GUIDELINE ANSWERS

PROFESSIONAL PROGRAMME

DECEMBER 2018

MODULE 1

THE INSTITUTE OF
Company Secretaries of India
भारतीय कम्पनी सचिव संस्थान
IN PURSUIT OF PROFESSIONAL EXCELLENCE
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These answers have been written by competent persons and the Institute hope that the **GUIDELINE ANSWERS** will assist the students in preparing for the Institute's examinations. It is, however, to be noted that the answers are to be treated as model answers and not as exhaustive and the Institute is not in any way responsible for the correctness or otherwise of the answers compiled and published herein.

The Guideline Answers contain the information based on the Laws/Rules applicable at the time of preparation. However, students are expected to be well versed with the amendments in the Laws/Rules made upto **six** months prior to the date of examination.

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MODULE 1

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PROFESSIONAL PROGRAMME EXAMINATION

DECEMBER 2018

ADVANCED COMPANY LAW AND PRACTICE

Time allowed : 3 hours *Maximum marks : 100*

NOTE : *1. Answer **ALL** Questions.*

2. All references to sections relate to the Companies Act, 2013 unless stated otherwise.

Question 1

(a) Sun Ltd made the following offers during the financial year 2017-18 on private placement basis :

(i) 10,00,000 equity shares of ₹10 each at an issue price of ₹25 each, to 230 persons, which included 25 Qualified Institutional Bidders;

(ii) Under the above equity issue, 10,000 shares offered to Ram, were allotted to Shyam, his brother in whose favor, Ram had renounced the offer;

(iii) 2,00,000 equity shares of ₹10 each to 50 employees of the Company under ESOP scheme;

(iv) 5,00,000 preference shares of ₹100 each at par, to 150 persons.

Do you find any violation of private placement provisions by the Company ? Will your answer be different if Sun Ltd was a housing finance company registered with the National Housing Bank under National Housing Bank Act 1987 ?
(5 marks)

(b) Draft a resolution to be passed by the Board of Directors of a Company for the removal of the auditor of the Company covering also the incidental matters.
(5 marks)

(c) Divya, a director in 3 companies, finds that she has three DIN obtained on different occasions by mistake. DIN 1 is mapped to X Ltd while DIN 2 is mapped to Y Ltd and DIN 3 to Z Ltd. Has she contravened any provision of the Act and if so, what is the remedy ? *(5 marks)*

(d) Target Ltd convened a meeting of the Board of Directors on 1st September 2018 to approve the financial statements of the Company as on 31st March 2018. The Board has strength of 5 directors and the quorum as per Articles of Association is 3 directors physically present. While 3 directors participated in the meeting physically, the fourth and the fifth directors participated through video conferencing. Do you see any violation on the part of the Company ?
(5 marks)

Answer 1(a)

As per Rule 14 of the Companies (Prospectus & Allotment of Securities) Rules 2014, an offer under private placement shall be made to not more than 200 persons in

the aggregate in a financial year, subject to a proviso that offer made to Qualified Institutional Buyers (QIB) and employees under ESOP scheme will not be counted for this limit of 200. Further, the above restriction will be reckoned individually to each kind of security. Rules provide that no person other than the person so addressed in the application form shall be allowed to apply through such application form and any application not conforming to this condition shall be treated as invalid.

In view of the above,

(i) the offer made to 230 persons including 25 QIBs is a violation of the rules, as the total number of offers made excluding QIBs exceeds 200.

(ii) Section 42 read with Rules provide that no person other than the person so addressed in the application form shall be allowed to apply through such application form and any application not conforming to this condition shall be treated as invalid. Therefore, Ram to whom the offer was made, cannot renounce in favor of Shyam and hence any allotment to Shyam is invalid in terms of private placement rules.

(iii) the offer made to 50 employees under ESOP scheme is in order as it is specifically excluded from the limit of 200.

(iv) offer of preference shares made to 150 persons is also in order as the limit of 200 is to be reckoned separately for each kind of security.

These limits are not applicable to a Housing Finance Company registered under the National Housing Bank Act, 1987 and hence, in that case, all the above offers of Sun Limited will be valid.

Answer 1(b)

BOARD RESOLUTION FOR REMOVAL OF THE AUDITOR

RESOLVED THAT pursuant to Section 140(1) of the Companies Act 2013 read with Rule 7 of the Companies (Audit and Auditors) Rules 2014, subject to the approval of shareholders at a general meeting and subject to the approval of Central Government (powers has been delegated to Regional Director) in this behalf, Mr. X, Chartered Accountant, the auditor of the Company be removed from his office as auditor.

RESOLVED FURTHER THAT an Extraordinary General Meeting of the Company be held at 1600 Hrs on 14th October 2018 at the Residency Hall, Mahatma Gandhi Road, Kanpur, to transact the business as set out in the draft notice of the meeting tabled at this meeting which, together with the explanatory statement to be annexed thereto, are approved.

RESOLVED FURTHER THAT Mr. Y, Company Secretary of the Company, is hereby authorized to issue the notice of the Extraordinary General Meeting to the members of the Company.

RESOLVED FURTHER THAT Mr. Y, Company Secretary of the Company, is hereby authorized to inform the Auditor of the decision of the Board as required under the Act.

RESOLVED FURTHER THAT Mr. Y, Company Secretary of the Company, is hereby

authorized to digitally sign e-form ADT-2 for making an application to the Central Government for approval for the removal of the Auditor under Section 140 of the Act.

Answer 1(c)

Sec 155 of the Companies Act, 2013 provides that no individual, who has already been allotted a DIN under Sec 154, shall apply for, obtain or possess another DIN. Thus, Divya has violated Sec 155 and has to surrender the two additional DIN possessed by her. She has to file e form DIR-5 to surrender the two extra DIN obtained by her, explaining that the two extra DIN were obtained by mistake and without any malafide intentions. MCA (Ministry of Corporate Affairs) has clarified in its website that in such cases, the oldest DIN will be retained and all the subsequent DIN in currency shall be surrendered. All the entities with which Divya is connected shall be mapped to the oldest DIN while subsequently obtained DIN will be cancelled. [Refer Rule 11(1)(f) of Chapter 11.]

Answer 1(d)

Rule 4 of the Companies (Meetings of Board and its Powers) Rules 2014 stipulates that approval of annual financial accounts cannot be dealt with in any meeting held through video conferencing or other audiovisual means. The board meeting held by Target Ltd on 1st September 2018 is attended by three directors physically present which satisfies the quorum requirement and hence is not a meeting conducted through video-conferencing or audiovisual means. Hence Target Ltd can transact the business of approval of financial statements of the company at such meeting. Sec 173(2) further provides that where there is quorum in a meeting through physical presence of directors, any other director may participate through video conferencing or other audiovisual means in such a meeting. In view of the above, Target Ltd has not violated any rule in the given occasion.

Attempt all parts of either Q. No. 2 or Q. No. 2A

Question 2

(a) X Ltd, an unlisted public company, with the following :

Paid-up share capital	*₹ 25 Crore*
Reserves & Surplus	*₹ 40 Crore*
Annual turnover	*₹ 300 Crore*

wants to accept deposits from its members and the public. Advise the company on the compliance required. *(4 marks)*

(b) Infra Ltd came out with an IPO of equity shares in April 2018. The prospectus issued for the purpose explained that the purpose of the IPO was to fund a 1000 MW mega solar power project and substantiated the position by citing the contract they have won from Solar Power Corporation with a tariff rate of ₹4.00 per kWhr. Prashant subscribed to the IPO for 50,000 equity shares at ₹10 each, which was duly allotted by the company. Subsequently in July 2018, the Company came out with an update that the tariff rate in the above contract has been slashed down to ₹3.00 per kWhr. Prashant is of the view that the company will lose money with such a low tariff and would not like to continue his investment

in the company. The said equity share was trading at ₹7.00 in the market. Is there any remedy available to Prashant ? Advise. *(4 marks)*

(c) *Liberty Ltd, an unlisted company, registered in the state of Maharashtra with 20 shareholders wants to organize the annual general meeting of the company for the financial year 2017-18 as under :*

(i) *The meeting shall be held on 17th September 2018 which happens to be Raksha Bandhan, a day declared as holiday by Maharashtra Government.*

(ii) *The venue for the meeting shall be Ootacamund, a hill resort in Tamil Nadu. Advise the Company on the feasibility of the above.* *(4 marks)*

(d) *Peak Ltd, a listed company, proposes to issue Non-Convertible Debentures for an amount of ₹500 Crores to the public, incorporating call and put options only to the retail investors. Enumerate the conditions to be complied for the purpose.* *(4 marks)*

OR (Alternate question to Q. No. 2)

Question 2A

(i) *Comment if the following transactions entered into by A Ltd attract compliance with provisions relating to acceptance of deposit.*

(a) *A sum of ₹5 lakh paid by Gautam towards subscription to equity shares on 1st April 2018 was adjusted towards sales invoices for goods supplied to him on 31st August 2018.*

(b) *Ashwin, a director of the Company, arranged for ₹10 lakh to meet an emergency requirement, by taking a personal loan from State Bank of India.*

(c) *Bharat, a customer who has bought a machinery from the Company has paid a sum of ₹5 lakh towards life-time warranty for the machinery.*

(d) *A sum of ₹1 lakh collected from every employee in April 2018 towards contribution to a Housing Society which will be formed in January 2019.* *(4 marks)*

(ii) *Smart Ltd, a listed company, has a paid-up share capital of ₹50 crore divided into 50 Lakh equity shares of ₹100 each, carrying a voting right of one vote per share. The Company needs infusion of funds but the promoters of the Company do not prefer dilution of control. Hence it is proposed to issue further equity shares carrying a voting right of one vote for every 10 equity shares. Advise the Board of Directors on the eligibility conditions to be complied.* *(4 marks)*

(iii) *Healthy Ltd provides the following information for the financial year ended 2017-18 :*

- *Paid-up share capital – ₹50 Crore*
- *Profit after tax – ₹10 Crore*
- *The investments have been valued at fair market value which resulted in a gain of ₹2 Crore.*

- *The fixed assets of the Company have been revalued during the year resulting in a gain of ₹1 Crore.*
- *Average dividends declared during the previous three years – 12%.*

Calculate the available surplus for the purpose of dividend and the maximum percentage of dividend that can be declared by the company, assuming a 100% payout.

Further, during the current financial year 2018-19, the Company has made a loss in the first two quarters and the company wants to declare an interim dividend of 15% for the financial year 2018-19. Is this feasible ? (4 marks)

(iv) X Ltd is a wholly owned subsidiary of Y Ltd. As on 31st March 2018, X Ltd owns 60% of equity in A Ltd and 26% of equity in B Ltd. Y Ltd has totally 8 shareholders. Y Ltd files consolidated accounts of all subsidiaries in accordance with Schedule III of the Act and the relevant accounting standards. Advise the Board of Directors of X Ltd if they are required to consolidate the financial statements of A Ltd and B Ltd while presenting their financial statements mandatorily. (4 marks)

Answer 2(a)

X Ltd does not fall under the definition of "eligible company" under the Companies (Acceptance of Deposits) Rules 2014, the primary condition of which is that a public company shall have net worth of not less than Rs. 100 crores or turnover of not less than Rs. 500 crore. In the present case, neither of the threshold limits are met, therefore, X Ltd is not an "eligible company".

In the present case, X Ltd can accept deposits only from members of the Company up to a limit of 35% of the aggregate of the paid-up share capital, free reserves and securities premium account. X Ltd can accept deposits from its members up to an amount of 35% of Rs. 65 Crore. They cannot accept any deposit from the public. However, there is no limit for acceptance of deposit from its directors.

X Ltd is required to ensure inter alia compliance of the following, for acceptance of deposits from members:

(i) The Company is required to pass an ordinary resolution in the shareholders meeting authorizing the acceptance of deposit from the members.

(ii) A Circular should be issued to its members in form DPT-1 and in addition, the company may publish the same in English language in one English newspaper and one vernacular language in vernacular newspaper having wide circulation in the state of the registered office of the company.

(iii) The Company should obtain a credit rating before the submission of the circular to the Registrar as disclosure of the same is required in the circular.

Answer 2(b)

Sec. 27 of the Companies Act, 2013 provides that where there is a variation in the contract indicated in the prospectus, on the basis of which the Company issued securities, the Company needs to get the approval of the shareholders in the general meeting by way of a special resolution. The dissenting shareholders, being those shareholders who

have not agreed to the proposal to vary the said terms of contract referred to in the prospectus, shall be given an exit offer by the promoters or controlling shareholders of the Company at such exit price and terms and conditions as may be specified by SEBI. Thus, Prashant can exercise the exit offer made by the Company and mitigate his loss.

Answer 2(c)

(i) Sec 96(2) of the Companies Act, 2013 provides that every annual general meeting shall be called on any day that is not a national holiday. Hence, Raksha Bandhan, not being a national holiday but only a local holiday declared by the Government of Maharashtra, calling of annual general meeting on that day does not violate the rules.

(ii) The Section further provides that the annual general meeting shall be held at the registered office of the company or at some other place within the city, town or village in which the registered office of the company is situated. The section has a proviso that the annual general meeting of an unlisted company may be held at any place in India if consent is given in writing or by electronic mode by all the members in advance. So, in this case, if Liberty Ltd, being an unlisted company, can obtain a consent in writing or through electronic mode from all the 20 shareholders of the Company, then the meeting can be validly held at Ootacamund.

Answer 2(d)

A call option is one where the company issuing the NCDs has a right to recall the securities prior to maturity and put option is one where the investors get a right to redemption of the securities prior to maturity.

Peak Ltd, while making the offer for issue of NCDs with call and put option only to the retail investors, shall ensure compliance with the following conditions:-

(i) Such right shall be exercised in accordance with the terms of issue like the date from which such right is exercisable, period of exercise which shall not be less than 3 working days, redemption amount including the premium or discount at which the redemption shall take place etc.

(ii) The call or put option may be exercised for the entire securities issued or invested or only for a part of the issue.

(iii) In case of exercise on part of the issue, it shall be done on proportionate basis only.

(iv) No such right shall be exercisable before the expiry of 24 months from the date of issue of the securities.

(v) Peak Ltd shall send notice to all the eligible holders of such securities at least 21 days before the date from which such right is exercisable.

(vi) Peak Ltd shall also provide a copy of such notice to the stock exchange where such securities are listed for wider dissemination and shall make an advertisement in the national daily having wide circulation indicating the details of such right and the eligibility of the holders who are entitled to avail such right.

(vii) The Company shall pay the redemption proceeds to the investors along with

interest due to the investors within 15 days from the last day within which such right can be exercised.

(viii) The company shall pay interest at 15% p.a. for the period of delay, if any.

(ix) After the completion of the exercise of such right, the company shall submit a detailed report to the stock exchange for public dissemination regarding the securities redeemed during the exercise period and details of the redemption thereof.

Answer 2A(i)

Rule 2 (c) of the Companies (Acceptance of Deposits) Rules, 2014 provides for inclusions and exclusions under the term "deposit" for the purpose of compliance of the rules. Part wise answer is given as under:-

(a) Sub-rule (vii) provides that the subscription money received against issue of securities is not a deposit provided in case of non-allotment of securities, the money is refunded to the subscriber within 60 days from the receipt of money. Further, adjustment of the money for any other purpose shall not be considered as a refund. Hence this is a case of deposit.

(b) Sub-rule (viii) provides that money received from a director as loan is not a deposit, provided the money is not given by the director out of any loan taken by him from others. In this case, since it is out of a loan from SBI, it does not fall under the exclusion. It is a case of deposit.

(c) Sub-rule (xii) (e) excludes from deposit, any advance received for warranty and maintenance, if the warranty period does not exceed the period prevalent as per common business practice or 5 years whichever is less. In this case, as it is a life-time warranty, it does not fall under the exclusion and hence it is a deposit.

(d) Sub-rule (x) excludes from deposit any non-interest-bearing amount received and held in trust. In this case, company has received the amount in trust, for a housing society to be formed for the benefit of the employees and the money is not interest bearing. Hence it is not a deposit.

Answer 2A(ii)

The case is related to issue of shares with differential rights. Rule 4 of the Companies (Share Capital and Debentures) Rules 2014 provides for the following conditions to be satisfied before issuing shares with differential rights: —

(a) Issue of shares with differential rights should be authorized by the articles and by an ordinary resolution in the shareholders' meeting and by postal ballot in the case of a listed company.

(b) The issue shall not exceed 26% of the total post-issue paid up equity share capital including the equity shares with differential rights, at any point of time.

(c) The Company should have consistent track record of distributable profits for the last three years.

(d) The Company has not defaulted in filing financial statements and annual returns

for three financial years immediately preceding the financial year in which it is decided to issue shares with differential rights.

(e) The Company has no subsisting default in payment of declared dividend to its shareholders or matured deposits or redemption of preference shares or debentures that have become due for redemption and the interest thereon.

(f) The Company has not defaulted in payment of dividend on preference shares or repayment of term loan from a public financial institution or state level financial institution or schedule bank that has become payable or interest thereon or dues with respect to statutory payments relating to employees or default in crediting the amount to IEPF;

Provided that a company may issue equity shares with differential rights upon expiry of 5 years from the end of the financial year in which such default was made good

(g) The Company has not been penalized by Court or Tribunal during the last 3 years of any offence under RBI Act, SEBI Act, Securities Contracts (Regulation) Act, FEMA Act or any other special Act under which such companies are being regulated by sectoral regulators.

(h) The Company cannot convert the existing equity shares into equity shares with differential rights and vice versa.

Answer 2A(iii)

Proviso to Sec 123 (1) of the Companies Act, 2013 stipulates that profits for the purpose of arriving at available surplus for dividend shall be computed after excluding any amount representing unrealized gains, notional gains or revaluation of assets and any changes in carrying amount of an asset or of a liability on measurement of the asset or liability at fair market value. Thus, Healthy Ltd has to deduct the gain of Rs. 2 Crore in valuation of investments at fair market value and revaluation gain of Rs. 1 Crore in respect of the fixed assets. Thus, the available surplus for the purpose of declaration of dividend shall be Rs. 7 Crore. The maximum percentage of dividend that can be declared shall be 14% (Rs 7 Crore on Rs 50 Crore paid up share capital) for the financial year 2017-18.

Proviso to Sec 123 (3) of the Act provides that in case the Company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividend declared by the Company during immediately preceding three financial years. Thus, Healthy Ltd cannot declare interim dividend in 2018-19 at a rate exceeding 12% as the Company has made a loss in the preceding two quarters.

Answer 2A(iv)

As per Sec 129(3) of the Act, a company which has one or more subsidiary or associate companies shall prepare consolidated financial statements in accordance with the provisions of Schedule III of the Act and the applicable accounting standards. Proviso to Rule 6 of the Companies (Accounts) Rules 2014 stipulates that consolidation of accounts by a Company is not required if —

- The Company is a wholly owned subsidiary or partly owned subsidiary of another

company and all its members have been informed in writing about the company not presenting consolidated financial statements and no member objects to it.

- The company is not listed or in the process of listing.
- The ultimate holding company or any intermediate holding company files consolidated financial statements with the Registrar which are compliant with the applicable accounting standards.

In respect of X Ltd, it is a wholly owned subsidiary of Y Ltd. Y Ltd files consolidated accounts with the Registrar in compliance with the rules. A Ltd is a subsidiary of X Ltd and B Ltd is an associated company of X Ltd.

Therefore, in accordance with second proviso to Rule 6 of the Companies (Accounts) Rules, 2014, X Ltd is not required to consolidate the accounts of A Ltd and B Ltd, if Y Ltd intimates in writing to X Ltd for not preparing consolidated financial statements. Provided that proof of delivery of such intimation shall be maintained with the X Ltd.

Attempt all parts of either Q. No. 3 or Q. No. 3A

Question 3

(a) A public company secured residential accommodation for the use of its Managing Director by entering into a leave and licence arrangement with the landlord. As per the terms of the agreement, the company deposited a sum of ₹5,00,000 as rental advance with landlord.

Can it be considered as a loan given to the director ?

Explain the relevant provisions.

(b) Cautious Ltd, an unlisted company with 1200 shareholders proposes to extend loans and make investments in excess of the limits prescribed under Sec 186(3) of the Act. As part of the compliance requirements, the Company is required to pass a special resolution. Advise the Company if a polling by show of hands is adequate or a poll is required.

(c) Fashion SpA is a Company incorporated in Italy, having a place of business in Mumbai for the conduct of its business. For the year ended March 2018, Fashion SpA filed their financial statements with the ROC in compliance with Sec 381 of the Act, which declared a turnover of ₹1,200 Crore and net profit of ₹49 Crore. Advise the Company on the applicability of CSR provisions and the compliance, if any, required.

(d) Flex Ltd, a Company incorporated in 2001, has 8 shareholders with a net worth of ₹2 Crore. During the month of August 2018, Flex Ltd got a term loan of ₹10 Crore sanctioned by a scheduled bank which was immediately availed. On 1st January 2018, based on their request, the Company registered the transfer of the entire shares held by 5 shareholders in favor of Ram, another shareholder of the Company. Discuss the consequences. *(4 marks each)*

OR (Alternate question to Q. No. 3)

Question 3A

Write short notes on the following :

(i) RUN

(ii) Valuation by Registered Valuer

(iii) Deposit insurance

(iv) Credit rating. *(4 marks each)*

Answer 3(a)

According to Section 185 (1) 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.

In the present case, housing accommodation is provided to the managing director. The company has not given any advance or loan to the Managing Director. The amount deposited with the landlord in respect of housing accommodation cannot be said to be an indirect loan to the Managing Director as the contract has been entered into by the company with the landlord. The company has paid the security advance on account of a bonafide business transaction towards the fulfillment of condition of contract entered by the company with the landlord. The company can at any time have the house vacated by the Managing Director and Company may accommodate any other person in the said house or company can use it for any other purpose at its own discretion. Hence, this transaction does not amount to loan by the company to the Managing Director. [case law *Dr. Fredie Ardeshir Mehta* V. *Union of India [1991] 70 Comp. Cas. 210 (Bom.)*]

Answer 3(b)

As per Rule 22(16) of the Companies (Management & Administration) Rules 2014, it is mandatory for a company with more than 200 members to transact the business of authorizing provision of loans or guarantees in excess of the limit specified under Sec 186(3) of the Act only through postal ballot and not by show of hands. Rule 20 regarding voting by electronic means shall apply, as far as applicable, mutatis mutandis to the postal ballot in respect of the voting by electronic means. Under the circumstances, it is mandatory for Cautious Ltd, being an unlisted company, with 1200 members to conduct a poll and electronic means to approve the lending under Sec 186(3) of the Act.

Answer 3(c)

Sec 135 of the Companies Act, 2013 provides the threshold limits for a company to get attracted by the CSR provisions as turnover of Rs. 1,000 Crore or more, networth of Rs. 500 Crore or more and net profit of Rs. 5 Crore or more. Rule 3 of the Companies (CSR Policy) Rules 2014 further clarifies that Sec 135 shall be applicable to a foreign company defined under Sec 2(42) of the Act and the threshold numbers for testing the applicability of Sec 135 shall be as per the financial statements filed by the foreign company under Sec 381 of the Act. Thus, Fashion SpA attracts the provisions of Sec 135 as they are above the threshold limit. Therefore, the Company has to form a CSR

Committee in line with the provisions, frame the CSR policy and spend at least 2% of the average profits of the Company for the preceding three financial years. The net profit for the purpose shall be computed in line with Sec 198 of the Act.

Answer 3(d)

Sec 3A of the Act provides that if at any time, the number of members of a company is reduced (in the case of public company below 7 and in case of private company below 2) and the company carries on business for more than 6 months while the number of members is so reduced, every person who is a member of the company during the time that it so carries on business after those 6 months and is cognizant of the fact that it is carrying on business with less than the required number, shall be severally liable for the payment of the whole debts of the company contracted during that time and may be severally sued therefor.

Flex Ltd by making a share transfer in January 2018 got its members reduced to 3, below the statutory minimum of 7. Thus, the Company will attract the provisions of Sec 3A when a term loan was availed by the Company from a scheduled bank. Under the circumstances, the remaining three shareholders shall become severally liable for the repayment of the term loan and the concerned scheduled bank can proceed against them individually.

Answer 3A(i)

RUN

RUN (Reserve Unique Name) is a process for reserving a name for a new company or for change of name of an existing Company.

An application for reservation of name shall be made through the web service available at www.mca.gov.in by using form RUN (Reserve Unique Name) along with fee which may either be approved or rejected, as the case may be, by the Registrar, Central Registration Centre after allowing re-submission of such application within fifteen days for rectification of the defects, if any.

The name approved under RUN Process for new Company registration is valid for a period of 20 days from the date of approval. In case of change of name of an existing company, the name shall be valid for 60 days from the date of approval.

Answer 3A(ii)

Valuation by Registered Valuer

Section 247 of the Companies Act 2013 provides for Valuation by Registered Valuer. It deals with the mechanism for valuation by the Registered Valuer.

Any property, stocks, shares, debentures, securities, goodwill or any other asset or net worth of a company or its assets or liabilities is to be valued by a person having such qualification and experience as a valuer in accordance with such rules as may be prescribed.

The valuer shall be appointed by Audit Committee or in its absence by the Board of Directors of the Company. The Valuer shall make impartial valuation and exercise due

diligence in making valuation. He is prohibited from undertaking valuation of any asset in which he has a direct interest or indirect interest.

If the Valuer contravenes the provisions of the law, he shall be punishable.

If he is punished under the provisions of this law, he shall be liable to:-

(i) refund the remuneration received by him to the company, and

(ii) pay for damages to the company or to any other person for loss arising out of incorrect or misleading statement of particulars made in his report.

Answer 3A(iii)

Deposit Insurance

Companies (Acceptance of Deposits) Rules 2014 has made it mandatory for companies inviting deposits from the public to buy a deposit insurance at least 30 days before the issue of the circular or advertisement or at least 30 days before the renewal of the deposit, as the case may be. Such deposit insurance shall provide that in case the company defaults in repayment of principal amount and interest thereon, the depositor shall be entitled to the repayment of principal amount of deposits and the interest thereon by the insurer up to the aggregate monetary ceiling as specified in the insurance contract. The deposit insurance contract shall provide for payment of not less than Rs. 20,000 for each depositor or the amount of deposit and interest due, whichever is lower. The premium payable on such insurance shall be borne by the company and shall not be recovered from the depositors by deducting the same from the principal amount or interest payable thereon.

If any company defaults in taking the insurance cover or any default is made in the terms and conditions of such cover, the company shall rectify the same within 30 days and the amount of deposit and interest in such cases, shall be paid within the next 15 days failing which the company shall be liable to pay interest at 15% per annum for the period of delay. In such circumstances, the company shall be treated as having defaulted and shall be liable to be punished in accordance with the provisions of the Act.

Amendments have been made from time to time to make this mandatory, subject to availability of this product of insurance and currently, the deposit insurance is mandatory from 31st March 2018.

Answer 3A(iv)

Credit Rating

As per Rule 3(8) of the Companies (Acceptance of Deposits) Rules 2014, credit rating is mandatory when a company wants to accept deposits from the public. Such a company has to obtain at least once a year, credit rating for the deposits accepted by it. A copy of the rating shall be sent to the Registrar of Companies along with the return of deposits in form DPT-3. Such credit rating shall not be below the minimum investment grade rating or other specified credit rating for fixed deposits, from any one of the approved credit rating agencies as specified for Non-Banking Financial Companies in the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions 1998 issued by the Reserve Bank of India.

Credit rating is also required when a listed company wants to issue securitized debt instruments as per Regulation 84 of SEBI (LODR) Regulations 2015. Such rating shall be periodically reviewed, preferably once a year, by a credit rating agency registered by SEBI. Any revision in ratings shall be disseminated by the stock exchanges.

Question 4

(a) Star Ltd is a company incorporated in Tamil Nadu in which 26% of the equity is held by the Government of Tamil Nadu in the name of the Governor of the State. When the Company proposed to hold its annual general meeting for the year 2017-18, the Collector of the District of Vellore where the company is situated, insisted on receiving the notice of the AGM and wanted to attend the meeting. Examine the legality of the claim. (4 marks)

(b) Noble Ltd has borrowed on various occasions from banks and institutions by securing its assets against the loans. Advise the company on the requirements of the Act relating to the register to be maintained by the Company for the charges filed. (4 marks)

(c) Medium Ltd, an unlisted company with a net worth of ₹5 Crore and turnover of 50 Crore has 200 shareholders spread across the country. Out of this, 175 shareholders hold their shares in dematerialized format while the rest hold in physical format. The Company wants to circulate the financial statements for the year ended 31st March 2018 in the most efficient way. Advise. (4 marks)

(d) Super Pharma Inc, a company registered in USA has a place of business in India with manufacturing operations and is dealing in Cardiac Stents in addition to other medical equipment. The overall turnover of the company is ₹200 crore during the financial year 2017-18 while the turnover relating to Cardiac Stents was ₹40 Crore. It is to be noted that out of this, ₹25 Crore related to the Cardiac Stents manufactured in its Indian facility while the balance ₹15 Crore related to the Cardiac Stents imported from their parent in USA and traded in the Indian market.

Advise the company on the applicability of Cost Records and Audit to the Company during the financial year 2018-19. Will the position differ, if the export turnover of Cardiac Stents for the company was ₹32 Crore during the said period? (4 marks)

Answer 4(a)

As per Sec 112 of the Companies Act, 2013, when the President of India or the Governor of a State is a member of a company, he may appoint such person as he thinks fit to act as his representative at any meeting of the company or at any meeting of any class of members of the company. A person so nominated shall be deemed to be a member of the Company and shall be entitled to exercise the same rights and powers, including the right to vote by proxy and postal ballot, as the President or Governor as the case may be, could exercise as a member of the company.

In view of the above, unless the Collector of the District of Vellore is nominated by the Governor of Tamil Nadu, he is not entitled to receive the notice of the AGM and he cannot be permitted to attend the meeting.

Answer 4(b)

As per Sec 85 of the Companies Act, 2013, every company shall maintain at its registered office a register of charges in Form CHG-7 which shall include therein details of all charges including floating charges affecting any property or assets of the company or any of its undertakings, indicating in each case such particulars as may be prescribed.

The entries in the register of charges maintained by the company shall be made forthwith after the creation, modification or satisfaction of the charge, as the case may be.

Such register of charges shall contain the particulars of all the charges registered with the Registrar on any of the property, assets or undertaking of the company and the particulars of any property acquired subject to a charge as well as particulars of any modification of a charge and satisfaction of charge.

All the entries in the register shall be authenticated by a director or the secretary of the company or any other person authorized by the Board for the purpose.

The register of charges shall be preserved permanently and the instrument creating a charge or modification thereon shall be preserved for a period of eight years from the date of satisfaction of the charge made by the company.

A copy of the instrument creating the charge shall also be kept at the registered office of the company along with the register of charges.

The register of charges and instrument of charges shall be kept open for inspection during the business hours by members or creditors without fees or any other person on payment of a fee, subject to reasonable restriction as the company may by its articles impose.

Answer 4(c)

Rule 11 of the Companies (Accounts) Rules 2014 provides for the manner in which circulation of financial statements can be made to the eligible members. In case of all listed companies and such public companies with a net worth of more than Rs. 1 Crore and turnover of Rs. 10 Crore, the financial statements may be sent-

- By electronic mode to such members whose shareholding is in dematerialized format and whose email ids are registered with Depository for communication purposes;
- Where shareholding is held otherwise than by dematerialized format, to such members who have positively consented in writing for receiving by electronic mode and;

For the rest, by dispatch of physical copies through any recognized mode of delivery such as registered post, speed post, courier etc. as specified under section 20 of the Act.

In view of the above, Medium Ltd can send the financial statements by electronic mode to the 175 shareholders who hold in dematerialized format and can approach the balance 25 shareholders to get their consent for receiving the financial statements by

electronic mode. To the extent, they succeed in getting such consent, the circulation will be efficient. Where they are not successful, they can send them in physical mode.

Answer 4(d)

As per Rule 3 of the Companies (Cost Records and Audit) Rules 2014, companies, including foreign companies, engaged in the production of goods or services specified in the table given in the Rule 3 having an overall turnover from all its products and services of Rs. 35 Crore or more during the immediately preceding financial year are required to maintain cost records for the products and services included in such table. Production, import and supply or trading of Cardiac Stents is included in Point No. 33 of such table under non-regulated sector. However, as per proviso to Rule 3, nothing contained in serial number 33 shall apply to foreign companies having only liaison offices.

Further, as per Rule 4, every company covered under Rule 3 in non-regulated sector shall get its cost records audited if the overall turnover of the company from all its products and services during the immediately preceding year is Rs. 100 Crore or more and the aggregate turnover of the individual product or service for which cost records are maintained is Rs. 35 Crore or more.

Therefore, in the instant case, since the Super Pharma has manufacturing operations in India and having overall turnover of Rs. 200 Crore and the turnover from Cardiac Stents is Rs. 40 Crore, cost audit is mandatory for the company for Cardiac Stents.

Rule 4(3) provides exemption from cost audit if the revenue from exports in foreign exchange exceeds 75% of its total revenue. Therefore, in case if Super Pharma Inc has an export turnover of 80% then they will be exempted from the requirement of cost audit in respect of Cardiac Stents.

Question 5

(a) Fortune Ltd proposes to draw a term loan of ₹20 Crore from Life Insurance Corporation. The Company owns a property comprising of land and buildings valued at ₹100 Crore. As per the sanction letters issued by the lender, a first charge on the above property is to be created in favor of LIC. Draft necessary resolution to give effect to the above charge creation. (8 marks)

(b) At the ensuing AGM of Quotient Ltd, Sriram wants to stand for directorship in the Company, even though he is not a retiring director of the company. His candidature is recommended by the Board of Directors. The Company is not required to constitute a Nomination and Remuneration Committee. Indicate the compliance required on the part of Sriram. (4 marks)

(c) Ram and Sam are the independent directors of Taurus Ltd. Ram was appointed for a period of 5 years on August 1, 2015 while Sam was originally appointed for 3 years on August 1, 2014 and was subsequently reappointed for 5 years on August 1, 2017. Now, in August 2018, the Company wants to remove both the independent directors. Is this feasible and if so, what is the procedure ? (4 marks)

Answer 5(a)

Resolution under Sec 180(1)(a) of the Companies Act, 2013 for creating a charge on company's assets

Kind of Meeting : Shareholders meeting

Type of Resolution : Special Resolution

To consider and, if thought fit, to pass with or without modification(s), the following resolution as a special resolution:

"**RESOLVED THAT** consent of the Company be and is hereby accorded in terms of Section 180(1) (a) and other applicable provisions, if any, of the Companies Act, 2013 to mortgaging and / or charging by the Board of Directors of the Company by way of equitable and / or legal mortgage on immovable property of the Company, both present and future, represented by land and buildings more specifically described in the loan agreement document signed by the Company with Life Insurance Corporation, together with power to take over the assets of the Company in certain events, to or in favor of Life Insurance Corporation of India (LIC) by way of first pari passu charge to secure the term loan of Rs. 20 Crore granted to the Company, together with interest at the agreed rate payable by the Company under the loan agreements, hypothecation deeds and other documents executed or to be executed by the Company in respect of the term loans from LIC.

RESOLVED FURTHER THAT the Board of Directors be and is hereby authorized to finalize with Life Insurance Corporation, the documents for creating the aforesaid mortgage or charge and to do all acts, deeds and things as may be required for giving effect to the above resolution.

Explanatory statement:

Life Insurance Corporation of India (LIC) have sanctioned term loan of Rs. 20 Crore to the company. This loan is to be secured by first charge on immovable property of the Company, both present and future, represented by Land and Buildings owned by the Company, in the manner as may be required by LIC. Such mortgage / charge shall rank first pari passu charge with the charges already created, if any, or to be created in favor of the participating institutions and banks for their assistance.

Section 180(1)(a) of the Companies Act, 2013 provides inter alia, that the Board of Directors of a public company shall not, without the consent of a public company in general meeting, sell, lease or otherwise dispose off the whole or substantially the whole of any such undertaking. Mortgaging / charging of the immovable property of the Company as aforesaid to secure the term loans may be regarded as disposal of the whole or substantially the whole of the said undertaking(s) of the Company and therefore requires consent of the Company pursuant to Section 180(1) (a) of the Companies Act, 2013.

The Directors recommend the resolution for approval of the shareholders as a special resolution under Sec 180(1) (a) of the Companies Act, 2013.

None of the directors are concerned or interested in the proposed resolutions.

Notes:

Section 180(1)(a) will arise only when the whole or substantially the whole of the

undertaking is being sold, leased or otherwise disposed off. If the company has land, say, worth about Rs. 5000 crores, it may not be attract the section.

Further, under Rule 22(16)(j), resolution under Sec. 180(1)(a) needs to be passed by postal ballot.

Answer 5(b)

As per Sec 160 of the Companies Act, 2013, a person, who is not a retiring director, may be proposed as a candidate for directorship of the company, either by himself or by any other member of the company, through a proper notice in writing at least 14 days before the ensuing AGM. The candidate is required to deposit a sum of Rs.1 lakh with the Company which shall be refunded to such person or the member as the case may be, if such person gets elected as a director or gets more than 25% of the total valid votes cast either on show of hands or on poll on such resolution.

The section also exempts from the requirement of making a deposit of Rs. 1 lakh if the Candidature is recommended by the Board of Directors of the company in case the company is not required to constitute a Nomination and Remuneration Committee.

Thus, Sriram can get his appointment recommended by the Board of Directors of Quotient Ltd for his candidature to the office of directorship at the ensuing AGM and seek appointment as a director without making any deposit of Rs.1 lakh. He has to ensure that a notice proposing his candidature is left at the Company either by himself or by any member of the company at least 14 days before the ensuing AGM.

Answer 5(c)

Sec 169 of the Companies Act, 2013 provides that a company may, by ordinary resolution, remove a director before the expiry of the period of office, after giving him a reasonable opportunity of being heard. The proviso to the section stipulates that an independent director re-appointed for a second term shall be removed by the company only by passing a special resolution and after giving him a reasonable opportunity of being heard.

In the instant case, Taurus Ltd. can remove Ram who was appointed on Aug 1, 2015 for a term of 5 years, by passing an ordinary resolution after giving him a reasonable opportunity of being heard, as this is the first term for Ram.

However, to remove Sam who was re-appointed for the second term on Aug 1, 2017, the Company needs to pass a special resolution and further give him a reasonable opportunity of being heard.

Question 6

(a) Draft a resolution by shareholders of X Ltd to convert the company into a private company. *(8 marks)*

(b) The Board of Directors of Zebra Ltd wants to enter into certain supply and service agreements with some of their related parties and would like to understand the compliance requirement based on the threshold limits fixed by the Act. Prepare a comprehensive note in this regard. *(4 marks)*

(c) Narrate the procedure for the appointment of Secretarial Auditor of Little Ltd having a paid-up share capital of ₹60 Crore. *(4 marks)*

Answer 6(a)

Resolution type : Special

Meeting : Shareholders' Meeting

RESOLVED THAT pursuant to proviso to Section 14(1) of the Companies Act 2013 and relevant Rules made thereunder in this behalf and subject to the approval of the National Company Law Tribunal, the status of the Company be and is hereby converted from a public limited into a private limited company.

RESOLVED FURTHER THAT the articles of association of the Company be and hereby altered by inserting the following new Article No 3A after Article No 3:

The Company is a private limited company and accordingly-

i. restricts the right to transfer its shares;

ii. limits the number of its members to two hundred:

Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member:

Provided further that—

(A) persons who are in the employment of the company; and

(B) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased,

iii. shall not be included in the number of members; and

iv. prohibits any invitation to the public to subscribe for any securities of the company;

RESOLVED FURTHER THAT the name of the Company be and is hereby accordingly changed from X Limited to X Private Limited and the Memorandum and Articles of Association of the Company shall be amended to that extent.

RESOLVED FURTHER THAT the Company Secretary of the Company be and is hereby authorized to make an application in the prescribed form and enclosures together with the applicable fee.

Explanatory Statement

The Company was originally incorporated as a public limited company. During the course of its operations, it was found that the Company has to comply with various provisions of the Act as applicable to public limited companies. Since the Company is a family owned Company with few shareholders, its requirements of funds are being met by the existing shareholders, director or their relatives. As the Company does not intend to borrow any public funds for its operations, there is no point in retaining the public character of the Company. The Board of Directors of the Company, at their meeting held on 4th September 2018 resolved to convert the Company into a private limited company.

Accordingly, it is proposed to pass a special resolution for conversion of the company into a private limited company and effect consequent alterations in the Articles of Association as applicable to a private limited company.

A copy of the existing Memorandum and Articles of Association of the Company is available for inspection at the Registered Office of the Company during business hours on any working day.

None of the directors is concerned or interested in the proposed resolution.

Answer 6(b)

Sec 188 of the Companies Act, 2013 read with Rule 15(3) of the Companies (Meetings of Board and its Powers) Rules 2014 stipulates the threshold limits of transactions with related parties for which the Company needs approval of the shareholders —

i. Sale, purchase or supply of any goods or materials directly or through appointment of agent- 10% or more of the turnover of the Company or Rs. 100 Crore whichever is lower

ii. Selling or otherwise disposing off or buying property of any kind, directly or through appointment of agent — 10% of the net worth of the Company or Rs. 100 Crore whichever is lower

iii. Leasing of property of any kind — 10% of the net worth of the Company or 10% of turnover of the Company or Rs. 100 Crore whichever is lower

iv. Availing or rendering of any services, directly or through appointment of agent — 10% of the turnover of the Company or Rs. 50 Crore whichever is lower. The limits specified above shall apply for transactions to be entered into either individually or taken together with the previous transactions in a year.

v. Appointment to any office or place of profit in the Company, its subsidiary company or associate company at a monthly remuneration exceeding Rs. 2,50,000.

vi. Remuneration for underwriting the subscription of any securities or derivatives thereof, of the Company exceeding 1% of the net worth of the Company.

The turnover and net worth referred to above shall be computed on the basis of the audited financial statements of the Company for the preceding financial year.

Answer 6(c)

The following procedure shall be adopted by Little Ltd for the appointment of a Secretarial Auditor for the Company —

- Ensure that the individual to be appointed satisfies the definition of company secretary in practice under Sec 2(25) of the Companies Act, 2013 viz., he is a member of the Institute of Company Secretaries of India and is not in full time employment anywhere.
- Further ensure that he has a certificate of practice from the Institute of Company Secretaries of India and the certificate is valid.
- Convene a board meeting of the Company by giving notice to all the directors of the company and in accordance with Sec 173 of the Companies Act, 2013. It may be noted that the appointment of secretarial auditor shall not be done by way of a circular resolution.

- Consider the proposal to appoint company secretary in practice as Secretarial Auditor and pass a resolution in the meeting confirming the appointment.
- The resolution should indicate the remuneration to be paid to such individual as Secretarial Auditor or authorize the Managing Director or any other director to fix the remuneration.
- File e-form MGT-14 for board resolution passed for appointment of secretarial auditor within 30 days of the appointment.

***

SECRETARIAL AUDIT, COMPLIANCE MANAGEMENT AND DUE DILIGENCE

Time allowed : 3 hours *Maximum marks : 100*

NOTE : *Answer **ALL** Questions.*

PART A

(Attempt all parts of either Q.No. 1 or Q.No. 1A)

Question 1

(a) XYZ Ltd., a listed company, seeks your advice, as the Secretarial Auditor of the company, on the inclusion of Extract Annual Return in the Board's Report for the financial year 2017-18. (5 marks)

(b) XYZ Ltd., a listed company, adopted Electronic Bidding Mechanism for its proposed issue of Debt Securities to the tune of ₹450 crore. The Board of directors wants you, as company secretary of the company, to ensure the post bid procedural compliances. Prepare a report to be submitted to the Board. (5 marks)

(c) Write short notes on :

(i) Qualified and Unqualified Secretarial Audit Report

(ii) Reliance of Secretarial Auditor on the reports of other designated auditors. (5 marks)

(d) XYZ Ltd. wants to avail the enabling provisions of Section 135 of the Companies Act, 2013 in rendering its Corporate Social Responsibility (CSR) activities through any other entity in 2018-19. Enlighten XYZ Ltd. in this regard. (5 marks)

(e) Does a company, incorporated in India, raising rupee denominated loan from a Non-resident Indian (NRI)/Person of Indian Origin (PIO) by way of Non-Convertible Debentures (NCDs) through a public offer get covered under the External Commercial Borrowings (ECB) framework ? (5 marks)

OR (Alternative Question to Q. No. 1)

Question 1A

(i) The Standard Rules and Regulations framed with ultimate knowledge and vision, for any discipline, act as a guide for ensuring integration, harmonization and compliance of the statutory and other requirements of that discipline. In this respect detail the procedure which shall be adopted by the Secretarial Standards Board for formulating and issuing Secretarial Standards. (5 marks)

(ii) Assumed discipline without insistence is the virtue to be adopted by all professionals in their course of conduct of their professionalism. Explain the application of this concept in relation to Secretarial Audit Report. (5 marks)

(iii) *XYZ Ltd. received a written request from Sumithra, the widow of the company's deceased shareholder Vedic Sharma to transfer in her name the shares of the company held by her deceased husband and also to advise her regarding fulfilling the procedure for the same. The shares are held in physical form. The share transfers are done in-house. As the company secretary of the company advise Sumithra suitably.* *(5 marks)*

(iv) *Is an employee who is also a promoter of a company eligible to obtain sweat equity shares and employee stock option ? Explain.* *(5 marks)*

(v) *List out compliances under the Foreign Direct Investments (FDI) Regulations of the Foreign Exchange Management Act, 1999 on issue of shares against import of capital goods.* *(5 marks)*

Answer 1(a)

As per the provisions under Section 92(3) of the Companies Act, 2013 read with rule 12 of the Companies (Management and Administration) Rules, 2014 an extract of the annual return in form MGT- 9 is to be attached with the Board's Report of the company.

However, the amendment in Section 92(3) through Companies (Amendment) Act, 2017 provides that every company shall place a copy of the Annual Return on the website of the Company, if any, and the web-link of such Annual Return shall be disclosed in the Board's Report. But the same is not yet notified.

Therefore, as a Secretarial Auditor of the company, it is advised that for the Financial Year 2017-18, the company should prepare the Extract of the Annual Return in Form MGT-9 and attach the same with the Board's report.

Answer 1(b)

To,
The Board of Directors
XYZ Ltd.

Sub : Report with respect to compliance of post-bid procedures in Electronic Bidding Mechanism for issuance of Debt Securities on private placement basis

Dear Sir(s),

I would like to bring to your kind information that as per SEBI (Issue and Listing of Debt Securities) Regulations,2008 the compliance with Post Bidding Procedure involves the following-

i. All bids received within bidding time window shall be provided by EBP (Electronic Book Provider) to the Issuer after bidding process is over;

ii. Issuer shall have the option to accept or reject bids received, if the issuer agrees to the yield so discovered;

iii. Issuer shall provide details of accepted bids to depositories to make allotment;

iv. EBP shall display bid details on the end of the bidding time window;

v. At the end of the bidding time window, EBP shall on an anonymous basis, disclose the aggregate volume data, including yield, amount including the amount of over subscription, total bids received, ratings(s), category of investor etc., to avoid any speculations;

vi. For issues below Rs. 500 crore, Issuer shall upload details as mentioned above with EBP and/or with information repository for corporate debt market as notified by SEBI, in the format as specified;

vii. EBP shall upload the allotment data on its website to be made available to the public.

As Company Secretary of the company, I ensure that all the above requirements are complied with including point "vi", as our issue size is Rs 450 crores.

For XYZ Ltd.

Sd/-

Company Secretary

Answer 1(c)

(i) **Unqualified Secretarial Audit Report** is one which indicates a clean report mentioning that company has complied with relevant law and procedural aspects of Secretarial Records and other relevant records with respect to the company law and other relevant industry specific laws applicable to the Company.

Qualified Report is one which indicates the non-compliances, with the provisions of law and procedures. Deviations from secretarial standards and frauds if any, are also reported. Qualifications, reservations and/or adverse remarks, if any, should be stated by the secretarial auditor at the relevant places in his report in bold type and italics.

Qualifications/reservations or adverse remarks, if any, should be stated by the secretarial auditor at the relevant places in his report in bold type and in italics. If the secretarial auditor is unable to express an opinion on any matter, he should mention that he is unable to express an opinion on that matter and the reasons therefor. If the scope of work required to be performed is restricted on account of restrictions imposed by the company or on account of circumstantial limitations (like certain books or papers being in the custody of another person who is not available or a Government Authority), the Report should indicate such limitations. If such limitations are so material that the secretarial auditor is unable to express any opinion, the secretarial auditor should state that in the absence of necessary information and records, he is unable to report on compliance(s) relating to such areas by the Company.

The Board's Report shall include its comments on the Secretarial Audit Report including the remedial measures adopted to rectify the qualifications, if any, stated in the Secretarial Audit Report.

(ii) **Reliance of Secretarial Auditors on the Reports of the other designated Auditors**

The mandatory audit areas to be covered during Secretarial audit include finance and taxation areas. The audit of finance is done by the Statutory Auditors of the Company and the details are covered in the Statutory Audit Report provided by him. Tax Audit is done by the Statutory auditor or any other designated auditor, who provides the Tax Audit Report covering the areas of Taxation.

The Secretarial Auditor may rely on the Reports given by these professionals on their respective areas while performing his audit duties. However, Secretarial Auditor is expected to report on the Board Processes, Secretarial Compliances as well as the laws covered in Form MR-3 along with the other applicable laws.

Answer 1(d)

As per the provisions of Rule 4(1) of the Companies (Corporate Social Responsibility Policy) Rules, 2014, the CSR activities shall be undertaken by the company, as per its stated CSR Policy, as projects or programs or activities (either new or ongoing),excluding activities undertaken in pursuance of its normal course of business.

However, Rule 4(2) of the Companies (Corporate Social Responsibility Policy) Rules, 2014 provides that the Board of a company may decide to undertake its CSR activities approved by the CSR Committee through

(a) a company established under section 8 of the Companies Act, 2013 or a registered trust or a registered society, established by the company, either singly or alongwith any other company, or

(b) a company established under section 8 of the Companies Act, 2013 or a registered trust or a registered society, established by the Central Government or State Government or any entity established under an Act of Parliament or a State legislature:

Provided that if, the Board of a company decides to undertake its CSR activities through a company established under section 8 of the Act or a registered trust or a registered society, other than those specified in this sub-rule, such company or trust or society shall have an established track record of three years in undertaking similar programs or projects; and the company has specified the projects or programs to be undertaken, the modalities of utilisation of funds of such projects and programs and the monitoring and reporting mechanism.

A company may also collaborate with other companies for undertaking projects or programs or CSR activities in such a manner that the CSR Committees of respective companies are in a position to report separately on such projects or programs in accordance with these rules.

Companies may build CSR capacities of their own personnel as well as those of their Implementing agencies through Institutions with established track records of at least three financial years but such expenditure including expenditure on administrative overheads, shall not exceed five percent of total CSR expenditure of the company in one financial year.

Therefore, advise to XYZ Ltd. in this regard would be- to identify such a trust or a society or a company as specified above having an established track record of three years in undertaking similar programs or projects which the company is going to undertake as a CSR activity or expenditure in this regard.

Answer 1(e)

No, NRI/PIO giving rupee denominated loan, to resident company by way of Non-Convertible Debentures (NCDs) through a public offer is not covered under the ECB framework. It is covered under Foreign Exchange Management (Borrowing and Lending in Rupees) Regulations, 2000 issued vide Notification No. FEMA 4/2000-RB dated May 3, 2000 as amended from time to time. As per the provisions contained in these Regulations, a company incorporated in India is permitted to raise Rupee denominated loan from an NRI / PIO only by way of issuance of NCDs through a public offer and is subject to other provisions contained in these Regulations like redemption period for such NCDs should not be less than 3 years, the rate of interest on such NCDs issued does not exceed the prime lending rate of the State Bank of India as on the date on which the resolution approving the issue is passed in the borrowing company's General Body Meeting, plus 300 basis points etc.

Answer 1A(i)

The following procedure shall be adopted for formulating and issuing Secretarial Standards:

1. The Secretarial Standards Board (SSB), in consultation with the Council of ICSI, shall determine the areas in which Secretarial Standards need to be formulated and the priority in regard to the selection thereof.
2. In the preparation of Secretarial Standards, SSB may constitute Working Groups to formulate preliminary drafts of the proposed Standards.
3. The preliminary draft of the Secretarial Standard prepared by the Working Group shall be circulated amongst the members of SSB for discussion and shall be modified appropriately, if so required.
4. The preliminary draft will then be circulated to the members of the Central Council as well as to Chairman of Regional Councils/Chapters of ICSI, various professional bodies, Chambers of Commerce, regulatory authorities such as the Ministry of Corporate Affairs, the Department of Economic Affairs, the Securities and Exchange Board of India, Reserve Bank of India, Department of Public Enterprises and to such other bodies/organisations as may be decided by SSB, for ascertaining their views, specifying a time-frame within which such views, comments and suggestions are to be received.

   A meeting of SSB with the representatives of such bodies/organisations may then be held, if considered necessary, to examine and deliberate on their suggestions.
5. On the basis of the preliminary draft and the discussion with the bodies/ organisations referred to in 4 above, an Exposure Draft will be prepared and published in the “Chartered Secretary”, the journal of ICSI, and also put on the Website of ICSI to elicit comments from members and the public at large.

6. The draft of the Secretarial Standard generally includes the following basic points:
   a. Concepts and fundamental principles relating to the subject of the Standard;
   b. Definitions and explanations of terms used in the Standard;
   c. Objectives of issuing the Standard;
   d. Disclosure requirements; and
   e. Date from which the Standard will be effective.
7. After taking into consideration the comments received, the draft of the Secretarial Standard will be finalised by SSB and submitted to the Council of ICSI.
8. The Council will consider the final draft of the Secretarial Standard and finalise the same in consultation with SSB. The Secretarial Standard on the relevant subject will then be issued under the authority of the Council.

Answer 1A(ii)

Secretarial Audit is a process to check compliance with the provisions of all applicable laws and rules/regulations/procedures; adherence to good governance practices with regard to the systems and processes of seeking and obtaining approvals of the Board and/or shareholders, as may be necessary, for the business and activities of the company, carrying out activities in a lawful manner and the maintenance of minutes and records relating to such approvals or decisions and implementation.

The objectives of Secretarial Audit may be summarized as under:

— To check & report on compliances of applicable laws and Secretarial Standards

— To point out non-compliances and inadequate compliances

— To protect the interest of various stakeholders, i.e., the customers, employees, society etc.

— To avoid any unwarranted legal actions/penalties by law enforcing agencies and other persons as well.

Under Section 204 of the Companies Act, 2013 read with Rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, the Secretarial Audit is mandatory for -

i. every listed company;
ii. every public company having a paid-up share capital of fifty crore rupees or more; or
iii. every public company having a turnover of two hundred fifty crore rupees or more.

Such companies are required to annex a secretarial audit report with its Board's report, with the comments of the board on the same in case such report contains any qualification, reservation or adverse remark or disclaimer etc., if any.

Since the Board has the overarching responsibility of ensuring transparent, ethical

and responsible governance of the company, it is important that the Board processes and compliance mechanisms of the company are robust. To ensure this, the companies may get the Secretarial Audit conducted by a competent professional. The Board should give its comments on the Secretarial Audit in its report to the shareholders where such report contains any qualification, reservation or adverse remark or disclaimer etc.

Answer 1A(iii)

The following advise shall be sent on the letter head of the Company to Sumithra-

To Date:

Sumithra

Address:

Madam

Sub: Transmission of shares - reg

Ref: Your letter dated xx/xx/xxxx

We are sorry for the sad demise of our beloved shareholder.

Kindly arrange to send the following documents to enable us to duly transmit the shares of our company from the name of your deceased husband to your name-

a. Original share certificate(s);

b. A copy of the Death Certificate of the deceased;

c. Succession Certificate/Legal Heir Certificate/Probate/Letter of Administration (anyone) in favour of you.

d. No Objection Certificate from the other legal heirs, if any, for transmission in your favour.

e. Your self-certified Income Tax PAN copy along with other KYC Documents.

Thanking You

For XYZ Ltd.

Sd/-

Company Secretary

Answer 1A(iv)

As per Rule 12 of Companies (Share Capital and Debentures) Rules, 2014, an employee who is also a promoter or person belonging to the promoter group is specifically excluded from obtaining shares issued under ESOP.

In case of a start-up company as defined in notification number G.S.R. 180(E) dated

17th February, 2016 issued by the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India, this condition shall not apply up to five years from the date of its incorporation or registration.

However, in case of sweat equity shares, the said exclusion is not specified in the provisions. Thus, an employee who is also a promoter of a company is eligible to get sweat equity shares.

Accordingly, the employee who is also promoter of the company is not entitled to get employee stock option subject to above exemption, however he is eligible to obtain the Sweat Equity shares.

Answer 1A(v)

Issue of equity shares against Import of capital goods / machinery / equipment (excluding second-hand machinery); is allowed under automatic route if the Indian investee company is engaged in a sector under automatic route or with prior Government approval if the Indian investee company is engaged in a sector under Government, subject to the compliance with the following conditions:

(a) The import of capital goods, machineries, etc., made by a resident in India, is in accordance with the Export / Import Policy issued by the Government of India as notified by the Directorate General of Foreign Trade (DGFT) and the regulations issued under the Foreign Exchange Management Act (FEMA), 1999 relating to imports issued by the Reserve Bank;

(b) There is an independent valuation of the capital goods /machineries / equipments by a third party entity, preferably by an independent valuer from the country of import along with production of copies of documents / certificates issued by the customs authorities towards assessment of the fair-value of such imports;

(c) The application should clearly indicate the beneficial ownership and identity of the importer company as well as the overseas entity; and

(d) All such conversions of import payables for capital goods into FDI should be completed within 180 days from the date of shipment of goods.

PART B

Attempt all parts of either Q. No. 2 or Q. No. 2A

Question 2

(a) Under the provisions of Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, examine the following:

Company A Ltd. has a paid-up share capital of ₹10,000 (1,000 shares of ₹ 10 each) and shareholder A is holding 50 shares totalling to ₹ 500. In case an open offer is made for 26% of the share capital and the shares tendered are 300 which are in excess of the 26% shareholding, how the shares will be accepted by the acquirer on a proportionate basis ? (5 marks)

(b) A subsidiary to a listed company, irrespective of its registered status, to a large

extent is treated as a listed company by the authorities. As the Secretarial advisor and auditor of XYZ Ltd., which is a Public Ltd. company and a subsidiary to a listed company ABC Ltd., how would you ensure the compliance of Corporate Governance requirements by XYZ Ltd., with reference to the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 ? *(5 marks)*

(c) *As per the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009, what are the conditions for preferential issue of specified securities by a listed issuer ?* *(5 marks)*

OR (Alternate Question to Q. No. 2)

Question 2A

(i) *SAM Ltd. and MAS Ltd. intend to amalgamate. The enterprise created as a result of such amalgamation will have assets worth ₹600 crore and turnover of ₹2,000 crore. Examine whether the proposed amalgamation attracts the provisions of the Competition Act, 2002 ?* *(5 marks)*

(ii) *The intent of the law makers is to be carried out in letter and spirit in complying with the regulatory requirements of Corporate Governance in a corporate. Elaborate this statement with explanations.* *(5 marks)*

(iii) *Ranjit is director in 11 companies. He has got two DINs (Director Identification Number) allotted to him inadvertently. Out of the 11 directorships he holds 5 with the DIN allotted to him at first and the rest with the DIN allotted to him later.*

He wants to surrender one of his DINs, but to keep all his 11 directorships. Advise him. *(5 marks)*

Answer 2(a)

No. of shares of A accepted = Total no. of shares offered in the open offer X Number of shares tendered by A divided by Total shares tendered in the Open offer by all investors = (260 X 50) / 300 = 43.33 shares = 43 shares

Shares which are invalid or are rejected due to the valid acceptances being more than the offer size are subsequently returned to the respective shareholders within 10 working days of the closure of the open offer.

Answer 2(b)

As per the Regulation 24 of the SEBI (LODR) Regulations, 2015, the following compliances are required to be ensured by a subsidiary of a listed company with reference to Corporate Governance:

(1) At least one independent director on the board of directors of the listed entity shall be a director on the board of directors of an unlisted material subsidiary, incorporated in India.

(2) The audit committee of the listed entity shall also review the financial statements, in particular, the investments made by the unlisted subsidiary.

(3) The minutes of the meetings of the board of directors of the unlisted subsidiary shall be placed at the meeting of the board of directors of the listed entity.

(4) The management of the unlisted subsidiary shall periodically bring to the notice of the board of directors of the listed entity, a statement of all significant transactions and arrangements entered into by the unlisted subsidiary.

Explanation.- For the purpose of this regulation, the term significant transaction or arrangement shall mean any individual transaction or arrangement that exceeds or is likely to exceed ten percent of the total revenues or total expenses or total assets or total liabilities, as the case may be, of the unlisted material subsidiary for the immediately preceding accounting year.

(5) A listed entity shall not dispose of shares in its material subsidiary resulting in reduction of its shareholding (either on its own or together with other subsidiaries) to less than fifty percent or cease the exercise of control over the subsidiary without passing a special resolution in its General Meeting except in cases where such divestment is made under a scheme of arrangement duly approved by a Court/Tribunal.

(6) Selling, disposing and leasing of assets amounting to more than twenty percent of the assets of the material subsidiary on an aggregate basis during a financial year shall require prior approval of shareholders by way of special resolution, unless the sale/disposal/lease is made under a scheme of arrangement duly approved by a Court/Tribunal.

(7) Where a listed entity has a listed subsidiary, which is itself a holding company, the provisions of this regulation shall apply to the listed subsidiary in so far as its subsidiaries are concerned.

As a Secretarial advisor and auditor of XYZ Ltd., which is a Public Ltd. company and a subsidiary to a Listed company ABC Ltd., I would focus on checking the compliance by XYZ Ltd. of the above cited points and thereby ensure the compliance of Corporate Governance requirements by XYZ Ltd., with reference to the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015.

Answer 2(c)

Conditions for preferential issue : According to Regulation 72 of the SEBI (ICDR) Regulations, 2009,

(1) A listed issuer may make a preferential issue of specified securities, if:

(a) a special resolution has been passed by its shareholders specifying the relevant date on the basis of which price of the equity shares to be allotted on conversion or exchange of convertible securities shall be calculated;

(b) all the equity shares, if any, held by the proposed allottees are in dematerialised form;

(c) the issuer is in compliance with the conditions for continuous listing of equity shares as specified in the listing agreement with the recognised stock exchange where the equity shares of the issuer are listed;

(d) the issuer has obtained the Permanent Account Number of the proposed allottees.

(2) The issuer shall not make preferential issue of specified securities to any person who has sold any equity shares of the issuer during the six months preceding the relevant date:

However, in respect of the preferential issue of equity shares and compulsorily convertible debt instruments, whether fully or partly paid, SEBI may grant relaxation from the requirements of this sub-regulation, if SEBI has granted relaxation in terms of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, to such preferential allotment except to the promoters or persons from promoter group.

(3) Where any person belonging to promoter(s) or the promoter group has previously subscribed to warrants of an issuer but failed to exercise the warrants, the promoter(s) and promoter group shall be ineligible for issue of specified securities of such issuer on preferential basis for a period of one year from:

(a) the date of expiry of the tenure of the warrants due to non-exercise of the option to convert; or

(b) the date of cancellation of the warrants as the case may be.

(4) Copy of the certificate of its statutory auditor be placed by the issuer before the General Meeting considering such preferential issue, certifying that the issue is being made in accordance with the requirements of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

(5) Valuation by an Independent Qualified Valuer be obtained while making preferential issue of specified securities to promoters, their relatives, associates and related entities for consideration other than cash, the valuation of the assets in consideration for which the equity shares are issued shall be done and it shall be submitted to the recognised stock exchanges where the equity shares of the issuer are listed.

(6) As a general rule, such allotment be completed within 15 days from the date of passing of such special resolution.

(7) The tenure of the convertible securities of the issuer shall not exceed eighteen months from the date of their allotment.

Answer 2A(i)

Sections 5 and 6 of The Competition Act, 2002 deal with the combination of enterprises and persons. The amalgamation of enterprises shall be a combination of such enterprises if the enterprise remaining after merger or the enterprise created as a result of the amalgamation, as the case may be, have,—

(A) either in India, the assets of the value of more than rupees two thousand crores or turnover more than rupees six thousand crores; or

(B) in India or outside India, in aggregate, the assets of the value of more than one billon US dollars, including at least rupees one thousand crores in India, or turnover more than three billion US dollars, including at least rupees three thousand crores in India.

Hence, in the present case, the proposed amalgamation of SAM Ltd. and MAS Ltd. will not attract the provisions of The Competition Act, 2002 as they have assets of value of Rs.600 crore and turnover of Rs.2000 less than the threshold specified under the provisions.

Answer 2A(ii)

Good Corporate Governance demands compliance levels that match the intentions of legislature, expectations of stakeholders and requirements of regulators. The compliances, however, generally found to fall in three categories, i.e., Apparent Compliances, Adequate Compliances and Absolute Compliances.

Apparent compliance is a disguise form of non-compliance, which is worse than a non-compliance.The classic example for Apparent Compliances are generating documents such as notice, agenda, minutes on papers for board and general meeting which are not actually held.

Adequate compliance is compliance in letters. The aspects specified in law are complied in letters, without getting into the spirit of the law, e.g. box ticking practices.

Absolute compliances are those which are in line with the spirit and intent of the law. A typical example in this regard is demonstrating shareholder democracy as prescribed by law. When a company complies with law in spirit it gains public confidence as well.

In order to attain corporate sustainability and to ensure a level playing field with international market, corporates need to necessarily increase their level of compliance from apparent to adequate, thereby leading to the level of absolute compliances.

Answer 2(A)(iii)

As per the requirements of the Companies Act, 2013, relevant to filing of form DIR 5 for surrendering the DIN, if a person possesses multiple DINs and wants to surrender them retaining only one DIN, he shall retain the DIN allotted to him in the first instance and surrender the others allotted later.

Applying the above provisions, the advice to Ranjit would be-

i. Regarding retaining 11 directorships, he could give resignation to companies' directorship which he is holding with the second DIN, and afterwards could be co-opted to the Board of such companies with the first DIN,

ii. After the above cited activities in point (i), he shall retain the DIN allotted to him at the first instance and surrender the second one allotted after the first by filing Form DIR 5 completed in all respects with the Registrar of Companies.

Question 3

(a) As per the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009, what are the conditions for offering specified securities at differential prices ? *(8 marks)*

(b) List out the key differences between Statutory Audit, Internal Audit and Due Diligence. *(7 marks)*

Answer 3(a)

Differential Pricing

According to Regulation 29 of the SEBI (ICDR) Regulations,2009, an issuer may offer specified securities at different prices, subject to the following:

(a) Retail individual investors or retail individual shareholders or employees entitled for reservation made under regulation 42 making an application for specified securities of value not more than two lakh rupees, may be offered specified securities at a price lower than the price at which net offer is made to other categories of applicants. Provided that such difference shall not be more than ten per cent of the price at which specified securities are offered to other categories of applicants;

(b) In case of a book building issue, the price of the specified securities offered to an anchor investor shall not be lower than the price offered to other applicants;

(c) In case of a composite issue, the price of the specified securities offered in the public issue may be different from the price offered in rights issue and justification for such price difference shall be given in the offer document.

(d) In case the issuer opts for the alternate method of book building in terms of Part D of Schedule XI, the issuer may offer specified securities to its employees at a price lower than the floor price: Provided that the difference between the floor price and the price at which specified securities are offered to employees shall not be more than ten per cent of the floor price.

Answer 3(b)

Parameter	*Statutory Audit*	*Internal Audit*	*Due Diligence*
Appointed by	Shareholder of a company	Management of the company	Normally by the buyers and, in certain cases by the management of the target.
Reader of the Report	Shareholders, regulatory authority	Management	Deal Making Parties.
Extent of Reliance on information provided by management	Relatively high	Relatively high	Low to medium; the information is first challenged/ tested for its reliability.
Mandatory	Mandatorily required under statute	Mandatorily required under statute for specified class of companies	Not Mandatory

Parameter	*Statutory Audit*	*Internal Audit*	*Due Diligence*
Objectives	To report on the truth and fairness of the financial statements	To report on specific issue with the internal processes of the company	To highlight exposures and upside of the targets
Scope	Defined by the statute itself mainly limited to financial analysis	Defined by the management – limited to financial analysis	No specific scope defined by the buyer or seller (in case of vendor due diligence). The scope largely depends on deal mechanics and the agreement among the parties involved. Includes not only analysis of the financial statements but also business sustainability of the business, future aspects, corporate and management structure, legal issues etc.
Perspective and focus	Focuses on historical information	Adopts a futuristic approach based on the available information	Blend of both historical and futuristic perspectives
Confidentiality	Low; in the case of listed companies, the audit report is publicly available and in other type of companies also it is available as a public document in public domain at a payment of prescribed fees to the MCA.	High normally, only management has access to the report	High; only the deal making parties have an access to the report
Type	Post mortem analysis	Analysis of the current situation like timely diagnosis and treatment	Useful for the future decisions

Parameter	*Statutory Audit*	*Internal Audit*	*Due Diligence*
Nature	Always uniform	May be modified with slight changes	Always flexible procedure based on the object of the exercise and who is doing such exercise

Question 4

(a) *The process of preparing search/status report enables determination out of total borrowing power, the extent upto which the company has already borrowed money or created charges on its movable and immovable properties and also the balance limit to borrow. However, there are certain exceptions to the term 'borrowing of money'. Enumerate those exceptions i.e., the borrowings which are not included in determining the limit on borrowings.* *(5 marks)*

(b) *List out the procedural steps for conducting Legal Due Diligence.* *(5 marks)*

(c) *Explain the terms 'Diversion of funds' and 'Siphoning of funds' with regard to due diligence for banks.* *(5 marks)*

Answer 4(a)

The term borrowing of money includes all type of borrowings whether secured or unsecured, loan in the nature of debentures or otherwise etc. However, the following are exceptions to it as enumerated under Section 180(1)(c) of the Companies Act, 2013:

1. *Temporary loans obtained from the company's bankers in the ordinary course of business* : the expression "temporary loans" means loans repayable on demand or within six months from the date of the loan such as short-term, cash credit arrangements, the discounting of bills and the issue of other short-term loans of a seasonal character, but does not include loans raised for the purpose of financial expenditure of a capital nature;

2. *Acceptance by a banking company* : In the ordinary course of its business, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise, shall not be deemed to be a borrowing of monies by the banking company within the meaning of Section 180(1)(c) of the Companies Act, 2013.

3. Contingent liability like amount outstanding on deferred payment agreement or under guarantees issued by bank or in respect of letter of Credit.

Answer 4(b)

There is no definitive process of a legal due diligence. The investigative aspects as well as Legal Due Diligence process varies depending upon the scope of work dictated by the client, the focus, special areas of weakness, the type of business, etc. In general, the following process is involved in legal due diligence:

— Entering of Memorandum of Understanding between the transacting parties along with confidentiality agreement.

— Determination of scope of Legal Due Diligence.

— Calculation of time frame.

— Drafting of various questionnaire and checklists.

— Obtaining of access to records and data room agreement.

— Interaction with management and key managerial persons with the questionnaires and checklists and for other material information.

— Interaction with regulatory authorities for independent check.

— Checking of regulatory and contractual compliance.

— Analysis of financial and non financial information.

— Collation with financial due diligence for confirmation of representations, warranties and liabilities.

— Investigation of material issues.

— Drafting of preliminary report.

— Discussions with the management of the target company.

— Finalisation of the Report.

— Determination of strategy.

While undergoing such procedure one has to consider organisational / internal aspects (MOA/AOA/Minutes/Statutory Registers documents filed with Regulatory Authorities, etc.), Financial aspects (financial statements, audit qualifications, internal audit report business projections etc.), IPR/Patents/R&D Details etc., HR Aspects, Environmental Aspects, Material contracts, etc. other relevant aspects as may be necessary with respect to the specific assignment.

Answer 4(c)

Diversion and Siphoning of funds

Diversion of funds, would be construed to include any one of the under noted occurrences:

(a) utilisation of short-term working capital funds for long-term purposes not in conformity with the terms of sanction;

(b) deploying borrowed funds for purposes/activities or creation of assets other than those for which the loan was sanctioned;

(c) transferring funds to the subsidiaries/Group companies or other corporates by whatever modalities;

(d) routing of funds through any bank other than the lender bank or members of consortium without prior permission of the lender;

(e) investment in other companies by way of acquiring equities/debt instruments without approval of lenders;

(f) shortfall in deployment of funds *vis-à-vis* the amounts disbursed / drawn and the difference not being accounted for.

Siphoning of funds, should be construed to occur if any funds borrowed from banks/ financial institutions are utilised for purposes un-related to the operations of the borrower, to the detriment of the financial health of the entity or of the lender. The decision as to whether a particular instance amounts to siphoning of funds would have to be a judgment of the lenders based on objective facts and circumstances of the case.

Question 5

(a) Answer the following :

(i) Under the provisions of Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, how do you determine whether the shares of the target company are frequently traded or infrequently traded ?

(ii) How is the offer price calculated in case shares are infrequently traded on the stock exchange ?

(iii) XYZ Ltd. which has listed its Indian Depository Receipts, seeks your advice, as its Company Secretary, as to the list of documents to be provided to the Indian Depository Receipt holders on an annual basis. (3 marks each)

(b) Write short notes on the following :

(i) Time limit for filing the forms for charges requiring registration with the Registrar of Companies.

(ii) Compliance Dash Board. (3 marks each)

Answer 5(a)(i)

Under the provisions of the SEBI (SAST) Regulations, 2011, the shares of the target company will be deemed to be frequently traded if the traded turnover on any stock exchange during the 12 calendar months preceding the calendar month, in which the public announcement is made, is at least 10% of the total number of shares of the target company. If the said turnover is less than 10%, it will be deemed to be infrequently traded.

Answer 5(a)(ii)

If the target company's shares are infrequently traded then the open offer price for acquisition of shares under the minimum open offer shall be highest of the following:

- Highest negotiated price per share under the share purchase agreement ("SPA") triggering the offer;
- Volume weighted average price of shares acquired by the acquirer during 52 weeks preceding the public announcement ("PA");
- Highest price paid for any acquisition by the acquirer during 26 weeks immediately preceding the PA;
- The price determined by the acquirer and the manager to the open offer after taking into account valuation parameters including book value, comparable trading multiples, and such other parameters that are customary for valuation of shares of such companies.

Answer 5(a)(iii)

Documents and Information to IDR Holder (Regulation 73 of SEBI (LODR) Regulations, 2015)

Check whether the listed entity disclose/send the following documents to IDR Holders, at the same time and to the extent that it discloses to security holders:

(a) Soft copies of the annual report to all the IDR holders who have registered their email address(es) for the purpose.

(b) Hard copy of the annual report to those IDR holders who request for the same either through domestic depository or Compliance Officer.

(c) The pre and post arrangement capital structure and share holding pattern in case of any corporate restructuring like mergers / amalgamations and other schemes.

Answer 5(b)(i)

Event	*Time Limit*	*Effect*
Creation of charge or modification of charge or acquisition of property which is subject to charge.	Within thirty days from the date of creation, modification or acquisition and, within 300 days in case the Registrar on being satisfied that the company had sufficient cause for not filing the particulars within 30 days.	The date when the event takes place is also included while calculating the limit. With the additional fees and on condonation of delay by the Registrar.
Satisfaction of the charge.	Within a period of thirty days from the date of payment or satisfaction in full of any charge registered under the Act. As per the Amendment Act, the Registrar of Companies may, on an application by the Company or charge-holder, allow such intimation of payment or satisfaction to be made within a period of 300 days of such payment or satisfaction.	The date when the event takes place is to be excluded while calculating thirty days .

Answer 5 (b)(ii)

The compliance dashboard helps in simplifying the compliance obligation, effectively managing the compliance risk, facilitating board oversight, effective co-ordination of functional units. Some of the features of an effective Compliance Dashboard is as follows:

- The Compliance Dashboard should alert the company in the risk prone areas or in case of non compliances.
- It should display the compliance obligations on the compliance calendar or dashboard.
- Before the date of regulatory mandate an e-mail should be sent to the compliance owner.
- The Compliance owner should send the response once compliance is done.

Question 6

(a) Section 3(1) of the Competition Act, 2002 prohibits five types of agreements between companies. Briefly explain those agreements.

(b) Ragul, a director in XYZ Ltd., did not attend the Board meetings held for a period of 12 months after seeking leave of absence.

Though as per Section 167(1)(b) of the Companies Act, 2013 his office of directorship was vacated :

(i) The Board of XYZ Ltd. wants to keep Ragul's directorship. Can it condone his absence for this purpose ?

(ii) Ragul also wants to keep the directorship in XYZ Ltd.

As the Company Secretary of the company the Board seeks your advice on this issue. (5 marks)

(c) Highlight the regulatory framework governing environmental aspects in India. (5 marks)

Answer 6(a)

Section 3 of the Competition Act, 2002 relates to "Anti-Competitive agreements".

Section 3(1) of the Competition Act, 2002 reads as under:

3(1) No enterprises or association of enterprises or person or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition within India.

In terms of Section 3(4), the following agreements are considered as an agreement in contravention of sub-section 3(1) of the Competition Act, 2002, if such agreement causes or is likely to cause an appreciable adverse effect on competition in India:

(a) "tie-in arrangement" includes any agreement requiring a purchaser of goods, as a condition of such purchase, to purchase some other goods;

(b) "exclusive supply agreement" includes any agreement restricting in any manner the purchaser in the course of his trade from acquiring or otherwise dealing in any goods of the competitor of the seller and other than those of the seller ;

(c) "exclusive distribution agreement" includes any agreement to limit, restrict or withhold the output or supply of any goods or allocate any area or market for the disposal or sale of the goods;

(d) "refusal to deal" includes any agreement which restricts, or is likely to restrict, by any method the persons or classes of persons to whom goods are sold or from whom goods are bought;

(e) "resale price maintenance" includes any agreement to sell goods on condition that the prices to be charged on the resale by the purchaser shall be the prices stipulated by the seller unless it is clearly stated that prices lower than those prices may be charged.

However, these agreements are not considered anti-competitive per se as in the case of horizontal agreements and have to be judged by the rule of reason.

Section 3(3) of the Competition Act, 2002 read as under:

In terms of Section 3(3) of the Competition Act, 2002, any agreement entered into between enterprises or associations of enterprises or persons or associations of persons or between any person and enterprise or practice carried on, or decision taken by, any association of enterprises or association of persons, including cartels, engaged in identical or similar trade of goods or provision of services, which -

(a) directly or indirectly determines purchase or sale prices;

(b) limits or controls production, supply, markets, technical development, investment or provision of services;

(c) shares the market or source of production or provision of services by way of allocation of geographical area of market, or type of goods or services, or number of customers in the market or any other similar way;

(d) directly or indirectly results in bid rigging or collusive bidding, shall be presumed to have an appreciable adverse effect on competition.

Answer 6(b)

As per Section 167(1)(b) of the Companies Act,2013 (Act), the office of a director shall become vacant in case, he absents himself from all the meetings of the Board of Directors held during a period of twelve months with or without seeking leave of absence of the Board.

Hence, the office of directorship of Ragul is automatically vacated on happening of the event of his absence from the Board meetings held for a period of 12 months. Getting leave of absence has no significance or relevance as per the provision in the Act in this regard.

There is no provision in the Act to empower the Board to waive the event of absence or to condone the absence or act in any manner which cause the vacation of office of director void.

Hence, the advice to the Board would be to co-opt Ragul on the board as an Additional Director in the subsequent Board meeting held after the cited 12 months during which Ragul did not attend the Board meetings, as there is no prohibition in the Act for such co-option and re-appointment.

Answer 6(c)

The Constitution of India, as amended casts obligations on the 'State' as well as the 'citizens' to conserve, perceive, protect and improve the environment. A number of Central/State Legislations/Regulations etc., govern environmental aspects in India. It includes the following:

— **The Water (Prevention and Control of Pollution) Act.** This Act was enacted in 1974 to provide for Prevention and control of water pollution, and for maintaining or restoring of wholesomeness of water in the country.

— **The Water (Prevention and Control of Pollution) Cess Act.** This Act was enacted in 1977, to provide the levy and collection of a cess on water consumed by persons operating and carrying on certain types of industrial activities and with a view to augment the resources of the Central Board and State Boards for the prevention and control of water pollution constituted under the water (Prevention and Control of Pollution) Act, 1974.

— **The Air (Prevention and Control of Pollution) Act.** This Act was enacted in 1981 and amended in 1967 to provide for the prevention, control and abatement of air pollution in India.

— **The Environment (Protection) Act.** This Act was enacted in 1986 with the objective of providing for the protection and improvement of the environment.

— **Public Liability Insurance Act, 1991.** This Act was enacted to provide for damages to victims of accident which occurs as a result of any hazardous activity or due to handling any hazardous substance.

— **National Green Tribunal Act, 2010.** This Act was enacted for effective and expeditious disposal of cases relating to environmental protection and conservation of forests and other natural resources including enforcement of any legal right relating to environment and giving relief and compensation for damages to persons and property and for matters connected therewith or incidental thereto.

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CORPORATE RESTRUCTURING, VALUATION AND INSOLVENCY

Time allowed : 3 hours *Maximum marks : 100*

NOTE : *1. Answer ALL Questions.*

2. All references to sections relate to the Companies Act, 2013 unless stated otherwise.

PART A

Question 1

(a) "Corporate Restructuring is an inorganic growth strategy that significantly changes a company's business model, management team or financial structure to address challenges and increase shareholders' value". Elucidate the statement with different options of Corporate Restructuring. (5 marks)

(b) XYZ Resources Ltd., a listed company, is in the process of merging into ABC Transactions Ltd., which is not a listed Company. As a Company Secretary, detail the additional aspects to be noted for the merger of XYZ Resources Ltd. and ABC Transactions Ltd. in terms of Companies Act, 2013 and Securities and Exchange Board of India (SEBI) Regulations. (5 marks)

(c) Secure Source Ltd., an Indian Company, is contemplating to take over Super Securers Pte. Ltd. of Singapore through a process of merger and its top Management seeks your advice. Suggest the required compliances. (5 marks)

(d) "Accounting treatment under AS 14 is confined to Amalgamations unlike Ind AS 103." Discuss how far Ind AS 103 can be distinguished with AS 14. (5 marks)

Answer 1(a)

Organic growth strategy in corporate restructuring relates to business or financial restructuring within the organization that results in enhanced customer base, higher sales, increased revenue, without resulting in change of corporate entity. In contrast, if there is involvement of other entities in the form of mergers, takeovers, divestment, etc. it is referred to as inorganic growth strategy in corporate restructuring. Obviously, the business model changes so also management positions, financial structure with sole object of enhancing the value to shareholders. Mergers, demergers, reverse mergers, disinvestments, takeovers, joint ventures, franchising, strategic alliances, slump sale are some options that are adopted as a measure to achieve inorganic growth strategy in Corporate Restructuring.

Orderly redirection of activities, redeployment of surplus cash in other enterprises, exploiting inter-dependence among present or future businesses within corporate portfolio, risk reduction and development of core competencies are some of the objectives within overall objective of increasing the value to the shareholders on resorting to restructuring. Corporates can achieve the economies of scale through vertical, horizontal integration of enterprises for maximization of profits.

Answer 1 (b)

In the given question, XYZ Resources Ltd. is the transferor and ABC Transactions Ltd. is the transferee company. Hence, any order of National Company Law Tribunal sanctioning the Scheme of Amalgamation does not automatically operate to make the transferee company a listed company. Further the scheme needs to have a provision for opting out of the scheme with proper compensation for the shareholders of the transferor listed company as per the provisions of section 232(3)(h) of the Companies Act, 2013.

In addition, XYZ Resources Ltd., being a listed company need to file the draft scheme with stock exchange well before filing it with the Tribunal to obtain No Objection or Observation Letter in compliance with SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. The validity of such "No Objection or Observation" Letter is six months and such letter need to be placed before the Tribunal considering the sanction of the Scheme.

Answer 1(c)

Since the matter involved pertains to cross border merger of companies, it is necessary to comply with the procedure as per rule 25A of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 inserted since 13th April 2017. In accordance with said rule, a foreign company incorporated outside India may merge with an Indian Company by filing petition with National Company Law Tribunal in terms of sections 230 to 232 of the Companies Act, 2013.

It is also necessary to obtain prior approval from Reserve Bank of India (RBI). RBI has also issued Foreign Exchange Management (Cross Border Merger) Regulations, 2018 for ease of doing compliance. Merger is generally permitted with companies incorporated in foreign countries whose securities regulator is a member of Organization of Securities Commission's Multilateral Memorandum of Understanding, Central Bank is enrolled with Bank of International Settlements (BIS) and identified with Financial Action Task Force.

Answer 1(d)

Ind AS-103 deals with accounting treatment in case of each and every kind of combinations unlike AS-14 that confine only to amalgamations. Even there are judicial pronouncements stating AS-14 is not applicable even for mergers. AS-14 describes two methods of amalgamation i.e. pooling of interests method and purchase method whereas Ind AS-103 prescribes only the acquisition method for each business combination. There is no amortisation of goodwill under Ind AS-103 but tested for impairment on annual basis as per Ind AS-36 but AS-14 requires goodwill to be amortised within a maximum period of five years. Reverse acquisitions are also dealt with under Ind AS-103 but not under AS-14. Under Ind AS-103, the consideration the acquirer transfers in exchange to the acquiree includes any asset or liability resulting from a contingent consideration arrangement but this aspect is not dealt with under AS-14.

Attempt all parts of either Q. No. 2 or Q. No. 2A

Question 2

(a) The unpalatable or inevitable recession can also be a key factor to trigger Mergers/ Takeovers—how far is it proved true ?

(b) *"There may be no express protection to any dissenting minority shareholder to file his objections as a matter of right, yet the Courts/Tribunals, while approving the Scheme, follow judicious approach by inviting objections through Public Notice in Newspapers." Elucidate.*

(c) *Is it possible to retain the same characters of various reserves of transferor Companies post amalgamation, mergers or demergers as per Standards of Accounting concepts or conventions ?* *(5 marks each)*

OR (Alternate Question to Q. No. 2)

Question 2A

(i) *"Due Diligence starts much before the process of restructuring and helps in better negotiation of deals, to handle taxation and stamp duty aspects in better manner, to minimise and resolve the human and cultural issues that may arise out of mergers/ amalgamation etc". Discuss the statement in view of the fact that Due Diligence is considered as 'background check'.*

(ii) *Briefly explain four major types of anti-takeover amendments.*

(iii) *"In addition to the normal event risks, stock swap mergers involve risks associated with fluctuations in the stock prices of the two companies". Comment on the statement in view of the funding through swaps or stock to stock mergers.* *(5 marks each)*

Answer 2(a)

The year 2008 witnessed the Global Economic Crisis, thereby, bringing the economic growth across the globe to a grinding halt. A survey and study by New Zealand Trade & Enterprise revealed acquisitions and strategic alliances as a key factor to overcome economic recession to strengthen, re-focus and position the company for increased growth and profitability. The mentioned research study has also identified that Companies made acquisitions to access new markets, products, technologies, customers and talent at an accelerated pace. There were the examples of organizations that have adopted, survived and prospered during recessionary periods. All the companies studied, achieved dramatic increase in growth and profitability during the period of economic downturn or in the following recovery period.

Answer 2(b)

As per section 230(4) of the Companies Act, 2013 it is provided that in a scheme of arrangement any person or persons holding at least 10% of the shareholding or 5% of the total outstanding debt can put objection to the proposed scheme. But this does not mean that others are disabled. There exists inbuilt safeguard in the form of serving notices to every individual shareholder and creditor, so also to various statutory authorities and sectoral regulators. Stakeholders with lesser than specified percentage of shareholding may utilize such forums. Public notices issued in Newspapers also open a forum to raise objections that are just and genuine but not frivolous. Securities and Exchange Board of India (SEBI) has powers to undertake investigation, if a complaint is received from an investor or otherwise against substantial acquisitions.

Answer 2(c)

Amalgamation may be either in the nature of merger or purchase as per Accounting Standards prescribed. In case of merger, the identity of the Reserves is retained and shall be reflected in the financial statements of the transferee company in the same form in which they appeared in the balance sheet of the transferor company prior to amalgamation.

General reserve of the transferor company remains part of general reserve of the transferee company and similarly, capital reserve or revaluation reserve forms part of the Capital or Revaluation Reserve of the transferee company. Consequently, reserves available for distribution of dividends prior to amalgamation would also be available for distribution of dividends post amalgamation. However, in case of purchase only statutory reserves retain the character for the unexpired period.

Answer 2A(i)

Due diligence is the process by which confidential, legal, financial and other material information is exchanged, reviewed and appraised by the parties to a business transaction, which is conducted prior to the transaction. It is the analysis and risk assessment of an impending business transaction. It is the careful and methodological investigation of a business or persons, or the performance of an act with a certain standard of care to ensure that information is accurate and to uncover information that may affect the outcome of the transaction. It is basically a "background check" to make sure that the parties to the transaction have the required information that is needed to proceed with the transaction.

Due diligence report should provide information and insight on aspects such as the risks of a transaction, the value at which a transaction should be undertaken, the warranties and indemnities that needs be obtained from the vendor, etc.

Answer 2A(ii)

Four major types of anti-takeover amendments are mentioned below:

1. **Supermajority Amendments** - These amendments require shareholders' approval by at least 2/3 vote and sometimes as much as 90% of the voting power. Pure or inflexible super majority provisions would seriously limit the management's scope of options and flexibility in takeover negotiations.
2. **Fair-Price Amendments** - These are supermajority provisions with a Board out clause and an additional clause waiving the supermajority requirement if a fair-price is paid for the purchase of all the shares. Thus, fair-price amendments defend against two-tier tender offers that are not approved by the target's Board.
3. **Classified Boards** - It provides for a staggered, or classified Board of Directors to delay effective transfer and control in a takeover.
4. **Authorization of Preferred Stock** - This device is a defense against hostile takeover bids. Under this provision, the Board of directors is authorized to create a new class of securities with special voting rights.

Answer 2A(iii)

Funding through swaps or stock to stock mergers

In stock swap mergers or stock to stock mergers, the holder of the target company's stock receives shares of the acquiring company's stock. The majority of mergers during the past few years have been stock for stock deals. A merger arbitrage specialist will sell the acquiring company's stock short, and will purchase a long position in the target company, using the same ratio as that of the proposed transaction. If the purchasing firm is offering a half share of its stock for every share of the target company, then the merger arbitrageur will sell half as many shares of the purchasing firm as he or she buys of the target company. By going long and short in this ratio, the manager ensures that the number of shares for which the long position will be swapped is equal to the number of shares sold short. When the deal is completed, the manager will cover the short and collect the spread that has been locked in.

As with all mergers, stock swap mergers may involve event risk. In addition to the normal event risks, stock swap mergers involve risks associated with fluctuations in the stock prices of the two companies.

The terms of the deal involve an exchange of shares and are predicted on the prices of the two companies' stock at the time of the announcement, drastic changes in the share price of one or both of the companies can cause the entire deal to be re-evaluated. Merger arbitrageurs derive returns from stock swap mergers when the spread or potential return justifies the perceived risk of deal's failing.

Question 3

(a) *"Price received on sale of an undertaking as a Going Concern is a Capital Receipt". Comment on the statement with judicial pronouncements, supporting the statement. (3 marks)*

(b) *Corporates encounter pitfalls in post-merger statutory approval due to certain common errors, that need to be taken care of. Try to point out certain errors that need to be taken care of. (3 marks)*

(c) *Enumerate certain circumstances that necessitates financial restructuring, being part of Internal Corporate Restructuring. (3 marks)*

(d) *Identify the factors which make a company a desirable candidate for a takeover from the acquirer's point of view. (3 marks)*

(e) *Is it possible for a shareholder to seek an amendment to exchange ratio embodied in the scheme while considering the resolution, put forth for approval. Support your answer with decided case law(s). (3 marks)*

Answer 3(a)

Any sale of an undertaking as a going concern for a lump sum consideration is a slump sale in which values are not assigned to individual assets and liabilities that are sold. Normally, any sale of a capital asset is considered as capital receipts and subjected to capital gain tax and stock in trade is subjected to tax as revenue profit or loss.

Supreme Court held in *CIT* v. *West Coast Chemicals and Industries Ltd. 46 ITR 135*

and *CIT* v. *Mugneeram Bangur & Co 57 ITR 299,* where a slump price is paid, and no portion is attributable to the stock-in-trade, since it may not be possible to say that there is a profit other than what is resulted as the appreciation of capital.

Gujarat and Bombay High Courts have also held that there will be a capital gain only when a sale of business as a whole occurs. Undertaking of a business is a capital asset as its disposal at slump price is capital receipt which can attract capital gain tax alone.

Answer 3(b)

Some common mistakes that need to be taken care of by Corporates after post-merger are:

(a) Ego problems result in clashes that make bad situations worse;

(b) Sudden and radical changes such as relocating the company's entire production operations should be carefully considered;

(c) While the company is focussed on integration, it furnishes an ideal time for competitors to make a run on the market;

(d) If the acquired business does not belong to the area / field in which the acquiring company operates then different apporaches need to be applied;

(e) A dangerous mistake is laying off crucial employees of the acquired company. It is very complicated, delicate matter and even the seller might not have accurate idea as job titles are normally misleading.

Answer 3(c)

During the life of a Company, any one or more of the following circumstances prompt for Company's restructuring:

(i) Injecting more working capital to meet the increased market demand.

(ii) Scenarios where a company is unable to fulfill its commitments.

(iii) If there is shortage in obtaining further credit from suppliers of raw materials, consumable stores, components, etc. and from other parties like those doing job work for the Company.

(iv) Failure to utilise optimum capacity for lack of liquid funds.

Financial restructuring involves rearrangement of its financial structure so as to make the Company's finances more balanced. Every Company targets to strike a balance in ever changing business environment.

Answer 3(d)

It is possible to identify some characteristics that make a company a desirable candidate for a takeover from the acquirer's point of view. These are:

— Low stock price in relation to the replacement cost of assets of their potential earning power;

— A highly liquid balance sheet with large amounts of excess cash, a valuable securities portfolio, and significantly unused debt capacity;

— Good cash flow in relation to current stock prices;

— Subsidiaries and properties which could be sold off without significantly impairing cash flow; and

— Relatively small stockholdings under the control of an incumbent management.

Answer 3(e)

A shareholder attending the meeting either can assent or dissent the resolution but cannot suggest any alteration in the scheme. It was held by Mumbai High Court in the matter of *Dinesh Veajlal Lakhani* v. *Parke Davis (India) Ltd [2005] 66 CLA 91 (Bom)* that the swap ratio forms integral part of scheme of amalgamation and the procedural provisions are embodied in the relevant rules. The exchange ratio is a matter of expert determination. Since it constitutes the foundation of the scheme of amalgamation any amendment to it will nullify that basis. Thus, the shareholder has no other right beyond assenting or dissenting the resolution put for voting.

PART B

Question 4

(a) *"Valuation is influenced not only by the motive of the acquirer company but also that of target company's objectives." Analyse the statement in brief. (5 marks)*

(b) *The Managing Director of a company decides that his company will not pay any dividend till he survives. His current life expectancy is 20 years. After that time it is expected that the company could pay dividend of ₹30 per share indefinitely. At present the company could afford to pay ₹5 per share forever. The shareholders of the company expect return on equity @ 10%.*

Find out :

(i) What would be the share price at the end of 20 years ?

(ii) What would be the present value of a share using discounting factor of 0.1468 (at 10% for 20 years period) ?

(iii) What is the current price of a share if dividend payment is Rs. 5 per share?

(iv) What is the loss to the shareholders in the aforesaid scenario ? (5 marks)

(c) *Explain Market Comparables Method of valuation. What are the steps involved in this method of valuation ? (5 marks)*

Answer 4(a)

Merger/Amalgamation/Takeover is backed by the aspect of valuation. Appropriate method of valuation of a business depends to a great extent on the acquisition motives. The reasons for valuation could be to achieve the objectives of the top management i.e. either purely financial aspects relating to taxation, assets stripping, financial restructuring or business related such as expansion or diversification.

However, behavioural reasons have more to do than personal ambitions or objectives of the top management. Normally, top management has desire to expand and diversify

the needs to be chosen between Make or Buy decision. A criterion adopted to arrive at a decision is to evaluate present value of the differential cash flows. Acquisitions are not only normally market driven but also influenced by non-financial considerations. Thus the value of a target gets affected not only by the motive of the acquirer, but also by the target company's objectives. The price could be affected by the motives of the other bidders as well.

Answer 4(b)

As per Managing Director's policy:

(i) The value of the share at the end of 20 years = 30/ 0.10 = Rs.300

(ii) The present value of share = 300 x (0.1468) = Rs.44.04

As per current status of company:

(iii) If the company could pay dividends of Rs.5 per share forever from the beginning, the current price of share would be = 5/0.10 = Rs.50.00

(iv) Thus, the loss to each shareholder is the difference of two prices : Rs.50 – Rs.44.04 = Rs. 5.96 per share

Answer 4(c)

Market Comparables : This method of valuation is generally applied in case of unlisted entities. This method estimates value by relating the same to underlying elements of similar companies for past years. It is based on market multiples of 'comparable companies'. For example:

— Earnings / Revenue Multiples (Valuation of Pharmaceutical Brands)

— Book Value Multiples (Valuation of Financial Institution or Banks)

— Industry Specific Multiples (Valuation of steel companies based on production capacities like price per ton capacity of steel, per store value in the days of retail boom, price per click in e-commerce)

— Multiples from recent M&A Transactions

Following steps are involved in this method of valuation:

1. Comparable assets are identified and their market values are obtained

2. Market values are converted into standardized values, since the absolute price cannot be compared

3. Standardised value or multiple for the asset being analysed are compared with the standardised value of the comparable asset, controlling for any difference between the firms that might affect the multiple, to judge whether the asset is under or over-valued.

Question 5

(a) *From the following information determine the possible value of brand :*

	(₹ in lakh)
Profit After Tax (PAT)	*2,000*
Tangible Fixed Assets	*8,000*
Identifiable intangible assets other than the brand	*1,200*
Weighted average cost of capital	*15%*
Normal return on tangible assets	*20%*
Capitalisation factor for intangible assets	*25%*

(b) *From the following information calculate the value of a share if you want to :*

(i) *buy a small lot of shares;*

(ii) *buy a controlling interest in the company.*

Year	*Profit (₹)*	*Capital Employed (₹)*	*Dividend (%)*
2015	*24,50,000*	*3,50,00,000*	*15*
2016	*40,00,000*	*5,00,00,000*	*18*
2017	*60,00,000*	*6,00,00,000*	*20*
2018	*72,00,000*	*6,00,00,000*	*25*

The market expectation is 15% from the similar industry.

(c) *"The key to valuation is finding a common ground between all the companies for the purpose of a fair evaluation." Comment with reference to factors influencing valuation.* *(5 marks each)*

Answer 5(a)

Calculation of possible value of brand

	(Rs. in lakh)
Profit after tax (PAT)	2,000
Less : Profit allocated to tangible assets (20% of Rs.8,000)	1,600
Profit allocable to intangible assets including brand capitalization factor = 25%	400
Capitalised value of intangible assets including brand (400/25x100)	1,600
Less : Identifiable intangible assets other than the brand	1,200
Value of the brand	400

Hence, value of the brand = Rs.400 lakh

Answer 5(b)

(i) *Buying a small lot of shares* : For this purpose dividend yield method is most appropriate for valuation of shares. For calculation of average dividend, weighted average will be more appropriate since dividend rate is rising :

Year	*Rate of dividend (%)*	*Weights*	*Products*
2015	15	1	15
2016	18	2	36
2017	20	3	60
2018	25	4	100
		10	211

Average dividend = 211/10 = 21.10%

Value of a share on the basis of dividend for buying a small lot =

(Average dividend rate / Market expectation) x 100

= (21.10 / 15) x 100 = Rs.140.67 per share

(ii) *Buying a controlling interest in the company* : For this purpose, total profit will be relevant to determine the value of shares as the shareholders have the capacity to influence the decision of distribution of profit. As the profit is displaying a rising trend, weighted average will be more appropriate for calculation purposes:

Year	*Yield (%) = (Profit/capital employed) x 100*	*Weights*	*Products*
2015	7	1	7
2016	8	2	16
2017	10	3	30
2018	12	4	48
		10	101

Average yield = 101/10 = 10.10 %

Average value per share = (10.10/15) x 100 = Rs.67.33

Answer 5(c)

Determining the value of a business is a complicated and intrinsic process. Valuing a business requires the determination of its future earnings potential, the risks inherent in those future earnings. Strictly speaking, a company's fair market value is the price at which the business would change hands between a willing buyer and willing seller when neither is under any compulsion to buy or sell and both parties have knowledge of relevant facts.

The other salient factors influencing valuation are:

– The stock exchange price of the shares of the two companies before the commencement of negotiations or the announcement of the bid.

– Dividends paid on the shares.

– Relative growth prospects of the two companies.

– In case of equity shares, the relative gearing of the shares of the two companies.

– Debenture stock to the amount of issued ordinary share capital.

– Net assets of the two companies.

– Voting strength in the merged enterprise of the shareholders of the two companies.

– Past history of the prices of shares of the two companies.

PART C

Attempt all parts of either Q. No. 6 or Q. No. 6A

Question 6

(a) Explain the concept "Ease of doing business includes easy exit by investors and creditors that prompts national policy makers' constant endeavour to reform law relating to Insolvency or Bankruptcy".

(b) The purpose of the Model Law is to provide effective mechanism for dealing with cases of cross-border insolvency. Comment upon the statement.

(c) Write a short note on winding up under the Companies Act, 2013 with special reference to Insolvency and Bankruptcy Code, 2016.

(d) There are certain persons who are not entitled to make application to NCLT for initiation of corporate insolvency resolution process. Explain. (5 marks each)

OR (Alternative question to Q. No. 6)

Question 6A

(i) "Committing default or failure of Resolution Plan may lead to liquidation of a body corporate under Insolvency and Bankruptcy Code, 2016 but could there be other circumstances for which a Tribunal may order for winding up ?" Examine and explain. (5 marks)

(ii) SARFAESI Act is a complete code in itself and there is no lacuna or ambiguity in it to warrant reading something more into it or to borrow anything from the Companies Act. Comment on the statement in light of decided case laws. (5 marks)

(iii) Write a note on "Effect of recognition of a foreign main proceeding" under the UNCITRAL Model law. (5 marks)

(iv) Write a short note on the role of Insolvency and Bankruptcy Board of India. (5 marks)

Answer 6(a)

Every stakeholder especially investors and creditors chose to get early return on their investments for sustenance. Hence, policy makers constantly reform law relating to insolvency for ease of doing business that includes easy exit also. During last two and half decades, Indian financial system has undergone tremendous transformation. Several financial reforms have been initiated to promote an efficient, well diversified and competitive financial system with ultimate objective of improving the allocative efficiency of resources so as to accelerate economic development. There are reforms in laws and systems to be at par with International Standards and to incentivise the foreign investors to invest in the Indian economy. Committees were formed to find ways to improve the law relating to Insolvency resulting into framing of Insolvency and Bankruptcy Code, 2016.

Answer 6(b)

The purpose of the Model Law is to provide effective mechanisms for dealing with cases of cross-border insolvency so as to promote the objectives of:

(a) Cooperation between the courts and other competent authorities of different countries dealing with cases of cross-border insolvency;

(b) Greater legal certainty for trade and investment;

(c) Fair and efficient administration of cross-border insolvencies that protects the interests of all creditors and other interested persons, including the debtor;

(d) Protection and maximization of the value of the debtor's assets; and

(e) Facilitation of the rescue of financially troubled businesses, thereby protecting investment and preserving employment.

Answer 6(c)

Winding-up under the Companies Act, 2013

The Companies Act, 2013 contain provisions for winding-up of companies on various grounds including inability of companies to pay their debts. The notification of the Insolvency and Bankruptcy Code, 2016 has deleted the provisions in the Companies Act, 2013 regarding winding-up of companies on the ground of inability to pay their debts and those relating to voluntary winding-up of companies and detailing the requirements for insolvency resolution of corporate persons and voluntary winding-up in the Code itself. The Code will exclusively be governing the insolvency resolution and liquidation of corporates.

The Companies Act, 2013 shall continue to govern winding-up of companies on various other grounds excluding inability to pay debts. Sections 270 to 288, Sections 290 to 303, Section 324 and Sections 326 to 365 of Chapter XX of the Companies Act, 2013 contain the provisions related to winding-up of the company.

Answer 6(d)

The following persons shall not be entitled to make application to NCLT for initiation of corporate insolvency resolution process:

(a) a corporate debtor undergoing a corporate insolvency resolution process; or

(b) a corporate debtor having completed corporate insolvency resolution process twelve months preceding the date of making of the application; or

(c) a corporate debtor or a financial creditor who has violated any of the terms of resolution plan which was approved twelve months preceding the date of making application; or

(d) a corporate debtor in respect of whom a liquidation order has been passed so that finality of the liquidation order is ensured.

For making an application, a corporate debtor includes a corporate applicant in respect of such corporate debtor.

Answer 6A(i)

In case the Resolution Professional is unable to come-up with a resolution plan approved by at least sixty six percent of the Committee of Creditors or the plan submitted does not confirm the requirements of the Code, the Tribunal may pass an order of liquidation of the Corporate Debtor in terms of Section 33 of the Insolvency and Bankruptcy Code, 2016 so also in case the approved resolution plan is contravened by the Corporate Debtor.

Apart from the above, Section 271 of the Companies Act, 2013 enumerates circumstances such as company's own resolution, fraudulent or felony activities, default in filing financial statements or annual returns for more than 5 consecutive years or just and equitable reasons for which Tribunal may order liquidation. If the company has acted against the interests of the sovereignty and integrity of India, the security of the State then also it may be wound-up.

Answer 6(A)(ii)

Pegasus Assets Reconstruction (P) Ltd v. *Haryana Concast Ltd.*, civil appeal nos. 3646 of 2011, 9293-9294 OF 2014 AND 14736 TO 14738 of 2015, date December 29, 2018, [2015] 64 taxmann.com 394 (SC)

Considering section 283 of the Companies Act, 2013 / Section 456 of Companies Act, 1956 read with section 13 of the SARFAESI Act, 2002, the Supreme Court in the matter of winding-up and custody of company's property opined that SARFAESI Act, 2002 is a complete code in itself and there is no lacuna or ambiguity in it to warrant reading something more into it or to borrow anything from Companies Act, 2013. The Court mentioned that as per section 13 of the SARFAESI Act, a secured creditor has right to enforce its security interest without intervention of Court or Tribunal and the powers under Companies Act, 2013 cannot be wielded by Company Judge to interfere with proceedings by a secured creditor who has opted to stay outside winding-up process to realize its secured interests as per provisions of SARFAESI Act.

Answer 6(A)(iii)

Effect of recognition of a foreign main proceeding (Article 20)

Once foreign proceeding is recognized which is a foreign main proceeding under the UNCITRAL Model Law, the following are the effects:

(a) Commencement or continuation of individual actions or individual proceedings concerning the debtor's assets, rights, obligations or liabilities is stayed;

(b) Execution against the debtor's assets is stayed; and

(c) The right to transfer, encumber or otherwise dispose of any assets of the debtor is suspended.

The effects provided by Article 20 are not discretionary in nature. These flow automatically from recognition of the foreign main proceeding. The automatic effects under Article 21 apply only to main proceedings.

Answer 6(A)(iv)

Role of the Insolvency and Bankruptcy Board of India (IBBI) is as under:

1. Regulating all matters related to insolvency and bankruptcy process.
2. Setting out eligibility requirements of insolvency intermediaries i.e., Insolvency Professionals, Insolvency Professional Agencies and Information Utilities.
3. Regulating entry, registration and exit of insolvency intermediaries.
4. Making model bye laws for Insolvency Professional Agencies.
5. Setting our regulatory standards for Insolvency Professionals.
6. Specifying the manners in which information utilities can collect and store data.

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