign Exchange Management Act, 1999.

i) If Mr. Ram can be considered 'person Resident in India' during the Financial year 2000-2001 and

ii) Is citizenship relevant for determining such a status?

Answer:

i) No. Mr. Ram cannot be considered 'Person resident in India' during the financial year 2000-2001 notwithstanding the purpose or duration of his stay in India during 2000-2001. An individual has to be present in India for more than 182 days in the preceding financial year. Mr. Ram does not satisfy this condition for the financial year 2000-2001.

ii) No. Citizenship is no more relevant for determining the status.

Question 7

Miss Alia is an airhostess with the British Airways. She flies for 12 days in a month and thereafter takes a break for 18 days. During the break, she is accommodated of 'base', which is normally the city where the airways are headquartered. However, for security considerations, she was based on Mumbai. During the financial year, she was accommodated at Mumbai for more than 182 days. What would be her residential status under FEMA?

Answer:

Miss Alia stayed in India at Mumbai 'base' for more than 182 days in the preceding financial year. The issue here is whether staying can be considered 'residing'. FEMA emphasises 'residing'. 'Stay' is a physical attribute, while 'residing' denotes permanency. Thus, while Miss Alia may have stayed in India for more than 182 days, it is doubtful whether she can be said to have 'resided' in India for more than 182 days.

Further under section 2(v)(a), she would become resident only if she has come to or stayed in India for employment. It would be doubtful and debatable, whether by staying at Mumbai base during the break, Miss Alia can be said to have come to stay in India for or on taking up employment. Hence, Miss Alia would continue to be non-resident.

Question 8

During the financial year 2010-11 Mr. Bhattacharyya resided in India for a period of 180 days and thereafter went abroad. On 1st April, 2011 Mr. Bhattacharyya came back to India as an employee of a business organization. Decide the residential status of Mr. Bhattacharyya during the financial year 2010-11 under the provisions of the Foreign Exchange management Act, 1999.

Answer:

Residential Status under Section 2(v) of Foreign Exchange Management Act, 1999: In accordance with the provisions of the Foreign Exchange Management Act, 1999, as contained in section 2(v), a person in order to qualify for the purpose of being treated as a '**Person Resident in India'' in any financial year, must reside in India for a period of more than 182 days during the preceding financial year.**

Mr. Bhattacharyya did not reside in India during the year 2010-2011 for more than 182 days and his residential status during the next year, i.e. 2011- 2012 is non-resident even though he stayed in India from 1st April, 2011 as an employee. His residential status in 2010-2011 cannot be ascertained as his stay in India during the previous year 2009-2010 is not known.

Question 9

Mr. Kishore resided in India during the Financial Year 2009- 2010 for less than 182 days. He came to India on 1 April, 2010 for business. He closed down his business on 30th April, 2011 and left India on 30th June, 2011 for the purpose of employment outside India. Decide the residential status of Mr. Kishore during the Financial Years 2010-2011 and 2011-2012 under the provisions of the Foreign Exchange Management Act, 1999.

Answer:

According to the **section 2(v)** of the Foreign Exchange Management Act, 1999, a person in order to qualify for the purpose of being treated as a "Person Resident in India" in any financial year, must reside in India for a period of more than 182 days during the preceding financial year.

Conclusion:

- In the given case, Mr. Kishore resided in India for less than 182 days during the financial year 2009 -

10. Hence, he cannot be considered as a "Person Resident in India" during the financial year 2010-11.

- During the financial year 2010-11, Mr. Kishore resided in India for more than 182 days. Normally, he would have been resident in India during the financial year 2011 -2012 but as he left India on 30th June, 2011 for the purpose of taking up employment outside India, he would cease to be resident in India from the date of his departure from India i.e. 30thJune, 2011.
- Therefore, Kishore cannot be called a person resident in India during the entire financial year 2011-2012.

Current Account Transactions (Sec 5)

Question 10

Explain the meaning of the term "Current Account Transaction" and the right of a citizen to obtain Foreign Exchange under the Foreign Exchange Management Act, 1999.

Answer:

The term "**current account transaction" is defined in section 2(j)** of Foreign Exchange Management Act, 1999. **It means a transaction other than a capital account transaction and includes:**

a) payments due in connection with **foreign trade**, **other current business, services, and short – term banking and credit facilities in the ordinary course of business**.
b) payments due as **interest on loans and as net income from investments**.
c) **remittances for living expenses of parents, spouse and children** residing abroad and
d) **expenses in connection with foreign travel education** and **medical care** of parents, spouse and children.

According to Section 5 of FEMA, 1999 **any person may sell or draw foreign exchange to or from an authorized person if such sale or drawal is a current account transaction**.

a) Provided that the Central Government may in public interest and in consultation with the Reserve Bank,
b) Impose **such reasonable restrictions for current account transactions** as may be prescribed.
c) Further, any person may sell or draw foreign exchange to or from an authorized person for a capital account transaction subject to the provisions of section 6(2).

Question 11

Mr. Ramesh of Nagpur wants to travel to Nepal and for this purpose proposes to draw Foreign Exchange. Specify.

What are the purposes for which Foreign Exchange drawal is not allowed for Current Account Transaction?

Answer:

Following are the transactions (current account) for which drawal of foreign exchange is prohibited.

a) Remittance out of **lottery winnings.**
b) Remittance of income from **racing/riding**, etc., or any other hobby.
c) Remittance for purchase of **lottery tickets, banned/prescribed magazines, football pools, sweepstakes** etc.
d) Payment of **commission on exports** made towards equity investment in Joint Ventures/Wholly Owned Subsidiaries abroad of Indian companies.
e) **Remittance of dividend** by any company to which the requirement of dividend balancing is applicable.

f) Payment of **commission on exports under Rupee State Credit Route,** except commission up to 10% of invoice value of exports of tea and tobacco.

g) Payment related to **"Call Back Services**" of telephones.

h) **Remittance of interest income on funds** held in Non-resident Special Rupee Scheme a/c.

Question 12

Mr. Sane, an Indian National desires to obtain Foreign Exchange for the following purposes:

i) Remittance of US Dollar 50,000 out of winnings on a lottery ticket.

ii) US Dollar 1,00,000 for sending a cultural troupe on a tour of U.S.A.

Answer:

Under provisions of section 5 of the Foreign Exchange Management Act, 1999 certain Rules have been made for drawal of Foreign Exchange for Current Account transactions. As per these Rules, **Foreign Exchange for some of the Current Account transactions is prohibited.** As regards some other Current Account transactions, Foreign Exchange can be drawn with prior permission of the Central Government while in case of some Current Account transactions, prior permission of Reserve Bank of India is required.

a) In respect of item No.(i), i.e., **remittance out of lottery winnings, such remittance is prohibited** and the same is included in First Schedule to the Foreign Exchange Management (Current Account Transactions) Rules, 2000. Hence Mr. Sane cannot withdraw Foreign Exchange for this purpose.

b) Foreign Exchange for meeting **expenses of cultural tour can be withdrawn by any person after obtaining permission from Government of India,** Ministry of Human Resources Development, (Department of Education and Culture) as prescribed in Second Schedule to the Foreign Exchange Management (Current Account Transactions) Rules, 2000. Hence, in respect of item (ii), Mr. Sane can withdraw the Foreign Exchange after obtaining such permission.

In all the cases, where remittance of Foreign Exchange is allowed, either by general or specific permission, the remitter has to obtain the Foreign Exchange from an Authorized Person as defined in Section 2(c) read with section 10 of the to the Foreign Exchange Management Act, 1999.

Question 13

State which kind of approval is required for the following transactions under the Foreign Exchange Management Act, 1999:

i) X, a Film Star, wants to perform along with associates in New York on the occasion of Diwali for Indians residing at New York. Foreign Exchange drawal to the extent of US dollars 20,000 is required for this purpose.

ii) R wants to get his heart surgery done at UK. Up to what limit Foreign Exchange can be drawn by him and what are the approvals required?

iii) L wants to pursue a course in Fashion design in Paris. The Foreign Exchange drawal is US dollars 20,000 towards tuition fees and US dollars 30,000 for incidental and stay expenses for studying abroad.

Answer:

Approval to the following transactions under FEMA, 1999:

i) Foreign Exchange **drawals for cultural tours require prior permission/approval of the Government of India irrespective of the amount of foreign exchange required**. Therefore, in the given case X, the Film Star is required to seek permission of the Government of India.

ii) Remittance in foreign exchange for **medical treatment abroad requires prior permission/approval of RBI when the expenditure in foreign currency exceeds the estimate of hospital/doctor abroad or estimate from doctor in India in that field of treatment**. Therefore, R can draw foreign exchange up to the estimate of hospital/doctor abroad or estimate from doctor in India in that field of treatment and prior permission/approval of RBI is required.

iii) **Release of foreign exchange for education abroad is permitted up to US$ 1,00,000 on self-declaration basis**. Therefore, L can draw foreign exchange on self-declaration basis for pursuing a course in fashion design in Paris.

Question 14

Referring to the provisions of the Foreign Exchange Management Act, 1999, state the kind of approval required for the following transactions:

i) M requires U.S. $ 5,000 for remittance towards hire charges of transponders.

ii) P requires U.S. $ 2,000 for payment related to call back services of telephones.

Answer:

Under section 5 of the Foreign Exchange Management Act, 1999, and Rules relating thereto, some current account transactions require prior approval of the Central Government, some others require the prior approval of the Reserve Bank of India, some are free transactions and some others are prohibited transactions. Accordingly,

a) It is a current account transaction, where M is required to take **approval of the Central Government for drawal of foreign exchange for remittance of hire charges of transponders.**

b) Withdrawal of foreign exchange for payment related to **call back services of telephone is a prohibited transaction**. Hence, Mr. P will not succeed in acquiring US $ 2,000 for the said purpose.

Question 15

Mr. Suresh resided in India during the Financial Year 2008-09. He left India on 15th July, 2009 for Switzerland for pursuing higher studies in Biotechnology for 2 years. What would be his residential status under the Foreign Exchange Management Act, 1999 during the Financial Years 2009-10 and 2010-11?

Mr. Suresh requires every year USD 25,000 towards tuition fees and USD 30,000 for incidental and stay expenses for studying abroad. Is it possible for Mr. Suresh to get the required Foreign Exchange and, if so, under what conditions?

Answer:

Residential Status:

According to section 2(v) of Foreign Exchange Management Act, 1999, 'Person resident in India' means a person residing in India for more than 182 days during the course of preceding financial year [Section 2(v)(i)].

However, it does not include a person who has gone out of India or who stays outside India for employment outside India or for any other purpose in such circumstances as would indicate his intention to stay outside India for an uncertain period.

Generally, a student goes out of India for a certain period. In this case, Mr. Suresh who resided in India during the financial year 2008-09 left on 15.7.2009 for Switzerland for pursuing higher studies in Biotechnology for 2 years, he will be resident for 2009-10, as he has gone to stay outside India for a 'certain period' (If he goes abroad with intention to stay outside India for an 'uncertain period' he will not be resident with effect from 15-7-2009.

Conclusion:

Mr. Suresh will not be resident during the Financial Year 2010-2011 as he did not stay in India during the relevant previous financial year i.e. 2009-10.

Foreign Exchange for studies abroad:

According to Schedule III read with Rule 5 of Foreign Exchange Management (Current Account Transactions) Rules, 2000 **release of foreign exchange for studies abroad exceeding the estimates from the institution abroad or USD 1,00,000 per academic year, whichever is higher requires prior approval of Reserve Bank of India**. In this case the foreign exchange required is only USD 55,000 per academic year and hence approval of RBI is not required.

Question 16

Mr. G., an Indian national desires to obtain Foreign Exchange on current account transactions for the following purposes:

a) Payment of commission on exports made towards equity investment in wholly owned subsidiary abroad of an Indian Company.
b) Remittance of hiring charges of transponder by TV channels

Advise G whether he can obtain Foreign Exchange and, if so, under what conditions?

Answer:

Under Section 5 of Foreign Exchange Management Act, 1999, certain rules have been framed for drawal of foreign exchange on current account. According to the said rules, drawal of foreign exchange for certain transactions are prohibited. In respect of certain transactions drawal of foreign exchange is permissible with the prior approval of Central Government. In respect of some of the transaction, prior permission of RBI is sufficient for drawal of foreign exchange.

a) In respect of item No.1 i.e. **Payment of Commission on exports made towards equity investment in wholly owned subsidiary abroad of an Indian company is prohibited.**

b) **Drawal of foreign exchange for remittance of hiring charges** of transponder by TV Channels, can be made **with the prior approval of the Central Government.**

In the case of (ii) above, approval of concerned authority is not required if the payment is made out of **funds held in Resident Foreign Currency (RFC) Account or Exchange Earner's Foreign Currency (EEFC) Account of the remitter.** Further foreign Exchange can be drawn only from an authorized person.

Question 17

Examine under the Foreign Exchange Management Act, 1999 whether "Payment of remuneration to foreign technicians" is a permissible transaction under the provisions of the said Act.

Answer:

Foreign Technician: **Salary payable to a foreign technician is a current account transaction.**

a) According to section 5 of the Foreign Exchange Management Act, 1999 any person can sell or draw foreign exchange to or from authorized person if such sale or drawal is a current account transaction.
b) Reasonable restrictions on current account transactions can be imposed by the Central Government.
c) Basically all current account transactions are free unless specifically restricted by the Central Government.

d) Hiring of foreign nations as technicians is permissible without restriction. There is no ceiling on salary which can be paid as per contract. Their salary can be remitted abroad after tax deducted at source.

Question 18

Mr. F, an Indian National desires to obtain foreign exchange for the following purposes:

i) Payment of US $10,000 as commission on exports under Rupee State Credit Route.

ii) US $ 30,000 for a business trip to U.K.

iii) Remittance of US $ 2,00,000 for payment as prize money to the winning team in a Hockey Tournament to be held in Australia.

Advise him, if he can get the Foreign Exchange and under what condition

Answer:

Under provisions of **section 5 of the Foreign Exchange Management Act, 1999** certain Rules have been made for drawal of Foreign Exchange for Current Account transactions. As per these Rules, Foreign Exchange for some of the Current Account transactions in prohibited. As regards some other Current Account transactions, Foreign Exchange can be drawn with prior permission of the Central Government while in case of some Current Account transactions, prior permission of Reserve Bank of India is required:

i) In respect of item No. (i), i.e., **payment of commission on exports under Rupee State Credit Route, such payment is prohibited** and the same is included in First Schedule to the Foreign Exchange Management (Current Account Transactions) Rules, 2000.

ii) **Foreign Exchange for business trip up to US$ 25,000 can be obtained by any person.** If a person wants to exceed this limit, then prior permission of Reserve Bank of India is required as per Third Schedule to the Foreign Exchange Management (Current Account Transactions) Rules, 2000. In respect of item (ii), since the amount involved is more than US $ 25,000, Mr. F can obtain the foreign exchange after getting the permission of Reserve Bank of India.

iii) The type of payment as envisaged in item No.(iii) is covered under Second Schedule to the Foreign Exchange Management (Current Account Transactions) Rules, 2000 and for remitting of **prize money exceeding US$ 1,00,000 for sports activity abroadother than International, National or State level body will require the prior permission of the Central Government.** (Ministry of Human Resource Development – Department of Youth Affairs and Sports). Since the amount involved in item No. (iii) of the question is more than US$ 1,00,000 and Mr. F is not an International, National or State level body, he has to obtain the permission of the Central Government before remitting the prize money of US$ 2,00,000.

In all the cases, where remittance of Foreign Exchange is allowed, either by general or specific permission, the remitter has to obtain the Foreign Exchange from an Authorized Person as defined in Section 2(c) read with section 10 of the to the Foreign Exchange Management Act, 1999.

Question 19

Examine with reference to the Provisions of the Foreign Exchange Management Act, 1999 and the rules made thereunder whether foreign exchange can be drawn for the following purposes:

Mr. Gopal, a cine artist in India proposes to organize a cultural programme at Dubai and requires to draw foreign exchange US $ 1,00,000 for this purpose.

Answer:

Drawal of Foreign Exchange

Cultural programme: Foreign exchange for meeting expenses of cultural tour can be withdrawn by a person after obtaining permission from the Government of India, Ministry of Human Resources Development (Department of Education and Culture) as prescribed in second schedule to the Foreign Exchange Management (Current Account Transactions) Rules, 2000. Hence, Mr. Gopal can withdraw US $ 1,00,000 after obtaining permission from the Government of India.

Question 20

Mr. Rohan, an Indian Resident individual desires to obtain Foreign Exchange for the following purposes:

a) US$ 1, 20,000for studies abroad on the basis of estimates given by the foreign university.
b) Gift Remittance amounting US$ 10,000.

Advise him whether he can get Foreign Exchange and if so, under what condition(s)?

Answer:

a) Remittance of Foreign Exchange for studies abroad: Foreign exchange may be **released for studies abroad up to a limit of US $ 2,50,000 for the studies abroad without any permission from the RBI**. Above this limit, RBI's prior approval is required. Further proviso to Para I of Schedule III states that individual may be allowed remittances (without seeking prior approval of the RBI) **exceeding USD 2,50,000 based on the estimate received from the institution abroad**. In this case since **US $ 1,20,000 is the drawal of foreign exchange, so permission of the RBI is not required.**

b) Gift remittance exceeding US $ 10,000: Under the provisions of Section 5 of FEMA 1999, certain Rules have been made for drawal of foreign exchange for current account transactions. Gift remittance is a current account transaction. Gift remittance exceeding US $ 2,50,000 can be made after obtaining prior approval of the RBI. In the present case, since the amount to be gifted by a individual, **Mr. Rohan is USD 10,000, so there is no need for any permission from the RBI.**

Question 21 ***(Nov 2016)***

Lifesys Limited, a billion dollar, Indian company wishes to create a chair in a reputed university in the U.S. This chair is for the department of computer science. The company wishes to obtain your advise in regard to the following with reference to the FEMA, 1999.

a) Is such "chair" creation permissible?
b) What is the maximum amount that can be denoted for such chair?
c) Any formalities to be complied with?

Answer:

As per Schedule III of the Foreign Exchange Management (Current Account Transactions) Rules, 2000, read with section 5 of the Foreign Exchange Management Act, 1999 donations exceeding one per cent of their foreign exchange earnings during the previous three financial years or USD 5,000,000, whichever is less, can be remitted by persons other than individuals for creation of Chairs in reputed educational institutes with the prior approval of the Reserve Bank of India. As per Schedule III of the Foreign Exchange Management (Current Account Transactions) Rules, 2000, read with section 5 of the Foreign Exchange Management Act, 1999 donations exceeding one per cent of their foreign exchange earnings during the previous three financial years or USD 5,000,000, whichever is less, can be remitted by persons other than individuals for creation of Chairs in reputed educational institutes with the prior approval of the Reserve Bank of India.

Considering the above provision-

i) In the first case, "chair" creation for the department of computer science in reputed university in the U.S. is permissible.

ii) Maximum amount that can be donated for such chair will be one per cent of their foreign exchange earnings during the previous three financial years or USD 5,000,000, whichever is less without prior approval of the Reserve Bank of India.

iii) In case where donations exceeds one per cent of their foreign exchange earnings during the previous three financial years or USD 5,000,000, it shall require prior approval of Reserve Bank of India.

Question 22 ***(Nov 2017)***

Mr. T. Raghava has secured admission in a reputed and recognized university in Germany, for the study of higher and technical education, outside India. After arrival in Germany, he has gone ill and wants medical treatment facility in a reputed German hospital. He desires to apply to the Government of India for availing the additional remittance beyond the limit approved for foreign currency exchange facility. He has already enjoyed the permitted facility of foreign exchange for studies abroad, for the said financial year. Decide the following as to the facts given in the question as per the provisions of the Foreign Exchange Management Act, 1999:

i) As an individual, to what extent Mr. T. Raghava may avail foreign exchange facilities for higher and technical study in Germany.

ii) Can Mr. T. Raghava avail the facility of additional remittance in foreign exchange, beyond the limit, for the medical treatment.

Answer:

According to the Schedule III of the FEM (current account transactions) Rules, 2000, following shall be the limit for the remittance of Foreign Exchange in the given situations:

i) **Remittance of Foreign Exchange for Studies Abroad:** Foreign exchange may be released for studies abroad up to a limit of US $ 2,50,000 without any permission from the RBI. Above this limit, RBI's prior approval is required.

ii) **Remittance for Medical Treatment:** Remittance of foreign exchange for medical treatment abroad requires prior permission or approval of RBI where the individual requires withdrawal of foreign exchange exceeding USD 2,50,000. The Schedule also prescribes that for the purpose of expenses in connection with medical treatment, the individual may avail of exchange facility for an amount in excess of the limit prescribed under the Liberalized Remittance Scheme, if so required by a medical institute offering treatment. Such amount shall be reduced from USD 2,50,000 by the amount so remitted.

Therefore, Mr. T. Raghava can draw foreign exchange exceeding USD 2,50,000 by taking prior permission/ approval of RBI.

Capital Account Transactions

Question 23

Explain the meaning of "Capital Account Transactions" under the Foreign Exchange Management Act, 1999. State its categories and also examine whether the following transactions are permissible or not under the above Act as Capital Account transactions:

a) Investment by person resident in India in Foreign Securities.

b) Foreign currency loans raised in India and abroad by a person resident in India.
c) Export, import and holding of currency / currency notes.
d) Investment in a Nidhi Company.
e) Trading in transferable development rights

Answer:

Meaning of Capital Account Transaction: It means a transaction which alters the assets or liabilities including contingent liabilities, outside India of person resident in India or assets or liabilities in India of a person resident outside India, and includes transactions referred to in sub-section (3) of section 6 of FEMA Act, 1999.

The Reserve Bank of India has formed Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000. The provisions of these regulations are as under:

Categories of Capital Account Transactions: As per these regulations, capital account transactions may be classified under the following heads.

a) Permissible capital account transaction of person resident in India (schedule 1)
b) Permissible Capital transactions of person resident outside India (schedule II).
c) Prohibited capital account transactions.

A person resident in India may enter into any of the following capital account transactions provided the regulations specified by the Reserve Bank of India in respect of such capital account transactions are complied with.

Conclusion:

In view of the above provisions: among five capital account transaction of question first three i.e. (i), (ii) and (iii) are permissible capital account transactions and rest two i.e., (iv) and v are prohibited capital transactions.

Question 24

Examine with reference to the provisions of the Foreign Exchange Management Act, 1999 whether there are any restrictions in respect of the following:-

i) Drawal of Foreign Exchange for payments due on account of Amortization of loans in the ordinary course of business.
ii) A person, who is resident of U.S.A. for several years, is planning to return to India permanently. Can he continue to hold the investment made by him in the securities issued by the companies in U.S.A.?
iii) A person resident outside India proposes to invest in the shares of an Indian company engaged in plantation activities.

Answer:

Capital Account Transactions: All the transactions referred to in the question are capital account transactions.

Section 6(2) of FEMA, 1999 provides that the Reserve Bank may in consultation with the Central Government specify the permissible capital account transactions and the limit upto which foreign exchange will be allowed for such transactions.

i) **Amortization of Loan:** According to proviso to section 6(2), the Reserve bank shall not impose any restriction on the drawal of foreign exchange for certain transactions. One such transaction is drawal of foreign exchange for payment due on account of amortization of loans in the ordinary course of business. Hence this transaction is permissible without any restrictions.

ii) **Person resident in USA returning permanently to India**: When the person returns to India permanently, he becomes a resident in India. Section 6(4) provides that a person resident in India may hold, own, transfer or invest in foreign currency, foreign security, etc. if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India. In view of this, the person who returned to India permanently can continue to hold the foreign security acquired by him when he was resident in U.S.A.

iii) **Investment in shares of Indian company by non-resident:** Reserve Bank issued Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000. Regulation 4(6) of the said Regulations prohibits a person resident outside India from making investment in India, in any form, in any Company or partnership firm or proprietary concern or any entity, whether incorporated or not, which is engaged or proposes to engage in agricultural or plantation activities. Hence it is not possible for a person resident outside India to invest in the shares of a plantation company as such investment is prohibited.

Question 25 ***(Nov 2012)***

Mrs. Chandra, a resident outside India, is likely to inherit from her father some immovable property in India. Are there any restrictions under the provisions of the Foreign Exchange Management Act, 1999 in acquiring or holding such property? State whether Mrs. Chandra can sell the property and repatriate outside India the sale proceeds.

Answer:

As per sub-section 5 of section 6 of the FEMA, 1999, **a person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India.**

Accordingly, in the problem, Mrs. Chandra, a resident outside India, may acquire or hold any immovable property of his father in India by way of inheritance in both the conditions, firstly, where her father, a resident outside India, had acquired the property in accordance with the provisions of the foreign exchange law in force at the time of acquisition by him or as per the provisions of these Regulations or secondly, where her father, a resident in India.

Repatriation of sale proceeds: A person referred to in sub-section (5) of section 6 of the Act, or his successor shall not, except with the prior permission of the Reserve Bank, repatriate outside India the sale proceeds of any immovable property.

Conclusion:

Thus, accordingly Mrs. Chandra can sell the property and repatriate outside India the sale proceeds only with the prior permission of the RBI.

Question 26 ***(May 2014)***

Mr. V, a person of Indian origin and resident of USA desires to acquire two immovable properties in India comprising

i) a residential flat in Mumbai and

ii) a farm house on the outskirts of Mumbai.

Explain the steps he has to take in this matter having regard to the provisions of FEMA, 1999

Answer:

Permissible Transactions: Acquisition and transfer of immovable property in India by a person resident outside India is a permissible transaction under the Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000.

Acquisition and transfer of property in India by a person of Indian origin:

A person of Indian origin resident outside India may acquire immovable property in India other than an agricultural property, plantation, or a farm house.

However, in case of acquisition of immovable property, payment of purchase price, if any, shall be made out of:

a) funds received in India through normal banking channels by way of inward remittance from any place outside India, or
b) funds held in any non-resident account maintained in accordance with the provisions of the Foreign Exchange Management Act, 1999, and the regulations made by the Reserve Bank of India.

Further**, no payment of purchase price for acquisition of immovable property shall be made either by traveller'scheque or by currency notes of any foreign country or any mode other than those specifically permitted by this clause.**

Conclusion:

Thus, by following the above steps as mentioned in the provisions of the Foreign Exchange Management Act, 1999, and the Regulations made thereunder, Mr. V, a person of Indian origin and resident of USA (i.e. resident outside India):

i) **can acquire a residential flat in Mumbai** and
ii) **cannot acquire a farmhouse on the outskirts of Mumbai**

Question 27 ***(May 2018)***

In terms of the provisions of the Foreign Exchange Management Act, 1999, Mr. SAM is a person of Indian origin resident outside India. He wants to acquire some immovable properties in India not being agricultural property, plantation or a farm house.

Referring to the provisions of the Foreign Exchange Management Act, 1999, state the permitted sources, means and restrictions imposed in this regard,

Also state the provisions where the acquisition will be in the form of gift or inheritance by Mr. SAM.

Answer:

Acquisition of immovable properties in India by a person of Indian origin resident outside India:

A person of Indian origin resident outside India may acquire immovable property in India other than an agricultural property, plantation, or a farm house.

Sources: In case of acquisition of immovable property, payment of purchase price, if any, shall be made out of

i) funds received in India through normal banking channels by way of inward remittance from any place outside India or
ii) funds held in any non-resident account maintained in accordance with the provisions of the Act and the regulations made by the Reserve Bank.

Restriction: It is also provided that no payment of purchase price for acquisition of immovable property shall be made either by traveller's cheque or by currency notes of any foreign country or any mode other than those specifically permitted by this clause.

Acquisition in the form of gift

A person of Indian origin resident outside India may acquire any immovable property in India other than agricultural land/farm house/plantation property by way of gift from a person resident in India or from a person resident outside India who is a citizen of India or from a person of Indian origin resident outside India.

Acquisition in the form of inheritance

A person of Indian origin resident outside India may acquire any immovable property, in India by way of inheritance from a person resident outside India who had acquired such property in accordance with the provisions of the foreign exchange law in force at the time of acquisition by him or the provisions of these Regulations or from a person resident in India.

Export of Goods and Services (Section 7)

Question 28

Referring to the provisions of the Foreign Exchange Management Act, 1999, examine whether V, an exporter is bound to make declaration of the following goods exported from India to United Kingdom:

a) Exports software valuing 50,000.
b) V gifts certain items of jewellery valued at Rs.20,000 to his friend in Australia.
c) V exports certain goods valuing US $ 5,000 to Myanmar under Barter Trade Agreement.

Answer:

In accordance with provisions of the FEMA, 1999 as contained in section 7 read with section 8, **it imposes on an exporter to make appropriate declaration of the value of the goods being exported and he is also required to repatriate the foreign exchange due to India in respect of such exports to India in the manner within the time as may be prescribed**. Under section 8, the exporter is under an obligation to realize and repatriate to India such foreign. However, if there is a delay in the receipt of export, it will not be a violation which shall be punishable. Section 8 applies to a resident who shall take all the reasonable steps, depending upon the individual case.

There are **certain categories of export for which declaration need not be made**. These are:

a) Export of goods/software not exceeding **25,000 in value.**
b) Export by way of gift not exceeding **1 lac in value**.
c) Export of goods not exceeding **US $ 1000 or its equivalent** per transaction to Myanmar under Barter Trade Agreement.

Taking into consideration the above, answer to the question are:

a) In the first case since the value is exceeding 25,000 in value, therefore, declaration has to be completed.
b) In the second case since the value of gift of jewellery to V's friend in Australia is less than 1 lac in value, the gift does not need any declaration to be completed.
c) In the third case since the value is more than U.S.$1,000, therefore, the declaration has to be completed.

Question 29 ***(May 2016)***

Indian Software Ltd. seeks to export software to its client in Indonesia. In this regard -

i) Explain the procedure to be adopted for export of software under the Foreign Exchange Management Act, 1999 and also state the period within which export value is to be realised.
ii) Explain the position in case of delay in receipt of payment from its client.

Answer:

i) **Procedure for the export of the software under the FEMA, 1999**

1. Furnishing of declaration- In case of exports taking place through Customs manual ports, every exporter of goods or software in physical form or through any other form, either directly or indirectly, to any place outside India, other than Nepal and Bhutan, shall furnish to the specified authority, a declaration in one of the forms set out in the Schedule and supported by such evidence as may be specified, containing true and correct material particulars including the amount representing-

   a) the full export value of the goods or software; or

   b) if the full export value is not ascertainable at the time of export, the value which the exporter, having regard to the prevailing market conditions expects to receive on the sale of the goods or the software in overseas market, and affirms in the said declaration that the full export value of goods (whether ascertainable at the time of export or not) or the software has been or will within the specified period be, paid in the specified manner.

2. Execution of declaration- Declarations shall be executed in sets of such number as specified.

3. Export of services without furnishing any declaration- In respect of export of services to which none of the Forms specified in these Regulations apply, the exporter may export such services without furnishing any declaration, but shall be liable to realise the amount of foreign exchange which becomes due or accrues on account of such export, and to repatriate the same to India in accordance with the provisions of the Act, and these Regulations, as also other rules and regulations made under the Act.

4. Realization of export proceeds- Realization of export proceeds in respect of export of goods / software from third party should be duly declared by the exporter in the appropriate declaration form.

   Period within which export value of goods/software to be realised.

   a) The amount representing the full export value of goods / software/ services exported shall be realised and repatriated to India within 9 months from the date of export, provided

   - that where the goods are exported to a warehouse established outside India with the permission of the Reserve Bank, the amount representing the full export value of goods exported shall be paid to the authorised dealer as soon as it is realised and in any case within fifteen months from the date of shipment of goods;

   - further that the Reserve Bank, or subject to the directions issued by that Bank in this behalf, the authorised dealer may, for a sufficient and reasonable cause shown, extend the period of nine months or fifteen months, as the case may be.

   b) Where the export of goods / software / services has been made by Units in Special Economic Zones (SEZ) / Status Holder exporter / Export Oriented Units (EOUs) and units in Electronics Hardware Technology Parks (EHTPs), Software Technology Parks (STPs) and Bio-Technology Parks (BTPs) as defined in the Foreign Trade Policy in force, then notwithstanding anything contained in sub-regulation (1), the amount representing the full export value of goods or software shall be realised and repatriated to India within nine months from the date of export.

   Provided further that the Reserve Bank, or subject to the directions issued by the Bank in this behalf, the authorised dealer may, for a sufficient and reasonable cause shown, extend the period of nine months.

- The Reserve Bank may for reasonable and sufficient cause direct that the said exporter/s shall cease to be governed by sub-regulation (2);

  Provided that no such direction shall be given unless the unit has been given a reasonable opportunity to make a representation in the matter.

- On such direction, the said exporter/s shall be governed by the provisions of sub-regulation (1), until directed otherwise by the Reserve Bank.'

ii) **Delay in Receipt of Payment –**

Where in relation to goods or software export of which is required to be declared on the specified form and export of services, in respect of which no declaration forms has been made applicable, the specified period has expired and the payment therefor has not been made as aforesaid, the Reserve Bank may give to any person who has sold the goods or software or who is entitled to sell the goods or software or procure the sale thereof, such directions as appear to it to be expedient, for the purpose of securing,

a) the payment therefor if the goods or software has been sold and

b) the sale of goods and payment thereof, if goods or software has not been sold or reimport thereof into India as the circumstances permit, within such period as the Reserve Bank may specify in this behalf ;

Provided that omission of the Reserve Bank to give directions shall not have the effect of absolving the person committing the contravention from the consequences thereof.

Question 30 ***(May 2017 & RTP May 2018)***

Ms. Ashima daughter of Mr. Mittal (an exporter), is residing in Australia since long. She wants to buy a flat in Australia. Since she is unmarried, she wants to make her father Mr. Mittal a joint holder in that flat, for which entire proceeds are to be paid by her.

i) State the provisions of FEMA governing such type of transaction?
ii) On Applying the relevant provisions, can Mr. Mittal join her daughter in acquiring such a flat in Australia?
iii) Mr. Mittal, wants to receive advance payments against his exports from a buyer outside India. Explain the relevant provisions?

Answer:

i) **The provisions governing the acquisition and transfer of immovable property outside India.**

1. A person resident in India may acquire immovable property outside India:

a) By way of gift or inheritance from a person referred to in sub-section (4) of Section 6 of the FEMA or referred to in clause (b) of regulation 4 acquired by a person resident in India on or before 8th July, 1947 and continued to be held by him with the permission of Reserve Bank.

b) by way of purchase out of foreign exchange held in Resident Foreign Currency (RFC) account maintained in accordance with the foreign exchange management (Foreign Currency accounts by a person resident in India) Regulations 2015.

c) Jointly with a relative who is a person resident outside India, provided there is no outflow of funds from India.

2. A person resident in India may acquire immovable property outside India, by way of Inheritance or gift from a person resident in India who has acquired such property in

accordance with the foreign exchange provision in force at the time of such acquisition.

3. A Company incorporated in India having overseas offices, may acquire immovable property outside India for its business and for residential purposes of its staff, in accordance with the direction issued by the Reserve Bank of India from time to time.

ii) In the light of above discussions in 1(c), it is quite clear that Mr. Mittal, a resident in India, can join his daughter who is a resident outside India, in acquiring a Flat at Australia.

iii) **Advance payment against export:**

The following are the provisions governing the advance payments against exports:

1. Where an exporter receives advance payments (with or without interest) from a buyer/ third party named in the export declaration made by the Exporter, outside India, the exporter shall be under the obligation to ensure that:

   a) The shipment of goods is made within one year from the date of receipt of advance payment.

   The rate of interest, if any, payable on the advance payment does not exceed the rate of interest London Inter-Bank Offered Rate (LIBOR) + 100 basis points and

   b) The documents covering the shipment are routed through the authorised dealer through whom advance payment is received.

   Provided that in the event of the exporter's inability to make the shipment, partly or fully, within one year from the date of receipt of advance payment or towards, no remittance towards refund of un-utilised portions of advance payment or towards payment of interest, shall be made after the expiry of the period of one year, without the prior approval of the Reserve bank of India.

2. Notwithstanding anything contained in clause (i) of sub-regulation (1), an exporter may receive advance payment where the export agreement itself duly provides for shipment of goods extending beyond the period of one year from the date of receipt of advance payment.

Question 31 ***(Nov 2018)***

Bharat Computer Hardware Ltd. received an advance -payment for export of high-tech hardware to a business concern in Singapore by entering into an export agreement to supply the hardware within six months from the date of receipt of advance payment. The shipment of hardware was made after 9 months and the documents covering the shipment were routed through an authorized dealer through whom the advance payment was received.

Examine whether Bharat Computer Hardware Ltd. has discharged its obligation in accordance with the provisions of the Foreign Exchange Management Act, 1999?

Is it possible to receive advance payment where the export agreement provides for shipment of goods within 15 months from the date of receipt of advance payment? Also identify the maximum rate of interest payable on the advance payment under the said Act.

Answer:

According to the Foreign Exchange Management (Export of Goods and Services) Regulations, 2015,

Advance payment against exports:

1) Where an exporter receives advance payment (with or without interest), from a buyer / third party named in the export declaration made by the exporter, outside India, the exporter shall be under an obligation to ensure that –

   (i) the shipment of goods is made within one year from the date of receipt of advance payment;

(ii) the rate of interest, if any, payable on the advance payment does not exceed the rate of interest London Inter-Bank Offered Rate (LIBOR) + 100 basis points and

(iii) the documents covering the shipment are routed through the authorised dealer through whom the advance payment is received;

Provided that in the event of the exporter's inability to make the shipment, partly or fully, within one year from the date of receipt of advance payment, no remittance towards refund of unutilized portion of advance payment or towards payment of interest, shall be made after the expiry of the period of one year, without the prior approval of the Reserve Bank.

2) Notwithstanding anything contained in clause (i) of sub-regulation (1), an exporter may receive advance payment where the export agreement itself duly provides for shipment of goods extending beyond the period of one year from the date of receipt of advance payment.

In the light of the provisions as enumerated above,

(i) Since Bharat Computer Hardware Ltd. has exported the hardware within 9 months of the date of receipt of advance payment, it has discharged its obligations within the provisions of the Foreign Exchange Management Act, 1999.

(ii) Yes, it is possible to receive advance payment where the export agreement provides for shipment of goods extending beyond the period of one year (here in question 15 months) from the date of receipt of advance payment.

The maximum rate of interest, if any, payable on the advance payment should not exceed the rate of interest London Inter-Bank Offered Rate (LIBOR) + 100 basis points.

Question 32 ***(May 2019)***

Sunita Garments Limited is engaged in the business of exporting leather garments. The company is neither located in a Special Economic Zone, nor has availed any special status like Status Holder Exporter, Export Oriented Unit or a unit under Bio-Technology Park.

The company seeks your advice regarding the time limit within which the company is required to realise and import into India the foreign exchange arising out of export of goods by them and to be paid to the authorised dealer. Referring to the provisions of the Foreign Exchange Management Act, 1999 advise the company.

Answer:

Period within which amount representing the export value shall be realized & repatriated as per **Section 7 of the FEMA, 1999** read with Foreign Exchange Management (Export of Goods and Services) Regulations, 2015:

The amount representing the full export value of goods / software/ services exported shall be realized and repatriated to India within nine months from the date of export, provided:

a) that where the goods are exported to a warehouse established outside India with the permission of the Reserve Bank, the amount representing the full export value of goods exported shall be paid to the authorized dealer as soon as it is realized and in any case within fifteen months from the date of shipment of goods;

b) **Extension of Period:** Further that the Reserve Bank, or subject to the directions issued by that Bank in this behalf, the authorized dealer may, for a sufficient and reasonable cause shown, extend the period of nine months or fifteen months, as the case may be.

Sunita Garments Limited may be advised as above.

Realisation and repatriation of foreign exchange (Sec 8)

Question 33

Mr. Ramesh is an exporter of goods and services. Explain briefly his duties under Foreign Exchange Management Act, 1999 with regard to the following:

a) Furnishing of information relating to such exports.
b) Realization and repatriation of foreign exchange on such exports.

Answer:

Duty of every exporter of goods and services under FEMA, 1999:

A. Furnishing of Information :-

a) Every exporter of goods is required the furnish to RBI or other prescribed authority **a declaration containing true and correct material particulars, including the amount representing full export value.**
b) If full exportable value is not ascertainable at the time of export due to prevailing market conditions, the exporter shall indicate the amount he expects to receive on sale of goods in a market outside India.
c) The exporter of goods shall also furnish to RBI such other information as may be required by RBI for the purpose of ensuring realization of export proceeds by such exporter [section 7(i)].
d) RBI can direct any exporter to comply with prescribed requirements to ensure that full export value of the goods or such reduced value of the goods as RBI determines, is received without delay [section 7(2)].
e) Every exporter of services shall furnish to RBI or other prescribed authority a declaration containing true and correct material particulars in relation to payment of such services [section 7(3)].

B. Realization and repatriation of foreign exchange:

a) Where any amount of foreign exchange is due or has accrued to any resident in India,
b) such person shall take all reasonable steps to realize and repatriate to India the foreign exchange within such period and in such manner as may be specified by RBI (section 8).
c) Mr. Ramesh as an exporter of goods and services must comply with the requirements of section 7 and 8 of FEMA, 1999 and also with the requirements under Foreign Exchange Management (Export of Goods and Services) Regulations, 2015

Exemption from Realisation and repatriation in certain cases (Sec 9)

Question 34

According to Foreign Exchange Management Act, 1999, a person resident in India shall take all reasonable steps to repatriate to India any amount of foreign exchange earned and accrued to him. What is meant by the expression 'Repatriate to India'? State the cases where foreign exchange can be held or need not be repatriated to India by a resident in India.

Answer:

The word "repatriate to India" is defined in section 2(y) of the FEMA, Act 1999. **'Repatriate to India' means the realized foreign exchange should be sold to an authorised person in India in exchange for rupees.** It also includes the holding of realised amount in an account with an authorised person in India to the extent notified by the Reserve Bank and includes use of the

realised amount for discharge of a debt or liability denominated in foreign exchange.

Exemption from holding/ repatriation.

Section 4 of the FEMA, 1999 prohibits holding of foreign exchange by a resident in India. Section 8 requires that foreign exchange earned by a resident in India is realised and repatriated to India.
However, in the following cases, the foreign exchange can be held or need not be repatriated to India:-

a) **Possession of foreign currency** – possession of foreign currency or foreign coins upto limit prescribed by RBI is permitted (section 9(a))

b) **Foreign currency account** – Foreign currency account can be held and operated by such persons and within such limits as specified by RBI (Section 9(b))

c) 3 **Foreign currency acquired before July 1947** – Foreign exchange acquired or received before 8th July 1947 or income arising or accruing thereon can be held outside India (section 9(c))

d) **Gift or inheritance** – If such foreign exchange is acquired as a gift or inheritance, that exchange and income arising therefrom can be held as foreign exchange in India or held abroad and need not be repatriated (Section 9(d)).

e) **Foreign exchange acquired abroad** – Foreign exchange acquired from employment, business, trade, vocation, services honorarium, gifts, inheritance, or any other legitimate means can be held as foreign exchange in India or it need not be repatriated to India subject to limits specified by RBI (Section 9(e))

f) **Any other receipts specified by RBI [Section 9(f)]**

Question 35

Mr. Raman is a software engineer of Armtek Ltd. The company sent him to Japan to develop a software programme there on deputation for 2 years. He earned a sum of US $ 3,000 as a honorarium there. On his return to India he wants to hold this foreign currency with him. Whether Mr. Raman will be allowed to keep the foreign currency with him.

Answer:

As per Section 8 of the Foreign Exchange Management Act, 1999 where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realize and repatriate to India such foreign exchange within such period and in such manner as may be specified by Reserve Bank of India.

But as per section 9(e) of the said Act, this provision shall not apply to foreign exchange acquired from employment, business trade, vocation, service honorarium, gifts, inheritance or any other legitimate means up to such limit as the Reserve Bank of India may specify.

The Reserve Bank of India has specified the following persons with the limits for possession and retention of foreign currency by a person resident in India:

a) Any person may possess foreign coins without any restriction to the amount.
b) Any person resident in India is permitted to retain in aggregate foreign currency not exceeding USD 2,000 or its equivalent in the form of currency notes/bank notes or travelers cheques acquired by him;
c) Any person resident in India but not permanently resident therein is permitted to hold the foreign currency without limit, if the foreign currency was acquired when he was resident outside India and was brought into India and declared to the custom authorities.

In the given case as Mr. Raman earned a sum of USD 3000 as a honorarium when he was in employment in Japan. But in view of the restrictions under FEMA and the aforesaid regulation he can retain foreign exchange up to USD 2000 only and not more than that.

Provision Related to Authorised Persons (Sec 10 – Sec 12)

Question 36 ***(May 2010)***

The Reserve Bank of India issued certain directions to Dream Construction Limited, an authorised person under the Foreign Exchange Management Act, 1999 to file certain returns. The Company failed to file the said returns. Decide, as to what penal provisions are applicable against the said authorised person under the said Act.

Answer:

Penal provisions: Section 11(3) of the Foreign Exchange Management Act, 1999 states that where any authorized person contravenes any direction given by the Reserve Bank of India under the said Act or fails to file any return as directed by the Reserve Bank of India, the Reserve Bank of India may, after giving reasonable opportunity of being heard impose a penalty which may extend to ₹ 10,000/- and in the case continuing contraventions with an additional penalty which may extend to ₹ 2,000/- for every day during which such contravention continues.

Question 37

The Reserve Bank of India receives a complaint that an authorized person has submitted incorrect statements and information to the Reserve Bank of India in respect of receipt and utilization of Foreign Exchange. Explain the powers of the Reserve Bank of India with regard to inspection of records of the above authorized person in respect of the above complaint.

Referring to the provisions of Foreign Exchange Management Act, 1999, state the duties of the above authorized person.

Answer:

As per section 12 of the Foreign Exchange Management Act, 1999: The Reserve Bank may, at any time, cause an inspection to be made by any officer of the Reserve Bank specially authorized in writing by the Reserve Bank in this behalf, of the business of any authorized person as may appear to it to be necessary or expedient for the purpose of:

a) **verifying the correctness of any statement, information or particulars furnished to the Reserve Bank;**
b) **obtaining any information or particulars** which such authorized person has failed to furnish on being called upon to do so;
c) **securing compliance with the provisions of this Act or of any rules, regulations, directions or orders made thereunder.**

It shall be the duty of every authorized person, and where such person is a company or a firm, every director, partner or other officer of such company or firm, as the case may be, to produce to any officer making an inspection under section 12 (1) such books, accounts and other documents in his custody or power and to furnish any statement or information relating to the affairs of such persons, company or firm as the said officer may require within such time and in such manner as the said officer may direct.

Question 38

Explain the meaning of the term "Adjudicating Authority" under the Foreign Exchange Management Act, 1999, the powers available with the said authority to pass orders imposing penalty and enforce the same in relation to violation of any provision of FEMA by Mr. Dubious, a resident in India.

Answer:

Adjudicating authority: According to Section 2(a) of FEMA, 1999, 'Adjudicating Authority' means an officer authorized under section 16(i)

Power of adjudicating authority:

Persons committing an **offence under FEMA are liable to penalty**.

An adjudicating authority appointed by the Central Government under FEMA can impose any penalty for violation of any provision of FEMA or contravention of any rule, regulation, directions or orders issued under the powers conferred by the Act.

Their jurisdiction will be prescribed by the Central Government (section 16(1) & (2)).

The **Adjudicating Authority can hold inquiry only on receiving a complaint from an authorized officer** (Section 16(3)).

They have to **follow principles of natural justice by giving opportunity** to Mr. Dubious **of making representation**. The adjudicating authority should endeavor to dispose off the complaint within **1 year** (Section 16(6))

Penalty Amount:

a) **Amount is quantifiable:**
   The **adjudicating authority can impose penalty up to3* sum involved in such contravention where the amount is quantifiable**.
b) **Amount is not quantifiable:**
   If the amount is not quantifiable, **penalty up to 2 lakhs can be imposed**. If contravention is of **continuing nature, further penalty up to Rs 5,000 per day** during which the default continues can be imposed [Section 13(i)].

The Adjudicating Authority adjudicating the contravention can also order **confiscation of any currency, security or any other money or property in respect of which the contravention has taken place**.

He can also direct that **foreign exchange holdings of any person committing the contravention shall be brought back to India or retained outside as per directions** (Section 13(2)).

Enforcement of orders of adjudicating authority.

a) Person on whom penalty is imposed is required **to make payment within 90 days of receipt of notice**. **If such payment is not made, he is liable to civil imprisonment [Section 14(i)].**
b) **Such civil imprisonment can be up to 6 months, if demand is for less than 1 crore. If demand exceeds 1 crore, civil imprisonment can be up to 3 years.**
c) **If he pays the amount, he shall be released**.
d) Order for arrest and **detention cannot be made unless a show because notice is issued to the defaulter.**
e) However, arrest can be made without show cause notice, if adjudicating authority is satisfied

i) that the defaulter has dishonesty transferred, concealed or removed his property or he is refusing or neglecting to pay even if he has means to pay [Section 14(2) (b)] and

ii) he is likely to abscond the local limits [Section14(3)].

If a person to whom show because notice is issued does not appear before Adjudicating authority, warrant of arrest can be issued [Section 14 (4)].

Question 39

Mr. X, an Indian national has failed to realize and repatriate foreign exchange worth more than 2 crores. Mr. X having realized that he had committed a contravention of the provisions of the Foreign Exchange Management Act, 1999, desires to compound the said offence. Advise Mr. X.

Answer:

a) Because of his **failure to realize and repatriate foreign exchange,** Mr. X has contravened the provisions of section 8 of FEMA and he is liable to the penalties leviable under section 13, followed by adjudication proceedings.

b) Section 15 of FEMA **permits the offending party to compound the contravention within 180 days from the date of receipt of application by the Director of Enforcement** or such other officers of the Directorate of Enforcement and officers of the Reserve Bank of India as may be authorized in this behalf by the Central Government in such manner as may be prescribed.

c) **No contravention shall be compounded unless the amount involved in such contravention is quantifiable**. Where a contravention has been compounded, no proceeding can continue or be initiated against the person in respect of the contravention so compounded.

Adjudication and Appeal (Sec 16 – Sec 35)

Question 40

A person aggrieved by an order made by the Special Director (Appeals) desires to file an appeal against the said order to the Appellate Tribunal but the period of limitation of 45 days as prescribed in Section 19(2) of the Foreign Exchange Management Act, 1999 has expired. Advise.

Answer:

Any person aggrieved by an order made by the Special Director (Appeals), may prefer an appeal to the Appellate Tribunal under Section 19 (1) of the Foreign Exchange Management Act, 1999. Every appeal under sub-section (1) shall be **filed within a period of 45 days from the date on which a copy of the order made by the Special Director (Appeals) is received** by the aggrieved person shall be in such form, verified in such manner and be accompanied by such fee as may be prescribed.

Provided that **the Appellate Tribunal may entertain an appeal after the expiry of the said period of 45 days if it is satisfied that there was sufficient cause for not filing it within that period.**

Question 41

India Exports Limited engaged in the export of software products to U.S. One party in U.S. to whom the company exported certain products failed to pay the amount due for these exports resulting into non repatriation of amount to India. The Adjudicating Authority on coming to know about this, levied a penalty on India Exports Limited under the provisions of the Foreign Exchange Management Act, 1999. The company seeks your advice as to which authority, to whom it can make an appeal against the decision of Adjudicating Authority. State also, the time limit within which the appeal can be lodged.

Answer:

In accordance with the provisions of the Foreign Exchange Management Act, 1999, as contained under Sections 17 and 19 appeals against orders of Adjudicating Authority can be made by India Exports Ltd., If the Adjudicating Authority is Assistant Director of the Enforcement or Deputy Director of Enforcement, appeal will lie to Special Director (Appeals). Further appeal shall lie with Appellate Tribunal for Foreign Exchange against the order of Adjudicating Authority and the Special Director (Appeals). However, if the Adjudicating Authority is senior to the Assistant Director of Enforcement or Deputy Director of Enforcement, then the appeal shall lie directly to the Appellate Tribunal.

Appeal to Special Director (Appeals):

Appeal against order of Assistant Director of Enforcement or Deputy Director of Enforcement can be filed with Special Director (Appeals) under section 17 within 45 days from the date on which the copy of the order made by the Adjudicating Authority is received by the aggrieved person. The Special Director (Appeals) can condone the delay in filing the appeal if he is satisfied that there was sufficient cause for not filing the appeal within the stipulated time. Special Director (Appeals) will hear the parties and then pass the order. Copy of the order shall be sent to the concerned parties and the Adjudicating Authority.

Appeal to Appellate Tribunal:

Appeal against the order of Adjudicating Authority being senior to Assistant Director of Enforcement or Deputy Director of Enforcement or against the order of Special Director (Appeals) can be made to the Appellate Tribunal for Foreign Exchange, 1999 within 45 days from the date on which the copy of the order was made by such Adjudicating Authority or Special Director (Appeals) is received by the aggrieved person. In this case also, the delay can be condoned by the Appellate Tribunal. In case of an appeal against the order imposing penalty, the applicant has to deposit the amount of such penalty with the authority prescribed by the Central Government. However, the Appellate Tribunal may waive such deposit to mitigate the likely hardship that may be caused to the appellant. After hearing of the appeal, the Appellate Tribunal shall pass the order.

Tribunal is the final fact finding authority and no appeal lies against the facts determined by the Tribunal.

Therefore, India Exports Ltd., **can go for appeals as stated above.**

Question 42

Mr. Bandha, a software Engineer, Indian Origin took employment in USA. He is a resident of USA for a long time. He desires

a) to acquire a farm house in Munar (Kerala).
b) to make investment in KLJ (Nidhi) Ltd., registered as Nidhi Company.
c) to make investment in Rose Real Estate Ltd., an Indian Company formed for the development of township.

Mr. Unsatisfactory, brother of Mr. Bandha residing at Chennai is aggrieved by an order made by Appellate Tribunal established under Foreign Exchange Management Act, 1999, desires to file further appeal.

With references to the provisions of Foreign Exchange Management Act, 1999, analyse whether there are any restrictions in respect of the transactions desired by Mr. Bandha. Also determine the appeal procedure to Mr. Unsatisfactory on the order of Appellate Tribunal under the said Act.

Answer:

a) Acquisition of a Farm House

Mr. Bandha, cannot acquire a farm house in Munnar (Kerala) because a person resident outside India who is a citizen of India may acquire immovable property in India other than an agricultural property, plantation, or a farm house.

b) Making Investments in KLJ Nidhi Limited

Mr. Bandha cannot make investment in KLJ (Nidhi) Ltd., as a person resident outside India is prohibited from making investments in India in any form, in any Company, or partnership firm or proprietary concern or any entity whether incorporated or not which is engaged or proposes to engage as Nidhi Company.

c) Making Investments in Rose Real Estate Limited

The person resident outside India is prohibited from making investments in India in any form, in any Company, or partnership firm or proprietary concern or any entity whether incorporated or not which is engaged or proposes to engage in real estate business, or construction of farm houses. However, development of townships shall not be included in the real estate business.

Thus, Mr. Bandha can make investment in Rose Real Estate Ltd.

Appeal to High Court (Section 35)

Any person aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the High Court within sixty days from the date of communication of the decision or order of the Appellate Tribunal on any question of law arising out of such Order.

However, the High Court may, if it is satisfied that the Appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.

Mr. Unsatisfactory can file an appeal to the High Court, as per the above procedure.

Question 43

A French Manufacturing Company desirous of setting up its branch office at Pune seeks your advice on the objects for which the company may be allowed to set up the desired branch office. Advise the company about the procedure as required under the Foreign Exchange Management Act, 1999 to be followed in this regards

Answer:

Setting up a branch office at Pune by a French company –

Objects and the procedure under the FEMA, 1999: Since setting up a branch office by a foreign company in India involves foreign exchange, permission of RBI is required.

Following are the objects for which RBI permits companies engaged in manufacturing and trading activities abroad to set up Branch Office in India:

a) To represent the parent company/other foreign companies in various matters in India e.g. acting as buying/selling agents in India.
b) To conduct research work in the area in which the parent company is engaged.
c) To undertake export and import trading activities.
d) To promote possible technical and financial collaborations between the Indian companies and overseas companies.

e) Rendering professional or consultancy services

f) Rendering services in information technology and development of software in India.

g) Rendering technical support to the products supplied by the partner/group companies.

Steps / procedure:

i) Foreign company can set up Branch Offices in India after obtaining approval from RBI.

ii) The office can act as a channel of communication between Head Office abroad and parties in India. It is not allowed to undertake any business activity in India and cannot earn any income in India. Expenses of such offices are to be met entirely through inward remittances of foreign exchange from the Head Office abroad.

iii) Permission to set up such office is initially granted for a period of 3 years and this may be extended from time to time by the Regional Office in whose jurisdiction the office is set up.

iv) The representative office will have to file an annual activity certificate etc. from a Chartered Accountant to the concerned Regional Office of the RBI.

Application is required to be made in Form FNC-1.

Ch. 2 – Securitisation And Reconstruction of Financial Assets And Enforcement of Security Interest Act, 2002

Definitions

Question 1 ***(Nov 2010)***

Explain Asset Reconstruction, Financial Assets under the Securitization and Reconstruction of Financial Assets Enforcement of Security and Interest Act 2002.

Answer:

Asset Reconstruction: 'Asset Reconstruction' means **acquisition by any securitization company or reconstruction company of any right or interest of any bank or financial institution in any financial assistance for the purpose of realization of such financial assistance**. (Section 2(b) of Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act,2002.)

Financial Assets: Financial Assets' means debt or receivables and includes:

a) a claim to any debt or receivables or part thereof, whether **secured or unsecured**; or any debt or **receivables secured by mortgage of, or charge on, immovable property**; or a mortgage, charge, hypothecation or pledge of movable property; or

b) any **right or interest in the security, whether full or part underlying such debt or receivables**; or

c) any **beneficial interest in property**, whether movable or immovable or in such debt, receivables, whether such interest is existing, future accruing, conditional or contingent ;or any **financial assistance.** (Section 2(1)).

Question 2 ***(May 2013)***

Explain briefly the concept of "Securitization" under the provisions of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

Answer:

a) The Securitization and Reconstruction of Financial Assets and Enforcement of Security InterestAct, 2002 came into force in **June, 2002**. The preamble of the Act says that this **Act has been enacted to regulate securitization and reconstruction of financial assets and enforcement of security interest and for matters connected therewith or incidental thereto.**

b) The legal framework for securitization in India emerged **to promote the setting up of asset reconstruction/securitization companies, which are supposed to take over the Non- Performing Assets (NPA)** accumulated with the banks and public financial institutions.

c) The Act provides special powers to **lenders** and securitization/ asset reconstruction companies, to enable them to take over assets of borrowers **without first resorting to courts.**

d) **Note**: The concept of securitization may also be explained by following **two approaches:**

Approach 1 . Securitization:

Securitization means acquisition of financial assets by any securitization company or reconstruction company from any originator,

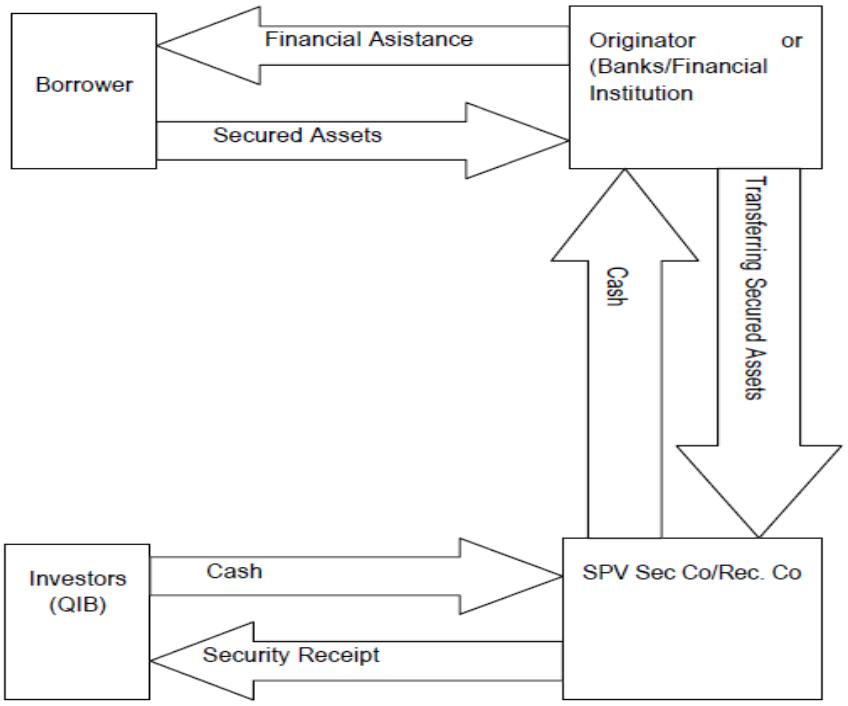
a) whether by raising of funds by such securitization company or

b) reconstruction company from qualified institutional buyers

By issue of security receipts representing undivided interest in such financial assets or otherwise [Section 2(z)].

Banks/Financial Institution (known as originators) give loans secured by properties to original borrowers. These loans or receivables are known as financial assets [Sec. 2(i)]. **These** financial assets are acquired by Securitization Company or reconstruction company (known as special purpose vehicles-**SPV**). The SPV issues **security receipts which are distributed to investors** (i.e. **Qualified Institutional Buyers**). **The SPV pays the bank/financial institution for the assets purchased** with the proceeds from the sale of securities.

In short: Securitization is a method adopted by banks/financial institutions for raising funds by way of selling receivables for money. These receivables are illiquid because these are non-performing assets.



Question 3 ***(May 2014)***

What are non-performing asset?

Answer:

"**Non-performing asset**" means an asset or account of a borrower, which has been classified by a bank or financial institution as **sub-standard, doubtful or loss asset**, in accordance with the directions or under guidelines relating to asset classifications issued by the Reserve Bank.

Regulation of Securitisation & Reconstruction of Financial Assets of Banks and Financial Institutions (Sec 3 – 12D)

Question 4

RST Ltd. is a securitization and reconstruction company under SARFAESI Act, 2002. The certificate of registration granted to it was cancelled. State the authority which can cancel the registration and the right of RST Ltd. against such cancellation.

Answer:

Cancellation of Certificate of Registration under SARFAESI Act, 2002:

a) The Reserve Bank of India**(RBI) may cancel a certificate of registration granted to a securitization and reconstruction company** for the reasons stated in Section 4 of SARFAESI Act, 2002.

b) RST Ltd., can prefer an **appeal to the Central Government** (Secretary, Ministry of Finance, Government of India**) within a period of 30 days** from the date on which order of cancellation was communicated to it.

c) The Central Government must also give such company **a reasonable opportunity of being heard before rejecting the appeal**.

If RST Ltd., is holding investments of qualified institutional buyers at the time of cancellation of certificate of registration, it shall be deemed to be a securitization and reconstruction company **until it repays the entire investments held by it, together with interest** if any, within such period as may be specified by the Reserve Bank.

Question 5 ***(Nov 2014)***

Referring to the provisions of the Securitization & Reconstruction of Financial Assets &Enforcement of Security Interest Act, 2002 state the circumstances under which the Reserve Bank of India may cancel the certificate of registration granted to a Securitisation Company.

Or

On what grounds the Reserve Bank of India can cancel a certificate of registration granted to an Asset Reconstruction Company. ***(RTP May 2019)***

Answer:

Cancellation of Certificate of Registration (Sections 3 and 4 of the securitization & reconstruction of financial assets & enforcement of Security Interest Act, 2002)

As per the section 4 of the Securitisation & Reconstruction of Financial Assets & Enforcement of security Interest Act, 2002, the Reserve Bank may cancel a certificate of registration granted to a securitization company or a reconstruction company, if such company-

a) ceases to carry on the business of securitization or asset reconstruction; or ceases to receive or hold any investment from a qualified institutional buyer; or
b) has failed to comply with any conditions subject to which the certificate of registration has been granted to it; or
c) at any time fails to fulfill any of the conditions referred to in clauses (a) to (g) of sub-section (3) of section 3; or
d) fails to-
   i) Comply with any direction issued by the Reserve Bank under the provisions of this Act; or
   ii) Maintain accounts in accordance with the requirements of any law or any direction or order issued by the Reserve Bank under the provisions of this Act; or
   iii) Submit or offer for inspection its books of account or other relevant documents when so demanded by the Reserve Bank; or
   iv) Obtain prior approval of the Reserve Bank required under sub-section (6) of section 3.

Enforcement of Security Interest (Sec 13, 14)

Question 6 ***(Nov 2011)***

Explain briefly the procedure relating to enforcement of security interest under SARFAESI Act, 2002.

Answer:

Procedure relating to enforcement of security interest (Section 13 of SARFAESI Act, 2002): Notwithstanding anything contained in section 69 or section 69A of the Transfer of Property Act, 1882 **(4 of 1882),** any security interest created in favor of any secured creditor may be enforced, without the intervention of the court or tribunal, by such creditor in accordance with the provisions of this Act.

a) Where any borrower, who is under a liability to a secured creditor under a security agreement,

b) makes any default in repayment of secured debt or any installment thereof, and his account in respect of such debt is classified by the secured creditor as non-performing asset, then,

c) **the secured creditor may require the borrower by notice in writing to discharge in full his liabilities to the secured creditor within 60 days from the date of notice** failing which the secured creditor shall be entitled to exercise all or any of the rights under sub-section (4) of section 13.

Provided that—

i) the **requirement of classification of secured debt as non-performing asset** under this sub-section shall **not apply to a borrower** who has **raised funds through issue of debt securities**; and

ii) in the **event of default**, the **debenture trustee shall be entitled to enforce security interest** in the same manner as provided under this section with such modifications as may be necessary and in accordance with the terms and conditions of security documents executed in favour of the debenture trustee;"

This notice shall give details of the amount payable by the borrower and the **secured assets intended to be enforced by the secured creditor in the event of non-payment of secured debts by the borrower.**

Sub-section (4) of section 13 provides that **if the borrower fails to discharge his liability in full within the above specified period, the secured creditor may take recourse to one or more of the following measures** to recover his secured debt: -

a) **take possession of the secured assets** of the borrower including the right to transfer by way of lease, assignment or sale for realizing the secured asset;

b) **take over the management** of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale and realize the secured asset;

c) **appoint any person** (hereafter referred to as the manager), to manage the secured assets the possession of which has been taken over by the secured creditor;

d) **require at any time by notice in writing**, any person who has acquired any of the secured assets from the borrower and from whom any money is due or may become due to the borrower, to pay the secured creditor, so much of the money as is sufficient to pay the secured debt.

[Note: Answer is revised as per the amendment made by the Enforcement of Security Interest and Recovery of Debts Laws and Miscellaneous Provisions (Amendment) Act, 2016 notified on 16th August 2016]

Question 7 ***(May 2017)***

Popular Limited defaulted in the repayment of term loan taken from a Bank against security created as a first charge on some of its assets. The bank issued notice pursuant to Section 13 of the SARFAESI Act, 2002 to the Company to discharge its liabilities within a period of 60 days from the date of the notice. The company failed to discharge its liabilities within the time limit specified.

Explain the measures to be taken by the Bank to enforce its security interest under the said Act.

Answer:

Sub-section (4) of section 13 of SARFAESI Act, 2002, provides that if the borrower fails to discharge his liability in full within the 60 days, the secured creditor may take recourse to one or more of the following measures to recover his secured debt:

i) take possession of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realising the secured asset;

ii) take over the management of the business of the borrower including the right to transfer by

way of lease, assignment or sale for realising the secured asset:

Provided that the right to transfer by way of lease, assignment or sale shall be exercised only where the substantial part of the business of the borrower is held as security for the debt:

Provided further that where the management of whole of the business or part of the business is severable, the secured creditor shall take over the management of such business of the borrower which is relatable to the security for the debt;

iii) appoint any person (hereafter referred to as the manager), to manage the secured assets the possession of which has been taken over by the secured creditor;

Question 8 ***(May 2018)***

Beta Ltd. failed to repay the amount borrowed from KMP Bank Ltd. in accordance with the terms of lending. The loan was granted against the mortgage of its Building. The Bank issued notice as required under Section 13 of the SARFAESI Act, 2002. It was decided by the bank to take possession of the Building after getting necessary assistance from the judicial authority. State the provisions enumerated under Section 14 of the SARFAESI Act, 2002 in this regard.

Answer:

Chief Metropolitan Magistrate or District Magistrate to assist secured creditor in taking possession of secured asset (Section 14)

The secured creditor may, for the purpose of taking possession or control of secured asset, request, in writing, the Chief Metropolitan Magistrate or the District Magistrate within whose jurisdiction any such secured asset or other documents relating thereto may be situated or found, to take possession thereof, and the Chief Metropolitan Magistrate or, as the case may be, the District Magistrate shall, on such request being made to him

a) take possession of such asset and documents relating thereto; and
b) forward such asset and documents to the secured creditor.

within a period of thirty days from the date of application.

Provided further that if no order is passed by the Chief Metropolitan Magistrate or District Magistrate within the said period of thirty days for reasons beyond his control, he may, after recording reasons in writing for the same, pass the order within such further period but not exceeding in aggregate sixty days.

Manner and effect of takeover of management (Sec 15, 16)

Question 9

Apex Limited failed to repay the amount borrowed from the bankers, ACE Bank Limited, which is holding a charge on all the assets of the company. The Bank took over management of the company in accordance with the provisions of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 by appointing four persons as directors. The company is managed by a Managing Director, Mr. X. Referring to the provisions of the said Act, examine whether Mr. X is entitled to compensation for loss of office and also explain the effect of such takeover on certain rights of the shareholders of the company

Or

Rockfort Limited failed to repay the loan borrowed from Nest Bank, which is holding a charge on all the assets of the company. The Bank took over management of the company in accordance with the provisions of the Securitization and Reconstruction of Financial Assets and Enforcement of

Security Interest Act, 2002 by appointing four persons as directors. The Company is managed by Managing Director Mr. Pawn, who has been now removed. Referring to the provisions of the said Act, examine whether Mr. Pawn is entitled to compensation for loss of office. ***(Nov 18)***

Answer:

Apex Limited failed to repay the amount borrowed from the bankers, ACE Bank Limited, which is holding a charge on all the assets of the company. The bank took over management of the company in accordance with the provisions of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 by appointing four persons as directors. The company is managed by a Managing Director, Mr. X.

Here, Apex Limited is a borrower and ACE Bank Limited is a secured creditor. Compensation to Managing director (Mr. X) for loss of office:

According to section 16 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, irrespective of anything contained in any contract or in any other law for the time being in force, no managing director or any other director or a manager or any person in charge of management of the business of the borrower shall be entitled to any compensation for the loss of office or for the premature termination under this Act. However any such managing director or any other director or manager or any such person in charge of management has the right to recover from the business of the borrower, moneys recoverable otherwise than by way of such compensation.

Effect of takeover on rights of the shareholders:

Where the management of the business of a borrower, being a company as defined in the Companies Act is taken over by the secured creditor, then, notwithstanding anything contained, such borrower-in the said Act or in the memorandum or articles of association of such company -

a) it shall not be lawful for the shareholders of such company or any other person to nominate or appoint any person to be a director of the company;
b) no resolution passed at any meeting of the shareholders of such company shall be given effect to unless approved by the secured creditor;
c) no proceeding for the winding up of such company or for the appointment of a receiver in respect thereof shall lie in any court, except with the consent of the secured creditor.

The secured creditor is under an obligation to restore the management of the business of the borrower, on realisation of his debt in full, in case of takeover of the management of the business of a borrower by such secured creditor.

Provided that if any secured creditor jointly with other secured creditors or any asset reconstruction company or financial institution or any other assignee has converted part of its debt into shares of a borrower company and thereby acquired controlling interest in the borrower company, such secured creditors shall not be liable to restore the management of the business to such borrower.

Question 10 ***(Nov 2018)***

The Management of Gangotri Ltd. was taken by LBV Bank Ltd. (secured creditor) complying the provisions of SARFAESI Act, 2002 and appointed two Directors. The Board of Directors of Gangotri Ltd., duly authorized by its Articles, appointed two Alternate Directors and the majority of the Directors made a declaration required for voluntary liquidation proceedings. A special resolution requiring the Company to be liquidated voluntarily by appointing an insolvency professional to act as the Liquidator was passed at the general meeting of the Company. The Board of Directors and the Shareholders passed the resolutions without the approval/consent of Directors appointed by LBV

Bank Ltd. Discuss the validity of the above resolutions under SARFAESI Act, 2002. Does an unsecured Creditor have recourse to this Act?

Answer:

Management of borrower taken by the secured creditor (Section 15 of the SARFAESI Act, 2002): Where the management of the business of a borrower, being a company is taken over by the secured creditor then, notwithstanding anything contained in the said Act or in the memorandum or articles of association of such borrower -

a) it shall not be lawful for the shareholders of such company or any other person to nominate or appoint any person to be a director of the company;

b) no resolution passed at any meeting of the shareholders of such company shall be given effect to unless approved by the secured creditor;

Accordingly, in the given situation in the question, appointment of alternate directors by the BOD of Gangotri Ltd. though authorised by its Articles, is not valid, and the special resolution so passed by majority for voluntary liquidation passed at general meeting shall not be given effect due to lack of consent of LBV Bank Ltd.

An unsecured creditor doesn't have recourse to this Act.

Borrower's rights in case of enforcement of security interest by secured creditors (Sec 17, 17A, 18, 18B and 19)

Question 11 ***(Nov 2017)***

Sharp Health Clinic Limited had availed the credit facilities from the United Bank Limited. The company made repayment of loan to some extent but not entirely and accordingly the Bank took recourse under the provisions of Section 13(2) the SARFAESI Act, 2002. Consequently, possession of the mortgaged property was taken up and it was duly advertised. The company also filed an application under Section 17(1)of the SARFAESI Act, 2002 before the Debts Recovery Tribunal, which was dismissed by the impugned order. Being aggrieved, the company approached court. Will the company succeed in its petition referring to in the SARFAESI Act, 2002?

Answer:

According to Section 18(1) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, any person aggrieved, by any order made by the Debts Recovery Tribunal under section 17, may prefer an appeal along with prescribed fees to the Appellate Tribunal within 30 days from the date of receipt of the order of Debts Recovery Tribunal.

Further, no appeal shall be entertained unless the borrower has deposited with the Appellate Tribunal 50% of the amount of debt due from him, as claimed by the secured creditors or determined by the Debts Recovery Tribunal, whichever is less. However, the Appellate Tribunal may, for the reasons to be recorded in writing, reduce the amount to not less than 25% of debt.

Thus, in the given situation Sharp Health Clinic Limited can appeal to the Appellate Tribunal (Now to NCLAT) by following the above provisions.

Ch. 3 – Prevention of Money Laundering Act, 2002

Basics of PMLA

Question 1 ***(May 2013)***

"Money Laundering" does not mean just siphoning of fund." Comment on this statement explaining the significance and aim of the Prevention of Money Laundering Act, 2002.

Answer:

"Money laundering" does not mean just siphoning of fund: Money Laundering is a **moving of illegally acquired cash** through financial systems so that it appears to be legally acquired. Thus, money laundering is not just the siphoning of fund but it is the conversion of money which is illegally obtained.

Prevention of Money Laundering Act, 2002 has been enacted with aim for combating channelizing of money into illegal activities.

Significance and Aim of Prevention of Money Laundering Act, 2002:

a) The preamble to the Act provides that it **aims to prevent money–laundering and to provide for confiscation of property derived from, or involved in, money–laundering and for matters connected therewith or incidental thereto.**

b) In order to further **strengthen the existing legal framework and to effectively combat money laundering, terror financing and cross-border economic offences, an Amendment Act, 2009** was passed.

c) The new **law seeks to check use of black money for financing terror activities**. Financial intermediaries like full- fledged money changers, money transfer service providers and credit card operators have also been brought under the ambit of The Prevention of Money-Laundering Act. Consequently, **these intermediaries, as also casinos, have been brought under the reporting regime of the enforcement authorities**.

d) It also checks the **misuse of promissory notes by FIIs, who would now be required to furnish all details of their source. The new law would check misuse of "proceeds of crime"** be it from sale of banned narcotic substances or breach of the Unlawful Activities (Prevention) Act.

The passage of the Prevention of Money Laundering (Amendment), 2009 have enabled India's entry into Financial Action Task Force (FATF), an inter-governmental body that has the mandate to combat money laundering and terrorist financing.

Definitions

Question 2 ***(May 2018)***

Explain the meaning of the term "Property" under the Prevention of Money Laundering Act, 2002.

Answer:

According to clause (v) of sub – Section (1) of Section 2 of the Prevention of Money Laundering Act, 2002, "property" means any property or assets of every description, whether corporeal or incorporeal, movable or immovable, tangible or intangible and includes deeds and instruments evidencing title to, or interest in, such property or assets, wherever located.

Explanation.— For the removal of doubts, it is hereby clarified that the term "property" includes property of any kind used in the commission of an offence under this Act or any of the scheduled offences.

Question 3 ***(May 2018)***

What is Payment System? Under the provisions of Prevention of Money Laundering Act, 2002

Answer:

In terms of clause (rb) of section 2 "payment system" means a system that enables payment to be effected between a payer and a beneficiary, involving clearing, payment or settlement service or all of them. It includes the systems enabling credit card operations, debit card operations, smart card operations, money transfer operations or similar operations.

Offence for Money Laundering (Sec 3 – Sec 4)

Question 4 ***(May 2012)***

Explain the term "Offence of Money Laundering" within the meaning of the Prevention of Money Laundering Act, 2002. State the punishment for the offence of money laundering.

or

Explain the meaning of the term "Money Laundering". Z, a known smuggler was caught in transfer of funds illegally exporting narcotic drugs from India to some countries in Africa. State the maximum punishment that can be awarded to him under Prevention of Money Laundering Act, 2002.

Answer:

Money Laundering: Whosoever directly or indirectly attempts to indulge or knowingly assists or knowingly is a party or is actually involved in any process or activity connected with the proceeds of crime and projecting it as untainted property shall be guilty of offence of money laundering. [Section 3 of the Prevention of Money Laundering Act, 2002]

Paragraph 2 of Part A of the Schedule to the Prevention of Money Laundering Act, 2002, covers Offences under the Narcotic Drugs and Psychotropic Substances Act, 1985. Illegal import into India, export from India or transshipment of narcotic drugs and psychotropic substances (section 23) is covered under paragraph 2 of Part A.

Punishment: Section 4 of the said Act provides for the punishment for Money-Laundering. Whoever commits the offence of money-laundering shall be **punishable with rigorous imprisonment for a term which shall not be less than 3 years but which may extend to 7 years and shall also be liable to fine.** But where the proceeds of crime involved in money- laundering relate to any offence specified under paragraph 2 of Part A of the Schedule, the **maximum punishment may extend to 10 years instead of 7 years.**

Question 5 ***(May 2018)***

Mr. Honest, a notorious, was caught in possession of Counterfeit Currency Notes, an offence specified under Part A - Paragraph 1 of the Schedule of the Prevention of Money Laundering Act, 2002. State the Punishment that can be awarded to him under the above Act. Also identify the punishment for the offence specified under Part A - paragraph 2 of the Schedule of the Prevention of Money Laundering Act, 2002.

Answer:

Section 4 of the Prevention of Money Laundering Act, 2002 provides for the punishment for Money-

Laundering. According to the Section, whoever commits the offence of money-laundering shall be punishable with rigorous imprisonment for a term which shall not be less than three years but which may extend to seven years and shall also be liable to fine. But where the proceeds of crime involved in money- laundering relate to any offence specified under paragraph 2 of Part A of the Schedule, the maximum punishment may extend to ten years instead of seven years.

Since, counterfeiting of currency notes is a predicate offence, specified under paragraph 1 of Part A of the Schedule (and not under paragraph 2 of Part A of the Schedule), Mr. Honest can be punishable with rigorous imprisonment for a term which shall not be less than three years but which may extend to seven years and shall also be liable to fine.

Where the offence specified falls under Part A- Paragraph 2 of the Schedule of PMLA, maximum punishment may extend to 10 years.

Question 6 ***(May 2019)***

Mr. Dawood Moosa, a known smuggler was caught in transfer of funds illegally exporting narcotic drugs from India to some countries in Africa. State the maximum punishment that can be awarded to him under Prevention of Money Laundering Act, 2002.

Answer:

Paragraph 2 of Part A of the Schedule to the Prevention of Money Laundering Act, 2002, covers Offences under the Narcotic Drugs and Psychotropic Substances Act, 1985. Whereby, illegal import into India, export from India or transshipment of narcotic drugs and psychotropic substances (section 23) is covered under paragraph 2 of Part A.

Punishment: Section 4 of the said Act provides for the punishment for Money- Laundering. Whoever commits the offence of money-laundering shall be punishable with rigorous imprisonment for a term which shall not be less than 3 years but which may extend to 7 years and shall also be liable to fine. But where the proceeds of crime involved in money-laundering relate to any offence specified under paragraph 2 of Part A of the Schedule, the maximum punishment may extend to 10 years instead of 7 years. Thus, in the given case, the maximum punishment may extend to 10 years.

Obligation of banking companies, Financial Institutions & Intermediaries (Sec 12 – 15)

Question 7 ***(Nov 2008)***

Enumerate the obligations of banking companies under the Prevention of Money Laundering Act, 2002.

Answer:

Section 12 provides for the obligation of Banking Companies, Financial Institutions and Intermediaries or a person carrying on a designated business or profession. According to sub-section (1), every banking company, financial institution and intermediary or a person carrying on a designated business or profession shall –

a) maintain a record of all transactions, including information relating to transactions covered under clause (b), in such manner as to enable it to reconstruct individual transactions;
b) furnish to the Director within such time as may be prescribed, information relating to such

transactions, whether attempted or executed, the nature and value of which may be prescribed;

c) ~~verify the identity of its clients in such manner and subject to such conditions, as may be prescribed;~~

d) ~~identify the beneficial owner, if any, of such of its clients, as may be prescribed;~~ (Deleted as per Amendments given in RTP)

e) maintain record of documents evidencing identity of its clients and beneficial owners as well as account files and business correspondence relating to its clients.

Every information maintained, furnished or verified, save as otherwise provided under any law for the time being in force shall be kept confidential.

The records referred to in clause (a) of sub-section (I) shall be maintained for a period of five years from the date of transaction between a client and the reporting entity.

The records referred to in clause (e) of sub-section (I) shall be maintained for a period of five years after the business relationship between a client and the reporting entity has ended or the account has been closed, whichever is later.

The Central Government may, by notification, exempt any reporting entity or class of reporting entities from any obligation under this chapter.

Question 8 ***(Nov 2013)***

PMT Limited, a banking company maintained the record of all transactions for a period of 5 years from the date of cessation of the transactions between the clients and the company. Decide whether the company has fulfilled its obligation under the provision of Money laundering Act, 2002.

Answer:

Obligation of Banking Companies:

Sec. 12 of the Prevention of Money Laundering Act, 2002 provides for the obligation of Banking Companies, Financial Institutions and Intermediaries of securities market. Such Obligations are;

1) **Maintenance of records: Every reporting entity shall-**

a) maintain a record of all transactions, including information relating to transaction covered under clause (b), in such a manner as to enable it to reconstruct individual transactions;

b) furnish to the Director within such time as may be prescribed, information relating to such transactions, whether attempted or executed, the nature and the value of which prescribed,

c) verify the identity of its clients in such manner and subject to such condition, as may be prescribed;

d) identify the beneficial owner, if any, of such of its clients, as may be prescribed;

e) maintain records of documents evidencing identity of its clients and beneficial owners as well as account files and business correspondence relating to its clients.

2) **Maintain of records: The records referred to in clause (a) shall be maintained for a period of 5 years from the date of transaction between a client and reporting entity. The records referred to in clause (e) shall be maintained for a period of 5 years after the business relationship between a client and the reporting entity has ended or the account has been closed, whichever is later.**

In the given case, PMT Limited,a banking company maintained the record of all transaction for a period of 5 years from the date of cessation of the transactions between the clients and the company.

Conclusion : The Company has fulfilled its obligation as record are maintained for 5 years as required by law.

Question 9 ***(Nov 2017)***

Manav Kalyan", a charitable organization, opened a current account with M/s ABZ Bank on 1st July, 2012. This account was closed on 30th June, 2016. Referring to the obligations of banking companies under the Prevention of Money Laundering Act, 2002, specify the period upto which the said bank has to maintain records relating to the account of "Manav Kalyan".

Answer:

Obligation of Banking Companies, Financial Institutions and Intermediaries: Section 12 of the Prevention of Money Laundering Act, 2002 provides for the obligation of Banking Companies, Financial Institutions and Intermediaries. According to sub-section (1), every Banking Companies, Financial Institutions and Intermediaries shall maintain the records referred to in clause (a) of sub-section (1) for a period of five years from the date of transaction between a client and the reporting entity. For the records referred to in clause (e) of sub-section (1), it shall be maintained for a period of five years after the business relationship between a client and the reporting entity has ended or the account has been closed, whichever is later.

As per the facts given in the questions, Manav Kalyan, a charitable organization opened current account with ABZ Bank on 1st July, 2012 and closed the account on 30th June 2016.

As per the above provisions, ABZ Bank shall maintain record of documents evidencing identity of its clients and beneficial owners as well as account files and business correspondence relating to its clients for a period of five years after the business relationship between a client and the reporting entity has ended or the account has been closed, whichever is later.

So, accordingly the ABZ Bank has to maintain the records relating to the account of "Manav Kayan" till 30th June, 2021.

Question 10 ***(May 2019)***

Who is a "Reporting Entity" under the Prevention of Money Laundering Act, 2002 and what are the obligations cast on them under Sec. 12 of the Act? The Bank account of Amar has been attached by the order of an Assistant Director for a period of 180 days. The lawyer of Amar objected to this attachment. Decide the validity of the attachment.

Answer:

"Reporting entity" means a banking company, financial institution, intermediary or a person carrying on a designated business or profession.

Section 12 of the Prevention of Money Laundering Act, 2002 provides for the obligation of Banking Companies, Financial Institutions and Intermediaries.

According to section 12,

1. Maintenance of records: Every reporting entity shall –
   (a) maintain a record of all transactions,
   (b) furnish to the Director information relating to such transactions, whether attempted or executed, the nature and value of the said transactions;
   (c) verify the identity of its clients
   (d) identify the beneficial owner, if any, of its clients,
   (e) maintain record of documents evidencing identity of its clients and beneficial owners as well as account files and business correspondence relating to its clients.

2. **Maintenance of records related to the transactions (i.e. for above clause a)**: The records shall be maintained for a period of five years from the date of transaction between a client and the reporting entity.

3. **Maintenance of records related to evidencing identity of its clients and beneficial owners (i.e., for above clause e):** The records shall be maintained for a period of five years after the business relationship between a client and the reporting entity has ended or the account has been closed, whichever is later.

In the instant case, the bank account of Amar has been attached by the order of an Assistant Director for a period of 180 days. As per section 5 of the Prevention of Money Laundering Act, 2002, attachment of a property can be done by the Director or any other officer not below the rank of Deputy Director. Here the order is issued by an Assistant Director who is below the rank of the Deputy Director. Therefore, the objection of the lawyer of Amar is valid.

Appellate Tribunal (Sec 25 - Sec 42)

Question 11 ***(May 2016)***

The Adjudicating Authority appointed under the Prevention of Money Laundering Act, 2002 issued an order attaching certain properties of XYZ Limited alleged to be involved in money laundering for a specified period. The company aggrieved by the order of the Adjudicating Authority seeks your advice about the remedy that is available under the Act. Advise explaining the relevant provisions of the Prevention of Money Laundering Act, 2002.

Or

The Adjudicating Authority appointed under the Prevention of Money Laundering Act, 2002 issued an order attaching certain properties of SVG Limited, alleging to be involved in money laundering for a specified period. The Company, aggrieved by the Order of the Adjudicating Authority,' seeks your advice about the remedy that is available under the Act. Analyse and apply the relevant provisions of the Act in relation to the above situation and advise. ***(May 2019)***

Answer:

Section 25 of Prevention of Money Laundering Act, 2002 empowers the Central Government to establish an Appellate Tribunal to hear appeal against order of the Adjudicating Authority and other authorities under the Act.

Section 26 deals with the right and time frame to make an appeal to the Appellate Tribunal. Any person aggrieved by an order made by the Adjudicating Authority may prefer an appeal to the Appellate Tribunal within a period of 45 days from the date on which a copy of the order is received by him. The appeal shall be in such form and be accompanied by such fee as may be prescribed. The **Appellate Tribunal may extend the period if it is satisfied that there was sufficient cause for not filing it within the period of 45 days.**

The Appellate Tribunal may after giving the parties to the appeal an opportunity of being heard, pass such order as it thinks fit, confirming, modifying or setting aside the order appealed against.
The Act also provides further appeal. According to Section 42 any person aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the High Court within 60 days from the date of communication of the order of the Appellate Tribunal.

In the light of the provisions of the Act explained above the company is advised to prefer an appeal to Appellate Tribunal in the first instance.

Question 12 ***(Nov 2018)***

An Appellate Tribunal consisting of two members was formed to hear the appeal preferred by Mr. Hari, being aggrieved by an Order made by the Adjudicating Authority under the Prevention of Money Laundering Act, 2002. Two members of the Bench differ in their opinion on a particular point referred in the appeal.

Explain the next course of action to be followed by the Bench members under the said Act.

Answer:

Decision to be by majority [Section 38 of the Prevention of Money Laundering Act, 2002]

If the Members of a Bench consisting of two Members differ in opinion on any point, they shall state the point or points on which they differ, and make a reference to the Chairman who shall either hear the point or points himself or refer the case for hearing on such point or points by third Member of the Appellate Tribunal and such point or points shall be decided according to the opinion of the majority of the Members of the Appellate Tribunal who have heard the case, including those who first heard it.

In the instant case, the above procedure has to be followed by the Bench members.

Special Courts (Sec 43 - Sec 47)

Question 13 ***(May 2015)***

How a trial under the Prevention of Money Laundering Act, 2002 is conducted in Special Courts?

Answer:

Sections 43 to 47 deal with provisions relating to Special Courts. **Section 43 empowers the Central Government** (in consultation with the Chief Justice of the High Court) for trial of offence of money laundering, to notify one or more Courts of Sessions as Special Court or Special Courts for such area or areas or for such cases or class or group of cases as may be specified in the notification to this effect. **Section 44 clearly provides for the offences triable** by Special Courts. It overrides the provisions of the Code of Criminal Procedure, 1973 and provides that –

a) The scheduled offence and the offence punishable under **section 4 shall be triable only by the Special Court constituted for the area in which the offence has been committed**.
b) A Special Court may, upon a complaint made by an authority authorized in this behalf under this Act take cognizance of the offence for which the accused is committed to it for trial. **The requirement of police report of the facts which constitute an offence under this Act is no more applicable.**

Question 14 ***(Nov 2012 & 2015)***

Mr. Gambler has been arrested for a cognizable and non-bailable offence punishable for a term of imprisonment for more than three years under the Prevention of Money Laundering Act, 2002. He seeks your advise as to how can he be released on bail. Advise him.

Or

Mr. Robert has been arrested for a cognizable and non-bailable offence under Part- A of the schedule punishable for a term of imprisonment for more than three years under the Prevention of Money Laundering Act, 2002. He seeks your advice as to how can he be released on bail. Advise him.

(May 2019)

Answer:

In accordance with the provisions of the Money Laundering Act, 2002, as contained under Section 45,

the offences under the Act shall be cognizable and non- bailable. Notwithstanding anything contained in the Code of Criminal Procedure, 1973, no person accused of an offence punishable for a term of imprisonment of more than 3 years under Part A of the Schedule shall be released on bail or on his own bond unless:

The public Prosecutor has been given an opportunity to oppose the application for such release and Where the Public Prosecutor opposes the application, the court is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while on bail.

In case of any person who is under the age of 16 years or in case of a woman or in case of a sick or infirm person, the Special Court can direct the release of such person on bail.
`Mr. Gambler may refer the above section 45 so that he can be released on bail.

Reciprocal Arrangement for Assistance in certain matters

Question 15 ***(May 2019)***

Mr. Manoranjan, an officer investigating a case of money laundering, is of the view that important evidence relating to the case is available in a foreign country, (Contracting State) with which agreement for exchange of information has already been entered into.
Advise Mr. Manoranjan, referring to the provisions of the Prevention of Money Laundering Act, 2002, about the procedure to be followed for collecting such evidence

Answer:

According to **Section 57** of the **Prevention of Money Laundering Act, 2002**, the following procedure may be followed for collecting evidence relating to the case that Mr. Manorajan is investigating:

1. **Issue of letter of request:** If, in the course of an investigation into an offence or other proceedings under this Act, an application is made to a Special Court by the Investigating Officer or any officer superior in rank to the Investigating Officer that any evidence is required in connection with investigation into an offence or proceedings under this Act and he is of the opinion that such evidence may be available in any place in a contracting State, and the Special Court, on being satisfied that such evidence is required in connection with the investigation into an offence or proceedings under this Act, may issue a letter of request to a court or an authority in the contracting State competent to deal with such request to-
   (i) examine facts and circumstances of the case,
   (ii) take such steps as the Special Court may specify in such letter of request, and
   (iii) forward all the evidence so taken or collected to the Special Court issuing such letter of request.
2. **Transmission of letter of request:** The letter of request shall be transmitted in such manner as the Central Government may specify in this behalf.
3. **Letter of request to be deemed as an evidence**: Every statement recorded or document or thing received shall be deemed to be the evidence collected during the course of investigation.

Miscellaneous

Question 16 ***(Nov 2018)***

Mr. Narayan willfully gives false information, refuses to give evidence and to sign statement made by him in the course of proceedings under the provisions of Prevention of Money Laundering Act, 2002.

Explain the penal provisions and mode of recovery of fine or penalty enumerated under the said Act.

Answer:

Punishment for false information or failure to give information, etc. [Section 63 of the Prevention of Money Laundering Act, 2002]

1. Any person willfully and maliciously giving false information and so causing an arrest or a search to be made under this Act shall on conviction be liable for imprisonment for a term which may extend to two years or with fine which may extend to fifty thousand rupees or both.
2. If any person,-

(a) refuses to give evidence and

(b) refuses to sign statement made by him in the course of proceedings

he shall pay, by way of penalty, a sum which shall not be less than 500 rupees but which may extend to 10,000 rupees for each such default or failure.

Mode of Recovery of fine or penalty [Section 69]

Where any fine or penalty imposed on any person under section 13 or section 63 is not paid within six months from the day of imposition of fine or penalty, the Director or any other officer authorised by him in this behalf may proceed to recover the amount from the said person in the same manner as prescribed in Schedule II of the Income-tax Act, 1961 for the recovery of arrears and he or any officer authorised by him in this behalf shall have all the powers of the Tax Recovery Officer mentioned in the said Schedule for the said purpose.

Question 17 ***(Nov 2018)***

Mr. JJ was found guilty by the authorities under Section 13 of the Prevention of Money Laundering Act, 2002 and monetary penalty was levied on Mr. JJ. But Mr. JJ could not pay the penalty amount. What is the mechanism to recover the fine or monetary penalty imposed on any person by the authorities under Section 13 or Section 63 of the Prevention of Money Laundering Act, 2002?

Answer:

Recovery of fine or penalty [Section 69 of the Prevention of Money Laundering Act, 2013]

Where any fine or penalty imposed on any person under section 13 or section 63 is not paid within six months from the day of imposition of fine or penalty, the Director or any other officer of the Adjudicating Authority authorised by him in this behalf may proceed to recover the amount from the said person in the same manner as prescribed in Schedule II of the Income-tax Act, 1961 for the recovery of arrears and he or any officer authorised by him in this behalf shall have all the powers of the Tax Recovery Officer mentioned in the said Schedule for the said purpose.

Ch. 4 – The Foreign Contribution (Regulation) Act, 2010

Question 1

State under what circumstances Government can cancel the certificate of registration granted to a person under FCRA?

Answer:

Yes. As per section 14 of the FCRA, Central Government may cancel the certificate, after carrying out an inquiry, on the following grounds –

a) the holder of the certificate has made an incorrect/false statement in the application for the grant of registration or renewal
b) the holder of the certificate has violated any of the terms and conditions of the certificate or renewal thereof
c) in the opinion of the Central Government, it is necessary in the public interest to cancel the certificate
d) the holder of the certificate has violated any of the provisions of this Act or rules or order made thereunder.
e) if the holder of the certificate has not been engaged in any reasonable activity in its chosen field for the benefit of the society for two consecutive years or has become defunct.

In any person whose certificate has been cancelled under this section shall not be eligible for registration or grant of prior permission for a period of three years from the date of cancellation of such certificate.

Question 2

X, is an association having registration to transfer the Foreign Contribution received by it to another organization? Is the valid act of X? If yes, then what is the process to do so? Is there any restriction on transfer of funds to other organisations?

Answer:

Yes X can transfer the Foreign Contribution received by it to another organization as section 7 of FCRA, 2010. According to the provision no person who –

a) is registered and granted a certificate or has obtained prior permission under this Act; and
b) receives any foreign contribution,

shall transfer such foreign contribution to any other person unless such other person is also registered and had been granted the certificate or obtained the prior permission under this Act:

Provided that such person may transfer, with the prior approval of the Central Government, a part of such foreign contribution to any other person who has not been granted a certificate or obtained permission under this Act in accordance with the rules made by the Central Government."

Restrictions on transfer: Rule 24 of FCRR, 2011, prescribes the procedure for transferring foreign contribution to any unregistered person as under:

A person who has been granted a certificate of registration or prior permission under section 11 and intends to transfer part of the foreign contribution received by him to a person who has not been granted a certificate of registration or prior permission under the Act, may transfer such foreign contribution to an extent not exceeding ten per cent of the total value thereof and for this purpose, make an application to the Central Government in the prescribed Form.

1) Every application made under sub-rule (1) shall be accompanied by a declaration to the effect that-

a) the amount proposed to be transferred during the financial year is less than ten per cent of the total value of the foreign contribution received by him during the financial year;

b) the transferor shall not transfer any amount of foreign contribution until the Central Government approves such transfer.

2) A person who has been granted a certificate of registration or prior permission under section 11 shall not be required to seek the prior approval of the Central Government for transferring the foreign contribution received by him to another person who has been granted a certificate of registration or prior permission under the Act provided that the recipient has not been proceeded against under any of the provisions of the Act.

3) Both the transferor and the recipient shall be responsible for ensuring proper utilisation of the foreign contribution so transferred and such transfer of foreign contribution shall be reflected in the returns in Form to be submitted by both the transferor and the recipient."

Question 3 ***(RTP May 2018)***

Can foreign contribution be received in and utilised from multiple Bank Accounts?

Answer:

The foreign contribution should be received only in the exclusive single foreign contribution account of a Bank (also called designated FC account), as mentioned in the order for registration or prior permission granted and should be separately maintained by the associations. However, one or more accounts (called Utilization Account) in one or more banks may be opened by the association for 'utilising' the foreign contribution after it has been received in the designated FCRA bank account, provided that no funds other than that foreign contribution shall be received or deposited in such account or accounts and in all such cases, intimation is to be given online within 15 days of opening of such account.

Question 4

Can capital assets purchased with the help of foreign contributions be acquired in the name of the Mr. Ram, an office bearers of the association?

Answer:

No. Every asset purchased with foreign contribution should be acquired and possessed in the name of the association since an association has a separate legal entity distinct from its members.

Question 5 ***(RTP May 2018)***

Whether foreign remittances received from a relative are to be treated as foreign contribution as per FCRA 2010?

Answer:

Foreign remittances received from a relative

- AS per Sec 4(e) of the Foreign Regulation Act 2010 and Rules of Foreign Contribution Regulation Rules 2011, even the persons prohibited u/s 3 i.e., person not permitted to accept foreign contribution, are allowed to accept foreign contribution from their relatives.
- However, in terms of Rule6 of Foreign Contribution Regulation Rules 2011 any person receiving

foreign contribution in excess of ₹ 1 lakh or equivalent thereto in financial year from any of his relatives shall inform the C.G in prescribed Form within 30 days from the date of receipt of such contribution.

Conclusion: Foreign remittance received from a relative is not treated as foreign contribution.

Question 6 ***(May 2018)***

Mr. Satish, General Secretary of a political party received an invitation from the American Labour Party. He wants to avail foreign hospitality. Define the term "foreign hospitality". In the light of the provisions of the Foreign Contribution (Regulation) Act, 2010, decide whether he can avail it. Discuss also the exception, if any, under which the provisions of the said Act may be relaxed.

Answer:

Definition of "Foreign Hospitality"

"Foreign hospitality" means any offer, not being a purely casual one, made in cash or kind by a foreign source for providing a person with the costs of travel to any foreign country or territory or with free boarding, lodging, transport or medical treatment. [Section 2(i) of the Foreign Contribution (Regulation) Act, 2010]

Whether Mr. Satish can avail foreign Hospitality?

As per Section 6 of the Act, Office bearers of political parties require prior approval from Ministry of Home Affairs before accepting Foreign Hospitality. In the instant case, Mr. Satish, General Secretary of a political party, before availing foreign hospitality shall require prior approval from Ministry of Home Affairs.

Exceptions

It shall not be necessary to obtain any such permission for an emergent medical aid needed on account of sudden illness contracted during a visit outside India. But, where such foreign hospitality has been received, the person receiving such hospitality shall give an intimation to the Central Government as to the receipt of such hospitality within one month from the date of receipt of such hospitality, and the source from which, and the manner in which, such hospitality was received.

Question 7 ***(RTP May 2019)***

X is an association having registration to transfer the Foreign Contribution received by it to another organization? Is the valid act of X? If yes, then what is the process to do so? Is there any restriction on transfer of funds to other organisations?

Answer:

Yes, X can transfer the Foreign Contribution received by it to another organization as section 7 of FCRA, 2010. According to the provision no person who –

a. is registered and granted a certificate or has obtained prior permission under this Act; and
b. receives any foreign contribution,

shall transfer such foreign contribution to any other person unless such other person is also registered and had been granted the certificate or obtained the prior permission under this Act:

Provided that such person may transfer, with the prior approval of the Central Government, a part of such foreign contribution to any other person who has not been granted a certificate or obtained permission under this Act in accordance with the rules made by the Central Government."

Restrictions on transfer: Rule 24 of FCRR, 2011, prescribes the procedure for transferring foreign

contribution to any unregistered person as under:

(1) A person who has been granted a certificate of registration or prior permission under section 11 and intends to transfer part of the foreign contribution received by him to a person who has not been granted a certificate of registration or prior permission under the Act, may transfer such foreign contribution to an extent not exceeding ten per cent of the total value thereof and for this purpose, make an application to the Central Government in the prescribed Form.

(2) Every application made under sub-rule (1) shall be accompanied by a declaration to the effect that- (a) the amount proposed to be transferred during the financial year is less than ten per cent of the total value of the foreign contribution received by him during the financial year; (b) the transferor shall not transfer any amount of foreign contribution until the Central Government approves such transfer.

(3) A person who has been granted a certificate of registration or prior permission under section 11 shall not be required to seek the prior approval of the Central Government for transferring the foreign contribution received by him to another person who has been granted a certificate of registration or prior permission under the Act provided that the recipient has not been proceeded against under any of the provisions of the Act.

(4) Both the transferor and the recipient shall be responsible for ensuring proper utilisation of the foreign contribution so transferred and such transfer of foreign contribution shall be reflected in the returns in Form to be submitted by both the transferor and the recipient.

Question 8 ***(Nov 2018)***

An Association registered under the Foreign Contribution (Regulation) Act, 2010 (the Act) received donation from a club registered in Singapore. The Association proposes:

(i) To transfer 10% of the donation to "Home for Aged Society", an unregistered person and 15% to "Welfare Club" a registered person under the Act,

(ii) To invest portion of the donation in Chits promising high returns.

In the light of provisions of the Foreign Contribution (Regulation) Act, 2010 decide whether the Association can carryout the above proposals and if so state the procedures to be followed under the said Act?

Answer:

i) According to Section 7 of the Foreign Contribution (Regulation) Act, 2010, a person who is registered and granted a certificate and receives any foreign contribution, shall not transfer such foreign contribution to any other person unless such other person is also registered and had been granted the certificate or obtained the prior permission under this Act.

However, that such person may transfer, with the prior approval of the Central Government, a part of such foreign contribution to any other person who has not been granted a certificate or obtained permission to an extent not exceeding ten per cent of the total value thereof and for this purpose, make an application to the Central Government in prescribed Form. [Read with *Rule 24 of FCRR, 2011*]

In the instant case, the association can transfer 10% of the donation to "Home for Aged Society" an unregistered person after making an application to the Central Government in prescribed form and can also transfer 15% to "Welfare Club" a registered person under the Act.

ii) According to proviso to Section 8 of the FCRA, 2010 any foreign contribution shall not be used

for speculative business.

Speculative activities have been defined in Rule 4 of FCRR, 2011 as under:-

a) any activity or investment that has an element of risk of appreciation or depreciation of the original investment, linked to market forces, including investment in mutual funds or in shares;

b) participation in any scheme that promises high returns like investment in chits or land or similar assets not directly linked to the declared aims and objectives of the organization or association.

In the instant case, the association cannot invest portion of the donation in Chits promising high returns.

Question 9 ***(May 2019)***

After giving a reasonable opportunity of being heard, Central Government cancelled the certification of registration of Toastea Ltd, a company registered under FCRA on the ground of public interest 2.5 years have passed since such cancellation. Company has submitted its written declaration not to involve in such activity again and request to restore the registration. Advise Toastea Ltd. on its eligibility for re-registration or grant of prior permission. Also state the circumstance under which Government can cancel the certificate of registration granted to a person under the Foreign Contribution (Regulation) Act, 2010.

Answer:

Restoration of Registration: As per section 14(3) of the Foreign Contribution (Regulation) Act, 2010, any person whose certificate has been cancelled under this section shall not be eligible for registration or grant of prior permission for a period of three years from the date of cancellation of such certificate.

In the instant case, Toastea Ltd. is not eligible for re-registration or grant of prior permission as only 2.5 years have passed since such cancellation. So, requirement of 3 years of cooling period from the date of cancellation of such certificate for re-registration is not complied with.

Circumstances for cancellation of certificate of registration [Section 14(1) of the Foreign Contribution (Regulation) Act, 2010]

The Central Government may, by an order, cancel the certificate if —

a) the holder of the certificate has made a statement in, or in relation to, the application for the grant of registration or renewal thereof, which is incorrect or false; or
b) the holder of the certificate has violated any of the terms and conditions of the certificate or renewal thereof; or
c) in the opinion of the Central Government, it is necessary in the public interest to cancel the certificate; or
d) the holder of certificate has violated any of the provisions of this Act or rules or order made there under; or
e) if the holder of the certificate has not been engaged in any reasonable activity in its chosen field for the benefit of the society for two consecutive years or has become defunct.

Ch. 5 – The Arbitration And Conciliation Act, 1996

Question 1 ***(RTP May 2018)***

In 2016, Company Amar, food processor manufacturing unit entered into a joint venture agreement with Company USHA, the largest manufacturer of Food processors for supply of parts of mixer & grinder for manufacturing its latest model. Both the companies are registered under the Companies Act 2013. Agreement carries the term that all disputes shall be arbitrated in Mumbai. State the type of arbitration agreement made between them.

What will happen if the agreement does not have any clause relating to arbitration? Disputes arose between them concerning quality of material supplied in 2017.

Answer:

There are two basic types of arbitration agreement are:

a) Arbitration clause - a clause contained within a principal contract. The parties undertake to submit disputes in relation to or in connection with the principal contract that may arise in future to arbitration.

b) Submission agreement - an agreement to refer disputes that already exist to arbitration. Such an agreement is entered into after the disputes have arisen.

In first case, the agreement already carries the term that all disputes shall be arbitrated in Mumbai at the time of entering into joint venture agreement. This would be an arbitration clause as it is contained in the principal contract (JVA) and no disputes have arisen till yet. It concerns future disputes that may arise.

In the second case, the Principal contract (JVA) does not have any term relating to arbitration. Disputes arose between the parties concerning quality of supplied goods in 2017. To resolve this dispute, parties later entered into an agreement "That all disputes including quality of goods supplied by Company USHA to Company Amar shall be submitted to arbitration. The parties hereby agree to abide by the decision of the arbitrator. " Such an agreement that is made after the disputes have arisen would be called a submission agreement.

Question 2

How important are the ideas of independence and impartiality in arbitration?

a) Is the arbitrator required to disclose anything to the parties?
b) Is membership of the same sports club as one of the parties problematic?

Answer:

a) The arbitrator are under a duty of disclose any relations with parties or their lawyer that might give rise to justifiable doubts as to their independence and impartiality.
b) Such an association is too remote to count as a relation that might lead to doubts of bias.

Question 3

Can an arbitrator resign on their own account? Do they have to give reasons for their resignation? Could an award be challenged on the ground that the arbitrator had resigned without giving any proper justifications?

Answer:

An arbitrator can resign when they want, without giving reasons for their resignation. This action does not affect the validity either of the arbitration proceedings or the arbitral award.

Question 4

Mr. X wants to start a bakery and so he contacts Mr. Y Confectioners & Bakers for supply of cakes and biscuits. The communication between the parties were over email. On e-mail, there was a term of service between the parties containing that "any disputes regarding quality or delivery shall be submitted to arbitration conducted under the guidance of Indian Confectionary Manufacturers Association. Please place your order if the above terms and conditions are agreeable to you." X placed an order. State the legal position as the validity of the arbitration agreement.

Answer:

As per the arbitration and Conciliation Act, an agreement must be in writing There is however no requirement for the same to be in writing in one document. There is also no particular form or template for an arbitration agreement. The communication over email of the term of services is a proper valid agreement and the same have been stood affirmed by reason of their conduct. This would be an arbitration agreement in writing contained in correspondence between the parties.

Question 5 ***(May 2018)***

Smart Automobiles Limited and Apex Four wheelers Limited entered into an agreement regarding annual maintenance services to be provided by Smart Automobiles for all vehicles within the state of Uttar Pradesh for five years. The agreement was containing a clause that in the event of a dispute between the parties the matter would be submitted to arbitration. At the end of the fifth year, the service agreement was not renewed.

Decide whether the arbitration. agreement should not be treated as terminated. Also describe the other grounds of termination of an arbitration agreement.

Answer:

Termination of an arbitration agreement

Just the way parties can enter into an arbitration agreement, they can also terminate an arbitration agreement. Thus, an arbitration agreement could be put to an end by:

1. Mutual consent: like any contract, the parties involved can jointly agree to put an end to a particular arbitration agreement.
2. Termination of principal contract: an arbitration agreement always operates in relation to a principal contract. If the principal contract is terminated through discharge or novation, the arbitration agreement terminates with the contract. However, if the principal contract is breached, then the arbitration agreement survives because of the operation of the doctrine of separability.

In the given instance, at the end of the fifth year, the Service Agreement was not renewed. Hence, the contract terminates, and along with it the arbitration agreement.

Question 6 ***(Nov 2018)***

Examine the validity of the following statements with reference to The Arbitration and Conciliation Act, 1996:

i) Every Court would be a Judicial Authority but every Judicial Authority would not be a Court.

ii) The disputes submitted to arbitration must be arbitrable.

Answer:

i) **Judicial authority** - The term judicial authority is not defined in Act. The Supreme Court in SBP v. Patel Engineering observed "A judicial authority as such is not defined in the Act. It would certainly

include the court as defined in Section 2(e) of the Act and would also, include other courts and may even include a special tribunal like the Consumer Forum." Therefore, it is a concept wider than courts as ordinarily understood and would include special tribunals and quasi-judicial authorities. The functions performed would include reference to arbitration. Every court would be a judicial authority, but every judicial authority would not be a court.

ii) **Arbitrability:** The disputes submitted/ proposed to be submitted to arbitration must be arbitrable. In other words the law must permit arbitration in that matter. There are certain disputes that the law retains exclusively for the court, and the same cannot be submitted for arbitration. The rationale is that given the nature of disputes, the courts are the only appropriate forum for adjudicating the matter.

For example, criminal offences, matrimonial disputes, guardianship matters, testamentary matters, mortgage suit for sale of a mortgaged property, etc. cannot be arbitrated.

Ch. 6 – Overview of Insolvency And Bankruptcy Code, 2016

Question 1

When will the provisions of insolvency and liquidation of corporate persons be applicable on a corporate person?

Answer:

The provisions relating to the insolvency and liquidation of corporate debtors shall be applicable only when the amount of the default is **one lakh rupees or more**. However, the Central Government may, by notification, **specify the minimum amount of default of higher value which shall not be more than one crore rupees**.

Question 2

Who may initiate corporate insolvency process against a corporate person?

Answer:

The corporate insolvency process may be initiated against any defaulting corporate debtor by -

a) Financial creditor,
b) Operational creditor
c) Corporate debtor

Question 3

What is the procedure of Insolvency Resolution Process for a Corporate Applicant?

Answer:

Where a corporate debtor has committed a default, a **corporate applicant thereof may file an application for initiating corporate insolvency resolution process with the Adjudicating Authority.**

The corporate applicant shall furnish the information relating to books of account and other documents and a resolution professional shall be appointed as interim resolution professional.

The Adjudicating Authority may either accept or reject the application **within fourteen days of receipt of application.** However, applicant should be allowed to rectify the defect within seven days of receipt of notice of such rejection.

Question 4

Is there any time limit for completion of the Insolvency Resolution Process?

Answer:

Section 12 of the Code states that any Insolvency Resolution Process shall be completed **within a period of one hundred and eighty days from the date of admission of the application to initiate the process.**

However the National Company Law Tribunal (NCLT) may on an application made by the resolution professional, under a resolution passed by the Committee of Creditors, by a vote of 75% of voting shares, **after consideration provide one extension which shall not extend more than 90 days.**

Provided further that the corporate insolvency resolution process shall mandatorily be completed within a period of three hundred and thirty days from the insolvency commencement date, including any extension of the period of corporate insolvency resolution process granted under this section

and the time taken in legal proceedings in relation to such resolution process of the corporate debtor:

Provided also that where the insolvency resolution process of a corporate debtor is pending and has not been completed within the period referred to in the second proviso, such resolution process shall be completed within a period of ninety days from the date of commencement of the Insolvency and Bankruptcy Code (Amendment) Act, 2019".

Question 5 ***(RTP May 2018)***

Wisdom Ltd. commits a default against the debts taken from the financial creditors. Mr. F, a financial creditor initiated the corporate insolvency resolution process against the Wisdom Ltd. Mr. X, another financial creditor, thereof files an application for initiating corporate insolvency resolution process with an Adjudicating Authority. State the validity as to the filing of an application by Mr. X for initiation of corporate insolvency resolution process?

Answer:

In the given problem, on commission of default by the Wisdom Ltd., Mr. F filed an application for initiating corporate insolvency resolution process before adjudicating authority. Further, Mr. X another financial creditor moved an application for initiation of insolvency resolution process against the Wisdom Ltd.

According to the section 6 of the Code, where any corporate debtor commits a default, a financial creditor, Operational creditor or the Corporate debtor itself may initiate insolvency resolution process against such corporate debtor.

But as per Section 13 of the Code, once an application is admitted by the Adjudicating authority, it shall by an order declare a moratorium for the purposes referred to in section 14. Then causes a public announcement of the initiation of CIRP by IRP and call for the submission of claims under section 15 and appoint an IRP in the manner as laid down in section 16 of the Code. Public announcement lays down all the relevant information related to the CIRP. So that the all creditors entitled under the law can raise their claim in this case.

So, no further application for initiation of CIRP against the same debtor (i.e, Wisdom Ltd.) can be initiated. So, Mr. X, cannot file an application on initiation of CIRP, however, is entitled under the law to raise his claim in this case against the Wisdom Ltd.

Question 6

What is the effect of order of moratorium?

Answer:

Moratorium has been explained in Section 14 of the Code, during the moratorium period the following acts shall be prohibited:

a) The **institution of suits or continuation of any pending suits or proceedings against the corporate debtor** including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;
b) **Transferring, encumbering, alienating or disposing of by the corporate debtor** any of its assets or any legal right or beneficial interest therein;
c) Any action to foreclose, **recover or enforce any security interest created by the corporate debtor** in respect of its property including any action under the SARFAESI Act, 2002

The recovery of any property by an owner or lessor where such property is occupied by or in the possession of the corporate debtor.

Question 7 ***(Nov 2017)***

Nature India Limited filed a petition under the Insolvency and Bankruptcy Code, 2016 with National Company Law Tribunal (NCLT) against Tulip Limited and the petition was admitted. After that, Nature India Limited wanted to withdraw the petition based on a settlement arrived between the parties. Whether it is permissible to withdraw the petition after it has been admitted? Decide.

Also explain the rules relating to the admission and rejection of application by an adjudicating authority under the Insolvency and Bankruptcy Code, 2016.

Answer:

withdrawal of Application/Petition:

As per Sec. 12A of IBC, 2016, the Adjudicating Authority may allow the withdrawal of Application admitted under section or section 9 or section 10, or an application in de by the applicant with the approval of 70% voting share of the committee of creditors, in such manner as may be specified.

In the given instance, Nature India Limited wanted to withdraw the petition after it was admitted by the adjudication authority.

Conclusion: Petition may be withdrawn subject to compliance of conditions as stated in Sec 12A

Rules relating to admission and rejection of application:

As per Sec: 9 of the IBC, 2016, the Adjudicating Authority shall, within 14 days of the receipt of the application, by an order:

a) admit the application and communicate such decision to the operational creditor and the corporate debtor if:

i) the application made is complete;

ii) there is no payment of the unpaid operational debt;

iii) the invoice or notice for payment to the corporate debtor has been delivered by the operational creditor

iv) no notice of dispute has been received by the operational creditor or there is no record of dispute in the information utility, and

v) there is no disciplinary proceeding pending against any Resolution Professional (RP) proposed, if any.

b) reject the application and communicate such decision to the operational creditor and the corporate debtor if-

i) the application made is incomplete;

ii) there has been payment of the unpaid operational debt;

iii) the creditor has not delivered the invoice or notice for payment to the corporate debtor:

iv) notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility; or

v) any disciplinary proceeding is pending against any proposed RP

Question 8 ***(Nov 2017 & RTP May 2018)***

Standard International Ltd. who is a foreign trade creditor having its office in Hong Kong wanted to file a petition under the Insolvency and Bankruptcy Code, 2016 on default of the debtor in India. It moved a petition u/s 9 of the Code seeking commencement of insolvency process. The foreign company was not having any office or bank account in India. Because of this, it could not submit a "Certificate from a financial institution" as required under the Code. Whether the petition is

permissible under the Insolvency and Bankruptcy Code, 2016? Decide.

Answer:

As per the definition of the Creditor given in Section 3(10) of the Insolvency and Bankruptcy Code, 2016, it means any person to whom a debt is owed and includes a financial creditor, an operational creditor, a secured creditor, an unsecured creditor, and a decree holder. So, Standard International Ltd. is a creditor under the purview of the Code.

As per the facts given in question, Standard International Ltd., is a foreign trade creditor. He wanted to file a petition under the under Section 9 of the Insolvency and Bankruptcy Code, 2016 for commencement of Insolvency process against the defaulter in India. Standard International Ltd. was not having any office or bank account in India.

As per the requirement of section 9 of the Code, along with application certain documents were needed to be furnished by the creditor to the Adjudicating authority. Being a foreign trade creditor, Standard International Ltd was also required to provide a copy of certificate from the financial institutions maintaining accounts of the creditor confirming that there is no payment of an unpaid operational debt by the corporate debtor. Since, Standard International Ltd. was not having any office or bank account in India, it cannot furnish certificate from financial institution. So, Petition under Section 9 of the Code is not permissible.

Question 9 ***(May 2018)***

M/s TAS Constructions Private Limited, an operational creditor on 2nd April, 2018 being the default date issued a demand notice through speed post to M/s Dheeraj Constructions Private Limited, an unpaid operational/corporate debtor demanding payment of its invoice dated 19th March, 2018 for ₹ 5,60,000 (15 days payment terms) towards supply of certain works contract services as per the provisions of section 8(1) of the Insolvency and Bankruptcy Code, 2016 and rules framed there under/s.

Dheeraj Constructions Private Limited on receipt of the demand notice informed the operational creditor, that vide their e-mail dated 30th March, 2018, addressed to the company and all its directors, they have disputed the invoice on the quality of the services rendered and were withholding payment till the dispute is settled but without initiating any legal proceedings under any law for the time being in force. The operational creditor on expiry of the period of 10 days from the date of delivery of the demand notice and non-payment of its dues approached the Adjudicating Authority for the initiation of the corporate insolvency resolution process under section 9(1) of the Insolvency and Bankruptcy Code, 2016. Will the application of the operational creditor filed under section 9(1) read with section 8(2) (a) of the Insolvency and Bankruptcy Code, 2016 be permitted?

Answer:

The given problem is based on Section 9(1) of the Insolvency and Bankruptcy Code, 2016. According to the provision, after the expiry of the period of ten days from the date of delivery of the notice or invoice demanding payment, if the operational creditor does not receive payment from the corporate debtor or notice of the dispute, the operational creditor may file an application before the Adjudicating Authority for initiating corporate insolvency resolution process.

However, as per Section 8(2)(a) of the Code, the corporate debtor shall, within a period of ten days of the receipt of the demand notice or copy of the invoice bring to the notice of the operational creditor about existence of dispute, if any, and record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute.

Facts given states that the Dheeraj Constructions Private Limited on receipt of the demand notice, informed M/s TAS Constructions Private Limited (Operational Creditor) that through email dated 30th March, 2018, addressed the company and all its directors, of the dispute on the invoice and withholding of the payment till the settlement of the dispute.

The provision of Section 8(2)(a) envisages existence of dispute, if any and record of the pendency of the suit or arbitration proceedings filed by the Corporate Debtor before receipt of such notice or invoice in relation to such disputes: thus existence of disputes and record of pendency of the suit or arbitration proceedings both are to be filed. Whereas, Section 5 (6) defines 'disputes" as disputes includes a suit or an arbitration proceedings relating to:

a) The existence of the amount of the debt
b) The quality of goods or service or
c) The breach of the representation or the warranties.

The Supreme Court has settled the position in the case of Mobilox Innovations Private Limited Vs. Kirusa Soft Ware Private Limited and Innoventive Industries Vs ICICI Bank by deciding that "and" used in Section 8(2)(a) has to be read as disjunctively and "and" to be read as "or" else, the purpose of the IBC will be defeated.

Hence, the requirement of Section 8, to bring to the notice of the operational creditor about an existence of dispute only and not along with the record of the pendency of the suit or arbitration proceedings as settled by the Supreme Court in the cases referred above filed before the receipt of such notice or invoice in relation to such dispute have been complied with and record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute, have been complied with.

So, the application of M/s TAS Constructions Private Limited (Operational Creditor) shall not be permitted under Section 9 of the Insolvency and Bankruptcy Code, 2016 as Dheeraj Construction Private Limited has complied the provisions of Section 8(2)(a) of the IBC, 2016.

Question 10 ***(May 2018)***

Rose Garden Ltd. was incurring continuous losses and its financial position went bad to worse. Black Stone (Private) Ltd., a trade creditor, issued notice under Section 271 of the Companies Act, 2013 for winding up of Rose Garden Ltd. on the ground that Rose Garden Ltd. was unable to pay its debts. After some time, Black Stone (Private) Ltd. being an operational creditor filed a petition before the Adjudicating Authority to initiate insolvency process under the Insolvency and Bankruptcy Code, 2016. Demand Notice and copy of invoice were not served to Rose Garden. Ltd. since a notice was earlier issued for winding up. All other formalities were complied with. The Adjudicating Authority initiated Insolvency Resolution Process by admitting the application and appointed Resolution Professional. After complying required formalities, the Adjudicating Authority issued orders for moratorium and other relief within the stipulated time. Being aggrieved by the order of Adjudicating Authority, Rose Garden Ltd. (Corporate debtor) filed an appeal before NCLAT under the Insolvency and Bankruptcy Code, 2016. Determine will the Company succeed in its appeal?

Answer:

As per Section 8 of the Insolvency and Bankruptcy Code, 2016, once a default has occurred, the operational creditor has to deliver a demand notice or a copy of invoice demanding payment of debt in default to the corporate debtor.

Since in the given case, demand notice and copy of invoice was not served to the Rose Garden Ltd., so the requirement for the initiation of the corporate insolvency resolution process by operational creditor under section 9 of the Code, was not in compliance. So, the admission of application in line

with the compliance of other required formality as to issue of order of moratorium and other relief, given by the NCLT was against the law.

As Rose Garden Ltd. (Corporate debtor) was aggrieved by the Order of the Adjudicating Authority on the non-compliance of requirement of Section 8, Rose Garden Ltd. will succeed in its appeal filed before the National Company Law Appellate Tribunal.

Question 11 ***(May 2018)***

M/s Systemtek India Private Limited (Appellant-Corporate Debtor) has challenged the order dated 3rd July, 2017 passed by the Adjudicating Authority (National Company Law Tribunal) Mumbai Bench, Mumbai, in the National Company Law Appellate Tribunal (NCLAT).

NCLT had admitted the application preferred by appellant under Section 10 of the Insolvency and Bankruptcy Code, 2016 and an order of Moratorium was passed and Insolvency Resolution Professional was ordered to be appointed by the Ld. Adjudicating Authority (NCLT).

The only grievance of the appellant in its challenge is that the movable and immovable property of Guarantor (promoter) has been attached pursuant to a Corporate Insolvency Resolution Process initiated under section 10 against the Appellant by the Ltd. Adjudicating Authority (NCLT) which is violative of section 14(1)(c) of the Insolvency and Bankruptcy Code, 2016 though the Code prescribes a Moratorium for certain types of transactions. Decide.

Answer:

As per the given facts in the question, Appellant, M/S Systemtek India Private Limited, challenged the order passed by the NCLT on the ground stating that the movable and immovable property of guarantor (Promoter) has been attached pursuant to a Corporate Insolvency Resolution Process initiated under Section 10 of the Code against the Appellant.

As per Section 14(1) of the Insolvency and Bankruptcy Code, 2016, on the Insolvency commencement date, the NCLT shall by order declare moratorium prohibiting certain acts by /against the Corporate Debtor. According to clause (c) of the said provision, the order prohibits any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect of its property including any action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

The order of moratorium shall have effect from the date of such order till the completion of the corporate insolvency resolution process.

The word 'its' used in clause (c) of sub-Section (1) of Section 14 of IBC, 2016, refers to corporate debtor and not the guarantors.

In view of this, the Order of NCLT under Section 14(1)(c) of IBC 2016 is not violative. However M/s Systemtek India Private Limited can challenge the Order of the NCLT on the ground that until the liability of the Company is decisively crystallize, the guarantor cannot be held liable.

Question 12 ***(May 2018)***

You are appointed as Interim Resolution Professional in XYZ Company Ltd. under the Insolvency and Bankruptcy Code, 2016. State the time limit to make Public Announcement? Also state the protocol for issuance of public notice. Who shall bear the expenses of public announcement?

Answer:

1) **Time Limit for making Public Announcement**
   Interim Resolution Professional shall make the Public Announcement immediately after his appointment. "Immediately" here means not more than three days from the date of appointment

of the Interim Resolution Professional. Hence, the time limit to make Public Announcement is within 3 days from the date of appointment of the Interim Resolution Professional.

2) Protocol for issuance of Public Notice

As per Section 15 of the Insolvency and Bankruptcy Code, 2016, public announcement shall include the following:-

a) Name & Address of Corporate Debtor under the Corporate Insolvency Resolution Process.
b) Name of the authority with which the corporate debtor is incorporated or registered.
c) Details of interim resolution Professional who shall be vested with the management of the Corporate Debtor and be responsible for receiving claims.
d) Penalties for false or misleading Claims.
e) The last date for the submission of the claims.
f) The date on which the Corporate Insolvency Resolution Process ends.

3) Expenses of Public Announcement

The expenses of public announcement shall be borne by the applicant which may be reimbursed by the Committee of Creditors, to the extent it ratifies them.

Question 13 ***(May 2018)***

BDLK Limited decided to go for voluntary winding up and accordingly the Board of Directors at a meeting of the Board are about to take the necessary steps to initiate the winding up proceedings. The Board of Directors of the company approached you for guidance in this regard. Please list out the steps required under the Insolvency & Bankruptcy Code 2016 before approval of such liquidation proposal with specific reference to meetings and actions of relevant stakeholders.

Answer:

Voluntary Winding Up: As per Section 59 of the Insolvency and Bankruptcy Code, 2016, the voluntary liquidation of a corporate person shall meet such conditions and procedural requirements as may be specified by the Board (IBBI).

Conditions of initiation of voluntary liquidation proceedings: Voluntary liquidation proceedings of a corporate person registered as a company shall meet the following conditions, namely:—

a) a declaration from majority of the directors of the company verified by an affidavit stating that -
   i) they have made a full inquiry into the affairs of the company and they have formed an opinion that 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;
b) the declaration given above shall be accompanied with the following documents namely:
   i) audited financial statements and record of business operations of the company for the previous two years or for the period since its incorporation, whichever is later;
   ii) a report of the valuation of the assets of the company, if any prepared by a registered valuer;
c) within four weeks of a declaration under sub-clause (a) above, there shall be—
   i) a **special resolution of the members of the company in a general meeting** requiring the company to be liquidated voluntarily and appointing an insolvency professional to act as the liquidator; or
   ii) a **resolution of the members of the company in a general meeting** requiring the company to be liquidated voluntarily **as a result of expiry of the period of its duration,** if any, fixed by its articles, or on the occurrence of any event in respect of which the articles provide that the

company shall be dissolved, as the case may be and appointing an insolvency professional to act as the liquidator:

Provided that the company owes any debt to any person, **creditors representing two thirds in value of the debt of the company shall approve the resolution passed** under sub-clause (c) within seven days of such resolution.

Notification to Registrar of company and the Board: The Company shall notify the Registrar of Companies and the Board about the resolution to liquidate the company within seven days of such resolution or the subsequent approval by the creditors, as the case may be.

Question 14

What are the eligibility criteria for appointment of an Insolvency Professional as a Resolution Professional for a corporate insolvency resolution process?

Answer:

As per Regulation 3 of Insolvency and Bankruptcy (Insolvency Resolution) Regulation, 2016, an insolvency professional shall be eligible for appointment as a resolution professional for a CIRP if he & all partners & directors of the insolvency professional entity of which he is partner or director are independent of the corporate debtor i.e.,

a) He is eligible to be appointed as an independent director on the board of the corporate debtor **u/s 149 of the Companies Act, 2013**, where the corporate debtor is a company.

b) He is **not a related party of the corporate debtor.**

c) He is **not an employee or proprietor or a partner of a firm of auditors or company secretaries in practice or cost auditors of the corporate debtor in the last three financial years**.

d) He is not an employee or proprietor or a partner of a legal or consulting firm that has or had **any transaction with the corporate debtor amounting to ten per cent or more of the gross turnover of such firm in the last three financial years.**

Question 15

When can a corporate person initiate voluntary liquidation process?

Answer:

Section 59 of the Code empowers a corporate person intending to liquidate itself voluntarily if it has not committed any default to initiate voluntary liquidation proceedings under the provisions of this Code.

Any corporate person registered as a company shall meet the following conditions to initiate a voluntary liquidation process:-

a) A declaration from majority of the directors of the company verified by an affidavit stating

i) That they have made a full inquiry into the affairs of the company and have formed an opinion that either the company has no debts 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) That the company is not being liquidated to defraud any person.

b) The declaration shall be accompanied with the following documents, namely:

i) Audited financial statements and a record of business operations of the company for the previous two years or for the period since its incorporation, whichever is later;

ii) A report of the valuation of the assets of the company, if any, prepared by a registered valuer.

c) After making the declaration the corporate debtor shall within four weeks -

i) Pass a special resolution at a general meeting stating that the company should be liquidated voluntarily and insolvency professional to act as the liquidator may be appointed.

ii) Pass a resolution at a general meeting stating that the company be liquidated voluntarily as a result of expiry of the period of its duration (fixed by its articles or on the occurrence of any event in respect of which the articles provide that the company shall be dissolved, if any) and appointing an insolvency professional to act as the liquidator.

Question 16

What is the Insolvency Resolution Process for financial creditors?

Answer:

A financial creditor either itself or along with other financial creditors may **lodge an application before the Adjudicating Authority** (National Company Law Tribunal) for initiating corporate insolvency resolution process against a corporate debtor who commits a default in payment of its dues.

The financial creditor shall along with the application give evidence in support of the default committed by the corporate debtor. **He shall also give the name of the interim resolution professional.**

Where the Adjudicating Authority is satisfied that a default has occurred and the application by the financial creditor is complete and there is no disciplinary proceedings pending against the proposed resolution professional, it may **admit such application made by the financial creditor**. Otherwise, the application may be rejected. However, the **applicant may rectify the defect within seven days of receipt of notice of rejection from the Adjudicating Authority**.

Question 17

What is the Insolvency Resolution Process for financial creditors?

Answer:

A financial creditor either itself or along with other financial creditors may **lodge an application before the Adjudicating Authority** (National Company Law Tribunal) for initiating corporate insolvency resolution process against a corporate debtor who commits a default in payment of its dues.

The financial creditor shall along with the application give evidence in support of the default committed by the corporate debtor. **He shall also give the name of the interim resolution professional.**

Where the Adjudicating Authority is satisfied that a default has occurred and the application by the financial creditor is complete and there is no disciplinary proceedings pending against the proposed resolution professional, it may **admit such application made by the financial creditor**. Otherwise, the application may be rejected. However, the **applicant may rectify the defect within seven days of receipt of notice of rejection from the Adjudicating Authority**.

Question 18 ***(RTP May 19)***

The financial creditor, Mr. Raman, was an investor and a debenture holder of 'Optionally Convertible Debenture Bond (OPDB)' payable on maturity, was issued by the M/s Asset Ltd. (corporate debtor). The zero interest OCD bonds amounted to 2 crore matured in 2016 . The liability to redeem the

debentures on maturity along with a redemption premium lay on the debtor, which was not made. Mr. Raman filed the Corporate Insolvency resolution process before the NCLT. Advise in the light of the given facts, the following situations:

(i) State whether Mr. Raman is eligible for filing of application for initiation of CIRP?

(ii) Do the redemption of debenture payable on the maturity date amounts to debt?

Answer:

As per Section 5(7) of the Insolvency and Bankruptcy Code, 2016, financial creditor means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to.

Whereas the term Financial debt defined under Section 5(8) means a debt along with interest, if any, which is disbursed against the consideration for the time value of money and includes any amount raised pursuant to the issue of bonds, notes, debentures, loan stock or any similar instrument.

As per the facts, Mr. Raman, was an investor and a debenture holder of 'Optionally Convertible Debenture Bond (OPDB)' issued by the Asset Ltd. With the debenture payable, as on the maturity date with interest, it was disbursed against consideration for the time value of the money. Thus, it can be said that debentures on maturity will come under that purview of Section 5(8)(c). Since Mr. Raman is a person to whom a financial debt is owed, he will come within the definition of Financial creditor. Being a debenture-holder and shareholder of the company he, being a creditor is entitled to claim debt amount. Therefore, as per section 7, Mr. Raman is entitled to file an application to initiate CIRP against the M/s Asset Ltd.

Question 19 ***(May 19)***

MF Capital Private Limited accepted inter-corporate deposits from JS financial Services Private Limited. MF Capital Private Limited is a Non-banking financial company which obtained a certificate from the Reserve Bank of India for carrying on the business of providing financial services. As there was a default in repayment of deposits, JS Financial Services Private Limited filed' an application with the NCLT under Section 7 of the Insolvency and Bankruptcy Code, 2016. Examine the validity of the Application.

Answer:

As per Section 2 of the Insolvency and Bankruptcy Code, 2016, the provisions of the Code shall apply for insolvency, liquidation, voluntary liquidation or bankruptcy of the following entities:-

a) Any Company incorporated under the Companies Act, 2013 or under any previous law.

b) Any other Company governed by any Special Act for the time being in force, except in so far as the said provision is inconsistent with the provisions of such Special Act.

c) Any Limited Liability Partnership under the LLP Act, 2008.

d) Any other body incorporated under any law for the time being in force, as the Central Government may by notification specify in this behalf.

e) personal guarantors to corporate debtors;

f) partnership firms and proprietorship firms; and

g) individuals, other than persons referred to in clause (e)

Further, Preamble to the Insolvency & Bankruptcy Code, implicit that the purpose of this Act is to consolidate and amend the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals.

Section 3(7) of Insolvency & Bankruptcy Code, 2016 states that "Corporate Person" shall not include any financial service provider such as Banks, Financial Institutions, Insurance Company, Asset Reconstruction Company, Mutual Funds, Collective Investment Schemes or Pension Funds.

As per decision in the case of Jindal Saxena Financial Services Vs Mayfair Capital (2018), NBFC which has obtained a certificate from the Reserve Bank of India will be considered as a financial service provider.

In view of above, filing of an application with NCLT under Section 7 of the IBC, 2016 by JS Financial Services Private Limited against MF Capital Private Limited is invalid.

Question 20 ***(Nov 18)***

Best Bank, a financial creditor sent a demand notice for a claim of ₹ 10.2 crores on XYZ Limited, a corporate debtor on 6th February, 2018. When the petition was filed before NCLT under Insolvency and Bankruptcy Code, 2016, Best Bank claimed that the XYZ Limited has defaulted ₹ 29.8 crores instead of original amount of ₹ 10.2 crores. NCLT appointed an interim insolvency resolution professional. XYZ Limited made an appeal with NCLAT demanding that the Best Bank's claim is not maintainable as there is a difference in the amount mentioned in the demand notice and the application filed under the Code. Decide whether the contention of XYZ Limited is correct. Also, state who can file Corporate Insolvency Resolution process under the Code.

Answer:

As per section 7 of the Insolvency and Bankruptcy Code, 2016, a financial creditor either by itself or jointly with other financial creditors, may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred. 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.

The Adjudicating Authority shall, within fourteen days of the receipt of the application, ascertain the existence of a default from the records of an information utility or on the basis of other evidence furnished by the financial creditor.

Here, in the given instance, Best Bank (Financial creditor) filed a petition against the XYZ Ltd. (Corporate debtor) for the default of ₹ 29.8 crore instead the earlier demanded amount of ₹ 10.2 Crore. As per the above provision, NCLT (Adjudicating Authority) shall, ascertain the existence of a default from the records of an information utility or on the basis of other evidence furnished by the financial creditor. When NCLT is satisfied, it admits the submitted application for initiation of corporate insolvency process. Therefore, contention of XYZ Ltd. as to filing of appeal before NCLAT demanding that the best
bank's claim is not maintainable due to difference in the claim amount, is incorrect.

Who can file insolvency resolution process: As per section 6 of the Code, where any corporate debtor commits a default, a financial creditor, an operational creditor or the corporate debtor itself may initiate corporate insolvency resolution process in respect of such corporate debtor.

Question 21 ***(Nov 18)***

Mr. SP booked office space with Elegant Construction Limited. At the time of booking ₹ 36 lakhs was paid. Remaining amount of ₹ 10 lakhs was paid at the time of taking delivery. He entered into

a Memorandum of Understanding (MOU) with the company having various terms and conditions of the sale/allotment. According to the MOU, Elegant Construction Limited was required to build and deliver the possession of the unit within 2 years from the date of execution of the MOU. It also stipulated payment of an assured return of ₹ 82,000 per month (subject to TDS u/s 194A of IT Act, 1961) till possession of the unit was delivered to Mr. SP. Elegant Construction Limited failed to pay the assured return. Thereafter, Mr. SP filed an application for initiating insolvency resolution process. Decide about the validity of the said application in view of the provisions of Insolvency and Bankruptcy Code, 2016 as regards the definition of a "Financial Creditor" under Section 5 (7) read with Section 5 (8) of the Code.

Answer:

Financial creditor means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred to [Section 5(7) of the IBC]

Financial Debt means a debt along with interest, if any, which is disbursed against the consideration for the time value of money. The financial debt besides with other debts, includes any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing [Section 5(8) of the IBC]

As per the given facts, Mr. SP booked office space with Elegant Construction Limited. He entered into MOU with the condition stating to build and deliver the possession of the unit within 2 years from the date of execution of MOU. MOU also stipulated payment of an assured return of ₹ 82,000 per month till possession of the unit was delivered. Elegant Construction Limited failed to pay the assured sum. Mr. SP filed an application for initiating insolvency resolution process against the Elegant Construction Limited.

In the light of the stated provisions in the given circumstances, assured returns are regular payment and qualify as financial debt. As to the promise to pay the assured return of ₹ 19,68,000 (i.e. 82,000 x 24 months) by Elegant Construction Limited to Mr. SP makes the Mr. SP (applicant) as Financial creditor.

Initiation of corporate insolvency resolution process by financial creditor

As per section 7 of the Code, a financial creditor by itself, may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred. A default includes a default in respect of a financial debt owed to the applicant financial creditor of the corporate debtor.

Hence, an application for initiating corporate insolvency resolution process against Elegant Construction Limited is valid.

Question 22 ***(Nov 18)***

XY Ltd. filed a petition under Insolvency and Bankruptcy Code, 2016 with NCLT against DF Ltd. (Corporate Debtor) and the petition was admitted. There were only three financial creditors including XY Ltd. During the Corporate Insolvency Resolution process, the Corporate Debtor settled the claims of all the 3 financial creditors. Whether such settlement agreement could be termed as a valid resolution plan? Also discuss whether a financial creditor in respect of whom there is no default can file an application before Adjudicating Authority (NCLT) for initiating corporate insolvency resolution process. Discuss.

Answer:

As per section 7 of the Insolvency and Bankruptcy Code, 2016, a financial creditor either by itself or jointly with other financial creditors, may file an application for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred.

As per the facts given, the Adjudicating Authority admitted the petition. During the Corporate Insolvency Resolution Process (CIRP), the DF (Corporate debtor) settled the claims of all the 3 financial creditors.

However, as per the Code, during the insolvency resolution process, the IRP/RP was appointed to collate the claims in a collective mechanism to propose a time bound solution to resolve the situation of insolvency and prepare the resolution plan as agreed to by the debtors and creditors and submit the same to Committee of Creditors for its approval.

Since in the give case, debtor itself settled the claims without following the said procedure. Therefore, such a settlement agreement cannot be termed as valid resolution plan.

As per requirement of the Code, the process of insolvency is triggered by occurrence of default. Default means non-payment of debt when whole or any part or installment of the amount of debt has become due and payable and is not repaid by the debtor or the corporate debtor, as the case may be. [Section 3(12)].So a financial creditor in respect of whom there is no default, cannot file an application for initiating insolvency resolution process.

Question 23 ***(May 19)***

Mr. Atul was appointed as the Insolvency Resolution Professional for XYZ Ltd. An application to replace the Insolvency resolution professional was filed before the Adjudicating Authority by some Financial Creditors. The financial Creditors propose to appoint Mr. K as the insolvency professional instead of Mr. Atul. Referring to the relevant provisions of the Insolvency and Bankruptcy Code 2016, decide whether Mr. Atul can be replaced and if so, state the procedure to be followed to appoint another IRP in place of existing one.

Answer:

Replacement of Resolution Professional (Section 27 of the Insolvency and Bankruptcy Code, 2016)

(1) Where, at any time during the corporate insolvency resolution process, the committee of creditors (comprising all financial creditors of the corporate debtor) is of the opinion that a resolution professional appointed under Section 22 is required to be replaced, it may replace him with another resolution professional.

(2) The committee of creditors [COC] may, at a meeting, by a vote of sixty-six per cent of voting shares, resolve to replace the resolution professional appointed under Section 22 with another resolution professional, subject to a written consent from the proposed resolution professional in the specified form.

(3) The committee of creditors shall forward the name of the insolvency professional proposed by them to the Adjudicating Authority.

(4) The Adjudicating Authority shall forward the name of the proposed resolution professional to the Board for its confirmation and a resolution professional shall be appointed in the same manner as laid down in section 16.

(5) Where any disciplinary proceedings are pending against the proposed resolution professional, the resolution professional appointed under Section 22 shall continue till the appointment of another resolution professional under this Section.

Hence, in the instant case, Mr. Atul can be replaced by the COC comprising of financial creditors of corporate debtors, by following the above procedure.

Question 24 ***(May 19)***

Continental Rubber Limited is a supplier of raw materials to Smooth Latex Limited. It filed a petition

before the NCLT for the recovery of ₹ 10,00,000 from Smooth Latex Limited. Smooth Latex Limited, the Corporate Debtor, has other financial creditors to the extent of ₹ 1,50,00,000 and they also joined together and filed petitions to NCLT. The Corporate Debtor has a total of 40 financial creditors and 2 operational creditors. Further, all the financial creditors are having equal voting rights/shares.

Notice was issued on 1st August, 2018 for the conduct of the first meeting to be held on 5th August, 2018 at a common venue. The meeting was attended by all 40 financial creditors and 2 operational creditors. A resolution was passed to appoint Mr. TK as a Resolution Professional. 25 of the financial creditors voted in favour of the resolution and 10 voted against the resolution and 5 financial creditors and 2 operational creditors abstained from voting. Decide whether the resolution passed is valid? In the light of the provisions of Insolvency and Bankruptcy Code, 2016 read with rules framed thereunder, explain the requirements of issue of notice and quorum for the conduct of the meeting.

Answer:

According to section 22 of the Insolvency and Bankruptcy Code, 2016,

First Meeting of Creditors

- The first meeting of the committee of creditors shall be held within seven days of the constitution of the committee of creditors.
- The committee of creditors in the first meeting may by a majority vote of not less than sixty-six per cent. of the voting share of the financial creditors, either resolve to appoint the interim resolution professional as a resolution professional or to replace the interim resolution professional by another resolution professional.

Notice of the Meeting

The resolution professional shall give notice of each meeting of the committee of creditors to:-

(a) Members of Committee of creditors, including the authorised representatives referred to in sub-sections (6) and (6A) of section 21 and sub-section (5);

(b) Members of the suspended Board of Directors or the partners of the corporate persons, as the case may be;

(c) Operational creditors or their representatives if the amount of their aggregate dues is not less than ten per cent. of the debt.

Quorum for the Meeting

A meeting of committee of creditors shall quorate if members of the committee of creditors representing at least thirty three percent of the voting rights are present either in person or by video/audio means.

- If the requisite quorum for committee of creditors is not fulfilled the meeting cannot be held and the meeting shall automatically stand adjourned at the same time and place on the next day.
- The adjourned meeting shall quorate with the members of the committee attending the meeting.

As per the facts of the question and the provisions of law:

(1) The first meeting of committee of creditors was validly held within three days of the constitution of the committee of creditors.

(2) The requisite quorum was present in the meeting as all 40 financial creditors attended the meeting.

The Act requires that not less 66% of the financial creditors shall resolve to appoint resolution professional. However, in the given case 71.4% [(25/35)* 100] voted in favour of Mr. TK. Hence, the

said appointment is valid.

Question 25 ***(May 19)***

The following particulars relate to M/s. Star House (P) Limited which has gone into Corporate Insolvency Resolution Process (CIRP):

Sr. No.	Particulars	Amount in ₹
1.	Amount realized from the sale of liquidation of Assets	7,00,000
2.	Secured Creditors who has relinquished the security	2,50,000
3.	Unsecured Financial Creditors.	2,00,000
4.	Income Tax Payable within a period of two years preceding the liquidation commencement date.	25,000
5.	Cess Payable to State Government within a period of one year preceding the liquidation commencement date.	10,000
6.	Fees payable to resolution professional.	37,500
7.	Expenses incurred by the resolution professional in running the business of M/s. Star House (P) Limited on going concern.	17,500
8.	Workmen salary payable for a period of thirty months preceding the liquidation commencement date. The workmen salary is equal per month.	1,50,000
9.	Equity Shareholders.	5,00,000

State the priority order in which the liquidator shall distribute the proceeds under the Insolvency & Bankruptcy Code, 2016.

Answer:

The priority order in which the liquidator shall distribute the proceeds will be as under:

Particulars	Amount (in ₹)	
Amount realised from the sale of liquidation of assets		7,00,000
Less: (i) Fees payable to resolution professional (ii) Expenses incurred by the resolution professional in running the business of M/s Star House (P) Ltd. on going concern	37,500 17,500	(55,000)
Balance available		6,45,000
Less: (i) Secured creditors who has relinquished the security (ii) Workmen salary payable for a period of 24 months preceding the liquidation commencement date [1,50,000*(24/30)]	2,50,000 1,20,000	(3,70,000)
Balance available		2,75,000
Less: Unsecured Financial Creditor	2,00,000	(2,00,000)
Balance available		75,000
Less: (i) Income tax payable (ii) Cess payable to State Government	25,000 10,000	(35,000)
Balance available		40,000

Less: Balance Workmen salary payable (apart for a period of 24 months preceding the liquidation commencement date) [1,50,000 – 1,20,000]	30,000	(30,000)
Balance Available for equity shareholders		10,000

Question 26 ***(Nov 18)***

As on March 31, 2019, the audited balance sheet of M/s. Sharp Industries Limited, revealed total assets of ₹ 1 crore. M/s. Sharp Industries Limited, in the capacity of a Corporate Debtor, filed an application on July 1, 2019 with the Adjudicating Authority for initiating a fast track corporate insolvency resolution process. Explain under the provisions of Insolvency and Bankruptcy Code, 2016 the following:

i) Whether the application made by M/s. Sharp Industries Ltd. for initiating a fast track corporate insolvency resolution process is admissible?

ii) The time period including the extension of time period, if any, within which the fast track corporate insolvency resolution process shall be completed?

Answer:

Fast Track Corporate Insolvency Resolution Process:

As per Sec. 55 of Insolvency and Bankruptcy Code, 2016, an application for fast track corporate insolvency resolution process may be made in respect of the following corporate debtors, namely: to

a) a small company as defined u/s2(85) of Companies Act, 2013; or

b) a Startup (other than the partnership firm); or

c) an unlisted company with total assets, as reported in the financial statement of the immediately preceding financial year, not exceeding 1 crore.

Conclusion: Based on the provisions as stated above, M/s. Sharp Industries Ltd. can initiate a fast Track corporate insolvency resolution process as its total asset as reported in the financial statement of the immediately preceding financial year, not exceeding 1 crore.

Time period for completion of fast track corporate insolvency resolution process: Sec. 56 of Insolvency and Bankruptcy Code, 2016 provides the following:

i) Fast track corporate insolvency resolution process shall be completed within a period of 90 days from the insolvency commencement date.

ii) The Resolution Professional shall file an application to the Adjudicating Authority to extend the period of the fast track corporate insolvency resolution process beyond 90 days if instructed to do so by a resolution passed at a meeting of the committee of creditors and supported by a vote of 75% of the voting share,

iii) On receipt of an application, if the Adjudicating Authority is satisfied that the subject matter of The case is such that fast track corporate insolvency resolution process cannot be completed a period of 90 days. It may, by order extend the duration of such process beyond the said period of 90 days try such further period, as it thinks fit, but her period, as it thinks fit, but not exceeding 45 days

07/11/19

NOV 2019

Final New Syllabus
Paper - 4
Corporate and Economic Laws

SMG2

Roll No. .....

Total No. of Printed Pages – **11**

Total No. of Questions – **6**

Maximum Marks – **70**

GENERAL INSTRUCTIONS TO CANDIDATES

1. The question paper comprises two parts, Part I and Part II.
2. Part I comprises Multiple Choice Questions (MCQs).
3. Part II comprises questions which require descriptive type answers.
4. Ensure that you receive the question paper relating to both the parts. If you have not received both, bring it to the notice of the invigilator.
5. Answers to Questions in Part I are to be marked on the OMR answer sheet only. Answers to Questions in Part II are to be written on the descriptive type answer book. Answers to MCQs, if written in the descriptive type answer book, will not be evaluated.
6. OMR answer sheet will be in English only for all candidates, including for Hindi medium candidates.
7. The bar coded sticker provided in the attendance register, is to be affixed only on the descriptive type answer book. No bar code sticker is to be affixed on the OMR answer sheet.
8. You will be allowed to leave the examination hall only after the conclusion of the exam. If you have completed the paper before time, remain in your seat till the conclusion of the exam.
9. Duration of the examination is 3 hours. You will be required to submit (a) Part I of the question paper containing MCQs, (b) OMR answer sheet thereon and (c) the answer book in respect of descriptive type answer book to the invigilator before leaving the exam hall, after the conclusion of the exam.
10. The invigilator will give you acknowledgement on Page 2 of the admit card, upon receipt of the above-mentioned items.
11. Candidate found copying or receiving or giving any help or defying instructions of the invigilators will be expelled from the examination and will also be liable for further punitive action.

PART – II

70 marks

1. Question paper comprises **6** questions. Answer Question No. 1 which is compulsory and any **4** out of the remaining **5** questions.
2. Working notes should form part of the answer.
3. Answers to the questions are to be given only in English except in the case of candidates who have opted for Hindi Medium. If a candidate has not opted for Hindi Medium, his/her answers in Hindi will not be evaluated.

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PART – II

1. (A) You are the CFO and in-charge of legal compliances of a large multi-national company in India. The Board of Directors of the Company are broad based and comprise of competent directors who are Indian as well as Foreign Nationals. Mr. 'X', who is a Director (Business Development) on the Board is very often on business tour abroad. He approached you and wants to know from you the regulatory provisions of the Companies Act, 2013 relating to appointment of Alternate Directors. Analyse the following situations and advise suitably, Mr. X referring to the provisions of the Companies Act, 2013. **8**

(a) To how many directors can a person be appointed as an alternate director and how many votes does he have in one Board Meeting ?

(b) If the original director joins the Board Meeting through video conferencing without returning to India, then, can the alternate director appointed in his place attend the same board meeting ? If yes, whose presence and vote will be counted ?

(c) In case of a private company, where an alternate director is appointed in place of a non-executive director whose term is indefinite, then, what will be the tenure of such alternate director, provided the original director does not return to India for a longer period say 3-4 years ?

(d) Can an Executive Director/Whole Time Director/Managing Director appoint alternate directors ?

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(B) The Articles of Association of M/s. DEF Limited (Non-Government Company) restricts the Company to contribute to National Defence Fund in any financial year for a sum not exceeding ₹ 5 Lakhs. The Articles is silent about contribution to bonafide Charitable Fund and to a Political Party. The Company earned net profit during the last five financial years as under : 6

Financial Year	Net Profit (₹ in Lakhs)
2018-19	45
2017-18	25
2016-17	20
2015-16	15
2014-15	10

The Board of Directors proposes to contribute in July 2019 for the first time during the financial year 2019-20 :

(i) ₹ 7 Lakhs to National Defence Fund

(ii) ₹ 3 Lakhs to a bonafide Charitable Fund

(iii) ₹ 5 Lakhs to a Political Party

The Company seeks your advice on the following matters in respect of each of the above proposals under the provisions of the Companies Act, 2013.

(i) The appropriate approving authority;

(ii) The quantum of contribution that can be made;

(iii) The mode of payment of such contribution.

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2. (A) A group of shareholders of M/s. FMG Limited made a complaint to the concerned Registrar of Companies (RoC) that the business of the Company is being carried on for unlawful and fraudulent purposes and filed an application to enquire into the affairs of the Company. Referring to and analyzing the provisions of the Companies Act, 2013, decide : 4

(i) Whether the RoC has the power to order for an inquiry into the affairs of the Company ?

(ii) If yes, state the procedure to be followed by the RoC.

(iii) Whether the inquiry should be pursued by the RoC in case the complaint is withdrawn by the same group of shareholders subsequent to the Order for enquiry ?

(iv) Whether the Central Government has the power to direct the RoC to carry out the inquiry ?

(B) At the meeting of the members of M/s QRS Limited, a scheme of compromise and arrangement was approved by requisite majority. The National Company Law Tribunal (NCLT) after complying the provisions, issued an Order, approving the scheme of compromise and arrangement. 4

List out the matters to be provided in the Order issued by NCLT under Section 230(7) of the Companies Act, 2013.

When shall the Order be filed with ROC ?

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(C) M/s AWP Limited defaulted in repayment of a term loan taken from a Nationalized Bank against the security created as first charge on its Land & Buildings. The Bank classified the debt from M/s AWP Limited as Non-Performing Asset. The Bank issued Notice pursuant to Section 13 of the SARFAESI Act, 2002 to the Company to discharge its liabilities in full within a period of 60 days from the date of Notice. The Company objected for full settlement and the time limit for settlement. The Bank did not respond to the objection of the Company. In the light of the provisions of the SARFAESI Act, 2002 decide : **6**

(i) Whether the objection of the Company is valid ?

(ii) Whether the Bank has to respond to the objection of the Company ?

(iii) Whether the Bank has right to enforce the security interest without the intervention of the Court ?

3. (A) In the light of the provisions of the Companies Act, 2013, examine whether the following Companies can be considered as a 'Foreign Company' : **8**

(i) M/s Red Stone Limited is a Company registered in Singapore. The Board of Directors meets and executes business decisions at their Board Meeting held in India.

(ii) M/s Blue Star Public Company Limited registered in Thailand has authorized Mr. 'Y' in India to find customers and to enter contracts with them on behalf of the Company.

(iii) M/s. Xex Limited Liability Company registered in Dubai has installed its main server in Dubai for maintaining office automation software by Cloud Computing for its client in India.

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(B) Mr. 'B' purchased a flat out of the proceeds earned by Drug Trafficking. The flat was attached by the Director, Director of Enforcement after complying the procedures under Section 5 of the Prevention of Money Laundering Act, 2002 (PMLA, 2002). Mr 'B' got a stay from the High Court for any proceedings under the said Act. The stay was subsequently vacated. **6**

State the relevant provisions of the PMLA, 2002 for computing the period of provisional attachment including extension, if any.

Whether Mr. 'C', son of Mr. 'B' can occupy the flat during the period of provisional attachment ?

4. (A) 'X' Stock Exchange Limited was granted recognition by Securities and Exchange Board of India (SEBI). The stock brokers of the Stock Exchange did not pay much heed to the concept of governance and focused on increasing their wealth and snubbed the protection of investors. Their activities were against the interest of the trade and general public. **4**

(i) Examine whether the Central Government / SEBI has the power to withdraw the recognition granted to 'X' Stock Exchange Limited under the provisions of Securities Contracts (Regulations) Act, 1956 ?

(ii) Whether a person can be a member of an unrecognized Stock Exchange for the purpose of performing any contracts in Securities ?

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(B) The composition of Audit Committee of M/s MKBTC Limited, an unlisted Public Company, as on 31-3-2019 comprised of 7 Directors including 4 Independent Directors. The majority of the members of the Audit Committee has the ability to read and understand the financial statements but none of them has accounting or related financial management expertise. The Company listed its Securities in a recognized Stock Exchange in the month of August 2019. Referring to the regulations of Securities and Exchange Board of India [Listing Obligations and Disclosure Requirements] Regulations 2015, decide whether the existing Audit Committee can continue after listing of its Securities ? **4**

(C) In the light of the provisions of the Foreign Contribution (Regulation) Act, 2010 examine and decide whether the following persons in India are permitted to receive the amount/articles in the following situations : **6**

(i) M/s KG & Co; a partnership firm obtained loan from a club registered in London for its business purpose.

(ii) Hello FM, a registered association, received funds from a foreign company for establishing Frequency Model Radio Station to broadcast audio news.

(iii) Mr. Happy received a wrist watch as marriage anniversary gift from his uncle, a citizen of USA. The market value of the wrist watch is ₹ 25,000.

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5. (A) Due to an unprecedented flood, all the fixed assets of a Company were damaged extensively beyond renovation or repair. The cost of replacement of assets were huge and the sum insured on the fixed assets did not cover all the assets. Therefore, the operations of the Company were permanently discontinued. Meanwhile, based on a winding-up petition filed by the secured creditors, the High Court passed a winding-up order. The workers of the Company opposed to the winding-up petition and also filed an appeal against the winding-up order. The workers are not sure whether their appeal would be heard in the winding-up proceedings. Examine, under the provisions of the Companies Act, 2013, whether the appeal filed by the workers would succeed and their dues / interest will be protected in priority ? **4**

(B) M/s KIL Limited, a listed company, proposed to acquire a plant for consideration other than cash from Mr. KK, a director. The Managing Director of the Company identified Mr. JK a registered valuer under the provisions of the Companies Act, 2013 for the purpose of valuation of the plant. Mr. KK acquired the plant 48 months back from a partnership firm in which the spouse of Mr. JK is a partner. The Managing Director of the Company issued an order appointing Mr. JK as a registered valuer. Examine and decide whether the decision of appointment and the mode of appointment is valid under the provisions of the Companies Act, 2013 ? **4**

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(C) In view of the deep recession prevailing in the market for the past three years, M/s. Infra Limited (Corporate Debtor), which was facing the brunt of financial crisis, could not pay salaries and wages to its workmen and employees for the past 6 months. The workmen and the employees, who are the members of a recognized Trade Union "Infra Labor Federation", made a complaint in this regard. Thereafter, the Trade Union approached and urged the Management of the Company in person and through representations in writing to settle the arrears of wages and salaries due to its members. The Corporate Debtor neither disputed nor took any actions to settle the amount. Under the circumstances, Infra Labor Federation filed an application before the Adjudicating Authority i.e. with the National Company Law Tribunal for initiating a Corporate Insolvency Resolution Process under the Insolvency and Bankruptcy Code, 2016. **6**

In the light of the provisions of the Insolvency and Bankruptcy Code, 2016, examine the following :

(i) Validity of the Application.

(ii) What will be the "Initiation date" for initiating the Corporate Insolvency Resolution Process ?

6. (A) Mr. 'K' is a small shareholder director in M/s KGP Tyres Limited from 1st April 2018 and in M/s VSR Cotton Mills Limited from 1st April 2019, in compliance with the relevant provisions of the Companies Act, 2013. M/s KGP Tyres Limited has not paid interest on the public deposits due from 1st July 2018. In the light of the information given above, examine the following under the provisions of the Companies Act 2013. **4**

(i) Whether the office of Mr. 'K', small shreholder director, shall become vacant in M/s KGP Tyres Limited and M/s VSR Cotton Mills Limited ?

(ii) If yes, state the period from which the office of the directorship shall become vacant.

OR

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Mr 'R' holds directorship in 10 Public Companies and 11 Private Companies as on 31.05.2019. One of the above Private Company is a dormant Company. Apart from the dormant Company, on 30.06.2019 a Private Company (in which Mr. R is holding directorship) has become a subsidiary of a Public Company. 4

In the light of the provisions of the Companies Act, 2013 examine and decide :

(i) The validity of holding directorship of Mr 'R' with reference to number of directorship as on 31.05.2019 and as on 30.06.2019.

(ii) Whether a Company has power to specify any lesser number of Companies in which a director of the Company may act as a director ?

(B) Mr. Thangavel is a Director in 7 Companies with a DIN (Director Identification Number) allotted to him. Again, another DIN was inadvertently allotted to him which was never used for filing any document with any Authority. He desires to surrender the second DIN and keep all his directorship with the first DIN. Advise him the procedure to be followed under the provisions of the Companies Act, 2013 and the Rules made thereunder for surrendering the second DIN inadvertently obtained by him. 4

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(C) Mr. 'K' used his car for smuggling cash and the Special Court found on conclusion of trial that an offence of money laundering was committed by Mr. 'K' under the provisions of the Prevention of Money Laundering Act, 2002 (PMLA, 2002). The car was under hypothecation to a Nationalized Bank for the car loan obtained. Referring to provisions of the PMLA, 2002, examine whether the car can be confiscated despite the existence of encumbrance ? 3

(D) The Committee of Creditors of M/s XYZ Limited proposes to appoint Mr. Ajit, an Insolvency Professional, as Insolvency Resolution Professional in the matter of corporate insolvency process of M/s XYZ Limited. Mr. Ajit was a promoter of M/s ABC Limited which is a holding company of M/s XYZ Limited. Examine and decide whether Mr. Ajit is eligible for appointment as an Insolvency Resolution Professional under the Provisions of Insolvency and Bankruptcy Code, 2016. 3

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