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<b>Question Paper Nov 2018</b>		

## **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 10<sup>th</sup> 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 30<sup>th</sup> 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 5<sup>th</sup> 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 30<sup>th</sup> 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 30<sup>th</sup> June 2014, due to the resignation of Ms. Sheela, should be filled up latest by 29<sup>th</sup> 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 10<sup>th</sup> 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 8<sup>th</sup> November 2014, provided the said meeting is the first meeting of the Board after 30<sup>th</sup> 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 26<sup>th</sup> 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 1<sup>st</sup> April, 2014 to 30<sup>th</sup> 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 5<sup>th</sup> 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 30<sup>th</sup> 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 **at 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 atleast 2 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 vacancies 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 in 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 1<sup>st</sup> April, 2015. He retired from service on superannuation on 31<sup>st</sup> 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 and 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 <u>Public Companies having paid up share capital of 10 crore rupees or more; or</u>
(2)	the <u>Public Companies having turnover of 100 crore rupees or more; or</u>
(3)	the <u>Public Companies which have, in aggregate, outstanding loans, debentures and deposits, exceeding 50 crore rupees.</u>

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 31<sup>st</sup> 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.

### ***Appointment of Directors Elected by Small Shareholders (Section 151)***

#### **Question 10**

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 11**

**(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 12**

**(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 13**

**(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.**

### ***Appointment of Directors (Section 152)***

### **Question 14**

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 15**

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 16**

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 1/3<sup>rd</sup> 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 17**

**(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 18**

**(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:

- Maximum number of persons, who can be appointed as directors not liable to retire by rotation.
- How many of the remaining directors will have to retire by rotation every year at the Annual General Meeting (AGM)?
- 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.
- Can the Board of Directors increase the strength of companies' directors to 18 from 11 by appointing additional directors through passing single resolution?

### **Answer**

- 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:  $11 * \frac{2}{3} = 7.3$  or 8

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

- 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. 14<sup>th</sup> 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].

### Director Identification Number (Section 153 to 159)

#### **Question 19**

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 20**

**(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 21**

(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 22**

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 23**

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 24**

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 25**

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 3<sup>rd</sup> April, 2014. Unfortunately Mr. C expired on 15<sup>th</sup> 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 15<sup>th</sup> 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 26**

***(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 abroad 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 27**

**(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 28**

(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 29**

(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 30**

(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.

### ***Appointment of Director to be Voted Individually (Section 162)***

### **Question 31**

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 32**

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 33**

**(May 18)**

Mr. Bond and Mr. James were appointed as Directors of Jamesbond Ltd. at the AGM held on 30<sup>th</sup> 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 34**

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 35**

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 1<sup>st</sup> 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 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.

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

- a) Non filing of financial statements for year ended 31<sup>st</sup> 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 1<sup>st</sup> 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 36**

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 37**

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 10<sup>th</sup> April, 2014 and such repayment has not been made till 5<sup>th</sup> 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 6<sup>th</sup> 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 38**

Mr. Ramanathan is a Director of Fraudulent Ltd., Honest Ltd. and Regular Ltd. for the financial year ended on 31<sup>st</sup> 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 1<sup>st</sup> 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 three 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 39**

**(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 31<sup>st</sup> 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.

## **Question 40**

**(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 41**

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 42**

**(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 1<sup>st</sup> 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 43**

**(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 1<sup>st</sup> 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 1<sup>st</sup> 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 44**

**(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 45**

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 46**

Mr. Raj, a director of POL Ltd., submitted his resignation from the post of director to the Board of Directors on 30<sup>th</sup> 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. 30<sup>th</sup> June 2014 as he has obtained the receipt of the notice on the same day.

## ***Removal of Directors (Section 169)***

### **Question 47**

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)].

Note: The Ministry of Corporate Affairs vide Notification S.O.1934[E] notifies sub section (4) to section 169 w.e.f. 1<sup>st</sup> June, 2016. For details refer Supplementary study paper on Corporate and Allied Laws.

## **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.
- 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 other 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 Rs. 30,000 to Rs. 45,000 per meeting **by passing a resolution in the Board Meeting and altering 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)**

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 4<sup>th</sup> 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;

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 31<sup>st</sup> 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.

Hence, Downhill Industries Limited can appoint Mr. Smart aged 71 years as Managing Director of Downhill Industries Limited 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 1<sup>st</sup> 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 1<sup>st</sup> 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.

### **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 basis 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.**

## 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.**

## **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**

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 1<sup>st</sup> April, 2015. The company has conducted four Board meetings during the financial year 2015-16 i.e. on 6<sup>th</sup> April, 2015, 28<sup>th</sup> August, 2015, 30<sup>th</sup> September, 2015 and 30<sup>th</sup> 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 5<sup>th</sup> 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 1<sup>st</sup> April, 2015 and conducted four Board meetings during the financial year 2015-16 on 6<sup>th</sup> April, 2015, 28<sup>th</sup> August, 2015, 30<sup>th</sup> September 2015 and 30<sup>th</sup> 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 6<sup>th</sup> April, 2015 and 28<sup>th</sup> August, 2015 is 143 days which is more than 120 days and similarly the gap between the meeting held on 30<sup>th</sup> 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 30<sup>th</sup> 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 off 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 30<sup>th</sup> 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 31<sup>st</sup> August, 2014, his appointment was declared invalid. But Mr. MTP continued to act as director even after 31<sup>st</sup> 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 31<sup>st</sup> August, 2014 shall be deemed to be invalid and not binding upon the Company.

### **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 5<sup>th</sup> June 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
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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
<b>TOTAL</b>	<b>66,00,000</b>
Average of net profits during three preceding financial	22,00,000
Five per cent thereof	<u>1,10,000</u>

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	<u>10 Crore</u>
Amount upto which the Board of Directors can further borrow without the approval of shareholders in a general meeting.	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 5<sup>th</sup> 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 ., of 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 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.**

*Company to contribute to bona fide and charitable funds etc. (Section 181)*

### **Question 34**

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 bonafide 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 35**

**(Nov 17)**

M/s Jai Industries Limited earned net profit for the last three years as under:

<b>Financial Year</b>	<b>Net Profit (Rs. in Crores)</b>
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 36**

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 37**

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 5<sup>th</sup> 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 5<sup>th</sup> 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 38**

**(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 39**

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 40**

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 41**

**(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: 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.

Thus, in the instant case, if PCS Ltd. wants to lend Rs. 5 Lakhs to Mr. DRT who is a director in PCS Ltd. and Rs. 2 Lakhs to his wife, then it is in violation of section 185 of the Companies Act, 2013.

## ***Loan and Investment by Company (Section 186)***

### **Question 42**

**(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**

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 sixty per cent. 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, except with the prior approval by means of a special resolution passed at a general meeting.

However, 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.

As per the given facts, ASK Housing Finance Company Limited was prepared to give housing loans to the employees of M/s NEWS Pharmacy Limited on the condition that such loans are guaranteed by the M/s NEWS Pharmacy Limited exceeding the limits prescribed in the Companies Act, 2013.

Here, 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 guarantees given for the employees. So, Section 186(2) shall not be applicable to it. Hence, it 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.

Answer will remain the same, even if the company provides security instead of guarantee as the provisions of the Section 186(2) are applicable for providing security also.

### **Question 43**

**(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**

Amar Cotton Co. Ltd. is not a wholly-owned subsidiary of Amar Textiles Ltd.

1. According to 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.

As the 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 exceeds the limit given under section 186 (2) of the Companies Act, 2013. It is therefore, necessary for Amar Textiles Ltd., to pass a special resolution of the members at a duly convened General Meeting before increasing its holding from 70% to 80%.

2. The **notice of special resolution must be accompanied by an explanatory statement** and must include full particulars of the investment proposed to be made along with the proposal of such investment in compliance with section 186 (4) of the Act.
3. According to **section 186(5)** of the Companies Act, 2013, 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 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 Industrial Development Bank of India (IDBI) which is not a public financial institution within the meaning under Section 2 (72) of the Companies Act, 2013 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.

4. Further, as required by provisions of Section 186 (5), the **investment proposal must be passed at the Board meeting by a unanimous decision of all the directors present at the meeting.**
5. The company must enter the prescribed particulars of investment in a register of investment required to be maintained under section 186(9) of the Act.

#### **Question 44**

**(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 instalments stipulated in the loan agreements. Based on the following financial data. Advise Star Limited about the legal position regarding the allowability 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 45**

**(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.

### ***Related Party Transaction (Section 188)***

#### **Question 46**

**(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.

### *Payment to directors for loss of office, Etc. in connection with transfer of undertaking, property or shares (Section 191)*

#### **Question 47**

**(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 47**

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 1<sup>st</sup> 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.

**(RTP Nov 18)**

### **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.**

## *Investigation into affairs of company by Serious Fraud Investigation office (Section 212)*

### **Question 6**

**(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 7**

**(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 8**

**(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 9**

**(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 15<sup>th</sup> February, 2017 passed an order of suspension without waiting the orders from Tribunal (after 30 days of making the application)

## **Question 10**

**(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 11**

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 12**

**(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 13**

**(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 complaint 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.

### *Inspector's Report (Section 223)*

#### **Question 14**

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 15**

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 16**

**(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 17**

**(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.**

## **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, majority of persons representing 3/4<sup>th</sup> 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.

### *Merger and Amalgamation of Companies (Section 232)*

#### **Question 4**

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 prerequisite to apply the provisions of section 235 of the Companies Act, 2013)].

## ***Merger or Amalgamation of certain Companies (Section 233)***

### **Question 5**

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 6**

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 conduct 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.

#### *Power of Central Government to provide for Amalgamation of Companies in Public Interest (Section 237)*

### **Question 7**

**(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 interest 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 8**

**(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 before the 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 oppression involving 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 latter are 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:

- Not less than 100 members of the company or not less than one-tenth of the total number of members, whichever is less; or
- 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 than 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 1/10<sup>th</sup> of 500); or

Members holding ₹ 50,00,000 share capital (being 1/10<sup>th</sup> 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 pendency 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 withdrawal 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 1/10th 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 practitioners 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 act 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 9**

**(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 practitioners 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.

## 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.

### Overriding Preferential Payment (Section 326)

#### Question 4

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.

$$\text{Workman's Share to Secured assets} = \frac{\text{Amount Realized} * \text{Workman's Dues}}{\text{Workman's Dues} + \text{Secured Loan}}$$

$$\text{Workman's Share to Secured Asset} = \frac{80,00,000 * 25,00,000}{25,00,000 + 75,00,000}$$

$$\text{Workman's Share to Secured Assets} = 20,00,000$$

$$\text{Amount available to secured creditor is ₹ 80 Lakhs} - ₹ 20 \text{ Lakhs} = ₹ 60 \text{ Lakhs}$$

Hence, no amount is available for payment of government dues and unsecured creditors.

### **Question 5**

XYZ Limited is being wound 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.

**Workman's Share to Secured = Amount Realized \* Workman's Dues**

**Workman's Dues + Secured Loan**

$$\text{Workman's Share to Secured Asset} = \frac{\text{Amount Realized} * \text{Workman's Dues}}{\text{Workman's Dues} + \text{Secured Loan}}$$
$$= \frac{4,00,00,000 * 1,25,00,000}{1,25,00,000 + 5,00,00,000}$$

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 6**

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 that date;**
- (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.**

## Question 7

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 mind of the company, acting through its directors, was 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 8**

Info-tech Overtrading Ltd. was ordered to be wound up compulsorily 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 15<sup>th</sup> 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 9**

Skyline Ltd. Was ordered to be wound up compulsorily on a petition filed on 10<sup>th</sup> 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 15<sup>th</sup> 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.**

*Liability where proper accounts not kept (Section 338)*

### **Question 10**

**(RTP Nov 18)**

M/s Sagar Retail Mega Mart Ltd. applied for winding up on 1<sup>st</sup> April, 2018 before the Honourable Tribunal by passing a special resolution as per the provision of section 271(1)(a) of the Companies Act, 2013 on account of fall in business and continued losses but not due to inability to pay debts. The company was in the business of ordinary retail trade of multiple branded goods. A few shareholders of the company have alleged before the Honourable Tribunal that the company had failed to maintain proper books of accounts for over a period of more than three years immediately prior to the date of winding up application and the sole reason cited by them in support of their allegation is that no proper statements of all goods sold and purchased by the company have been kept as such every officer in default must be punished as per the provisions of the Companies Act, 2013. Mr. Ravi the CFO and officer in default do not refute the allegation of non-maintenance but is of the opinion that this act as per the provision of the Companies Act, 2013 is not punishable. Decide whether the opinion of the CFO is correct. Would your answer be different had the business of the company be wholesale trade instead of ordinary retail trade?

### **Answer**

#### **Failure to maintain proper books of accounts [Section 338(1) of the Companies Act, 2013]**

- where a company is being wound up, if it is **shown that proper books of account were not kept by the company throughout the period of two years immediately preceding the commencement of the winding up,**
- every officer of the company who is in default shall, unless he shows that he acted honestly and that in the circumstances in which the business of the company was carried on, the default was excusable,
- be punishable with **imprisonment for a term which shall be not less than one year but which may extend to 3 years and with fine which shall not be less than 1 lakh rupees but which may extend to 3 lakh rupees.**

### Conditions when it shall be deemed that proper books of account have not been kept

**[Section 338(2) of the Act]:** For the purposes of sub-Section (1), it shall be deemed that proper books of account have not been kept in the case of any company,—

- where the business of the company has involved dealings in goods, statements of the annual stock takings and, except in the case of goods sold by way of ordinary retail trade, of all goods sold and purchased, have not been kept.

In the instant case, no proper statements of all goods sold and purchased by the company engaged in ordinary retail trade is kept. It shall be deemed that proper books of account have been kept as ordinary retail trade is an exception under sub- Section (2). Thus, opinion of CFO is correct.

If the company is engaged in wholesale trade instead of ordinary retail trade, then it is deemed that proper statements of all goods sold and purchased by the company engaged in wholesale retail trade is not kept for more than 3 years period immediately prior to the date of winding up application. Hence, in this case, the CFO opinion will not hold good and will be punishable.

### *Power of Tribunal to assess damages delinquent directors, etc. (Section 340)*

#### **Question 11**

What is meant by "misfeasance"? Who can initiate misfeasance proceedings and is there any time limit for initiating such proceedings ? Examine the extent to which the legal representatives of a deceased Director, against whom misfeasance proceedings were initiated, can be held liable under the provisions of the Companies Act, 2013

#### **Answer**

##### **Misfeasance:**

The term 'misfeasance' has not been defined in the Companies Act, 2013. It can be considered as an act or omission in the nature of breach of trust in relation to the company which causes losses or injuring to the company.

##### **Initiation of Proceeding:**

As per section 340 of the Companies Act, 2013, proceedings may be initiated on the application of the Official Liquidator, or company liquidator, any creditor or contributory.

##### **Time limit:**

The time limit for initiating such an application is five years from the date of the order for winding up, or of the first appointment of the liquidator in winding up, or of the misfeasance/breach of trust, whichever is longer.

##### **The extent of liability of the Legal Representative:**

Misfeasance proceeding can be continued against the legal representatives of the deceased director and the amount declared to be due in such misfeasance proceeding can be realized from the estate of the deceased in the hands of his legal representatives. The court further held that the legal representatives would not, however, be liable for any sum beyond the value of the estate of the deceased in their hands.

## **Question 12**

Winding up proceedings has been commended by the tribunal against DEF Limited, a government company (Central Government is a member). Even after completion of one year from the date of commencement of winding up proceedings, it has not possible to conclude the same. The liquidator is of the opinion that the statement shall be filled with tribunal and registrar only.

- i) Validate the opinion made by the liquidator and penalty can be imposed on the liquidator for contravention of the provision as per companies act, 2013.
- ii) What will be your answer if the DEF Limited is a non-government company?

## **Answer**

**Section 348** of the Companies Act, 2013 states that, if the winding up of a company is not concluded within one year after its commencement then the Company Liquidator shall file a statement in such form containing such particulars as may be prescribed. **Such statement shall be filled within two months of the expiry of such year and it shall be filled continuously thereafter until the winding up is concluded**, at intervals of not more than one year or at such shorter intervals as may be prescribed. The statement shall be duly audited, by a person qualified to act as auditor of the company and position of with respect to the proceedings in the liquidation, the Tribunal. **A copy shall simultaneously be filed with the Registrar and shall be kept by him along with the other records of the company**.

Where a statement relates to a Government company in liquidation, the Company Liquidator shall forward a copy thereof,

- i) To the **Central Government, if that Government is a member of the Government company;**
- ii) To any **State Government, if that Government is a member of the Government company;** or
- iii) To the **Central Government and any State Government, if both the Governments are members of the Government company.**

### **DEF Limited is a Government Company**

In the current scenario, we can understand that the DEF Limited is a government company in which Central Government is a member and hence statement is also required to file to the Central Government along with the Tribunal and Registrar. So, the opinion by the Company Liquidator is not tenable in the eyes of the law and he is liable for penal action under the act.

The **company liquidator shall be punishable with fine which may extend to five thousand rupees for every day during which the failure continues.**

### **DEF Limited is a Non-Government Company**

In the current scenario, the DEF Limited is a non-government company hence statement is only required to file with the Tribunal and Registrar only. **So, the opinion by the Company Liquidator is tenable in the eyes of the law and he is not liable for any penal action under the act.**

## **Question 13**

**(RTP May 2018)**

Winding up proceedings has been commended by the Tribunal against Paramount Limited, a government company (Central Government is a member). Even after completion of one year from the date of commencement of winding up proceedings, it has not possible to conclude the same. The liquidator is of the opinion that the statement shall be filed with tribunal and registrar only.

- i) Decide validity to the opinion made by the liquidator and penalty that can be imposed on the liquidator for contravention of the provision as per the Companies Act, 2013.
- ii) Discuss, if the Paramount Limited is a non-government company?

## **Answer**

**Section 348** of the Companies Act, 2013 states that, if the winding up of a company is not concluded within one year after its commencement then the Company Liquidator shall file a statement in such form containing such particulars as may be prescribed. **Such statement shall be filled within two months of the expiry of such year and it shall be filled continuously thereafter until the winding up is concluded, at intervals of not more than one year or at such shorter intervals as may be prescribed.** The statement shall be duly audited, by a person qualified to act as auditor of the company and position of with respect to the proceedings in the liquidation.

The statement shall be filled with the tribunal in the case of a winding up by the Tribunal. A copy shall simultaneously be filed with the Registrar and shall be kept by him along with the other records of the company.

- Where a **statement relates to a Government company in liquidation, the Company Liquidator shall forward a copy thereof, to the Central Government, if that Government is a member of the Government company;**
- to any **State Government, if that Government is a member of the Government company;** or
- to the **Central Government and any State Government, if both the Governments are members of the Government company.**

### **Paramount Limited is a Government Company**

In the current scenario, we can understand that the Paramount Limited is a government company in which Central Government is a member and hence statement is also required to file to the Central Government along with the Tribunal and Registrar. So, the opinion by the Company Liquidator is not tenable in the eyes of the law and he is liable for penal action under the Act.

The **company liquidator shall be punishable with fine which may extend to five thousand rupees for every day during which the failure continues.**

### **Paramount Limited is a Non-Government Company**

In the current scenario, the Paramount Limited is a non-government company hence statement is only required to file with the Tribunal and Registrar only. So, the opinion by the Company Liquidator is tenable in the eyes of the law and he is not liable for any penal action under the Act.

## **Ch 8 – Producer Companies**

### *Formation of Producer Company & its Registration (Section 581C)*

#### **Question 1**

A group of 8 individuals together with a producer institution approached the Registrar for incorporation of a producer company under Section 581 of the Companies Act, 1956. Can the Registrar go ahead with the registration and incorporation? Discuss.

#### **Answer**

**Formation and Registration of producer company:** According to Section 581C of the Companies Act, 1956, any ten or more individuals, each of them being a producer, or any two or more producer institutions, or a combination of ten or more individuals and producer institutions, desirous of forming a producer company having its objects specified in section 581B and otherwise complying with the requirements and provisions of this Act in respect of registration, may form an incorporated company as a Producer Company under this Act.

If the Registrar of Companies is satisfied that all the requirements of this Act have been complied with in respect of registration and matters precedent and incidental thereto, he shall, within thirty days of the receipt of the documents required for registration, register the memorandum, the articles and other documents, if any, and issue a certificate of incorporation under this Act.

In the problem given here, a group of 8 individuals together with a producer company approached the registrar for incorporation of a producer company. Since the requirements "combination of ten or more individuals and producer institutions" of this provision has not been complied with in respect of registration, so registrar cannot proceed with the registration and incorporation of the company.

#### **Question 2**

What are the modes of investment, from and out of its general reserves, available to a Producer Company formed and registered under Section 581C of the Companies Act, 1956?

#### **Answer**

- i) As per Producer Companies (General Reserves) Rules, 2003 issued by the Ministry of Corporate Affairs, Ministry of Finance, Government of India on 7th August, 2003 a producer company formed and registered under section 581C of the Companies Act, 1956, shall make investments from and out of its general reserves in the following manner, namely:-
  - a) in approved securities, fixed deposits, units and bonds issued by the Central or State

- Governments or cooperative societies or scheduled bank; or
- b) in a co-operative bank, state co-operative bank, co-operative land development bank or central co-operative bank; or
  - c) with any other scheduled bank; or
  - d) in any of the securities specified in section 20 of the Indian Trusts Act, 1882; or
  - e) in the shares or securities of any other multi-state co-operative society or any co-operative society; or
  - f) in the shares, securities or assets of a public financial institutions specified under section 4A of the Companies Act, 1956.

### *Memorandum of Producer Company (Section 581F & 581H)*

#### **Question 3**

A group of individuals eligible to form a Producer Company within the meaning of the Companies Act, 1956 has entrusted you with the job of preparing the Memorandum of Association of the proposed Producer Company. You are required to state the matters, which are required to be included in such Memorandum of Association.

#### **Answer**

As per section 581F of the Companies Act, 1956, the Memorandum of Association of a Producer Company has to state the following:

- a) The name of the company with "Producer Company Limited" as the last words of the name of such Company;
- b) The State in which the registered office of the Producer Company is to situate;
- c) The main objects of the Producer Company confirming to the objects specified in section 581B of the Companies Act, 1956;
- d) The names and addresses of the persons who have subscribed to the memorandum of Association;
- e) The amount of share capital with which the Producer Company is to be registered and division thereof into shares of a fixed amount;
- f) The names, addresses and occupations of the subscribers being producers, who shall act as the first directors in accordance with section 581J(2) of the Companies Act, 1956;
- g) That the liability of its members is limited;
- h) Opposite to the subscriber's name the number of shares each subscriber takes (Each subscriber must take at least one share);
- i) In case the objects of the Producer Company are not confined to one State, the States to whose territories the objects extend.

#### **Question 4**

A producer company proposes to amend the objects specified in its Memorandum of Association and certain provisions in its Articles of Association. The Company also proposes to shift its registered office from the State of Kerala to Tamil Nadu. Explain the requirements under the provisions of the Companies Act, 1956 to give effect to these proposals.

#### **Answer**

- i) **Alteration in Memorandum of Association of producer company:** According to section 581H of the Companies Act, 1956, a producer company shall not alter the conditions contained in its memorandum except in the cases, by the mode and to the extent for which express provision is made in this Act. However, a producer company may, by special resolution, not inconsistent with Section 581B, alter its objects specified in its memorandum.

**A copy of the amended memorandum, together with a copy of the special resolution duly certified by two directors, shall be filed with the Registrar within 30 days from the date of adoption of resolution.**

- ii) **Alteration in Articles of Association:** As per section 581-I, any amendment to the articles should be proposed by not less than two-third of the elected directors or by **not less than one-third of the members of the producer company, and adopted by the members by a special resolution.**

A copy of the amended articles together with the copy of the special resolution, both duly certified by two directors, should be filed with the Registrar within thirty days from the date of its adoption.

- iii) **Shifting of the registered office:** Section 581H contains the provision as to shifting of the registered office. According to the provisions, in case of transfer of the registered office of a producer company from the jurisdiction of one Registrar to another, certified copies of the special resolution certified by **two directors shall be filed with both the Registrars within thirty days,** and each Registrar shall record the same, and thereupon the Registrar from whose jurisdiction the office is transferred, shall forthwith forward to the other Registrar all documents relating to the producer company.

The alteration of the provisions of memorandum relating to the change of the place of its registered office from one State to another shall not take effect unless it is confirmed by the Company Law Board (Tribunal) on petition.

#### **Question 5**

Explain the provisions under the Companies Act, 1956 for amendment of Articles of Association of a producer company.

#### **Answer**

- Amendment of articles (Section 581-I of the Companies Act, 1956):** Any amendment of the

articles shall be proposed by not less than two-third of the elected directors or by not less than **one-third of the members of the producer company, and adopted by the members by a special resolution.**

A copy of the amended articles together with the copy of the special resolution, both duly certified by two directors, should be filed with the Registrar within thirty days from the date of its adoption.

#### *Provisions relating to Inter-state Co-operative societies (Section 581J & 581N)*

### **Question 6**

The existing Inter-state Cooperative Society seeks your advice regarding the papers to be submitted to the Registrar of Companies for its registration as a Producer Company under the provisions of the Companies Act, 1956. You are required to prepare a list of such papers.

### **Answer**

As per section 581J of the Companies Act, 1956, any Inter-State Co-operative Society with objects not confined to one State may make an application to the Registrar of Companies for registration as a Producer Company.

The application for registration as a producer Company is to be submitted along with the following:

- a) A **copy of the special resolution, of not less than two-third of total members of Inter-State Co-operative Society**, for its incorporation as a Producer Company under the Companies Act;
- b) A statement showing:
  - **Names and addresses or the occupation of the directors** and Chief Executive, if any, by whatever name called, of such inter-State Co-operative Society, and
  - **list of members of such Inter-State Co-operative Society**;
- c) a **statement indicating that the Inter-State Co-operative Society is engaged in any one or more of the objects specified in section 581B** of the Companies Act, 1956;
- d) a **declaration by two or more directors of the Inter-state co-operative society certifying that particulars given in the above statements are correct.**

### **Question 7**

The Executive Committee of an Inter-state Co-operative society decides to convert the society into a 'Producer Company' under the provisions of the Companies Act, 1956. You being a practicing Chartered Accountant are approached by the society for advice. Advise the society on the following matters:

- i) The steps to be taken for conversion of the society into a 'Producer Company'.
- ii) Manner in which voting rights of members of Producer company after conversion may be exercised.

## **Answer**

Conversion of interstate cooperative society into producer company: As a practicing Chartered Accountant the following advise can be given to the inter-state society which wants to get converted into a 'Producer company' under the provisions of Companies (Amendment) Act, 2002.

i) Steps to be taken for conversion (Section 58IJ):

Any inter-state cooperative society having objects for multiplicity for states may make an application to the Registrar for registration as producer company. Such application should be accompanied by –

- a) A copy of the special resolution, of not less than 2/3<sup>rd</sup> of total member of Inter-State Cooperative Society, for its incorporation as a producer company.
- b) A Statement showing : (i) names and address or the occupation of the directors and Chief Executive, if any, by whatever name called, of such inter-state cooperative society; and (ii) list of members of such inter-state cooperative society.
- c) A statement indicating that the inter-state cooperative society is engaged in any one or more of the objects specified in section 581B.
- d) A declaration by two or more directors of the inter-state cooperative society certifying that particulars given in clauses (a) to (c) given above are correct.

The word "Producer Company Ltd." should form part of its name to show its identity. On compliance with the requirements of the Act, the Registrar shall, within a period of 30 days of the receipt of application, certify under his hand that the society applying for registration is registered and thereby incorporated as a producer company.

Upon registration as a producer company, the Registrar of Companies who registers the company is required to intimate the Registrar with whom the erstwhile inter -State cooperative society was earlier registered for appropriate deletion of the society from its register.

ii) Manner in which voting rights of members can be exercised (Section 581Z):

Section 581Z of the Companies Act, 1956 states that subject to the provisions of sub-sections (1) and (3) of Section 581D, every member shall have one vote and in the case of equality of votes, the chairman or the person presiding shall have a casting vote except in the case of election of the chairman. As regards the voting rights it may be noted that:

- a) Where individual is a member of the producer company, he has one vote irrespective of the size of his holding.
- b) Where both individuals and producer institutions are members – single vote for every member.
- c) Where membership is confined to producer institutions only, in the first year of registration of the company, the voting rights shall be based on the size of the

shareholding of the member institution and in the following years it will be based on participation by the respective institutions in the business of the producer company in the previous year (as may be specified in the Articles),

- d) A producer company, may, if authorized by the Articles, restrict the voting rights to active members of the producer company, and

Casting vote can be cast by the presiding member (Chairman) in case of equality of votes on any resolution (except for election of the Chairman)

### *Management of Producer Company (Section 581-O – 581Z)*

#### **Question 8**

Mr. Z an expert in modern agriculture practices is willing to lend his services as a director of M/s. Lord Krishna Cotton Producer Company Ltd. registered under Section 581C of the Companies Act, 1956. Advise Mr. Z as to how he can be appointed as a director including (1) The total number of directors that can be appointed (2) The tenure of the directors (3) The time limit within which the appointment should be made (4) the co-option of directors and (5) the voting powers of such co-opted directors.

#### **Answer**

According to section 581P of the Companies Act, 1956 the members who sign the memorandum and the articles may designate (not less than five) as first directors and who shall govern the affairs of the company until the directors are appointed at the Annual General Meeting.

- a) According to section 581-O every producer company shall have at least five and not more than fifteen directors.
- b) The period of office of director shall be not less than one year and not exceeding 5 years as may be specified in the articles.
- c) The election of directors shall be conducted within 90 days from the date of registration of the producer company. In the case of Inter-state co-operative society the election shall be held within a period of 365 days.
- d) The directors are normally elected and appointed by the members in the Annual General Meeting. The Board may also co-opt one or more expert directors as an additional director. Such directors cannot exceed 1/5th of the total number of directors.
- e) The expert directors shall not have the right to vote in the election of Chairman but shall be eligible to be elected as Chairman if it is provided by the articles.

Thus Mr. Z can be appointed as expert director but he will not have any voting right in the election of chairman of the Board of directors. His tenure of office can be between one to five years.

## **Question 9**

XYZ Producer Company Limited was incorporated on 1<sup>st</sup> April, 2003. At present it has got 200 members and its board consists of 10 Directors. The Board of directors of the company seeks your advice on the following proposals:

- i) Appointment of one expert Director and one Additional Director by the Board for a period of four years.
- ii) Loan of Rs 10,000 to Mr. X, a Director of the company repayable within a period of six months.
- iii) Donation of Rs. 10,000 to a Political Party.

Advise the Board of directors explaining the relevant provisions of the Companies Act, 1956.

## **Answer**

- i) **Appointment of expert director or additional director:** Section 581P(6) of the Companies Act, 1956 empowers the Board of directors of a producer company to co-opt one or more expert directors or an additional director not exceeding one fifth of the total number of directors for such period as the Board may deem fit. But the maximum period shall not exceed the period specified in the Articles of the company (Second Proviso to section 581P(6)).

The number of directors proposed to be co-opted is only 2 and it does not exceed one-fifth of the total number of directors. They can hold office for the period specified by the Board provided it does not exceed the period specified in the Articles (Section 161(1) of the Companies Act, 2013 stipulating that the additional director can hold office only upto 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, is not applicable to a producer company). Hence the proposed appointment of one expert director and one additional director is in order.

- ii) **Loan to a director:** Section 581ZK empowers the Board of directors to provide financial assistance to the members of the producer company subject to the provisions made in articles and also subject to certain conditions laid down in 581ZK(b). But any loan or advance to any director or his relative shall be granted only after the approval by the members in general meeting. (Proviso to Section 581ZK).

In view of the above, the directors must convene the general meeting and get the approval of the members before granting the proposed loan of `10,000 to X, a director of the company (According to Section 581C(5)a producer company is a private limited company and there is no limit to the number of its members).

- iii) **Donation to a Political Party:** Producer company shall not make directly or indirectly to any political party or for any political purpose to any person any contribution or subscription or make available any facilities including personnel or material (Second proviso to Section 581ZH). As the donation to a political party is prohibited, the company cannot donate Rs. 10,000 to a political party.

## **Question 10**

DHP Producer Company Limited, a producer company is having an average turnover of ` 7 crores in the last five years. Referring to the provisions of the Companies Act, 1956, answer the following:

- a) Is it obligatory for the company to appoint a whole time secretary?
- b) What consequences will follow in case the company does not comply with the provisions in relation to the above?

## **Answer**

**Secretary of Producer Company:** As per the provisions of Section 581X of the Companies Act, 1956, every Producer company having an average annual turnover exceeding rupees five crores in each of three consecutive financial years shall have a whole-time secretary, who possesses membership of the Institute of Company Secretaries of India constituted under the Company Secretaries Act, 1980. Hence, it is obligatory for DHP Producer Company Limited to appoint a whole time secretary. If a producer company fails to comply with this requirement, the company and every officer of the company who is in default, shall be punishable with fine which may extend to five hundred rupees for every day during which the default continues.

In the proceedings against a person in respect of an offence under this section, it shall be a defence to prove that all reasonable efforts to comply with the provisions of this section were taken or that the financial position of the company was such that it was beyond its capacity to engage a whole time secretary.

### **Annual General Meeting (Section 581ZA)**

## **Question 11**

A producer company was incorporated on 1<sup>st</sup> September, 2009. At present the paid-up share capital of the company is Rs. 10 lakhs consisting of 1,00,000 equity shares of ` 10 each fully paid-up held by 200 individuals and 20 producers institutions. You are required to answer the following with reference to the provisions of the Companies Act, 1956:-

- i) What is the time limit for holding the First Annual General Meeting and the subsequent Annual General Meetings?
- ii) What is the Quorum for the Annual General Meeting?
- iii) State the manner in which the voting rights of the members are determined.
- iv) Is it possible to remove a member?

## **Answer**

- i) **Annual General Meeting – The first annual general meeting of a producer company shall be held within 90 days of incorporation** i.e. on or before 29<sup>th</sup> November, 2009 in this case [Sec. 581 ZA(2)]. In the case of subsequent AGMs gap between two AGMs must not be more than 15 months. Registrar of Companies may extend the time for holding any AGM other than the first AGM by a period not exceeding 3 months for any special reason

[581ZA(i)]

- ii) Quorum Unless the articles of association of the producer company provide for a larger number, 1/4th of the total number of members of the producer company shall be the quorum for its annual general meeting. In this case the company has got 220 members. Hence the quorum is 55 [Sec. 581ZA(8)].
- iii) **Voting rights of members:** It depends on the type of membership. Where the membership consists of individuals and producer institutions, (as in this case) voting rights should be computed on the basis of a single vote for every member [Section 581D(c)]
- iv) **Removal of member:** No person, who has any business interest which is in conflict with business of the producer company, shall become a member of that company (Section 581D(4)). A person who has become a member of the producer company acquires any business interest which is in conflict with the business of the producer company, shall cease to be a member of that company and be removed as a member in accordance with the articles (Sec. 581D(5)).

### *Share Capital and Member Right (Section 581ZB – 581ZD)*

#### **Question 12**

Mr. Zameen, a member of a Producer Company, wants to transfer his shares. You are required to state as to how he can transfer his shares under the provisions of the Companies Act, 1956.

#### **Answer**

According to the provisions of section 581ZD (1) and (2) of the Companies Act, 1956, the shares of a member of a Producer Company shall not be transferable but a member of a Producer Company may after obtaining the previous approval of the Board, transfer the whole or part of his shares along with any special rights, to an active member at par value.

Based on the above provisions relating to the transfer of shares of a member in a Producer Company, Mr. Zameen has to obtain prior approval of the Board and then transfer his shares to an active member of the Producer Company at par value.

#### **Question 13**

An Inter-state co-operative society was incorporated on 1<sup>st</sup> May 2011 as a Producer company under the provisions of the Companies Act, 1956. Advise the company in respect of the following proposals:

- i) The company decides to have 18 Directors on its Board after incorporation.
- ii) Transferability of shares and
- iii) Share capital and voting rights.

#### **Answer**

- i) **Appointment of 18 directors:** According to Section 581O of the Companies Act, 1956, every producer company shall have at least 5 directors and not more than 15 directors. The

proviso to the Section states that in the case of the Inter-State Co-operative Society incorporated as a producer company, such company may have more than 15 directors for a period of one year from the date of its incorporation as a producer company.

Thus, in the instant case, an Inter-State Co-operative Society which was incorporated on 1st May, 2011 as a producer company can appoint 18 directors on its Board for a period of one year after incorporation.

ii) **Transferability of shares (Section 581ZD): According to the said provisions,**

- a) The shares of a member of a producer company shall not be transferable except as otherwise provided in sub-sections (2) to (4),
- b) A member of a producer company may, after obtaining the previous approval of the Board, transfer the whole or part of his shares along with any special rights, to an active member at par value.
- c) Every member within three months of his becoming a member, of Producer Company, nominate, as specified in articles, a person to whom his shares in the producer company shall vest in the event of his death.
- d) The nominee shall, on the death of the member, become entitled to all the rights in the shares of the producer company and the Board of that Company shall transfer the shares of the deceased member to his nominee:

Provided that in a case where such nominee is not a producer, the Board shall direct the surrender of shares together with special rights, if any, to the producer company at par value or such other value as may be determined by the Board.

e) Where the Board of a producer company is satisfied that—

- any member has ceased to be a primary producer; or
- any member has failed to retain his qualifications to be a member as specified in articles, the Board shall direct the surrender of shares together with special rights, if any, to the producer company at par value or such other value as may be determined by the Board:

Provided that the Board shall not direct such surrender of shares unless the member has been served with a written notice and given an opportunity of being heard.

iii) **Share capital and voting rights:** The share capital of a producer company shall consist of equity shares only. The shares held by a member in a producer company, shall as far as may be, be in proportion to the patronage of that company. (Section 581ZB)

The articles of any producer company may provide for the conditions, subject to which a member may continue to retain his membership, and the manner in which voting rights shall be exercised by the members. (Section 581D)

These voting's rights are:

- a) In a case where the member consists solely of individual member, the voting rights shall be based on a single vote for every member, irrespective of his shareholding or patronage of the producer company.
- b) In a case where the member consists of producer institutions only, the voting rights of such Producer institutions shall be determined on the basis of their participation in the business of the producer company in the previous year, as may be specified by articles.

Provided that during the first year of registration of a producer company, the voting rights shall be determined on the basis of the shareholding by such Producer institutions.

- c) In a case where the member consists of individuals and producer institutions, the voting rights shall be computed on the basis of a single vote for every member. However, a producer company may, if so authorised by its articles, restrict the voting rights to active member, in any special or general meeting.

Subject to Sections 581D, (1) & (3), every member shall have one vote and in the case of equality of votes, the Chairman or the person presiding shall have a casting vote except in the case of election of the Chairman.

### **Question 14**

Mr. Ramu, one of the members, nominated his son, Mr. Krishnan to be entitled to his shares in the event of his death. Mr. Ramu died. State the action that can be taken by the producer company in case Mr. Krishnan is not a producer.

### **Answer**

**Rights of the nominee related to transfer of shares of the deceased member** - According to Section 581ZD (3) every member shall within three months of his becoming a member of producer company nominate, as specified in articles, a person to whom his shares in the producer company shall vest in the event of death. The nominee shall become entitled to all the rights in the shares of the producer company in the event of death of the member. The Board of Directors of the producer company shall transfer the shares of Mr. Ramu to his nominee Mr. Krishnan.

In this case as the nominee is not a producer, action may be taken by the company under proviso to Section 581ZD(4). The Board of Directors of the producer company shall direct Mr. Krishnan to surrender the shares together with special rights. The surrender may be made either at par value or such other value as may be determined by the Board of Directors of the producer company.

### **Finance Accounts and Audit (Section 581ZE – 581ZJ)**

### **Question 15**

A Producer Company wants to issue bonus shares. You are required to state the relevant provisions of the Companies Act, 1956 in this regard.

## Answer

As per provisions of section 581ZJ of the Companies act 1956, any Producer Company may, upon recommendation of the Board and passing of resolution in the general meeting, issue bonus shares by capitalisation of amounts from general reserves referred to in section 581ZI in proportion to the shares held by the Members on the date of the issue of such shares.

## Question 16

- i) A two year old Producer Company registered under Section 581C of the Companies Act, 1956 wants to donate some amount. The Chief Executive of the Producer Company has approached you to advise him as to how and for what purposes the donation can be made by such company. Also state the monetary restrictions, if any, laid down in the Companies Act, 1956 on making donations by a Producer Company. You are informed that as per the Profit & Loss account of the Producer Company for its last accounting year, net profit was Rs. 20.00 lacs.
- ii) Is it obligatory for every producer company to appoint a whole time secretary under the provisions of the Companies Act, 1956?

## Answer

- i) As per provisions of section 581 ZH of the Companies Act, 1956, a Producer Company may, by special resolution, make donation or subscription to any institution or individual for the following purposes:-
  - a) For promoting the social and economic welfare of Producer Members or Producers or general public; or
  - b) For promoting the mutual assistance principles.

Thus as per the above stated provisions of the Companies Act, 1956, a Producer Company may make a donation by passing a special resolution and for the above mentioned purposes.

The 1<sup>st</sup> Proviso to the said section 581ZH lays down the monetary limit for making the donation by a Producer Company. According to the said proviso the aggregate amount of all such donation and subscription in any financial year shall not exceed 3% of the net profit of the Producer Company in the financial year immediately preceding the financial year in which the donation or subscription was made.

Since the net profit of the Producer Company as per its last profit & loss account was ` 20.00 lacs, it can make a total donation of Rs. 60,000/- in this year being three percent thereof.

- ii) Under section 581X of the Companies Act, 1956 every Producer Company having an average turnover exceeding Rs. 5 crores in each of three consecutive financial years shall have a whole time secretary who is a member of ICSI.

### **Question 17**

A Producer Company has received applications from Mr. Ramanathan, a Director of the Company, and Mr. Prem, a member of the Company, for grant of loan of ₹ 2,00,000 and ₹ 25,000 respectively. Discuss the relevant provision of the Companies Act, 1956 as to how the applications for grant of loan will be disposed of by the Company.

### **Answer**

Under Section 581ZK of the Companies Act, 1956, the Board of the Producer Company may, subject to the provision in the Articles of Association, **provide financial assistance by way of loan and advances against such security as may be specified in its Articles of Association** to any member repayable within a period exceeding three months but not exceeding seven years from the date of disbursement of such loan or advances.

In the instant case, member has applied for loan of Rs. 25,000. The period is not specified in the question. The Company may grant the member a loan of Rs. 25,000 against such security and at such rate of interest as may be specified in the Articles. **However, in the case of a director, loan of Rs. 2 lakh can be granted only after its approval by the members in general meeting.**

### **Question 18**

Southern India Sugar Producer Company Limited, having paid-up capital of Rs. 5 lakh and free reserves of 3 lakh, propose to make the following loans and investments:

- i) Loan of Rs. 2 lakh to Mr. Ram, a member of the Company, for a period of one year and a loan of Rs. 1 lakh to Mr. Shekhar, Director of the Company for a period of six months;
- ii) Investment of Rs. 3 lakh in the equity shares of XYZ Marketing Limited.

State the restrictions, if any, in this regard and also the legal requirements to be complied with by the Company under the provisions of the Companies Act, 1956.

### **Answer**

i) **Loan, etc., to member:** As per section 581ZK of the Companies Act, 1956, the Board may provide financial assistance to the members of the producer company, subject to the provisions made in articles, by way of—

- a) Credit facility, to any member, in connection with the business of the Producer company, for a period **not exceeding six months**;
- b) Loans and advances, against security specified in articles to any member, **repayable within a period exceeding three months but not exceeding seven years from the date of disbursement of such loan or advances.**

However, any loan or advance to any director or his relative shall be granted only after the approval by the members in general meeting.

Thus, according to the above provision, Southern India Sugar Producer Company Limited can give loan to Mr. Ram, a member of the company for the Period of 1 year as the Act provides that Board may provide loan to any member repayable within a period exceeding three months but not exceeding seven years from the date of disbursement of such loan.

Whereas in respect of Mr. Shekhar, a Director, company may give the loan only after the approval by the members in general meeting.

- ii) **Investment in other companies**: As per section 581ZL of the Companies Act, 1956, any producer company, either by itself or together with its subsidiaries, may invest, by way of subscription, purchase or otherwise, shares in any other company other than a producer company for an amount not exceeding thirty per cent of the aggregate of its paid -up capital and free reserves. Further, the provision provides that a producer company may, by special resolution passed in its general meeting and with prior approval of the Central Government, invest in excess of the limits.

Thus, according to the above provision, the Southern India Sugar Producer Company Limited cannot invest an amount exceeding thirty per cent of the aggregate of its paid-up capital and free reserves i.e. Rs. 2,40,000/- (i.e., 30% of 8,00,000) in XYZ Marketing Limited. However, the company may invest in excess of the limits (more than 2,40,000) by special resolution passed in its general meeting and with prior approval of the Central Government.

### ***Re-Conversion of Producer Company to Inter – state Co-operative Society (Section 581ZS)***

#### **Question 19**

NKM Producer Company passed a resolution at its general meeting on 30<sup>th</sup> April 2013 to reconvert the producer company into inter-state co-operative society under the provisions of the Companies Act, 1956. Advise the Company, as a professional, regarding the method to be followed for re-conversion of Producer Company to inter-state co-operative society under the above Act.

#### **Answer**

Reconversion of Producer Company into Inter-State Co-Operative Society: As per the provisions of Section 581ZS of the Companies Act, 1956, following is the method of reconversion:

- 2) **Application to the High Court**: Any producer company, being former an inter-State co-operative society, may make an application to the High Court for its re-conversion-
- after passing a resolution in the general meeting by not less than two third of its members present and voting;** or
  - on request by its creditors representing three-fourth value of its total creditors,**
- 3) **Holding of meeting**: The High Court shall, on the application made, direct holding of meeting of its members or such creditors, to be conducted in such manner as it may direct.

- 4) **Majority in agreement with reconversion:** If a majority in number representing three-fourths in value of the creditors, or members, present and voting in person at the meeting conducted in pursuance of the directions of the High Court, agree for re-conversion, if sanctioned by the High Court, be binding on all the members and all the creditors, and also on the company which is being converted. Before sanctioning reconversion, the court should be satisfied by affidavit or otherwise containing all material facts relating to the company.
- 5) **Filing of certified copy with Registrar:** An order made by the Court shall have no effect until a certified copy of the order has been filed with the Registrar.
- 6) **Copy of order to be annexed with every copy of Memorandum:** A copy of every such order shall be annexed to every copy of the Memorandum of the company issued after the certified copy of the order has been filed as aforesaid, or in the case of a company not having a Memorandum, to every copy so issued of the instrument constituting or defining the constitution of the company.
- 7) **Default in filing of certified copy:** If default is made in complying with filing of certified copy with the Registrar, the company, and every officer of the company who is in default, shall be punishable with fine which may extend to ` 100, for each copy in respect of which default is made.
- 8) **Stay on suit/proceeding until the disposal of application :** The Court may, at any time after an application has been made to it, stay the commencement or continuation of any suit or proceeding against the company, until the application is finally disposed of.
- 9) **Filing of an application under the Co-operative Society Act etc. after being sanctioned re-conversion by the High-Court:** Every producer company which has been sanctioned re-conversion by the High Court, shall make an application, under the Multi-State Co-operative Societies Act, 2002 or any other law for the time being in force for its registration as multi-State co-operative society or co-operative society, within six months of sanction by the High Court and file a report thereof to the High Court and the Registrar of Companies and to the Registrar of the co-operative societies under which it has been registered as a multi-State co-operative society or co-operative society as the case may be.

### Miscellaneous

#### Question 20

Under provisions of Companies Act, 1956, relating to producer company, examine whether the office of director of such company shall fall vacant in the following circumstances:

- i) X a Director of ABC Ltd., a producer company has made a default in payment of loan taken from a company and default continues for 60 days.
- ii) Z a Director of the above company could not call the Annual General Meeting for the company due to some natural calamity which occurred three days before the Schedule date.

## Answer

### **Producer Company – Vacation of Office of a Director:**

- i) According to provisions of Companies Act, 1956, as contained in section 581Q, if the producer company in which a director has made a default in repayment of any advances or loans taken from any company or institution or any other person and such default continues for 90 days, the office of such director shall become vacant. In the given case the default on the part of X, the director continues for less than 90 (i.e. only 60 days) days, the office of director shall not fall vacant.
- ii) The office of director of a producer company shall become Vacant if the Annual General Meeting or extraordinary general meeting of the producer company, in which he is a director, is not called in accordance with the provisions of this Act except due to natural calamity or such other reason. In the given case since the Annual General Meeting could not be held due to some natural calamity, the office of Z, the director shall not fall vacant. This is an exception.

## **Question 21**

Ideal Producer Co. Ltd. was incorporated on 1<sup>st</sup> April, 2009. Its paid up capital of ₹ 10 Lakh consists of 1 lakh equity shares of ₹ 10 each held by 100 individuals. There are 6 directors on its Board. Referring to the provisions of the Companies Act, 1956, answer the following:

- i) What is the quorum for the Annual General Meeting?
- ii) What is the quorum for the Board Meeting?
- iii) The Board of Directors wants to co-opt one expert in the field of agronomics, as Director on its Board. Whether is it permissible?
- iv) Is it obligatory for this company to have internal audit of its accounts for Financial Year 2015-16?

## Answer

- i) As per section 581 Y of the Companies Act, 1956, unless the Articles requires a larger number, one fourth of the total number of members of the producer company shall be the quorum at a general meeting. In this case, the company has got 100 members and hence, the quorum is 25.
- ii) Section 581 V of the Companies Act, 1956, provides that the quorum for a meeting of the Board shall be one third of the total strength of directors, subject to a minimum of three. In the given case, 1/3 of 6 directors comes to 2, but minimum required is 3, hence, the quorum will be 3 directors for a board meeting.
- iii) Section 581 P of the Companies Act, 1956, empowers the Board of Directors of a producer company to co-opt one or more experts as director, but not exceeding one fifth of the total number of directors. As there are 6 directors in the given case, hence, co-opting one expert on the Board will be in order.
- iv) Yes, as per section 581 ZF of the Companies Act, 1956, every producer company is

required to have internal audit of its accounts carried out by a Chartered Accountant at such intervals and in such manner as may be specified in the Articles.

### **Question 22**

**(RTP Nov 18)**

Raj shree Producer Co. Ltd. was incorporated on 1<sup>st</sup> April 2010. Its paid up capital is ₹ 10 lacs consists of 1 lac equity shares of ₹ 10 each held by 100 individuals. There are 6 directors on its Board. Referring to the provisions of the Companies Act, 1956, answer the following:

- (i) What is the quorum for the Annual General Meeting?
- (ii) What is the quorum for the Board Meeting?
- (iii) The Board of Directors wants to co-opt one expert in the field of agronomics, as Director on its Board. Whether is it permissible?
- (iv) Is it obligatory for this company to have internal audit of its accounts for Financial Year 2018-19?

### **Answer**

- (i) As per Section 581Y of the Companies Act, 1956, unless the Articles requires a larger number, one fourth of the total number of members of the producer company shall be the quorum at a general meeting. In this case, the company has got 100 members and hence, the quorum is 25.
- (ii) Section 581 V of the Companies Act, 1956 provides that the quorum for a meeting of the Board shall be one third of the total strength of directors, subject to a minimum of three. In the given case, 1/3 of 6 directors comes to 2, but minimum required is 3, hence, the quorum will be 3 directors for a board meeting.
- (iii) Section 581 P of the Companies Act, 1956 empowers the Board of Directors of Producer Company to co-opt one or more experts as director, but not exceeding one fifth of the total number of directors. As there are 6 directors in the given case, hence, co-opting one expert on the Board will be in order.
- (iv) Yes, as per Section 581ZF of the Companies Act, 1956, every producer company is required to have internal audit of its accounts carried out by a Chartered Accountant at such intervals and in such manner as may be specified in the Articles.

### **Question 23**

**(Nov 17)**

Examine whether the office of the director of the below mentioned producer company shall fall vacant in the following circumstances under the Companies Act, 1956/2013.

- (i) Mr. Right a director of Strawberry Limited a producer company has made a default in payment of loan taken from a company and the default continued for 60 days.
- (ii) Mr. Pure a director of the above company could not call an annual general meeting for the company due to some natural "calamity occurred three days before the scheduled date.

### **Answer**

- (i) In the question default is made by Mr Right, the director and hence he is covered in Section

**581Q(1)(c)** of the Companies Act, 1956 which provide that the office of the director of a producer company shall become vacant if he has made default in repayment of any advances or loans taken from the producer companies in which he is a director. Assuming that 'a company' referred in the question is Strawberry Limited, a producer company where he is a director, he vacates the office even when the default is for 60 days.

- (ii) The office of director of a producer company shall become vacant if the Annual General Meeting or extraordinary general meeting of the producer company, in which he is a director, is not called in accordance with the provisions of this Act except due to natural calamity or such other reason. In the given case, since the Annual General Meeting could not be held due to some natural calamity, the office of Mr. Pure, the director shall not fall vacant.

## **Question 24**

AVM Producer Company Ltd. seeks your advise on the following aspects of the working of a Producer company under the Companies Act, 1956 :-

- i) Criteria for appointment of Secretary as also the legal position, if its financial position is unsatisfactory.
- ii) Can the Board of Directors of the company direct its member to surrender his shares to the company, if so, under what circumstances?
- iii) Provisions relating to donation to any institution, as also to a political party.
- iv) Provisions relating to investment of general reserves, as also investment in the shares of a company, other than a Producer company.

## **Answer**

- i) **Secretary of a producer company** (Section 581X of the Companies Act, 1956): Every producer company having an average annual turnover exceeding five crore rupees in each of three consecutive financial years shall have a whole-time secretary, who possesses membership of the Institute of Company Secretaries of India constituted under the Company Secretaries Act, 1980. If a producer company fails to comply with this, the company and every officer of the company who is in default shall be punishable with fine which may extend to five hundred rupees for every day during which the default continues.

In any proceedings against a person in respect of an offence, under this section, it shall be a defense to prove that all reasonable efforts to comply with the provisions of section were taken or that the financial position of the company was such that it was beyond its capacity to engage a whole-time secretary.

- ii) **Surrender of shares** [Section 581ZD (5) of the Companies Act, 1956]: Where the Board of a producer company is satisfied that—
  - a) any member has ceased to be a primary producer; or
  - b) any member has failed to retain his qualifications to be a member as specified in articles, the Board shall direct the surrender of shares together with special rights, if

any, to the producer company at par value or such other value as may be determined by the Board:

Provided that the Board shall not direct such surrender of shares unless the member has been served with a written notice and given an opportunity of being heard.

iii) **Surrender of shares** [Section 581ZD (5) of the Companies Act, 1956]: Where the Board of a producer company is satisfied that—

- a) any **member has ceased to be a primary producer**; or
- b) any **member has failed to retain his qualifications to be a member as specified in articles**, the Board shall direct the surrender of shares together with special rights, if any, to the producer company at par value or such other value as may be determined by the Board:

Provided that the Board shall not direct such surrender of shares unless the member has been served with a written notice and given an opportunity of being heard.

iv) **Donations or subscription by producer company** (Section 581ZH of the Companies Act, 1956): A producer company may, by special resolution, make donation or subscription to any institution or individual for the purposes of—

- a) **promoting the social and economic welfare of producer member or producers or general public**; or
- b) **promoting the mutual assistance principles**:

Provided that the aggregate amount of all such donation and subscription in any financial year shall **not exceed three per cent of the net profit of the producer company in the financial year immediately preceding the financial year in which the donation or subscription was made**.

Further, no producer company shall make directly or indirectly to any political party or for any political purpose to any person any contribution or subscription or make available any facilities including personnel or material.

v) **Investment in other companies, formation of subsidiaries, etc.** (Section 581ZL): The producer company has to follow the following provisions under this section.

- a) The general reserves of any producer company shall be invested to secure the highest returns available from approved securities, fixed deposits, units, bonds issued by the Government or co-operative or scheduled bank or in such other mode as may be prescribed.
- b) Any producer company may, for promotion of its objectives acquire the shares of another producer company.
- c) Any producer company may subscribe to the share capital of, or enter into any agreement or other arrangement, whether by way of formation of its subsidiary company, joint venture or in any other manner with anybody corporate, for the

purpose of promoting the objects of the producer company by special resolution in this behalf.

- d) Any producer company, either by itself or together with its subsidiaries, may invest, by way of subscription, purchase or otherwise, shares in any other company, other than a producer company, specified under sub-section (2), or subscription of capital under sub-section (3), for an amount not exceeding thirty per cent of the aggregate of its paid-up capital and free reserves:

Provided that a producer company may, by special resolution passed in its general meeting and with prior approval of the Central Government, invest in excess of the limits specified in this section.

- e) All investments by a producer company may be made if such investments are consistent with the objects of the producer company.
- f) The Board of a producer company may, with the previous approval of members by a special resolution, dispose of any of its investments referred to in sub-sections (3) and (4).
- g) Every producer company shall maintain a register containing particulars of all the investments, showing the names of the companies in which shares have been acquired, number and value of shares; the date of acquisition; and the manner and price at which any of the shares have been subsequently disposed off.

The register referred to in sub-section (7) shall be kept at the registered office of the producer company and the same shall be open to inspection by any member who may take extracts there from.

## **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 purposes 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 and 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, telemedicine, 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.

#### *Documents etc. to be delivered to registrar by foreign companies (Section 380)*

#### 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 purposes 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. Ziyah 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, 2013.

## **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. Ziyah 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 Mandarin 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.

## **Question 7**

**(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 the foreign company to which the documents relate.

### ***Display of Name Etc. of Foreign Company (Section 382)***

#### **Question 8**

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 9**

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 10**

- 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 purposes 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.**

## **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 in 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.

*Government Companies (Section 394 – 395)*

**Question 2**

- 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 3**

BUI Limited had filed certain documents with the Registrar of Companies. The said documents were authenticated by the ROC and kept on record. In a suit against the company the ROC produced the said documents in the court of law. BUI Limited intends to raise objection on the said documents on the ground that the documents need to be authenticated with further proof or production of the original document as evidence. Advise BUI Limited.

#### **Answer**

**Admissibility of certain documents as evidence:** **Section 397** of the Companies Act, 2013 provides for admissibility of certain documents as evidence. According to the provisions of that section, any document reproducing or derived from returns and documents filed by a company with the Registrar on paper or in electronic form or stored on any electronic data storage device or computer readable media by the Registrar, and authenticated by the Registrar or any other officer empowered by the Central government in such manner as may be prescribed, shall be deemed to be a document for the purposes of this Act and the rules made thereunder and shall be admissible in any proceedings thereunder without further proof or production of the original as evidence of any contents of the original or of any fact stated therein of which direct evidence is admissible.

On the grounds stated above, **BUI Limited cannot validly raise any objection on the documents already filed by it with the Registrar.**

#### **Question 4**

**(RTP Nov 18)**

XYZ Ltd. had filed certain documents with Registrar of Companies (RoC). The said documents were authenticated by the ROC and kept on record. In a suit against the company the RoC produced the said documents in the court of law. XYZ Ltd. intends to raise objection on the said documents on the ground that the documents need to be authenticated with further proof or production of the original document as evidence. Advice XYZ Ltd. as per the provisions of the Companies Act, 2013.

## **Answer**

### **Admissibility of certain documents as evidence:**

Section 397 of the Companies Act, 2013 provides for admissibility of certain documents as evidence. According to the provisions of that section, any document reproducing or derived from returns and documents filed by a company with the Registrar on paper or in electronic form or stored on any electronic data storage device or computer readable media by the Registrar, and authenticated by the Registrar or any other officer empowered by the Central Government in such manner as may be prescribed, shall be deemed to be a document for the purpose of this Act and the rules made thereunder and shall be admissible in any proceedings thereunder without further proof of production of the original as evidence of any contents of the original or of any fact stated therein of which direct evidence is admissible.

On the ground stated above, XYZ Ltd. cannot validly raise any objection on the documents already filed by it with the Registrar.

## **Miscellaneous Provisions**

### **Question 5**

**(May 2017 & RTP – May 2018)**

Mr. Atharva, a director of Northway highway Tolls Private Limited, authorised by board of directors to prepare and file return, report or other documents to registrar on behalf of the company. He timely filed all the required documents to Registrar; however, subsequently it is found that the filed documents are false in respect to material particulars (knowing it to be false) submitted to registrar. Explain the penal provision under the Companies Act, 2013.

## **Answer**

According to **section 448** of the Companies Act, 2013, if any person makes a statement which is false in any material particulars, knowing it to be false or omits any material facts, knowing it to be material, such person shall be liable under section 447. As per Section 447, any person who is found to be guilty under this section 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. Provided that, **where the fraud involves public interest, the term of imprisonment shall not be less than 3 years.**

Hence, Mr. Atharva, a director of Northway highway Tolls Private Limited shall be punishable with imprisonment and fine prescribed as aforesaid.

### **Question 6**

Gulmohar Ltd., a company registered under Indian law owns a factory in Calcutta, wherein it manufactures jute products. By a notification of the State Government, issued during October, 2013, due to a strike and lock-out, it was declared a relief undertaking. After four months, in February, 2014, the lock-out was lifted. However, during the said period the company's directors defaulted in payment of Provident Fund (PF) and other ancillary dues. During the month of December, 2013, the Regional PF Commissioner initiated criminal proceedings against the company and its directors under the Employees PF and Miscellaneous Provisions

Act, 1952, for default and delay in payment of PF dues.

Immediately the directors of the company applied to the High Court for relief under Section 463 of the Companies Act, 2013, praying for relief from liability under the PF law. The petition is now pending before a single judge. The company desire to know from you, as to the tenability of their claim for relief at the High Court, and as to whether they would be excused and exonerated by the High Court, in respect of the contraventions committed under the PF law.

Briefly discuss the law on the subject and state whether the petition filed by the directors would be admitted or not under the Companies Act, 2013.

### **Answer**

The crux of the matter involved in the above case, is whether under **section 463 (1)** the words “any proceeding” against an officer of a company, would mean only a proceeding under the Companies Act or any Criminal proceeding under any other law. The provisions of the Companies Act, define “officer” and “officer in default” but there is no definition for the word “proceeding”. In the present case, the proceeding has not resulted from or has not been brought about as a consequence of default, refusal, contravention, non-compliance or failure under the Companies Act, 2013, but has come about as a result of certain acts and omissions committed by the directors of Gulmohar Ltd., under the Employees PF and Misc. Provisions Act, 1952.

It should be noted that the Court has powers under **Section 463** to grant relief only to a director/officer of a company, and is not applicable to the company. Hence, the company cannot claim relief under section 463 of the Companies Act, 2013.

The significance of the words “in any proceeding” at the beginning of Section 463(1) require to be understood.

The facts of the case, bear resemblance to those which came up before their Lordships of the Supreme court in Rabindra Chamaria and Others Vs Registrar of Companies, West Bengal and others, 1992 (73) Comp. Cas. 257 (SC).

Going by the tenor of section 463 of the Companies Act, 2013 and the Supreme Court ruling the **directors of Gulmohar Ltd., cannot avail of relief under Section 463 of the Companies Act, 2013 and their Petition is not likely to succeed. It is liable to be dismissed.**

### **Question 7**

It is apprehended by the Directors of a Public Company that they are likely to be prosecuted for an offence under the Companies Act, 2013 which is not compoundable. Explain the provisions of the Companies Act, 2013 under which the Directors can seek relief from the liability for offence. What will be the position in case prosecution has already been launched?

### **Answer**

**Relief under Section 463:** Under section 463(1) of the Companies Act, 2013 if in any proceeding for negligence, default, breach of duty, misfeasance or breach of trust against an

officer of a company, it appears to the court hearing the case he is or may be liable in respect of the negligence, default, breach of duty, misfeasance or breach of trust, but that he has acted honestly and reasonably, and that having regard to all the circumstances of the case, including those connected with his appointment, he ought fairly to be excused, the court may relieve him, either wholly or partly, from his liability on such terms, as it may think fit.

**Provided that in a criminal proceeding under this sub-section, the court shall have no power to grant relief from any civil liability which may attach to an officer in respect of such negligence, default, breach of duty, misfeasance or breach of trust.**

In the given case, the offence is not compoundable i.e. it carries imprisonment as a punishment either alone or with a fine. In either case, it would indicate that a criminal liability is indicated. Hence, the court will not have the power to grant relief under section 463. However, the nature of the offence will have to be examined.

## **Question 8**

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 20 lakh rupees or with both.**

## **Question 9**

**(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'.**

## **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.

## **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 1<sup>st</sup> April, 2014 vide notification dated 26<sup>th</sup> 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 aggrieved 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 class 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.

## **Ch 12 – National Company Law Tribunal and Appellate Tribunal**

### *Qualification of President and Members of Tribunal (Section 409)*

#### **Question 1**

As per the Companies Act, 2013, what are the required qualifications for appointment as President and Judicial members of the National Company Law Tribunal

#### **Answer**

Section 409 of the Companies Act, 2013, deals with qualifications of the President and members of Tribunal.

- (i) **Qualification for the President:** He shall be a person who is or has been a Judge of a High Court for five years.
- (ii) **Qualification for the Judicial member:** A person shall not be qualified for appointment as a Judicial Member unless he is or has been—
  - a) a judge of a High Court; or
  - b) a District Judge for at least five years; or
  - c) an advocate of a court for at least ten years.

For the purposes of clause (3) above, in computing the period for which a person has been an advocate of a court, there shall be included any period during which the person has held judicial office or the office of a member of a tribunal or any post, under the Union or a State, requiring special knowledge of law after he become an advocate.

### *Term of Office of President, Chairperson and other Members (Section 413)*

#### **Question 2**

Mr. D was appointed as a Technical Member of the National Company Law Tribunal (NCLT) on 1st July, 2012 for a period of 5 years. He will be completing 62 years on 30th June, 2017.

Whether he can be re-appointed on the NCLT on completion of his tenure in 2017?

#### **Answer**

1. **Term of holding office in the case of Tribunal:** According to section 413 (1), the President and every other Member of the Tribunal shall hold office for a term of 5 years from the date on which he enters upon his office and shall be eligible for re appointment for another term of 5 years.
2. **Age bar on holding of office:** Under section 413 (2), a Member of the Tribunal shall hold office as such until he attains,—
  - (a) in the case of the President, the age of 67 years;
  - (b) in the case of any other Member, the age of 65 years.

In the instant case, Mr. D was appointed as a technical Member of the NCLT on 1st July, 2012 for a period of 5 years. He will be completing 62 years on 30th June, 2017. He can also be re-appointed after his initial term of five years is over. But since he shall be attaining the age of 65 years as on 30th June, 2020, he will have to step down from the post on his attaining the age of 65 years i.e. on 30th June, 2020.

### *Resignation of Members (Section 416)*

#### **Question 3**

Mr. Ram was appointed as the member of the National Company Law Tribunal. He (at the age of 63 years) has now resigned from his office by giving a notice to the Central Government, by stating that he will stop acting as a member to NCLT with immediate effect.

The Central Government tells him that you have to continue in office for 3 more months. Is the contention of Central Government correct?

#### **Answer**

According **section 416**, the President, the Chairperson or any Member may, by notice in writing under his hand addressed to the Central Government, resign from his office.

Provided that the President, the Chairperson, or the **Member shall continue to hold office until the expiry of 3 months** from the date of receipt of such **notice by the Central Government or until a person duly appointed as his successor enters upon his office or until the expiry of his term of office, whichever is earliest.**

Thus, Mr. Ram shall continue to hold office until the expiry of 3 months from the date of receipt of such notice by the Central Government or until a person duly appointed as his successor enters upon his office, whichever is earliest.

**Hence, the contention of Central Government is correct.**

### *Removal of Members (Section 417)*

#### **Question 4**

**(RTP Nov 18)**

Mr. PRTJ was appointed as a member of the National Company Law Appellate Tribunal. During the month of April, 2018, he was adjudged as an insolvent by a competent authority. The Central Government after consultation with the Chief Justice of India removed Mr. PRTJ from the membership of the National Company Law Appellate Tribunal. Being aggrieved by the decision of the Central Government, Mr. PRTJ approached you to confirm himself whether the decision of the Central Government was appropriate since, he was not given a reasonable opportunity of being heard as a matter of principle of natural justice. Advise him.

Also state the circumstances in which the Central Government after consultation with the Chief Justice of India can remove any person from the office of President, Chairperson or any Member of the National Company Law Appellate Tribunal.

Your answer should refer to the relevant provisions of the Companies Act, 2013.

## **Answer**

According to **Section 417(1)** of the Companies Act, 2013, the Central Government may, after consultation with the Chief Justice of India, remove from office the President, Chairperson or any Member, who—

- (a) has been **adjudged an insolvent**; or
- (b) has been **convicted of an offence** which, in the opinion of the Central Government, involves moral turpitude; or
- (c) **has become physically or mentally incapable of acting as such President, the Chairperson, or Member**; or
- (d) **has acquired such financial or other interest as is likely to affect prejudicially his functions as such President, the Chairperson or Member**; or
- (e) **has so abused his position as to render his continuance in office prejudicial to the public interest**:

Provided that the President, the Chairperson or the Member shall not be removed on any of the grounds specified in clauses (b) to (e) without giving him a reasonable opportunity of being heard.

As per the proviso stated above, in case of sub-clause (a), i.e. where there is a case of insolvency, there is no requirement of giving an opportunity of being heard by the member of the NCLAT. Hence, the action taken by the Central Government against PRTJ is valid.

### **Circumstances under which the Central government can remove the President, the Chairperson etc.,**

According to Section 417(2) of the Companies Act, 2013, the President, the Chairperson or the Member shall not be removed from his office except by an order made by the Central Government on the ground of proved misbehavior or incapacity after an inquiry made by a Judge of the Supreme Court nominated by the Chief Justice of India on a reference made to him by the Central Government in which such President, the Chairperson or Member had been informed of the charges against him and given a reasonable opportunity of being heard.

In the instant case, it is advised that the decision of the Central Government to remove (without giving reasonable opportunity of being heard) **Mr. PRTJ, member of NCLAT who was adjudged as an insolvent by a competent authority is appropriate as per the clause (a) of Section 417(1) of the Companies Act, 2013**

### ***Appeal to Supreme Court (Section 423)***

## **Question 5**

***(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 5<sup>th</sup> 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 5<sup>th</sup> 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 – 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 2<sup>nd</sup> 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 1<sup>st</sup> 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 Chairman 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 2<sup>nd</sup> 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."

# **CA Final Corporate and Economic Laws**

**Nov 2018**

**Q 1)**

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

- i) It is 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 director can be consider as an Independent Director?
- iv) When does a person appointed as a small shareholders director vacate his office?

Advice suitably in the light of the provisions of the Companies Act, 2013 and the rules frame thereunder.

**(8 Marks)**

b) 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 on 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?

**(6 Marks)**

- c)
- i) 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.

**(2 Marks)**

- ii) 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.

**(4 Marks)**

Q 2)

- a) (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?
- iii) (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. **(7 Marks)**

- b) An investigation was ordered by the Central Government under Section 216 of the Companies Act, 2016, against PKR Limited for determining the true membership of the Company. In connection with this investigation, it appears to the Tribunal that there is good reason to find out the relevant facts about 9% Redeemable Cumulative Preference Shares (RCPS) issued by the Company on 15.10.2017 and the Tribunal is of the opinion that unless restriction is imposed on further issue of such shares, the purpose cannot be solved. Accordingly, the Tribunal, by an Order dated 15.08.2018, directed the Company that the further issue of RCPS shall be subject to restrictions for a period of four years. Despite the Order of the Tribunal as above, PKR Limited proceeded with further issue of RCPS on 20.08.2018 in order to fund the working capital requirements for its expansion project. Referring to the provisions of the Companies Act, 2013, examine the following:
- Can the Tribunal restrict further issue of RCPS? If yes, then to what period?
  - What are the penal provisions in case of contravention to the above Order? **(5 Marks)**

- c) What are the powers of the Central Government under the Companies Act, 2013 regarding appeal against acquittal? **(2 Marks)**
- d) An Association registered under The Foreign Contribution (Regulation) Act, 2010 (the Act) received donation from a club registered in Singapore. The Association proposes :
- 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,
  - 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? **(6 Marks)**

Q 3)

- a) 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 of 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 is valid and maintainable? **(3 Marks)**

- b) In the light of the provisions of the Companies Act, 2013 explain whether the following Companies can be considered as a 'Foreign Company':
- A Company which has no place of business established in India, yet, is doing online business through telemarketing in India.
  - A Company which is incorporated outside India employs agents in India but has no place of business in India.
  - A Company incorporated outside India having shareholders who are all Indian citizens.

**(8 Marks)**

- c) 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, 1957. Also state whether any question of fact arising out of the Order of SAT can be challenged in the appeal?

**(3 Marks)**

- d) 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.

**(6 Marks)**

Q 4)

- a) Mr. Gopi is the Managing Director of LGB Limited. The Company wants to vacate the post of Managing Director on March 31, 2018 and appoint Mr. Lakshmikant in place of Mr. Gopi due to hands on experience and better track records. The tenure of appointment of Mr. Gopi is upto 30th June, 2022 with the condition that he will get compensation in case of early vacation of his office due to the Company's requirements. Mr. Gopi was drawing following remuneration during the last five financial years:

Financial Year	Remuneration (₹ in Lakhs)
2013-14	30
2014-15	35
2015-16	40
2016-17	45
2017-18	50

Mr. Gopi approaches you to know the amount of compensation he will eligible to get from LGB Limited as per the provisions of the Companies Act, 2013. Advise.

What will be your answer if a person is only an ordinary director but neither the Managing Director nor a manager of the Company? **(8 Marks)**

- b) 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? **(6 Marks)**

- c) A Bank issued a notice pursuant to Section 13 of the SARFAESI Act, 2002 to a Company to discharge its loan which has already become time barred under the Limitation Act, 1963. The Company did not settle the loan beyond the prescribed notice period. The Bank took recourse under Section 13(4) of the SARFAESI Act, 2002 to take possession of the building to enforce its Security interest. Discuss whether the Bank will succeed in its attempt. State whether the provision of SARFAESI Act, 2002 can override any other law? **(2 Marks)**

- d) As on March 31, 2018, 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, 2018 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? **(4 Marks)**

Q 5)

- a) VGP Ltd. is a listed public Company with a paid up capital of ₹ 100 crores as on 31<sup>st</sup> March, 2018. Mrs. Jasmine, who was one of the promoters of PDS Ltd. (a joint venture company of VGP Ltd.), was appointed as woman director on the Board of VGP Ltd. VGP Ltd has the following proposals:

- i) To remove Mr. Z, an Independent Director who re-appointed for a second term.
- ii) To appoint Mr. N, a nominee Director in the Board as an Independent Director.
- iii) To appoint Mrs. Jasmine as an Independent-cum-Woman Director.

With reference to the relevant provisions of the Companies Act, 2013, examine:

- i) The validity the above proposals and the appointment of Woman Director already made.
- ii) Whether Mr. N, can be appointed as an Independent Director of PDS Ltd.?
- iii) Is an Independent Director entitled for stock option? **(8 Marks)**

- b) Rajshree Producer Co. Ltd. was incorporated on 1st April, 2010. Its paid up capital ₹ 10 Lakhs consists of 1 Lakh equity shares of ₹ 10 each held by 100 individuals. There are 6 directors on its Board.

Referring to the provisions of the Companies Act, 1956, answer the following:

- i) What is the quorum for the Annual General Meeting?
- ii) What is the quorum for the Board Meeting?
- iii) The Board of Directors wants to co-opt one expert in the field of agronomics, as Director on its Board. Whether it is permissible?
- iv) Is it obligatory for this Company to conduct internal audit of its accounts for Financial Year 2017-18? **(6 Marks)**

- c) XY Ltd. filed a petition under Insolvency and Bankruptcy Code, 2016 with NCLT against DP Ltd. {Corpora 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 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. **(6 Marks)**

Q 6)

- a) The Articles of Association of a listed company provides for fixed payment of sitting fee for each meeting of Directors subject to maximum of ₹ 30,000. In view of the increased responsibilities of Independent Directors of listed Companies, the Company proposes to increase the sitting fee to ₹ 45,000 per meeting. Advise the Company about the requirement under the Companies Act, 2013 to give effect to the proposal. **(4 Marks)**

OR

ABC Limited is an unlisted public Company having a paid up equity share capital of ₹ 20 Crores and a turnover of ₹ 150 Crores as on 31st March, 2018. The total number of Directors on the Board is 13.

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

- i) The minimum number of Independent Directors that the Company should appoint.
  - ii) How many Independent Directors are to be appointed in case ABC Limited is a listed Company?
- 
- b) 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. **(2 Marks)**

c) 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'? **(8 Marks)**

d) 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? **(3 Marks)**

e) 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. **(3 Marks)**