GUIDELINE ANSWERS

PROFESSIONAL PROGRAMME

JUNE 2015

MODULE 1

THE INSTITUTE OF
Company Secretaries of India
IN PURSUIT OF PROFESSIONAL EXCELLENCE
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These answers have been written by competent persons and the Institute hopes 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.

C O N T E N T S

NOTE: Guideline Answers of the last Four Sessions need to be updated in the light of changes and references given below:

PROFESSIONAL PROGRAMME

UPDATING SLIP

ADVANCED COMPANY LAW AND PRACTICE

MODULE – I – PAPER 1

Examination Session	*Question No.*	*Updating required in the answer*
All previous sessions	—	All answers are based on the notified provisions of Companies Act, 2013 and the provisions of Companies Act, 1956 which are still in force. SEBI (ICDR) Regulations, 2009 as amended from time to time.

UPDATING SLIP

SECRETARIAL AUDIT, COMPLIANCE MANAGEMENT AND DUE DILIGENCE

MODULE – I – PAPER 2

Examination Session	*Question No.*	*Updating required in the answer*
All previous sessions	—	All answers are based on the notified provisions of Companies Act, 2013 and the provisions of Companies Act, 1956 which are still in force. SEBI (SAST) Regulations, 2011 as amended from time to time. SEBI (ICDR) Regulations as amended from time to time. Consolidated FDI Policy as amended from time to time.

UPDATING SLIP

CORPORATE RESTRUCTURING, VALUATION AND INSOLVENCY

MODULE – I – PAPER 3

Examination Session	*Question No.*	*Updating required in the answer*
All previous sessions	—	All answers are based on the notified provisions of Companies Act, 2013 and the provisions of Companies Act, 1956 which are still in force. However the provisions under Companies Act, 2013 pertaining to mergers/ acquisitions/winding up are yet to be notified and the provisions relating to buy back and alteration of capital are already notified. Accordingly most of the answers are based on the Companies Act, 1956. SEBI (SAST) Regulations, 2011 as amended from time to time.

PROFESSIONAL PROGRAMME EXAMINATION

JUNE 2015

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,1956 unless stated otherwise.

Question 1

Answer the following :

(a) Within what period subscribers to the memorandum are required to bring in share application money in the company ? Explain with relevance to obtaining certificate of commencement of business and issue of share certificates to the subscribers.

(b) Explain with reference to the provisions of the Companies Act, 2013 whether an independent director is entitled to :

(i) Sitting fee;

(ii) Remuneration; and

(iii) Employees stock option.

(c) "No company shall enter into any contract or arrangement with a related party." Examine the validity of the statement.

(d) "All resolutions, no matter how simple they are, should be drafted in clear and distinct terms, since resolutions embody the decisions of the meeting." Comment with reasons. *(5 marks each)*

Answer 1(a)

Sub-section (1) of Section 11* of the Companies Act, 2013 provides that a company having a share capital shall not commence any business unless a declaration is filed by a director in INC.21 along with the fee and the contents of the form duly verified by a Company Secretary in practice or a Chartered Accountant or a Cost Accountant in practice, with the Registrar that every subscriber to the memorandum has paid the value of the shares agreed to be taken by him and the paid-up share capital of the company is not less than five lakh rupees in case of a public company and not less than one lakh rupees in case of a private company on the date of making of this declaration.

Further, sub-section (3) of section 11 provides that where no such declaration has been filed with the Registrar within a period of one hundred and eighty days of the date of incorporation of the company and the Registrar has reasonable cause to believe that the

* Section 11 of the Companies Act, 2013 has been omitted vide Companies (Amendment) Act, 2015 w.e.f. May 29, 2015. Student who gives the updated answer may be given marks.

company is not carrying on any business or operations, he may initiate action for the removal of the name of the company from the register of companies under Chapter XVIII.

Further, Schedule I, Table F, Regulation II(2) of the Companies Act, 2013 state that every person whose name is entered as a member in the register of members shall be entitled to receive within two months after incorporation, in case of subscribers to the memorandum, certificate(s) for all his shares.

Answer 1(b)

Section 149(9) clearly states that notwithstanding anything contained in any other provision of this Act, but subject to the provisions of sections 197 and 198, an independent director shall not be entitled to any stock option and may receive remuneration by way of fee provided under sub-section (5) of section 197 i.e. sitting fee for attendingmeetings, reimbursement of expenses for participation in the Board and other meetings and profit related commission as may be approved by the members.

Rule 4 of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, states that the amount of sitting fees payable to a director for attending meetings of the Board or committees thereof may be such as may be decided by the Board of directors or the Remuneration Committee thereof which shall not exceed the sum of rupees one lakh per meeting of the Board or committee thereof. Further, the Board may decide different sitting fee payable to independent and non-independent directors other than whole-time directors. For giving sitting fee, only board resolution is sufficient. Sitting fees payable to Independent Directors shall not be less than sitting fees payable to other Directors.

Answer 1(c)

"No company shall enter into any contract or arrangement with a related party"- The statement is not valid. A company may enter into any contract or arrangement with a related party subject to section 188. The section provides for approval from the Board/ members for various contracts or arrangementswith a related party with respect to -

(a) sale, purchase or supply of any goods or materials;

(b) selling or otherwise disposing of, or buying, property of any kind;

(c) leasing of property of any kind;

(d) availing or rendering of any services;

(e) appointment of any agent for purchase or sale of goods, materials, services or property;

(f) such related party's appointment to any office or place of profit in the company; and its subsidiary company or associate company; and

(g) underwriting the subscription of any securities or derivatives thereof, of the company.

The first proviso read with Rule 15 of the companies (Meetings of Board and its Powers) Rules, 2014 further provides for a resolution in a general meeting where the transaction amount exceeds certain limits. Approval in General meeting is not required

in case the transactions are entered into by the company in its ordinary course of business which are on an arm's length basis.

The term 'Related Party' is defined under section 2(76) of the Companies Act, 2013

* The resolution contemplated by the first proviso was a special resolution but w.e.f May 2015 it is ordinary resolution. The requirement of Board resolution is not applicable for transactions in between Holding and its wholly owned subsidiary. Student who gives the updated answer may be given marks.

Answer 1(d)

The following points should be remembered while drafting resolutions, both for Board and general meetings:

(a) AII essential facts are included in the resolution e.g. the resolution for re-appointment of a managing director should indicate that the re-appointment is subject to the approval of the Central Government, if approval of the Central Government is required and should also cover the period of appointment, terms and conditions of such appointment.

(b) Surplus and meaningless words or phrases should not be included in resolutions.

(c) Reference to documents approved at a meeting should be clearly identified, i.e. the re-appointment of a managing director should indicate that such appointment is on the terms and contained in the draft agreement, a copy of which was placed before the meeting and initialled by the chairman for the purpose of identification.

(d) Resolution must indicate the relevant provisions or sections of the Act and the Rules pursuant to which they are being passed.

(e) If a resolution is one which requires the approval of the members/ Central Government or confirmation of the National Company Law Tribunal /Court, this must be stated in the resolution.

(f) A resolution must indicate when it will become effective.

(g) A resolution must confine to one subject matter and two distinct matters should not be covered in one resolution.

(h) A resolution should be crisp, concise and precise and should be flexible enough to take care of eventualities.

(i) Where lengthy resolutions have to be approved, they should be arranged in their logical order having regard to the subject matter of the resolution.

(ii) A resolution must be self explanatory i.e. so drafted that anybody not present at the meeting or anybody referring to it at a later date will know clearly what the decision was at that meeting without referring to any other document.

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

Question 2

(a) Explain the term 'private placement' in relation to issue of securities by a company. What conditions must be fulfilled by a company under the Companies Act, 2013 before issuing securities on private placement basis.

(b) Explain the term 'preferential offer'. Whether a company issuing securities on preferential basis is also required to comply with the conditions concerning private placement ?

(c) Distinguish between 'defunct company' and 'dormant company'.

(d) Explain the provisions governing one person company (OPC). Can a person incorporate more than one OPC ? (4 marks each)

OR

Question 2A

(i) Discuss the concept of 'rotation of auditors' of a company as per provisions of the Companies Act, 2013. Is the concept also applicable to secretarial auditor? (4 marks)

(ii) Explain the provisions governing vigil mechanism under the Companies Act, 2013. Is it applicable to all companies ? (4 marks)

(iii) A company may issue secured debentures if it fulfills certain conditions. State the conditions to be fulfilled. (4 marks)

(iv) ABC Ltd. appointed Anil as director on 1st November, 2014. Subsequently, Anil obtained his DIN on 10th November, 2014. ABC Ltd. filed DIR-12 on 15th November, 2014. Examine the legal validity of the appointment of Anil. (4 marks)

Answer 2(a)

Explanation II (ii) to section 42 (1) defines the term "private placement" to mean any offer of securities or invitation to subscribe securities to a select group of persons by a company (other than by way of public offer) through issue of a private placement offer letter in form PAS-4 [Rule 12 of the Companies (Prospectus and Allotment of Securities) Rules, 2014] and which satisfies the conditions specified in section 42 of the Companies Act, 2013.

Under private placement, the offer of securities or invitation to subscribe securities, shall be made to such number of persons not exceeding fifty or such higher number as may be prescribed in a financial year for each kind of security, (excluding qualified institutional buyers, and employees of the company being offered securities under a scheme of employee stock option), and on such conditions as may be specified under Rule 14(2) of Companies (Prospectus and Allotment of Securities) Rules, 2014. Rule 14(2) prescribes the limit of two hundred persons in aggregate in a financial year.

The following conditions to be fulfilled by a company before issuing securities on private placement basis:

— the proposed offer of securities has been previously approved by the shareholders of the company, by a Special Resolution, for each of the offers or invitation.

— If the said offer or invitation is for non-convertible debentures, it shall be sufficient if the company has passed a previous special resolution only once in a year for all the offers or invitation for such debentures during the year.

— The value of such offer or invitation per person shall be with an investment size of not less than 20,000 rupees of face value of the securities.

— All monies payable towards subscription of securities under this section shall be paid through cheque or demand draft or other banking channels but not by cash.

— The payment to be made for subscription to securities shall be made from the bank account of the person subscribing to such securities and the company shall keep the record of the Bank account from where such payments for subscriptions have been received. The monies payable on subscription to securities to be held by joint holders shall be paid from the bank account of the person whose name appears first in the application.

— All offers shall be made only to such persons whose names are recorded by the company prior to the invitation to subscribe, and that such persons shall receive the offer by name.

— Offer letter should be accompanied by application form serially numbered and addressed specifically to a person and should be sent in 30 days from recording of names [sec 42(7)].

— No person other than addressee can apply for shares.

— Complete information about offer should be filed with the Registrar in 30 days of circulation of offer.

— In the explanatory statement justification for price should be given.

Answer 2(b)

Explanation (i) to rule 13(1) of the Companies (Share Capital and Debentures) Rules, 2014, explains the term 'preferential offer' to mean an issue of shares or other securities, by a company to any select person or group of persons on a preferential basis and does not include shares or other securities offered through a public issue, rights issue, employee stock option scheme, employee stock purchase scheme or an issue of sweat equity shares or bonus shares or depository receipts issued in a country outside India or foreign securities.

As per section 62(1)(c), where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares may be offered by way of a preferential offer, to any persons whether or not the holder of equity shares or employee of the company, if authorised by a special resolution passed in a general meeting.

The company issuing securities on preferential basis should also comply with conditions laid down in section 42 of the Act for private placement.

Answer 2(c)

In accordance with Section 455 of the Companies Act, 2013, Dormant Company is one which has obtained such status in a certificate from the Registrar of Companies. It is an inactive company which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years, or has not filed financial statements and annual returns during the last two financial years. The application may be made to the ROC for obtaining the status of a dormant company in form MSC-1.

The Registrar may send notice to a company which has not filed financial statements or annual returns for two financial years consecutively, and enter the name of the company in Register of dormant companies.

A company, once identified as dormant, will need to maintain only a minimum number of directors and pay some annual fees as prescribed in the Companies (Registration Offices and Fees) Rules, 2014 to retain its dormant statusand may become active company on making an application accompanied by prescribed documants and fees.

Defunct company has been mentioned in section 560 of the Companies Act, 1956. Defunct company is a company which is not operating or functioning; not carrying on any business or in operation. Generally, it is evident from the latest available balance sheet of a company, if a company is not filing its balance sheet for many years then also the concerned ROC has reasonable cause to believe that the company is not in operation. It is a company without any assets or liabilities. It has paid up capital / reserves on the left hand side of Balance sheet and losses on the right hand side.

As per section 560 of the Companies Act'1956, Any defunct company desirous to strike off its name from the register of Registrar of company can apply in Form FTE for strike off its name from the register maintained by ROC as per Guidelines for 'FAST TRACK EXIT MODE' issued vide General Circular No. 36/2011 dated 07.06.2011.

For the purpose of applying for the FTE scheme, a defunct company means a company which has:

— Nil asset and nil liability, and

— Not commenced any business or activity since incorporation or

— Not been carrying any business operation since last one year before making an application under Fast Track Exit Scheme.

Answer 2(d)

Section 2(62) of the Companies Act, 2013 defines "one person company" as a company which has only one person as member.

Section 3 of the Companies Act, 2013 read with Rule 3 of the Companies (Incorporation) Rules, 2014 state that only a natural person who is an Indian citizen and resident in India:-

(a) shall be eligible to incorporate a One Person Company;

(b) shall be a nominee for the sole member of a One Person Company.

The subscriber to the memorandum of a One Person Company shall nominate a person, in form INC 2 after obtaining prior written consent of such person, who shall, in the event of the subscriber's death or his incapacity to contract, become the member of that One Person Company. The name of the person nominated shall be mentioned in the memorandum of One Person Company and such nomination shall be filed with the Registrar at the time of incorporation of the company along with its memorandum and articles.

The nomination has to be filed with Registrar. Nomination filed can be withdrawn at

later date. New nomination to be filed in 15 days in Form INC 4 along with written consent in INC 3.

OPC will lose its status if paid up capital exceeds Rs. 50 lakhs or average annual turnover is more than 2 crores in three immediate preceding consecutive years.

OPC can not convert itself in any othjer kind of company before two years of incorporation except under criteria of capital and turnover as mentioned above.

No minor shall become member or nominee of the One Person Company or hold share with beneficial interest.

A One Person Company needs to have minimum of one director. It can have directors up to a maximum of 15 which can also be increased by passing a special resolution as in case of any other company.

At least one meeting of the Board of Directors to be conducted in each half of a calendar year. Gap between the two meetings should not be less than ninety days.

OPC can not be incorporated or converted into sec 8 company. OPC cannot carry out NBFC business. A private company can be converted into OPC subject to certain conditions.

A person can incorporate only one "One Person Company".

Answer 2A(i)

In terms of Section 139(2) read with rule 5 of the Companies (Audit and Auditors) Rules, 2014, the provisions of rotation of auditors is applicable to -

(i) listed companies;

(ii) All unlisted public companies having paid up share capital of Rs. 10 crores or more;

(iii) All private limited companies having paid up share capital of Rs. 20 crores or more;

(iv) All companies having paid up share capital of below threshold limit specified in (i) and (ii) above; but having public borrowings from banks, financial institutions or public deposits of Rs.50 crores or more.

(v) The concept of rotation of auditors shall not apply to one person companies and small companies.

No individual shall be appointed or reappointed as auditor for more than one term of 5 consecutive years and an individual auditor who has completed five consecutive years shall not be eligible for re-appointment as auditor in the same company for 5 years from the date of completion of the first term of five years.

No audit firm shall be appointed or re-appointed as auditor for more than two terms of 5 consecutive years and the audit firm which has completed its two terms of five consecutive years, shall not be eligible for re-appointment as auditor in the same company for 5 years from the completion of such terms. Firm shall include a limited liability partnership.

The concept of rotation of auditors is applicable only in case of statutory auditor and not in case of secretarial auditor.

Answer 2A(ii)

Section 177(9) of the Companies Act 2013 read with Rule 7 of the Companies (Meetings of Board and its Powers) Rules 2014 has made it mandatory to establish vigil mechanism in all listed companies and companies that accept deposits from public and companies which borrow money from bank and public institutions in excess of Rs. 50 Crores. This is to enable a company to evolve a process to ensure ethical corporate behaviour, while rewarding employees for their integrity and for providing valuable information to the management on deviant practices.

It gives protection to the persons who has observed something wrong happening in the company and wants to draw attention of the management to such wrong.

Sub-section (10) of section 177 further provides that the vigil mechanism shall provide for adequate safeguards against victimisation of persons who use such mechanism and make provision for direct access to the chairperson of the Audit Committee in appropriate or exceptional cases.

In case company does not have a Audit committee, a director has to be designated to play a role of audit committee.

The details of establishment of such mechanism shall be disclosed by the company on its website, if any, and in the Board's report. Repeated frivolous should be dealt with appropriately.

Answer 2A(iii)

Section 71(3) states that a company may issue secured debentures subject to terms and conditions as prescribed in Rule 18(1) of the Companies (Share Capital and Debentures) Rules, 2014. The company shall not issue secured debentures, unless it complies with the following conditions :-

(a) An issue of secured debentures may be made, provided the date of redemption shall not exceed ten years from the date of issue. However, a company engaged in the setting up of infrastructure projects or infrastructure finance companies, or Infrastructure Debt fund NBFC may issue secured debentures for a period exceeding ten years and but not exceeding thirty years;

(b) such an issue of debentures shall be secured by the creation of a charge, on the properties or assets of the company, having a value which is sufficient for the due repayment of the amount of debentures and interest thereon;

(c) the company shall appoint a debenture trustee before the issue of prospectus or letter of offer for subscription of its debentures and not later than sixty days after the allotment of the debentures execute a debenture trust deed to protect the interest of the debenture holders as per sec 71(5) and in compliance with conditions as in Rule 18(2) ; and

(d) the security for the debentures by way of a charge or mortgage shall be created in favour of the debenture trustee on-

  (i) any specific movable property of the company (not being in the nature of pledge); or

(ii) any specific immovable property wherever situate, or any interest therein.

Answer 2A(iv)

Section 152(3) of the Companies Act, 2013, prescribes that no person shall be appointed as a director of a company unless he has been allotted the Director Identification Number (DIN) under section 154.

Further sub-section (4) prescribes that every person proposed to be appointed as a director by the company in general meeting shall furnish his DIN.

In addition, rule 9 of the Companies (Appointment and Qualification of Directors) Rules, 2014 prescribes that every individual, who is to be appointed as director of a company shall make an application electronically in Form DIR-3 to the Central Govt. for the allotment of a DIN.

Based upon the legal provisions of the Act and rules made thereunder, the appointment of Anil as director by ABD Ltd. is not valid.

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

Question 3

(a) Give a specimen of Board resolution for appointment of whole-time key managerial personnel under section 203.

(b) Shine Ltd. wishes to appoint PMQ firm for the first time as the auditor of the company for a period of 5 years at the company's annual general meeting to be held on 30th June, 2015. You are required to —

(i) Draft a resolution to be passed at the AGM; and

(ii) State whether PMQ firm can be re-appointed on the expiry of the above tenure.

(c) Royal Ltd. wishes to appoint an independent director on the Board of the company.

Explain the procedure and also draft a resolution to be passed by the shareholders of Royal Ltd.

(d) BST is a company incorporated as a company not for profit under section 25 of the Companies Act, 1956. The Board of BST has decided to convert the same into a public company under section 2(71). Explain the procedure governing conversion of BST into BST Ltd. (4 marks each)

OR (Alternate question to Q.No. 3)

Question 3A

Write notes on the following :

(i) Conditions for issuance of sweat equity shares

(ii) Declaration of dividend

(iii) Auditors not to render certain services

(iv) XBRL filing. (4 marks each)

Answer 3(a)

"Resolved that pursuant to provisions of the sections 196 and 203 of the Companies Act, 2013 and rules made thereunder, Mr. ……. Director of the company, be and is hereby appointed as a managing director of the company for a period of 5 years effective from 1st July, 2015 and that he may be paid remuneration as follows:

(a) Monthly salary of Rs….. lakh and a commission of 1% on the Net Profits of the company, if any.

(b) Perquisites in accordance with Part II of Schedule V of the Companies Act, 2013.

(c) Housing, medical reimbursement, home town concession, conveyance, health insurance, gratuity and provident fund, as per the company's rules.

(d) In case of inadequacy of profits, the remuneration payable to him shall be subject to the limits as specified in section 197 and Schedule V of the Companies Act, 2013.

Resolved further that the other terms and conditions of the appointment shall be as per the draft agreement tabled before the meeting duly initialed by the Chairman of the meeting for the purpose of identification and that Mr …. Director of the company is hereby authorized to execute the agreement for and on behalf of the company as per the said draft.

Resolved further that the Mr….. Company Secretary of the company be and is hereby authorized to affix digital signature and submit Form DIR-12 and MR 1 with the Registrar of Companies and to do all such acts and deeds as may be required to be done in this regard.

Date _____, 2015.

Sd/-
Board of Directors

Answer 3(b)(i)

Specimen resolution for appointment of first auditors

"RESOLVED THAT pursuant to section 139 and other provisions of the Companies Act, 2013 as may be applicable, M/s PMQ , Chartered Accountants, having firm registration number ... be and are hereby appointed as Statutory Auditors of the Company to hold office from the conclusion of this Annual General Meeting till the conclusion of the Annual General Meeting to be held for the year ending 31.03.2019.

RESOLVED FURTHER THAT remuneration payable to the Auditors be decided mutually between the Auditors and the Board of Directors of the Company."

Answer 3(b)(ii)

In case of specified companies, the concept of rotation of auditor applies. Section 139(2) provides that in such companies, an audit firm may be appointed or reappointed as auditor upto two consecutive terms of five consecutive years. Accordingly, the PMQ firm can be re-appointed on the expiry of the tenure of five years.

Note : It is not clear in the question that whether Shine limited is covered under

section 139(2). Also whether or not, PMQ is a sole proprietor firm or partnership firm. The answer would be changed accordingly.

Answer 3(c)

Procedure for appointment of Independent Director

(1) Appointment process of independent directors shall be independent of the company management; while selecting independent directors the Board of Royal Ltd. shall ensure that there is appropriate balance of skills, experience and knowledge in the Board so as to enable the Board to discharge its functions and duties effectively.

(2) The Board of directors of the Royal Ltd., depending on the requirements of the Royal Ltd. and profile of independent directors may select the independent director from data bank maintained by any notified body, Institute or association.

(3) Ensure that any individual who intends to be an independent director of the Royal Ltd. should have Directors Identification Number (DIN).

(4) Ensure that the proposed person has furnished to the Royal Ltd. consent in writing in form DIR-2 to act as such director on or before his/her appointment.

(5) Ensure that the person intended to be an independent director should not be already director in more than prescribed number of companies.

(6) Arrange to obtain a declaration from the director that he meets the criteria of independence as required under section 149(6) of the Companies Act, 2013 at the first meeting of the Board of Royal Ltd. in which he participates as a director.

(7) The appointment of independent director(s) of the Royal Ltd. shall be approved at the meeting of the shareholders.

(8) Arrange to send the notice of meeting to the members along with explanatory statement.

(9) Ensure that the explanatory statement attached to the notice of the meeting for approving the appointment of independent director shall include a statement that in the opinion of the Board, the independent director proposed to be appointed fulfils the conditions specified in the Act and the rules made thereunder and that the proposed director is independent of the management.

(10) Ensure that the appointment of independent directors shall be formalized through a letter of appointment.

(11) Arrange to file with the Registrar Form DIR-12 within thirty days of his/her appointment.

(12) Arrange to enter the name of director in the Register of Directors and Key Managerial personnel.

Specimen ordinary Resolution for appointment of independent director

"RESOLVED that pursuant to the provisions of Sections 149, 152 and any other applicable provisions of the Companies Act, 2013 and the rules made there under (including any statutory modification(s) read with Schedule IV to the Companies Act, 2013, Mr. ……..(DIN No……..), be and is hereby appointed as an Independent Director of the …… to hold the office for a period of 5 years i.e. up to (date)."

RESOLVED FURTHER THAT Shri ……. Secretary/Director be and is hereby authorized to do all such acts and deeds as may be required to be done in this regard."

Answer 3(d)

Conversion of BST into BST Ltd. (a section 8 company into a public company)

The company is required to comply with Rule 21 of the Companies (Incorporation) Rules, 2014.

(1) BST shall have to pass a special resolution at a general meeting for approving such conversion.

(2) Convene a Board Meeting to decide to convert the Company into Public Limited Company, fixing time and agenda for convening a General Meeting to alter the Articles of Association and consequently the name, by Special Resolution.

(3) Issue notice along with explanatory statement. The explanatory statement annexed to the notice convening the general meeting shall set out in detail the reasons for opting for such conversion and the other points as required under Rule 21 of the Companies (Incorporation) Rules, 2014.

(4) The BST shall send a copy of the notice, simultaneously with its publication, together with a copy of the application and all attachments by registered post or hand delivery, to the Chief Commissioner of Income Tax having jurisdiction over the company, Income Tax Officer who has jurisdiction over the company, the Charity Commissioner, the Chief Secretary of the State in which the registered office of the BST is situated, any organization or Department of the Central Government or State Government or other authority under whose jurisdiction the company has been operating and if any of these authorities wish to make any representation to Regional Director, it shall do so within sixty days of the receipt of the notice, after giving an opportunity to the BST.

(5) At the general meeting, after ascertaining the quorum, pass the Special Resolution to the effect:

  (a) To delete the clauses from the Articles of Association which are not mandatory in case of a Public Limited Company.

  (b) Insert such clauses in the Articles of Association which are not there but required in case of a Public Limited Company.

  (c) Insert the word "Ltd" in the name of the company.

(6) A certified true copy of the special resolution along with a copy of the Notice convening the meeting shall be filed with the Registrar in Form MGT.14 along with the fee within 30 days of the meeting.

(7) The BST shall file an application in Form INC.18 with the Regional Director with the fee along with a certified true copy of the special resolution and a copy of the Notice convening the meeting including the explanatory statement for approval for converting itself into a company of any other kind and the BST shall also attach the proof of serving of the notice served to all the authorities mentioned above.

(8) A copy of the application with annexures as filed with the Regional Director shall also be filed with the Registrar.

(9) The BST shall, within a week from the date of submitting the application to the Regional Director, publish a notice at its own expense, and a copy of the notice, as published, shall be sent forthwith to the Regional Director and the said notice shall be in Form No. INC.19 and shall be published in newspaper and on the website of the BST, if any, and as may be notified or directed by the Central Government.

(10) The Board of directors shall give a declaration to the effect that no portion of the income or property of the company has been or shall be paid or transferred directly or indirectly by way of dividend or bonus or otherwise to persons who are or have been members of the company or to any one or more of them or to any persons claiming through any one or more of them.

(11) Where the BST has obtained any special status, privilege, exemption, benefit or grant(s) from any authority such as Income Tax Department, Charity Commissioner or any organization or Department of Central Government, State Government, Municipal Body or any recognized authority, a "No Objection Certificate" must be obtained, if required under the terms of the said special status, privilege, exemption, benefit or grant(s) from the concerned authority and filed with the Regional Director, along with the application.

(12) The BST shall attach with the application a certificate from practicing Chartered Accountant or Company Secretary in practice or Cost Accountant in practice certifying that the conditions laid down in the Act and these rules relating to conversion of a company registered under section 8/section 25 as applicable, into any other kind of company, have been complied with.

(13) The Regional Director may require the applicant to furnish the approval or concurrence of any particular authority for grant of his approval for the conversion and he may also obtain the report from the Registrar.

(14) On receipt of the application, and on being satisfied, the Regional Director shall issue an order approving the conversion subject to such terms and conditions as may be imposed.

(15) Before imposing the conditions or rejecting the application, the company shall be given a reasonable opportunity of being heard by the Regional Director.

(16) On receipt of the documents as mentioned above, the Registrar shall register the documents and issue the fresh Certificate of Incorporation.

(17) In case the number of directors in the company is less than three then increase the number of directors to atleast three.

(18) In case the number of members in the company is less than seven then increase the number of members to atleast seven.

Answer 3A(i)

Section 54 of the Companies Act, 2013 provides that, a company may issue sweat equity shares of a class of shares already issued, if the following conditions are fulfilled, namely:-

(a) The issue is authorized by a special resolution passed by the company;

(b) The resolution specifies the number of shares, the current market price,

consideration, if any, and the class or classes of directors or employees to whom such equity shares are to be issued;

(c) Not less than one year has, at the date of such issue, elapsed since the date on which the company had commenced business; and

(d) Where the equity shares of the company are listed on a recognized stock exchange, the sweat equity shares are issued in accordance with the regulations made by SEBI in this behalf and if they are not so listed, the sweat equity shares are issued in accordance with such rules made under Chapter IV of the Companies Act, 2013.

Issue of sweat equity shares is also subject to the provisions as given under Rule 8 of the Companies (Share Capital and Debentures) Rules, 2014.

Answer 3A(ii)

Chapter VIII of the Companies Act, 2013 deals with declaration and payment of dividend. Section 123 provides for declaration of dividend. A company shall declare dividend and pay it, only out of profits of the company for the financial year arrived at after providing for depreciation or out of undistributed profits of any previous financial year or out of both.

In case, any guarantee given by any Government (Central or State), the company may declare dividend out of money provided by that government for payment of dividend after providing for depreciation in accordance to Schedule II.

Before declaration of dividend, a company may transfer a portion from the profit to the reserves of the company. The company is free to decide the percentage for such transfer to the reserve. There is no compulsion to transfer any amounts to reserves though it is a prudent practice.

Where a company does not have adequate profit or any profit in a financial year or any accumulated profit to distribute as dividend, it may declare dividend out of reserves in accordance with the rules made by the government. The company may pay dividend only from free reserves, not from any other reserves.

Interim dividend can be declared by the Board of directors subject to certain condition of sub-section 3 of section 123.

Amount of dividend declared shall be deposited in a scheduled Bank within 5 days from the date of declaration. Dividend is to be paid only in cash or by Cheque of ECS to the registered shareholder or his order / Banker.

Answer 3A(iii)

Section 144 provides that an auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case may be, (of the company concerned) but shall not include any of the following services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company), namely,

(a) Accounting and book keeping services;

(b) Internal audit;

(c) Design and implementation of any financial information system;

(d) Actuarial services;

(e) Investment advisory services;

(f) Investment banking services;

(g) Rendering of outsourced financial services;

(h) Management services; and

(i) Any other kind of services as may be prescribed;

This is a new provision and there was no restriction of this type in the Companies Act 1956. Therefore, an auditor or audit firm who or which has been performing any non-audit services on or before the commencement of this Act shall comply with the provisions of this section before the closure of the first financial year after the date of commencement of the Act i.e within 31st March, 2015.

The explanation at the end of the section has explained the meaning of the words 'Directly and Indirectly'. Rendering of prohibited services by relatives of the individual Auditor or a partner of the firm or any other connected, associated or controlled person, or where the brand is used by the auditor of such service provider, is not permitted.

Answer 3A(iv)

XBRL (eXtensible Business Reporting Language) is a data-rich dialect of XML (Extensible Markup Language), the universally preferred language for transmitting information via the Internet. It is a language for the electronic communication of business and financial data which is revolutionising business reporting around the world.

The Ministry of Corporate Affairs has mandated the following select class of companies mentioned below to file financial statements in XBRL mode and by using the XBRL taxonomy:

(i) all companies listed with any Stock Exchange(s) in India and their Indian subsidiaries; or

(ii) all companies having paid-up capital of Rupees five crore and above; or

(iii) all companies having turnover of Rupees one hundred crore and above; or

(iv) all companies who were required to file their financial statements for FY 2010-11, using XBRL mode.

However, banking companies, insurance companies, power companies and Non-Banking Financial Companies (NBFCs) are exempted from XBRL filing.

Question 4

Explain the following quoting relevant case law, if any :

(a) Red Cap Ltd. wants to reduce its equity share capital to extinguish the holding of only non-promoter shareholders on payment of the value of their shares. Reduction was approved by the requisite majority of equity shareholders including non-promoter shareholders. Will such selective reduction be sanctioned ?

(6 marks)

(b) *Smart Ltd. wants to include a provision in the articles of association by altering it to limit the company's share capital to a fixed amount. Can it do so ? Will your answer be different if 100% shareholders agree for such alteration ?* (5 marks)

(c) *Northern Ltd. is a company engaged in manufacture of mobile phones. The name of the company was struck-off on an application under 'simplified exit scheme'. However, subsequently the market conditions became favourable. Hence, the shareholders want to revive the company. Will shareholders' plea for restoration be approved by Court ?* *(5 marks)*

Answer 4(a)

Such reduction in equity capital to extinguish the holding of only non-promoters will be sanctioned. In the matter of *Sandvik Asia Ltd.* v. *Bharat Kumar Padamsi* (2009) 151 Com Cases 251 (2010) 2 Com L J 255 (Bom), where the object of reduction was to extinguish the holding of non-promoter shareholders on payment of fair value for their shares and reduction was approved by a majority of equity shareholders including majority of non-promoter shareholders, the reduction was sanctioned.

Answer 4(b)

A provision of the Articles which has the effect of limiting the company's share capital to a fixed amount would have no effect being contrary to the Act. [*Miheer Hemant Mafatlal* v. *Mafatlal Industries Ltd.* (1987) 89 Bom LR 86 (Bom).

The legal position shall not change even if 100% shareholders agree for such alteration as all members become bound by a valid alteration whether they voted for or against the resolution.

The Smart Ltd. cannot include a provision in the articles of association by altering it to limit the company's share capital to a fixed amount.

Answer 4(c)

The name of a company was struck off on an application under "Simplified Exit Scheme." The shareholders subsequently sought to revive the company because of the favourable market conditions. The court directed restoration of the company's name. [*VI Brij Fiscal Services P. Ltd.* v. *Registrar of Companies* (2010) 155 Com Cases 157 (MP)].

The plea for restoration made by the shareholders of Northern Ltd. shall be approved by the Court.

Question 5

(a) *A charge is a right created by any person, including a company, referred to as 'the borrower', on its assets and properties, present or future, in favour of a financial institution or a bank, referred to as 'the lender' which has agreed to extend financial assistance. Discuss the provisions of the Companies Act, 2013 relating to registration of charge.*

(b) *Manohar Motors Ltd. has a paid-up share capital of 10 crore and free reserves of 5 crore. The Board of directors want to borrow a sum of 20 crore for its long-term capital requirements from the market. Discuss whether they can do so and*

if yes, what are the requirements under the Companies Act, 2013 which they have to comply with.

(c) *Pankaj is a whole-time director of a listed company and also an independent director in two other listed companies out of which he is also the Chairman of the audit committee of one company. He is also on the Board of 5 other public companies which are not listed companies. Three other private companies which are not subsidiary companies of any public company have invited him to join them as a director on their Board. Discuss in the light of the provisions of Companies Act, 2013 whether Pankaj can accept the directorship of said private limited companies.*

(d) *Is Company Secretary a 'managerial personnel' for the purpose of restrictions on remuneration under section 197 ? Is his salary considered for the purpose of computation of managerial remuneration ? Would it make any difference if he is also a director of a company ?* *(4 marks each)*

Answer 5(a)

Section 2(16) of the Companies Act, 2013 defines charge so as to mean an interest or lien created on the property or assets of a company or any of its undertakings or both as security and includes a mortgage.

Provisions with respect to registration of a Charge are as under:

As per the provisions of section 77 of the Companies Act, 2013, It shall be the duty of every company creating a charge within or outside India, on its property or assets or any of its undertakings, whether tangible or otherwise, and situated in or outside India, to register the particulars of the charge signed by the company and the charge-holder together with the instruments, if any, creating such charge in such form, on payment of such fees and in such manner as may be prescribed, with the Registrar within thirty days of its creation.

It is further provided that the Registrar may, on an application by the company, allow such registration to be made within a period of three hundred days of such creation on payment of such additional fees as may be prescribed.

It is provided further that if registration is not made within a period of three hundred days of such creation, the company shall seek extension of time in accordance with section 87.

It is also provided that any subsequent registration of a charge shall not prejudice any right acquired in respect of any property before the charge is actually registered.

Where a charge is registered with the Registrar, he shall issue a certificate of registration of such charge in such form and in such manner as may be prescribed to the company and, as the case may be, to the person in whose favour the charge is created.

Notwithstanding anything contained in any other law for the time being in force, no charge created by a company shall be taken into account by the liquidator or any other creditor unless it is duly registered and a certificate of registration of such charge is given by the Registrar.

If company fails to register the charge as per section 77, the person in whose favour charge is created can apply to the Registrar for registration of Charge. (section 78)

Modification in charge is also required to be registered so also the existing charge on the property acquired by the company. (section 79)

The registration of charge is deemed to be the notice on the person acquiring property. (section 80). Register of Charges is kept by the Registrar in prescribed form. (sec 81)

Answer 5(b)

In terms of Section 180(1)(c) of the Companies Act, 2013, a company can borrow money, where the money to be borrowed, together with the money already borrowed by the company exceeds aggregate of its paid up share capital and free reserves, only with the consent of company by special resolution.

Temporary loans obtained from the Bankers are not to be considered while calculating the limits. [Proviso to section 180(1) (c)]

In this case under consideration, we should see if the Articles of Association of Manohar Motors Ltd. allow such borrowings. If not, comapny should alter its articles to provide for the same. The company should hold a general meeting in which a special resolution be passed authorising the Board of Directors to borrow money up to Rs. 20 crores. As this limit exceeds the paid-up capital of Rs. 10 crores and free reserves of Rs. 5 Crores.

The other requirements to be complied with inter alia include provisions in the Articles of Association, holding BOD meeting to decide special resolution to be passed, approving notice of General Meeting, draft of special resolution and also Explanatory statement thereto, holding General Meeting by giving 21 days clear notice, getting the special resolution passed and filing the same with the ROC within 30 days, after this the BOD can go ahead to borrow up to Rs. 20 Crores.

The resolution of the Board of Directors should be passed at a meeting. Section 179(3) (d)

Answer 5(c)

In terms of Section 165 of the Companies Act, 2013, a person cannot hold office at the same time as director in more than 20 companies and maximum number of public companies in which a person can be appointed as a director shall not exceed 10.

Clause 49 of the Listing Agreement provides that a director shall not be a member in more than ten committees or act as Chairman of more than five committees across all companies in which he is a director and also provides that a person shall not serve as an independent director in more than seven listed companies. Further, any person who is serving as a whole time director in any listed company shall serve in not more than three listed companies, as an independent director.

Thus, Mr. Pankaj can accept the offer of joining three other private limited companies as a director on their Board.

Answer 5(d)

As per section 197 of the Companies Act, 2013, the total managerial remuneration payable by a public company to its directors, including managing director and whole

time director and its manager in respect of any financial year shall not exceed eleven per cent of the net profits of that company.

As such, Company Secretary is not a 'managerial personnel' for purpose of restriction on remuneration under section 197 of the Companies Act, 2013. His salary is not considered for purpose of computation of 'managerial remuneration' under section 197, if he is a director of a company the provisions of section 197 of the Act shall prevail upon.

Question 6

(a) What items of business are required to be transacted through postal ballot in terms of provisions of the Companies Act, 2013 ?

(b) "Apart from general secretarial duties entrusted, the Companies Act, 2013 has entrusted and prescribed some duties and authorities." Discuss the statutory duties and liabilities of a Company Secretary under the Act.

(c) The Companies Act, 2013 has introduced several provisions which would change the way Indian corporates do business and one such provision is spending on corporate social responsibility (CSR) activities which has assumed considerable importance. Discuss the provisions governing CSR as provided in the Companies Act, 2013 and rules made thereunder.

(d) The primary objective of compliance management backed by secretarial audit is to safeguard the interests of the company and its stakeholders. Discuss the provisions governing secretarial audit under the Companies Act, 2013 and the applicable rules made thereunder. (4 marks each)

Answer 6(a)

Pursuant to clause (a) of sub-section (1) of section 110 of the Act read with Rule 16 of Companies(Management and Administration) Rules, 2014, the following items of business shall be transacted only by means of voting through a postal ballot:-

1. Alteration of the object clause of the Memorandum of Association,
2. Alteration of Articles of Association in relation to insertion or removal of provisions which are required to be included in iits articles of the company in order to constitute it a private company,
3. Change in the place of registered office outside the local limits of any city, town,or village,
4. Change in objects for which the company has raised money from public through prospectus and still has any unutilised amount out of the money so raised,
5. Issue of shares with differential rights as to voting or dividend or otherwise,
6. Variation in the rights attached to a class of shares/debentures/ other securities,
7. Buy-back of shares,
8. Election of a director under section 151 of the Act,
9. Sale of the whole or substantially the whole of an undertaking of the company,

10. Giving loans or extending guarantee or providing securities in excess of the limit specified under section 186(3).

One Person Company and companies having members up to 200 are not required to transact any business through postal ballot in terms of Proviso to Rule 22(16).

Answer 6(b)

According to section 205 of the Companies Act, 2013, the functions of the company secretary shall include,—

(a) to report to the Board about compliance with the provisions of this Act, the rules made thereunder and other laws applicable to the company;

(b) to ensure that the company complies with the applicable secretarial standards;

(c) to discharge such other duties as may be prescribed.

Further the Rule 10 of Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014 codify the duties of Company Secretary which are as follows :-

1. providing to the directors of the company, collectively and individually, such guidance as they may require, with regard to their duties, responsibilities and powers;
2. facilitating the convening of meetings and attending Board, committee and general meetings and maintaining the minutes of these meetings;
3. obtaining approvals from the Board, general meeting, the government and such other authorities as required under the provisions of the Act;
4. representing before various regulators, and other authorities under the Act in connection with discharge of various duties under the Act;
5. assisting the Board in the conduct of the affairs of the company;
6. assisting and advising the Board in ensuring good corporate governance and in complying with the corporate governance requirements and best practices;
7. discharging such other duties as have been specified under the Act or rules; and
8. discharging such other duties as may be assigned by the Board from time to time.

Section 205(2) provides that provisions contained in section 204 in relation to secretarial audit and section 205 in relation to functions of company secretary shall not affect the duties and functions of the Board of Directors, chairperson of the company, managing director or whole- time director under this Act, or any other law for the time being in force.

Answer 6(c)

The provisions of Corporate Social Responsibility are dealt under section 135 read with the Companies (Corporate Social Responsibility Policy) Rules, 2014 and clarifications issued by the Ministry from time to time. Some of the important provisions are as under:

— As per Section 135 of the Companies Act 2013, every company having net worth of Rs. 500 crores or more, or turnover of Rs. 1000 crores or more or a net profit

of Rs. 5 crores or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors out of which at least one director shall be an independent director. There need not be any independent director on the CSR Committee if the Company is unlisted Public Company or a Private Company.

— In case of Private Company CSR committee can be formed with two members.

— CSR Committee shall formulate and recommend Corporate Social Responsibility Policy which shall indicate the activity or activities to be undertaken by the company as specified in Schedule VII and also recommend the amount of expenditure to be incurred on CSR activities.

— The Board of every company shall ensure that that the company spends in every financial year at least 2% of the average net profit of the company made during the three immediately preceding financial years in pursuance of its CSR policy.

  — Net Profit of a company for the purposes of Section 135 of the Companies Act, 2013 does not include the profit arising from any overseas branch of the company and the dividends received from other companies in India which are complying with Section 135 of the Companies Act, 2013.

— Where the company fails to spend such amount, the Board shall in its report specify the reasons for not spending the amount. The approach is to comply or explain.

— The company shall give preference to local areas where it operates, for spending amount earmarked for CSR activities.

— 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.

— The Board of a company may decide to undertake its CSR activities approved by the CSR committee, through a registered trust or a registered society or a company established by the company or its holding or subsidiary or associate company under section 8 of the Act or otherwise.

— The CSR projects or programs or activities undertaken in India only shall amount lo CSR expenditure.

— The CSR projects or programs or activities that benefit only the employees of the company and their families shall not be considered as CSR activities in accordance with section 135 of the Act.

— Contribution of any amount directly or indirectly to any political party under section 182 of the Act, shall not be considered as CSR activity.

— In case the company has failed to spend the two percent of the average net profit of the last three financial years or any part thereof, the company shall provide the reasons for not spending the amount in its Board report.

— The reporting on Corporate Social Responsibility is to be made with the Registrar in e-form AOC-4.

— The CSR Policy of the company is required to be displayed on Company's website.

— The term CSR is not defined under the Act but Schedule VII of the Companies Act 2013 requires that the CSR policy created by the CSR committee must involve atleast one of the focus areas as mentioned in that schedule.

— The CSR activities should be according to the stated CSR policy, as projects or programs or activities (either new or ongoing).

— The CSR activities may be decided by the board to be undertaken through a registered trust or a registered society or a company established by the company or its holding or subsidiary or associate company, provided that —

  — if such trust, society or company is not established by the company or its holding or subsidiary or associate company, it shall have an established track record of three years in undertaking similar programs or projects;

  — the company has specified the project or programs to be undertaken through these entities, the modalities of utilization of funds on such projects and programs and the monitoring and reporting mechanism.

— A company may also collaborate with other company but the reports of such projects shall be separately made as per the rules.

— CSR projects or programs or activities undertaken in India shall amount to CSR expenditure.

— CSR projects that benefits only the families of the employees shall not be considered as CSR activities.

— Companies can either conduct CSR activities by mobilizing their own personnel or through institutions having a track record of at least three years but such expenditure must exceed 5% of total CSR expenditure in one financial year.

— Contribution made to the any political party shall not be considered as CSR activity.

Answer 6(d)

Section 204 of the Companies Act, 2013 provides for mandatory secretarial audit for following companies:

(a) every listed company;

(b) every public company having a paid-up share capital of fifty crore rupees or more; or

(c) every public company having a turnover of two hundred fifty crore rupees or more.

The Secretarial Audit is applicable to a private company which is a subsidiary of a public company, and which falls under the prescribed class of companies.

The companies which are not covered under section 204 may obtain Secretarial

Audit Report voluntarily as it provides an independent assurance of the compliances of applicable laws of the company.

As per sub-rule (2) of rule 9, the format of the Secretarial Audit Report shall be in Form No. MR.3 and secretarial audit report shall be annexed with the Board's report.

In terms of section 204(1), only a member of the Institute of Company Secretaries of India holding certificate of practice (company secretary in practice) can conduct Secretarial Audit and furnish the Secretarial Audit Report to the company.

As per rule 8 of the Companies (Meetings of Board and its powers) Rules, 2014, secretarial auditor is required to be appointed by means of resolution at a duly convened board meeting of the company.

Section 204(2) of the Companies Act, 2013 provides that it is the duty of the company to give all assistance and facilities to the company secretary in practice, for auditing the secretarial and related records of the company.

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) *"Secretarial Standards Board is doing multifarious functions." Comment.* *(5 marks)*

(b) *You are the Company Secretary of Star Infrastructure Ltd. Your Chairman has asked you to submit a note regarding compliances required to be made and the restrictions if any imposed by section 92 of the Companies Act, 2013 with respect to filing of annual return. Draft the note.* *(5 marks)*

(c) *"Secretarial audit is prevention rather than post-mortem." In the light of this statement explain the need of secretarial audit particularly with reference to corporate law compliances.* *(5 marks)*

(d) *Board of directors of Charming Entertainment Ltd. in its meeting held on 16th April, 2015 declared an interim dividend on its paid-up equity share capital. Now, the Board wants to revoke the said declaration in its next Board meeting scheduled on 3rd May, 2015. You as a Company Secretary of the company, advise the Board with the relevant provisions of the Companies Act, 2013, whether the Board of directors can do so ?* *(5 marks)*

(e) *Explain the provisions contained in the Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004 related to investment by Indian entities in overseas joint ventures and wholly owned subsidiaries abroad.* *(5 marks)*

OR (Alternate question to Q.No. 1)

Question 1A

(i) *Prepare a checklist of compliances with respect to loans, investments, guarantees and securities by a company for the purpose of secretarial audit.* *(5 marks)*

(ii) *"Compliance of secretarial standards is good for governance." Explain. (5 marks)*

(iii) *Amit, the director of Smile Ltd., did not attend the meetings of the Board of directors of the company during the last twelve months with the leave of absence. Comment on his status as director.* *(5 marks)*

(iv) *Ms. Mansi was the properly appointed director of Excellent Ltd. Subsequently, the company altered its articles of association and made it a compulsory*

qualification for the director to be a qualified Company Secretary. Ms. Mansi, not being a qualified Company Secretary, was asked to vacate the office. Decide whether the action of Excellent Ltd. is valid as per the relevant provisions of the Companies Act, 2013. *(5 marks)*

(v) Merry Ltd. is planning to access the external commercial borrowings under approval route for the expansion of its business. As a Company Secretary, prepare a checklist in this regard. *(5 marks)*

Answer 1(a)

Secretarial Standards Board (SSB) is doing multifarious functions. The scope of SSB is to identify the areas in which Secretarial Standards need to be issued by the Council of ICSI and to formulate such Standards, taking into consideration the applicable laws, business environment and best secretarial practices. SSB will also clarify issues arising out of such Standards and issue guidance notes for the benefit of members of ICSI, corporates and other users. Thus, main functions of SSB are:

(i) Formulating Secretarial Standards;

(ii) Clarifying issues arising out of the Secretarial Standards;

(iii) Issuing Guidance Notes; and

(iv) Reviewing and updating the Secretarial Standards / Guidance Notes at periodic intervals.

Answer 1(b)

To

The Chairman
Star Infrastructure Ltd.

Note: Compliance with respect to filing of annual return

As per section 92 of the Companies Act, 2013 with respect to filing of annual return the company is required to comply with the following:

1. The company has filed annual return within sixty days from the date of holding of the annual general meeting (AGM).
2. The annual return has been filed within sixty days from the date on which the annual general meeting should have been held together with the statement specifying the reasons for not holding the annual general meeting, if the annual general meeting has not been held.
3. The annual return is prepared in Form No. MGT.7 referred to in Rule 11 of the Companies (Management and Administration) Rules, 2014.
4. In case company does not have a company secretary the annual return has been signed by a Company Secretary in practice.
5. In case of a listed company or a company having paid-up share capital of ten crore rupees or more or turnover of fifty crore rupees or more, the annual return is

certified by a Company Secretary in practice and the certificate is in Form No. MGT.8 of aforesaid Rules.

6. The extract of the annual return is attached to the Board's report in Form MGT. 9 as per Rule 12.1.

Mr. X
Company Secretary
Star Infrastructure Ltd.

Answer 1(c)

Secretarial Audit is the process of independent verification, examination of level of compliance of applicable Corporate Laws to a company. The audit process if properly devised ensures timely compliance and eliminates any un-intended non compliance of various applicable rules and regulations. An action plan of the Corporate Secretarial Department is to be designed so as to ensure that all event based and time based compliances are considered and acted upon. Secretarial Audit is to be on the principle of "Prevention is better than cure" rather than post mortem exercise and to find faults. Broadly, the need for Secretarial Audit is:

— Effective mechanism to ensure that the legal and procedural requirements are duly complied with.

— Provides a level of confidence to the directors, officers in default, Key Managerial Personnel etc.

— Directors can concentrate on important business matters as Secretarial Audit ensures legal and procedural requirements.

— Strengthen the image and goodwill of a company in the minds of regulators and stakeholders.

— Secretarial Audit is an effective compliance risk management and governance tool.

— It helps the investor in analyzing the compliance level of companies, thereby increases the reputation.

Answer 1(d)

Dividend which includes interim dividend as per Section 2 (35) of Companies Act, 2013, is a due from the company once it is properly declared. Interim dividend is declared by the Board of Directors and once it is declared, it thus becomes due from the company. Section 123(4) further provides that the amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate account within five days from the date of declaration of such dividend. If the articles of the company do not authorize so, it has to be amended accordingly.

Section 127 of the Companies Act, 2013 provides for penalty to directors for any default in not paying dividend within 30 days from the date of declaration. However, no offence under this section shall be deemed to have been committed:

— Where the dividend could not be paid by reason of the operation of any law;

— Where a shareholder has given directions to the company regarding the payment of the dividend and those directions cannot be complied with and the same has been communicated to him;

— Where there is a dispute regarding the right to receive the dividend;

— Where the dividend has been lawfully adjusted by the company against any sum due to it from the shareholder; or

— Where, for any other reason, the failure to pay the dividend or to post the warrant within the period under this Section was not due to any default on the part of the company.

In the given case, interim dividend has to be paid and cannot be revoked once it is declared as the exceptions given above do not apply in the given case.

Answer 1(e)

Section 6 of the Foreign Exchange Management Act, 1999 provides powers to the Reserve Bank to specify, in consultation with the Government of India, the classes of permissible capital account transactions and limits up to which foreign exchange is admissible for such transactions. Section 6(3) of the aforesaid Act provides powers to the Reserve Bank to prohibit, restrict or regulate various transactions referred to in the sub-clauses of that sub-section, by making Regulations.

Accordingly Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2004 vide Notification No. FEMA.120/RB-2004 dated July 7, 2004 was notified which seeks to regulate acquisition and transfer of a foreign security by a person resident in India i.e. investment by Indian entities in overseas joint ventures and wholly owned subsidiaries as an investment by a person resident in India in shares and securities issued outside India. In terms of Regulation 4 of the Notification, general permission has been granted to persons residents in India for purchase/acquisition of securities in the following manner:

(a) out of the funds held in resident foreign currency (RFC) account;

(b) as bonus shares on existing holding of foreign currency shares; and

(c) when not permanently resident in India, out of their foreign currency resources outside India.

General permission is also available to sell the shares so purchased or acquired.

This Regulation also provides for the sectors abroad like real estate and banking in which investments can be made only with prior approval of RBI. Investments abroad by Indian entities are possible under Automatic Route and Approval Route. If the conditions mentioned in Automatic Route are met like investment limits, permissible instruments, the entity being not under RBI's Exporters Caution List etc, the investment need not have prior approval of RBI.

Answer 1A(i)

As per section 186 of the Companies Act, 2013 a company is required to comply

with the following requirement with respect to loans, investments, guarantees and securities:

Check whether

1. The board resolution/ special resolution have been passed with respect to loans and investments by the company.
2. The company has made any investment through more than two layers of investment companies.
3. The company has not defaulted repayment of deposit while granting loans/ giving guarantee/ providing security.
4. The company has disclosed financial statements the full particulars of the loans given investment made or guarantee given as prescribed under the Act.
5. The company maintains register containing such particulars in form MBP-2 at the registered office of the company.
6. The company has obtained prior approval of the public financial institution if any term loan from the public financial institution is subsisting**.**

Answer 1A(ii)

The ultimate goal of the Secretarial Standards is to promote good corporate practices leading to better corporate governance. The Standards are only for good secretarial practices and desirable corporate governance with a view to ensuring shareholders democracy and utmost transparency, integrity and fair play, going beyond the minimum requirements of law. The adoption of the Secretarial Standards by the corporate sector will, over the years have a substantial impact on the improvement of quality of secretarial practices being followed by companies, making them comparable with the best practices in the world.

By following the Secretarial Standards in true letter and spirit, companies will be able to ensure adoption of uniform, consistent and best secretarial practices in the corporate sector. Such uniformity of best practices, consistently applied, will result in furthering the shareholders democracy by laying down principles for better corporate disclosures thus adding value to the general endevour to strive for good governance.

The Companies Act, 2013 has given recognition vide sub section 10 of section 118 for observation with respect to general meetings and Board of Directors Meeting. (SS-1 & SS-2). It is beginning of new era where non financial standards have been given importance and statutory recognition beside Financial Standards. It clearly indicates that law makers recognise the importance of Secretarial Standards in achieving the better practices leading to better governance.

Answer 1A(iii)

Section 167 of the Companies Act, 2013 deals with vacation of office of director. Section 167 (1) (b) provides that 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, in the given case, though Mr. Amit, the Director of the Smile Ltd. has taken the leave of absence from the board, the office of director shall become vacant, as section 167 clearly states that "with or without seeking leave of absence" for the said purpose.

Answer 1A(iv)

The problem given in the question is related to disqualification of director or vacation of office of director as Ms. Manasi has already been duly appointed as a director. The provisions relating to disqualification for appointment of directors are envisaged under section 164 of the Companies Act, 2013. Although as per provisions of Section 164(3), Private Limited Company may by its articles provide for additional disqualification in addition.

In the given case Excellent Limited is a public company and although they have altered its articles of association, but Ms. Manasi is not disqualified as she is not falling under the grounds mentioned under section 164 for the said purpose. Therefore, Section 167(1)(a) which provides for vacation, if disqualified under Section 164 also will not apply. Thus the action taken by Excellent Ltd. is not valid as it is not in accordance with the provisions of the companies Act, 2013.

Answer 1A(v)

For accessing External Commercial Borrowing under approval route the following is required to be complied by Merry Ltd.:

1. Check the Eligibility of borrower
2. Check the recognition of lender.
3. Check whether total outstanding stock of ECBs (including the proposed ECBs) from a foreign equity lender should not exceed seven times the equity holding, either directly or indirectly of the lender (in case of lending by a group company, equity holdings by the common parent would be reckoned)
4. Check the All in cost Ceiling.
5. Check the permitted end use requirements.
6. Check whether the proposed parking of ECB funds is as per the norms.
7. Check whether RBI permission is obtained for Pre-payment of ECB for amounts exceeding USD 500 million.
8. Check the provisions regarding refinancing/rescheduling of ECB if any.

PART B

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

Question 2

(a) Sharda Fertilizers Ltd., a listed company, proposes to make an issue of foreign currency convertible bonds (FCCBs) under the automatic route. You are required to answer the following with reference to the scheme, viz. the Issue of Foreign

Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 —

(i) Is there any ceiling on the issue of FCCBs ?

(ii) Whether FCCBs can be attached with warrants ?

(iii) What should be the minimum maturity time ?

(iv) How much can be the issue related expenses ?

(v) What information should be furnished to the RBI after completion of the issue ? *(5 marks)*

(b) The accounts of Varsha Goldmine Ltd., a listed company, for the year ended 31st March, 2014 were finalised on 31st May, 2014. The company has paid-up share capital of ₹50 lakh and free reserves of ₹100 lakh. The company did not have any accumulated losses.

The Board of directors of the company wishes to make a public issue of equity shares amounting to ₹10 crore by public offering through offer document, firm allotment and promoters' contributions during the year 2015-16. State how can this be done under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009. *(5 marks)*

(c) "Environmental failures may lead to financial loss, reputational damage and business discontinuity." Comment with reference to leading case laws on the subject. *(5 marks)*

OR (Alternate question to Q.No. 2)

Question 2A

(i) Prime Bank had advanced a substantial amount to ABC Ltd. The bank suspects that the amount advanced is not properly utilised by the company. The bank appoints you as a Practising Company Secretary to submit a fact finding report on the same. Draft the report. *(5 marks)*

(ii) Soha Ltd. wants to go for initial public offer. Ms. Pia, the Company Secretary of the company, has to advise to the management of the company about the conditions for making initial public offer. What should be Ms. Pia's advice ? *(5 marks)*

(iii) Pratham Ltd. issued convertible debentures during the financial year 2013-14. Now it wants to alter the terms of redemption. Is it permissible under the provisions of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009? Give reasons. *(5 marks)*

PART B

Answer 2(a)(i)

The issue of FCCBs shall be subject to a ceiling of US $500 million in any one financial year.

Answer 2(a)(ii)

No, Issue of FCCBs with attached warrants is not permitted.

Answer 2(a)(iii)

The maturity of the FCCB shall not be less than 5 years. The call and put option, if any, shall not be exercisable prior to 5 years.

Answer 2(a)(iv)

The issue related expenses shall not exceed 4% of issue size and in case of private placement, shall not exceed 2% of the issue size.

Answer 2(a)(v)

The issuing entity shall, within 30 days from the date of completion of the issue, furnish a Report to the concerned Regional Office of the Reserve Bank of India through a designated branch of an Authorized Dealer giving the details and documents as under:

(a) The total amount of the FCCBs issued

(b) Names of investors' resident outside India and number of FCCBs issued to each of them.

Answer 2(b)

Facts of the Case

Varsha Goldmine Ltd. has a paid up capital of Rs. 50 lakhs and free reserve of Rs. 100 lakhs as on the year ending 31.3.2014. It is a listed company. Now it wants to make a further public issue of Rs. 10 crores. The question is what are the relevant regulations as per SEBI (ICDR) Regulations, 2009.

Relevant Law

Regulation 27 of SEBI (ICDR) Regulations, 2009 provides for the conditions for making further public offer by a listed company while Regulation 26 provides for conditions for making IPO by a company. Regulation 27 provides that an issuer may make a further public offer if it satisfies the conditions specified in clauses (d) and (e) of Regulation 26 (1) **and** if it does not satisfy those conditions, it may make a further public offer (**only)** if it satisfies the conditions specified in Regulation 26 (2).

Regulation 26 (1) (d) provides that the aggregate of the proposed issue and all previous issues made in the same financial year in terms of issue size does not exceed five times its pre-issue net worth as per the audited balance sheet of the preceding financial year.

Regulation 26 (1) (e) provides for change of name within last one year and this condition does not apply to the present case.

Regulation 26 (2) provides that the issue can be made through book building process and the issuer undertakes to allot at least 75 % of the net offer to public, to qualified institutional buyers and to refund the full subscription money if it fails to make the said minimum allotment to QIBs.

Applicability of Law to the Facts of the Case

In the given case, Varsha Goldmine Ltd. is a listed company. The paid up capital and free reserves of the company as on 31.3.2014 amounted to Rs. 1.5 crores. The company wants to make a further issue during the year 2015-16 of Rs. 10 crores. It is more than 5 times the pre issue net worth as at the end of the previous financial year. Therefore, it is not complying with the condition specified in Regulation 26 (1) (d). It can make a public issue now only if it fulfils the conditions specified in Regulation 26 (2).

Decision

Varsha Goldmine Ltd. therefore has to do the following as per Regulation 26(2):

(a) The proposed public issue must be made through book building process.

(b) The company should undertake to allot at least 75% of the net offer to public to QIBs.

(c) The company should also undertake to refund full subscription money if it fails to make the said minimum allotment (75%) to QIBs.

Answer 2(c)

Environmental failures may lead to financial, reputational damage and business discontinuity as well. Environmental non-compliances may, not only result in huge financial liability or reputation wreck, but also may result in business discontinuity or huge public damage. The following case studies would throw some light on the impact of environmental failures.

1. **Sri Ram Food and Fertilizer Case** *(M.C. Mehta* v. *Union of India, AIR 1987 SC 1086*)

   In that case, a major leakage of Oileum Gas affected a large number of persons, both amongst the workmen and public. The Supreme Court held that where an enterprise is engaged in a hazardous or inherently dangerous activity and harm results to any one on account of an accident in the operation of such hazardous and inherently dangerous activity resulting in the escape of toxic gas the enterprise is strictly and absolutely liable to compensate all those who are affected by the accident and such a liability is not subject to any exception.

2. **Dehradun Valley Case** *(Rural Litigation & Entitlement Kendra* v. *Slate of U.P., AIR 1985 SC 652; see also AIR 1988 SC 2187)*

   In that case, carrying on haphazard and dangerous limestone quarrying in the Mussorie Hill range of the Himalaya, mines blasting out the hills with dynamite, extracting limestone from thousands of acres had upset the hydrological system of the valley. The Supreme Court ordered the closing of limestone quarrying in the hills and observed and this would undoubtedly cause hardship to them, but it is a price that has to be paid for protecting and safeguarding the right of the people to live in healthy environment with minimal disturbance of ecological balance.

3. **Effluents by tanneries in river Ganga** (*M.C. Mehta* v. *Union of India*)

   In *M.C. Mehta* v. *Union of India*, the Court directed that the work of those tanneries be stopped, which were discharging effluents in River Ganga and which did not

set up primary effluent treatment plants. It held that the financial incapacity of the tanners to set up primary effluent treatment plants was wholly irrelevant. The Court observed the need for (a) imparting lessons in natural environment in educational institutions, (b) group of experts to aid and advise the Court to facilitate judicial decisions, (c) constituting permanent independent centres with professional public spirited experts to provide the necessary scientific and technological information to the Court, and (d) setting up environmental courts on regional basis with a right to appeal to the Supreme Court.

Answer 2A(i)

Prime bank suspects that the amount advanced to ABC Ltd. is not properly utilised by the company. You are a practising company secretary and the bank appoints you to submit a fact finding report on the utilisation of loan advanced by the bank.

To

Prima bank

The following aspects may be specifically examined to ensure that consistency has been maintained in utilisation of moneys advanced to the mortgagor:

(a) funds have been utilised for the purposes laid down in the loan agreement. Where funds have not been so utilised, the requisite permission has been taken;

(b) requisite conditions laid down to qualify for the outstanding balance of the loan have been fulfilled;

(c) the drawls from the loan are being kept in a separate Scheduled Bank Account, payments there from are being made in the manner laid down in the agreement, the said scheduled bank has foregone its right to set-off or lien, in respect of the said account, and the mortgagor is maintaining the records pertaining to the said account, as provided in the agreement.

(d) no part of the loan moneys has been transferred to call, short term, fixed or any other deposits, without prior consent. Where such consent has been obtained, the scheduled bank has foregone its right to set off any amount due from the company, against the deposits, the deposits have been realised on their due dates and the proceeds thereof re-deposited in the special account;

(e) the expenditure has been financed in the manner provided for in the agreement; and

(f) any changes/deviations in the time schedule for completion of the project have been made in consultation with the bank(s)/financial institution(s).

Mr. Y
Practising Company Secretary
YZ Company Secretaries & Associates

Answer 2A(ii)

To

The Board of Directors
Soha Ltd.

Note: Conditions for making Initial Public Offer

A company may make an initial public offer provided it fulfils all the following five

conditions laid down under regulation 26 (1) and (2) of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009:

1. (a) it should have net tangible assets of at least three crore rupees in each of the preceding three full years (of twelve months each), of which not more than fifty per cent are held in monetary assets. However, if more than fifty per cent of the net tangible assets are held in monetary assets, the issuer should have made firm commitments to utilise such excess monetary assets in its business or project;

   Provided further that the limit of fifty per cent on monetary assets shall not be applicable in case the public offer is made entirely through an offer for sale.

   (b) it should have a minimum average pre-tax operating profit of rupees fifteen crore, calculated on a restated and consolidated basis, during the three most profitable years out of the immediately preceding five years.

   (c) it should have a net worth of at least one crore rupees in each of the preceding three full years (of twelve months each);

   (d) the aggregate of the proposed issue and all previous issues made in the same financial year in terms of issue size does not exceed five times its pre-issue net worth as per the audited balance sheet of the preceding financial year;

   (e) if it has changed its name within the last one year, at least fifty per cent. of the revenue for the preceding one full year has been earned by it from the activity indicated by the new name.

2. An issuer not satisfying any of the above conditions stipulated in sub-regulation (1) may make an initial public offer if the issue is made through the book-building process and the issuer undertakes to allot, at least seventy five percent of the net offer to public, to qualified institutional buyers and to refund full subscription money if it fails to make the said minimum allotment to qualified institutional buyers.

Ms. Pia
Company Secretary
Soha Ltd.

Answer 2A(iii)

As per regulation 24 of SEBI (ICDR) Regulations, 2009, no issuer shall alter the terms (including the terms of issue) of specified securities which may adversely affect the interests of the holders of that specified securities, except with the consent in writing of the holders of not less than three-fourths of the specified securities of that class or with the sanction of a special resolution passed at a meeting of the holders of the specified securities of that class. So in the given case Pratham Ltd. has to obtain the consent in writing of at least three-fourths convertible debenture holders by passing a special resolution passed at the meeting of the convertible debenture holders if the alteration is likely to adversely affect the interests of debenture holders.

Question 3

(a) Effective compliance programme should have the ability to monitor audit compliance in a 'real time manner'. To facilitate this, explain the role of information technology in compliance management. *(5 marks)*

(b) "Roll-over of non-convertible portion of partly convertible debt instruments is possible subject to certain conditions." Comment. (5 marks)

(c) As a Practising Company Secretary, you have been assigned to carry out legal due diligence on the financial aspects of a company. Prepare a checklist on the different aspects to be considered in this regard. (5 marks)

Answer 3(a)

A critical component of an effective compliance program is the ability to monitor the audit compliance in a "real time manner." Yet, as companies cross geographical and industry boundaries, it is becoming harder to perform this role in the traditional manner. As a result, companies are increasingly seeking technology solutions.

Information Technology can play an effective role in implementation of a Corporate Compliance Management Programme across various departments of an organization in terms of real-time compliance reminders, generation of reports, sending warning signals, generation of compliance calendar etc. Many companies are introducing comprehensive web-based compliance systems that link various offices/units for better co-ordination and continued compliance. Companies prefer to introduce full-fledged compliance management systems for smooth compliance of multiple laws. Web-based compliance software are available industry-wise and tailor made compliance software can also be made according to company specifications which has to be updated on continuous basis.

Answer 3(b)

Roll-over of non-convertible portion of partly convertible debt instruments issued by a listed issuer, the value of which exceed fifty lakh rupees may be rolled over without change in the interest rate, subject to compliance with the conditions stipulated under regulation 21 of SEBI (ICDR) Regulations, 2009, which are as follows:

(a) seventy five per cent of the holders of the convertible debt instruments of the issuer have, through a resolution, approved the rollover through postal ballot;

(b) the issuer has, along with the notice for passing the resolution, sent to all holders of the convertible debt instruments, an auditors' certificate on the cash flow of the issuer and with comments on the liquidity position of the issuer;

(c) the issuer has undertaken to redeem the non-convertible portion of the partly convertible debt instruments of all the holders of the convertible debt instruments who have not agreed to the resolution;

(d) credit rating has been obtained from at least one credit rating agency registered with the SEBI within a period of six months prior to the due date of redemption and has been communicated to the holders of the convertible debt instruments, before the roll over.

Answer 3(c)

Legal due diligence of financial aspects includes thorough reading of the balance sheet to identify the financial obligations of the company, penalties paid for violations of

laws in the past etc. The following are the different aspects in this regard to check while conducting legal due diligence:

- Financial Statements for the last five years
- Auditors Qualifications if any
- Recent unaudited financial statements
- Details of various financial reports published under listed agreement
- Capital Budgets and projections
- Details of fixed and variable expenses
- Internal Audit Report if any
- Strategic plans
- Details of internal control procedures
- Unrecorded liabilities
- Commitments, contingencies
- Accounting policies
- Relationship between profit and operating cash flows
- Reliance on debt funds and usage of debt
- Debt repayment and potential debt trap
- Working capital lock up.

Question 4

(a) Explain the purpose and projects for which environmental impact assessment (EIA) is undertaken. Which areas should be addressed while preparing EIA report? (8 marks)

(b) Your client is intending to enter into a major commercial agreement for collaboration. You as a Company Secretary have been asked to conduct due diligence for the prospective company. Which factors you will keep in mind while conducting due diligence ? (7 marks)

Answer 4(a)

The purpose of Environmental Impact Assessment (EIA) is to identify and evaluate the potential impacts (beneficial and adverse) of development and projects on the environmental system. It is a very useful aid for decision making based on understanding of the environment implications including social, cultural and aesthetic concerns which could be integrated with the analysis of the project costs and benefits. The projects which could be the candidates for detailed Environment Impact Assessment include the following:-

- Those which can significantly alter the landscape, land use pattern and lead to concentration of working and service population;

— Those which need upstream development activity like assured mineral and forest products supply or downstream industrial process development;

— Those involving manufacture, handling and use of hazardous materials;

— Those which are sited near ecologically sensitive areas, urban centers, hill resorts, places of scientific and religious importance;

— Industrial Estates with constituent units of various types which could cumulatively cause significant environmental damage.

The Environmental Impact Assessment (EIA) should be prepared on the basis of the existing background pollution levels vis-a-vis contributions of pollutants from the proposed plant. The EIA should address some of the basic factors listed below:

— Meteorology and air quality Ambient levels of pollutants such as Sulphur Dioxide, oxides of nitrogen, carbon monoxide, suspended particulate matters, should be determined at the center and at 3 other locations on a radius of 10 km with 120 degrees angle between stations.

— Additional contribution of pollutants at the locations are required to be predicted after taking into account the emission rates of the pollutants from the stacks of the proposed plant, under different meteorological conditions prevailing in the area.

— Hydrology and water quality

— Site and its surroundings

— Occupational safety and health

— Details of the treatment and disposal of effluents(liquid, air and solid) and the methods of alternative uses

— Transportation of raw material and details of material handling

— Control equipment and measures proposed to be adopted.

Preparation of Environmental Management Plan is required for formulation, implementation and monitoring of environmental protection measures during and after commissioning of projects.

Answer 4(b)

The goal of due diligence is to provide the party proposing the transaction with sufficient information to make a reasoned decision as to whether or not to complete the transaction as proposed. The following factors may be kept in mind in this regard:

(i) Be clear about your expectations in terms of revenues, profits and the probability of the collaboration to provide you the same.

(ii) Consider whether you have resources to make the business succeed and whether you are willing to put in all the hard work, which is required for any new or collaborated venture.

(iii) Consider whether the prospective business gives you the opportunity to put your skills and experience to good use.

(iv) Learn as much as you can about the industry you are interested in from media reports, journals and people in the industry.

Planning the schedule

Once it is decided for a particular business, make sure of the following things:

— Steps to be followed in due diligence process

— Areas to be checked

— Aspects to be checked in each area

— Information and other material to be requested from the seller

Negotiation for time

Some times, it may be the case that, the other party in the collaboration wants the process to get over as soon as possible and try to hurry the proceedings. When the other party gives a short review period, negotiations can be made for adequate time to have a complete review on crucial financial and legal aspects.

Risk Minimisation

All the information like financials, tax returns, patents, copyrights and customer base should be double checked to ensure that the company does not face a lawsuit or criminal investigation. The financials are very important and one needs to be certain that the other company did not engage in creative accounting. The asset position and profitability of the company are vital. Since, due diligence exercise deals with the overall business, it is important to consider aspects such as:

— background of promoters of the collaborator

— performance of senior management team of the collaborator

— organizational strategy

— business plans

— risk management system

— technological advancement

— infrastructure adequacy

— optimum utilization of available resources.

Information from external sources

The company's customers and vendors can be quite informative. It may be found from them whether the other company falls in their most favoured clients list. Any flaws that the audit uncovers would help to negotiate down the sale price. Due diligence is "a chance to get a better deal". But one should not go overboard. It should be remembered that the whole point of buying a company is to add people to your own organization. Even if the seller and staff do not stay on after the deal, they may prove useful as advisers in the future.

Limit the report with only material facts

While preparing the report it is advisable to be precise and only the information that has a material impact on the target company is required to be included.

Structure of information

Once the due diligence process is over, while preparing the report, information has to be structured in an organized manner in order to have a better correlation on related matters.

Question 5

(a) Write notes on the following :

(i) Compliance programme

(ii) Securitisation

(iii) Wilful default. *(3 marks each)*

(b) Distinguish between the following :

(i) 'Legal due diligence' and 'financial due diligence'.

(ii) 'Foreign currency convertible bonds (FCCBs)' and 'depository receipts (DRs)'. *(3 marks each)*

Answer 5(a)(i)

Compliance Programme

The objective of compliance programme is to manage the compliance risk effectively, to promote ethical culture in the organisation, resulting in the maintenance and enhancement of the reputation of the Company. Through an effective Compliance Programme, the business and its stakeholders learn about the compliance responsibilities individually and for the organisation as a whole, making them a part of business processes; the compliance programme reviews operations to ensure responsibilities are carried out and requirements are met. It helps the management to take corrective action wherever necessary.

Answer 5(a)(ii)

Securitisation

The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 defines "securitisation" as -

- acquisition of financial assets by any securitisation company or reconstruction company from any originator,
- whether by raising of funds by such securitisation company or reconstruction company
- from qualified institutional buyers
- by issue of security receipts representing undivided interest in such financial assets or otherwise.

Securitisation is the process of conversion of existing assets or future cash flows into marketable securities. Securitisation deals with the conversion of assets which are not marketable presently into marketable ones. Thus, it is conversion of illiquid assets into liquid assets.

Answer 5(a)(iii)

Wilful default

A "wilful default" is deemed to have occurred if any of the following events is noted:-

(a) The company has defaulted in meeting its payment/repayment obligations to the lender even when it has the capacity to honour the said obligations.

(b) The company has defaulted in meeting its payment/repayment obligations to the lender and has not utilised the finance from the lender for the specific purposes for which finance was availed of but has diverted the funds for other purposes.

(c) The company has defaulted in meeting its payment/repayment obligations to the lender and has siphoned off the funds so that the funds have not been utilised for the specific purpose for which finance was availed of, nor are the funds available with the unit in the form of other assets.

Thus, there must be a default and it must be wilful, knowing default.

Answer 5(b)(i)

'Legal due diligence' and 'financial due diligence'

Both legal and financial due diligence are necessary in any transaction of intra or inter corporate nature. However, they differ mainly in the following:

A legal due diligence covers the legal aspect of a business or business transaction while financial due diligence takes care of financial aspects of a business or business transaction. Due the above difference, legal due diligence covers preparation of regulatory checklists, meeting with personnel, independent check with regulatory authorities etc. apart from document verification while financial due diligence covers review of accounting policies, review of internal audit procedures, quality and sustainability of earnings and cash flow, condition and value of assets, potential liabilities, tax implications of deal structures, examination of information systems to establish the reliability of financial information, internal control systems etc.

Answer 5(b)(ii)

'Foreign Currency Convertible Bonds (FCCBs)' and 'Depository Receipts (DRs)'

According to Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993, Foreign Currency Convertible Bonds (FCCBs) means a bond issued by an Indian company expressed in foreign currency, the principal and interest in respect of which is payable in foreign currency and on maturity it is convertible into equity shares of the Indian issuing company.

According to the Depository Receipts Scheme 2014, 'depository receipt' means a foreign currency denominated instrument, whether listed on an international exchange or

not, issued by a foreign depository in a permissible jurisdiction on the back of permissible securities (known as underlying securities) issued or transferred to that foreign depository and deposited with a domestic custodian and includes 'global depository receipt' as defined in section 2(44) of the Companies Act, 2013.

Question 6

(a) PK Cement Ltd., incorporated in January, 2014, is engaged in the business of manufacturing cement. The company is facing stiff competition and with a plan to increase its market share, the Board has decided to reduce the price of cement bags. The cost structure of one cement bag is as under :

(i) Cost of production : ₹185

(ii) Selling price : ₹245

Now, since the company has started to sell its cement bag @ ₹210, other cement manufacturers made a complaint to the Competition Commission of India stating that PK Cement Ltd. is guilty of predatory pricing having the effect of reducing the competition or eliminating the competition. Advise PK Cement Ltd. as to the meaning of predatory pricing and whether the company can be said to have indulged in the said practice having regard to the provisions of the Competition Act, 2002. *(5 marks)*

(b) Star Ltd. and its group company Earth Ltd. acquired shares of Mars Ltd. (the target company) over a period of time. On 17th December, 2014, Star Ltd. and Earth Ltd. were holding 13.86% and 4.74% shares respectively of the target company. Both these companies want to further acquire shares in the target company. You are asked to advise the companies whether these companies can freely acquire further shares in the target company as per the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

(5 marks)

(c) The balance sheet of Neeraj Fertilizer Ltd. as at 31st March, 2015 disclosed the following details :

	(₹ in crore)
Authorised shares capital (equity shares)	*500*
Paid-up share capital	*200*
Statement of profit and loss (Cr.)	*30*
General reserve	*70*
Debenture redemption reserve	*50*
Loan (long-term)	*50*
Temporary loan payable on demand	*20*
Short-term loan	*15*

Board of directors of the company wishes to borrow an additional sum of ₹300 crore from the company's financial institution. The borrowing was duly approved at a Board meeting. One of the directors had raised objection for such borrowing and argued that said borrowing was beyond the powers of the Board of directors.

The Board of directors seeks your advice, being a company's advisor, about the borrowing limits and compliances required with the provisions of the Companies Act, 2013. Advise the company. *(5 marks)*

Answer 6(a)

Section 4 of the Competition Act, 2002 prohibits abuse of dominant position. In particular, section 4 **(**2) (a) which provides that there shall be an abuse of dominant position, if an enterprise or a group, directly or indirectly, imposes unfair or discriminatory—

(i) condition in purchase or sale of goods or service; or

(ii) price in purchase or sale (including predatory price) of goods or service.

For the purpose of section 4, the expression "predatory price" means the sale of goods or provision of services, at a price which is below the cost, as may be determined by regulations, of production of the goods or provision of services, with a view to reduce competition or eliminate the competitors.

In the given case PK Cement Ltd. has reduced the selling price of its cement bag from Rs. 245 to Rs. 210 per bag and the cost of production is Rs. 185 per bag. So, the selling price is above the cost of production. As per the provisions of the Section 4 (2) (a), the company can not be said to have indulged in the said practice with respect to Competition Act, 2002. Thus the concept of predatory pricing applies only when the sale price is below the cost of production. In this case, they have only reduced their profits and thus the provisions relating to predatory pricing will not apply.

Answer 6(b)

As per regulation 3 (1) of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 which provides that no acquirer shall acquire shares or voting rights in a target company which taken together with shares or voting rights, if any, held by him and by persons acting in concert with him in such target company, entitle them to exercise twenty-five per cent or more of the voting rights in such target company unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations.

So, in the present case, the holdings of Star Ltd. and Earth Ltd in the target company (Mars Ltd.) is 13.86 % and 4.74 % which is collectively 18.60 %. Both these companies want to further acquire shares in the target company. So as per the provisions of regulation 3(1) only if this further acquiring would result in entitling them to exercise 25 % or more of the voting rights in such target company, then they have to make open offer before acquiring such additional shares.

Answer 6(c)

Section 180(1)(c) of the Companies Act, 2013 prohibits the Board of directors of a company from borrowing a sum which together with the monies already borrowed exceeds the aggregate of the paid-up share capital of the company and its free reserves apart from temporary loans obtained from the company's bankers in the ordinary course of business unless they have received the prior sanction of the company by a special resolution in general meeting.

Explanation to section 180(1) (c) provides that 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.

According to the above provisions, the board of directors of Neeraj Fertilizer Ltd. can borrow without the approval of the shareholders in the general meeting, up to an amount calculated as follows:

Paid up share capital	=	Rs. 200 crores
Free reserves (Profit & and loss+ General reserve) - 30+70	=	Rs. 100 crores
		Rs. 300 crores
Further, the company has long term loan of Rs. 50 crores		- Rs. 50 crores
Total amount up to which the company can borrow	=	Rs. 250 crores

So, in the given case, the board of directors of Neeraj Fertilizer Ltd. wishes to borrow an additional sum of Rs. 300 crores from the company's financial institution. Thus, the objection of one of director is correct and the said borrowing will be beyond the powers of the Board of directors.

So, in order to borrow the said amount the company has to comply with the following requirements:

(i) Hold the Board Meeting and issue the notice of general meeting.

(ii) Hold general meeting and pass the special resolution for transacting the matter stated above.

(iii) File Form No. MGT-14 with the fee or additional fee as provided in the Companies (Registration of Offices and fees) Rules, 2014 with the ROC within 30 days of passing the special resolution.

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, 1956 unless stated otherwise.

PART A

Question 1

(a) While combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India is prohibited under section 6 of the Competition Act, 2002, certain transactions are exempted and are, therefore, not prohibited.

List out the transactions or dealings which are not hit by section 6 of the Competition Act, 2002. (5 marks)

(b) The draftsmen of the Competition Act, 2002 had demonstrated utmost concern and care in identifying questionable combinations and prohibiting such combinations. In order to achieve this object, extra territorial jurisdiction is conferred on the Competition Commission of India (CCI) to inquire and pass orders even if both the parties to an agreement are outside India.

List out the circumstances where the CCI can pass orders consequent to extra territorial jurisdiction conferred on it. (5 marks)

(c) Brown Ltd. committed certain defaults in repayment of deposits. Subsequently, the said defaults were remedied and a period of 30 months has lapsed after such defaults ceased to subsist.

Brown Ltd. desires to purchase its own shares. Do you think Brown Ltd. is entitled to proceed with the proposed buy-back of shares ?

Give reasons for your answer quoting the relevant provisions applicable to the issue under consideration.

(d) The paid-up capital of Cool Ltd. as on 31st March, 2014 is 10 crore and its free reserves as on the same date was 10 crore. Cool Ltd. proposes to buy-back its shares for a value upto 15% of its paid-up capital.

State whether the Board of Cool Ltd. can approve buy-back of company's shares upto 15% of the paid-up capital under the provisions of the Companies Act, 2013. (5 marks)

Answer 1(a)

The provisions of section 6 do not apply to share subscription or financing facility or any acquisition, by a public financial institution, foreign institutional investor, bank or

venture capital fund, pursuant to any covenant of a loan agreement or investment agreement. This exemption appears to have been provided in the Act to facilitate raising of funds by an enterprise in the course of its normal business. Under section 6(5), the public financial institution, foreign institutional investor, bank or venture capital fund, are required to file in prescribed form, details of the control, the circumstances for exercise of such control and the consequences of default arising out of loan agreement or investment agreement, within seven days from the date of such acquisition or entering into such agreement, as the case may be.

Answer 1(b)

Extra Territorial Jurisdiction of Commission

Section 32 extends the jurisdiction of Competition Commission of India to inquire and pass orders in accordance with the provisions of the Act into an agreement or dominant position or combination, which is likely to have, an appreciable adverse effect on competition in relevant market in India, notwithstanding that,

(a) an agreement referred to in section 3 has been entered into outside India; or

(b) any party to such agreement is outside India; or

(c) any enterprise abusing the dominant position is outside India; or

(d) a combination has taken place outside India; or

(e) any party to combination is outside India; or

(f) any other matter or practice or action arising out of such agreement or dominant position or combination is outside India.

The above clearly demonstrate that acts taking place outside India but having an effect on competition in India will be subject to the jurisdiction of Commission. The Competition Commission of India will have jurisdiction even if both the parties to an agreement are outside India but only if the agreement, dominant position or combination entered into by them has an appreciable adverse effect on competition in the relevant market of India.

Answer 1(c)

Under Section 70 of the Companies Act, 2013, no company shall directly or indirectly purchase its own shares or other specified securities under Certain circumstances. One of such prohibition is, if a default, is made by the company, in the repayment of deposits accepted either before or after the commencement of this Act, interest payment thereon, redemption of debentures or preference shares or payment of dividend to any shareholder, or repayment of any term loan or interest payable thereon to any financial institution or banking company: However, the buy-back is not prohibited, if the default is remedied and a period of three years has lapsed after such default ceased to subsist. In this case Brown Ltd. has to wait for 6 more months because from the date the default has made good to now only 30 months has been be passed which shall be atleast 3 years i.e. 36 months.

Answer 1(d)

Board of directors can approve buy-back up to 10% of the total paid-up equity capital and free reserves of the company and such buy back has to be authorized by the board by means of a resolution passed at the meeting. Accordingly, 10% of paid-up equity

capital and free reserves amounts to Rs 2 crores(i.e10% of 20 crores). Thus, Board of directors can approve the buy back of shares of Rs 1.5 crores(15% of paid up capital).

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

Question 2

(a) Aspire Ltd. is the target company in respect of which an acquirer made an open offer for acquisition of shares and the open offer has commenced. Dreams Ltd. is the subsidiary of Aspire Ltd.

Dreams Ltd. signed the loan agreements with financial institutions for major capital expenditure for its expansion project and started withdrawing the loan amount during the open offer period. The said borrowings are clearly within the ordinary course of its business.

No approval was taken by Aspire Ltd. from its shareholders nor did Dreams Ltd. obtain the approval from its shareholders. The internal auditors have opined that the target company has violated the provisions of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 as no approval was obtained by the shareholders of the target company for the borrowings effected. The statutory auditors have agreed with the views of the internal auditors and pointed out that the target company Aspire Ltd. has failed in its obligations that are required to be complied with during the offer period in terms of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 as approval of its members by way of special resolution through the mechanism of postal ballot was not obtained. Moreover, they maintained that Dreams Ltd. borrowed money for its expansion programme when the open offer of target company was on and therefore Dreams Ltd. violated the provisions of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

State in clear terms whether there is a violation of the provisions of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 by Aspire Ltd. or Dreams Ltd. (6 marks)

(b) As per the scheme of arrangement, textiles undertaking of Cotton Ltd. is proposed to be demerged to Jutewel Ltd. under sections 391 and 394 of the Companies Act, 1956. One of the conditions of the aforesaid scheme is that any excess in the value of net assets of textiles undertaking proposed to be transferred to the resulting company shall be credited to general reserve.

If you as an advisor to the parties to the arrangement are asked to advise, what will be your response considering the applicable accounting standards and legal provisions applicable to the aforesaid case. (5 marks)

(c) In an open offer, the schedule of activities and the timelines of all competing offers shall be identical. Explain. (4 marks)

OR (Alternate Question to Q.No. 2)

Question 2A

Comment on the following statements :

(i) In terms of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, 'offer period' and 'tendering period' are one and the same. (3 marks)

(ii) *The acquirer can opt out of the open offer process at any point of time by informing stock exchange wherein the shares of the target company are listed and furnishing a copy of the communication to the target company. (3 marks)*

(iii) *Revision of offer price can be made by the acquirer upward but that can be exercised only in the event of there being a competing offer. (3 marks)*

(iv) *Acquisition pursuant to a scheme made under section 18 of the Sick Industrial Companies (Special Provisions) Act, 1985 or any statutory modification thereto shall be automatically exempt from the obligation to make an open offer under Regulations 3 and 4 of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 but not the acquisition made pursuant to the provisions of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002. (3 marks)*

(v) *The acquisition of shares resulting from invocation of pledge by a public financial institution is exempt from open offer obligation. (3 marks)*

Answer 2(a)

As per Regulation 26(2)(b), during the offer period, unless the approval of shareholders of the target company by way of a special resolution by postal ballot is obtained, the board of directors of either the target company or any of its subsidiaries shall not effect any material borrowings outside the ordinary course of business. In the given case the borrowings by Dreams Limited, a subsidiary of Aspire Limited, the acquirer, was in the ordinary course of business.

Thus there is no violation of the provisions of SEBI(SAST) Regulations 2011 neither by Aspire Ltd. nor by Dreams Ltd.

Answer 2(b)

The given case is similar to the case of demerger of software undertaking of Sony India limited, where it was decided that AS-14 is not applicable to Demergers. The Delhi High Court (the High Court), while approving scheme of arrangement between Sony India and Sony Software in 2012 has clarified that AS-14 (i.e., accounting standards issued by the Institute of Chartered Accountants) is applicable only to amalgamations and not to demerger.

As per the scheme of arrangement, 'Software Undertaking' of Sony India is proposed to be transferred to Sony Software under Sections 391 to 394 of the Companies Act, 1956. One of the conditions of the scheme was that any excess in the value of net assets of software undertaking transferred to the resulting company shall be applicable for distribution to the shareholders of the resulting company. Regional Director of Northern Region, Ministry of Corporate has raised objection in his affidavit filed with the High Court stating that excess if any, in the value of the net assets of the software undertaking should be adjusted to the capital reserve as prescribed in AS-14 and not to the general reserve as proposed in the scheme of arrangements. The petitioners contended that AS-14 is applicable only to amalgamations and not to demerger. It was clarified that AS-14 is applicable only to amalgamations and not to demerger. On a plain reading of the accounting standard under reference, it is clear that the same is applicable only in case of an amalgamation and not in case of demergers. This has also been held by the Gujarat High Court in the case of 2010 1 CLJ 351 tiled Gallops Realty (P) Ltd.

Answer 2(c)

Competitive offer is an offer made by a person, other than the acquirer who has made the first public announcement. A competitive offer shall be made within 15 working days of the date of the Detailed Public Statement (DPS) made by the acquirer who has made the first PA. If there is a competitive offer, the acquirer who has made the original public announcement can revise the terms of his open offer within 14 days of competitive offer provided the revised terms are favourable to the shareholders of the target company. Further, the bidders are entitled to make revision in the offer price up to 3 working days prior to the opening of the offer. The schedule of activities and the offer opening and closing of all competing offers shall be carried out with identical timelines.

Answer 2A(i)

Offer period and tendering period

The term 'offer period' pertains to the period starting from the date of the event triggering open offer till completion of payment of consideration to shareholders by the acquirer or withdrawal of the offer by the acquirer as the case may be.

The term 'tendering period' refers to the 10 working days period falling within the offer period, during which the eligible shareholders who wish to accept the open offer can tender their shares in the open offer.

Answer 2A(ii)

The statement is not correct. As per Regulation 23 an open offer once made cannot be withdrawn except in the following circumstances:

— Statutory approvals required for the open offer or for effecting the acquisitions attracting the obligation to make an open offer have been refused subject to such requirement for approvals having been specifically disclosed in the Detailed Public Statement of the letter of offer;

— Any condition stipulated in the agreement attracting the obligation to make the open offer is not met for reasons outside the reasonable control of the acquirer, subject to such conditions having been specifically disclosed in the DPS and the letter of offer;

— Sole acquirer being a natural person has died;

— Such circumstances which in the opinion of SEBI merit withdrawal of open offer.

Answer 2A(iii)

Revision of offer price [Regulation 18(4&5)]

Irrespective of whether a competing offer has been made, an acquirer may make upward revisions to the offer price, and subject to the other provisions of these regulations, to the number of shares sought to be acquired under the open offer, at any time prior to the commencement of the last three working days before the commencement of the tendering period.

Answer 2A(iv)

Under Regulation 10 of SEBI(SAST) Regulations 2011, certain acquisitions shall be exempt from the obligation to make an open offer under regulation 3 and regulation 4

subject to fulfillment of the conditions stipulated therefor. One of such exemption is acquisition pursuant to a scheme made under section 18 of the Sick Industrial Companies (Special Provisions) Act, 1985 or any statutory modification or re-enactment thereto and acquisition pursuant to the provisions of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

Answer 2(A)(v)

As per Regulation 10 of SEBI(SAST) Regulations 2011, an acquisition in the ordinary course of business by invocation of pledge by Scheduled Commercial Banks or Public Financial Institutions shall be exempt from the obligation to make an open offer under regulation 3 and regulation 4.

Question 3

(a) *Flying Ltd. got demerged and the resulting company Soars Ltd. was formed. It was a demerger within the meaning of section 2(19AA) of the Income-tax Act, 1961. Your advice is sought by Flying Ltd. regarding the tax concession available to a demerged company. (5 marks)*

(b) *Alps (Pvt.) Ltd. is taking over an unlisted company Mountain Ltd., through the route stipulated under section 395 of the Companies Act, 1956. Alps (Pvt.) Ltd. wants to compulsorily acquire the shares of minority shareholders of Mountain Ltd. A group of minority shareholders objected to the compulsory acquisition of their shares by Alps (Pvt.) Ltd.*

(i) *Will their objections stand good as per the provisions under section 395 of the Companies Act, 1956 ?*

(ii) *Will Alps (Pvt.) Ltd. be entitled to carry forward unabsorbed depreciation and accumulated losses of Mountain Ltd ? (5 marks)*

(c) *Hardnut Ltd. wants to buy-back its equity shares. The company has equity share capital of ₹100 crore (face value of ₹10 fully paid-up) and free reserves of 200 crore. Partly paid equity shares are ₹60 crore. Preference share capital of face value ₹100 fully paid is ₹40 crore. The company seeks your opinion about the quantum of shares that can be bought back. (5 marks)*

Answer 3(a)

If any demerger takes places within the meaning of section 2(19AA) of the Income-tax Act, the following tax concessions shall be available to:

1. Demerged company.
2. Shareholders of demerged company.
3. Resulting company

Tax concession to demerged company

(i) *Capital gains tax not attracted [Section 47(vib)]*

According to section 47(vib), where there is a transfer of any capital asset in case of a demerger by the demerged company to the resulting company, such

transfer will not be regarded as a transfer for the purpose of capital gain provided the resulting company is an Indian company.

(ii) *Tax concession to a foreign demerged company [Section 47(vic)]*

Where a foreign company holds any shares in an Indian company and transfers the same, in case of a demerger, to another resulting foreign company, such transaction will not be regarded as transfer for the purpose of capital gain under section 45 if the following conditions are satisfied:

(a) at least seventy-five per cent of the shareholders of the demerged foreign company continue to remain shareholders of the resulting foreign company; and

(b) such transfer does not attract tax on capital gains in the country, in which the demerged foreign company is incorporated.

(iii) *Reserves for shipping business* : Where a ship acquired out of the reserve is transferred in a scheme of demerger, even within the period of eight years of acquisition there will be no deemed profits to the demerged company.

Answer 3(b)(i)

Section 395 of the Companies Act contains a compulsory acquisition mode for the transferee company to acquire the shares of minority shareholders of Transferor Company. Where the scheme has been approved by the holders of not less than nine tenth (90%) in value of the shares of the transferor company whose transfer is involved, the transferee company, may, give notice to any dissenting shareholders that transferee company desires to acquire their shares. The scheme shall be binding on all the shareholders of the transferor company (including dissenting shareholders), unless the Court Orders otherwise (i.e. that the scheme shall not be binding on all shareholders).

Case Law 1 : Power of Acquisition of Shares of dissentient minority shareholders is not ultra vires the constitution of India. S Viswanathan v. East India Distilleries & Sugar Factories Limited(1957) 27 Com Cases 175:AIR 1957 Mad 341.

Case Law 2 : Where the scheme or contract has been approved by 90% of the shareholders, the offer of the transferee company will be treated as prima-facie a fair one and the onus will be on the dissentients to show the contrary. Benarasi Das Saraf v. dalmia Dadri Cement Ltd(1958)28 Com cases 435(Punj).

The objections of minority shareholders may not hold good.

Answer 3(b)(ii)

The takeover achieved through this Section 395 of the Act will not fall within the meaning of amalgamation under the Income Tax Act and as such benefits of amalgamation provided under the said Act will not be available to the acquisition under consideration. The takeover in the above process will not enable carrying forward of unabsorbed depreciation and accumulated losses of the transferor Company in the transferee Company for the reason that the takeover does not result in the transferor Company losing its identity.

Answer 3(c)

Quantum of Buyback

(a) Board of directors can approve buy-back up to 10% of the total paid-up equity capital and free reserves of the company and such buy back has to be authorized by the board by means of a resolution passed at the meeting.

(b) Shareholders by a special resolution can approve buy-back up to 25% of the total paid-up capital and free reserves of the company. In respect of any financial year, the shareholders can approve by special resolution upto 25% of total equity capital in that year.

Quantum of buy-back with the approval of Board

Total paid up equity capital is	Rs 100 Crore
Partly paid Equity Capital	Rs 60 crores
Free reserves	Rs 200 crores

10 % total paid up equity capital and free reserves would be 10% of Rs 360 crores i.e Rs 36 crores

Quantum of buy-back with the approval of shareholders

Total paid up equity capital	Rs 100 Crore
Partly paid Equity Capital	Rs 60 crores
Free reserves	Rs 200 crores
Paid up preference capital	Rs 40 crores

25% of total paid up capital and free reserves would be 25% of 400 crores which is Rs 100 crores. Buy-back in a financial year is 25% of paid up equity capital which is 25% of Rs 100 Crores which is Rs 25 crores.

(Note:- Partly paid shares shall not be bought– Back , only those shares which are fully paid up can be buy-back.)

PART B

Question 4

(a) Zen Ltd. has earned a profit of ₹40,00,000 before tax for the year ended 31st March, 2014. Tax amounts to ₹11,40,000. The share capital of the company is 60,00,000 (4,00,000 equity share of ₹10 each and 2,00,000, 7% preference shares of 10 each). Compute earnings per share (EPS) of Zen Ltd. *(5 marks)*

(b) Valuation of shares of an enterprise demands a detailed and comprehensive analysis embracing a host of factors at macro and micro level.

List out five important factors that influence the determination of price of the shares. *(5 marks)*

(c) How is the open offer price for acquisition of shares of a listed target company whose shares are frequently traded determined ? *(5 marks)*

Answer 4(a)

Earnings per Share of Zen Limited

Earnings before tax	40,00,000
Less:Tax	11,40,000
Earnings after tax	28,60,000
Less : Preference Dividend	1,40,000
Earnings after tax and preference dividend	27,20,000

Earnings per share = 27,20,000/400000 which is Rs 6.8.

Answer 4(b)

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 a willing seller when neither are under any compulsion to buy or sell, and both parties have knowledge of relevant facts. Arriving at the transaction price requires that a value be placed on the company for sale. The process of arriving at this value should include a detailed, comprehensive analysis which takes into account a range of factors including the past, present, and most importantly, the future earnings and prospects of the company, an analysis of its mix of physical and intangible assets, and the general economic and industry conditions. The other salient factors include:

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

(2) Dividends paid on the shares.

(3) Relative growth prospects of the two companies.

(4) In case of equity shares, the relative gearing of the shares of the two companies. ('gearing' means ratio of the amount of Issued preference share capital and debenture stock to the amount of issued ordinary share capital.)

(5) Net assets of the two companies.

(6) Voting strength in the merged (amalgamated) enterprise of the shareholders of the two companies.

(7) Past history of the prices of shares of the two companies.

Answer 4(c)

If the target company's shares are frequently 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;

— Volume weighted average market price for sixty trading days preceding the PA.

Question 5

(a) Various judicial pronouncements on valuation principles demonstrate salient dicta of courts in relation to the subject. You are required to list out the principles set-out by the courts in this regard. (6 marks)

(b) Blue Ltd. and Moon Ltd. have agreed to amalgamate to form a new company Blue Moon Ltd. After negotiation, the two companies have decided on the balance

		(₹ in '000)
	Blue Ltd.	*Moon Ltd.*
EQUITY AND LIABILITIES		
(1) Shareholders' funds		
(a) Share capital		
Equity shares of ₹10 each	*5,00,000*	*10,00,000*
(b) Reserves and surplus		
Reserve fund	*20,000*	*—*
Surplus	*40,000*	*40,000*
(2) Current liabilities		
Trade payables	*40,000*	*60,000*
TOTAL	*6,00,000*	*11,00,000*

		(₹ in '000)
	Blue Ltd.	*Moon Ltd.*
ASSETS		
(1) Non-current assets		
(i) Tangible assets		
(a) Land and building	*2,00,000*	*4,25,000*
(b) Plant and machinery	*1,70,000*	*2,75,000*
(ii) Intangible assets (Goodwill)	*50,000*	*1,00,000*
(2) Current assets		
(a) Inventories	*80,000*	*1,20,000*
(b) Trade receivables	*30,000*	*1,00,000*
(c) Cash and cash equivalents	*70,000*	*80,000*
TOTAL	*6,00,000*	*11,00,000*

The assets and liabilities are taken over by Blue Moon Ltd. Compute the total number of shares of the Blue Moon Ltd. having a value of ₹10 each to be issued to the shareholders of Blue Ltd. and Moon Ltd. using net asset value method. *(5 marks)*

(c) In which circumstances, is the market based approach to valuation not relevant and useful ? *(4 marks)*

Answer 5(a)

Judicial Pronouncement on Valuation Principles/Valuation Reports

Some of the salient dicta of Courts in relation to valuation principles and valuation reports are stated under:

In *Bahoo J. Coyajee* v. *Shanta Genevieve Prommeret Parulekar* [1991] (3) Bom. LR 319, the Court observed:

"If the thing complained of is a thing which in substance the majority of the company are entitled to do or if something has been done irregularly which the majority of the company are entitled to do regularly, or if something has been done illegally which the majority of the company are entitled to do legally, there can be no use in having litigation about it, the ultimate end of which is only that a meeting has to be called, and then ultimately the majority gets its wishes".

In *Miheer H. Mafatlal* v. *Mafatlal Industries Ltd.* [1996] 87 Comp. Cas. 792 (SC), the Hon'ble Supreme Court held:

"If Share Exchange Ratio is fixed by Chartered Accountant upon consideration of various factors and approved by majority of shareholders in meeting, the Court will not disturb ratio".

In *Re. Maknam Investments Ltd.* [1995] (4) Comp.LJ page 330, the Calcutta High Court observed:

"Court does not go into the matter of fixing of exchange ratios in great detail or to sit in appeal over the expert decision of concerned chartered accountant of repute. Court only sees whether there is any manifest unreasonableness or manifest fraud involved in the matter".

In *Hindustan Lever Employees Union* v. *Hindustan Lever Limited* [1995] (Supp.) (1) SCC 499 at 517(519), the Hon'ble Court stated:

"The valuation of shares is a technical matter. It requires considerable skill and experience. There are bound to be differences of opinion among accountants as to what is the correct value of the shares of a company. It was emphasized that more than 99% of the shareholders had approved the valuation. The test of fairness of this valuation is not whether the offer is fair to a particular shareholder…. who may have reasons of his own for not agreeing to the valuation of the shares, but the overwhelming majority of the shareholders have approved of the valuation. The Court should not interfere with such valuation".

The Hindustan Lever case also repelled the case that valuation particulars needed a proper disclosure as material facts in the Explanatory Statement. It confirmed the judgment

of *Jitendra R. Sukhadia* v. *Alembic Chemical Works Co. Ltd.*,(1987) 3 Comp.L.J 141 (Guj) as follows:

"How this exchange ratio was worked out, however, was not required to be stated in the statement contemplated under Section 394(1)(a)".

The Hindustan Lever's judgment (1995) Supp. (1) SCC 499 at 502 noted:

"In the absence of it being shown to be vitiated by fraud and malafide, the mere fact that the determination done by slightly different method might have resulted in different conclusion would not justify interference of Court."

Answer 5(b)

Number of shares of Blue Moon Limited to be issued to the shareholders of Blue Limited and Moon Limited.

Amt in '000

Particulars	*Blue Limited*	*Moon Ltd*
Land and Building	2,00,000	4,25,000
Plant and Machinery	1,70,000	2,75,000
Goodwill	50,000	1,00,000
Stock	80,000	1,20,000
Trade Receivable	30000	1,00,000
Cash and Bank	70,000	80,000
Total Assets	6,00,000	11,00,000
Les sundry creditors (Trade Payable)	40,000	60,000
Net assets takenover	5,60,000	10,40,000
Number of shares to be issued to the shareholders of Blue Limited		560 lakh shares
Number of shares to be issued to the shareholders of Moon Limited		1040 lakh shares
Total number of shares to be issued by blue moon limited		1600 lakh shares

Answer 5(c)

Market Price Method of valuation is not relevant in the following cases:

— Valuation of a division of a company

— Where the share are not listed or are thinly traded

— In the case of a merger, where the shares of one of the companies under consideration are not listed on any stock exchange

— In case of companies, where there is an intention to liquidate it and to realise the assets and distribute the net proceeds.

PART C

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

Question 6

Write notes on the following :

(a) Four grounds on which a company may be wound-up

(b) 'State' with reference to the UNCITRAL model law

(c) Types of foreign proceedings covered

(d) Protection of creditors and other interested persons under the UNCITRAL model law

(e) Mode of recovery of debt determined by Debt Recovery Tribunal (DRT).

(4 marks each)

OR (Alternate question to Q.No. 6)

Question 6A

(i) "The effects provided by Article 20 of the UNCITRAL model law in respect of recognition of a foreign main proceeding are discretionary in nature." Comment whether the statement is correct or not and state the effects of recognition of a foreign main proceeding as per Article 20. (5 marks)

(ii) "The official liquidator cannot have recourse to the doctrine of election. He can challenge the order passed by the recovery officer and appeal under the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 but cannot approach the company court to set aside the auction or confirmation of sale when the same has been confirmed by the recovery officer under the Act."

Comment on the above statement giving the options, if any, available to the official liquidator in this regard. (5 marks)

(iii) The provisions of the Securities and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 do not apply to certain cases. List out six such cases where the provisions of the Act do not apply. (5 marks)

(iv) Explain the salient features of Chapter 11 dealing with the US Bankruptcy Code. (5 marks)

Answer 6(a)

A company under Section 433 may be wound up by the Court if

(a) the company has passed a special resolution of its being wound up by the Court; or

(b) default is made in delivering the statutory report to the Registrar or in holding the statutory meeting; or

(c) it does not commence business within a year from its incorporation or suspends business for a whole year; or

(d) the number of its members in the case of a public company is reduced below seven and in the case of a private company, below two; or

(e) it is unable to pay its debts; or

(f) the Court is of the opinion that it is just and equitable that it should be wound up; or

(g) if the company has made a default filing with the Registrar its balance sheet and profit and loss account or annual return for any five consecutive financial years; or

(h) if the company has acted against the interests of the sovereignty and integrity of India, the security of the state, friendly relations with foreign states, public order, decency or morality; or (It may be noted that the tribunal shall make an order for winding up of a company under clause (h) on application made by the Central Government or a State Government)

(i) If the tribunal is of opinion that the company should be wound up under the circumstances specifiedin Section 424 G (i.e winding up of a sick company):

Answer 6(b)

The word "State", as used in the preamble and throughout the Model Law, refers to the country that enacts the Law (the "enacting State"). The term should not be understood as referring, for example, to a state in a country with a federal system.

Answer 6(c)

Types of foreign proceedings covered

To fall within the scope of the Model Law, a foreign insolvency proceeding needs to possess certain attributes. These include the basis in insolvency-related law of the originating State; involvement of creditors collectively; control or supervision of the assets and affairs of the debtor by a court or another official body; and reorganization or liquidation of the debtor as the purpose of the proceeding. Within those parameters, a variety of collective proceedings would be eligible for recognition, be they compulsory or voluntary, corporate or individual, winding-up or reorganization. It also includes those in which the debtor retains some measure of control over its assets, albeit under court supervision (e.g. suspension of payments, "debtor in possession"). An inclusive approach is used also as regards the possible types of debtors covered by the Model Law.

Answer 6(d)

Protection of creditors and other interested persons

Foreign creditors have the same rights regarding the commencement of and participation in a proceeding under the laws of the enacting state relating to insolvency as creditors in the state.

The Model Law contains following provisions to protect the interests of the creditors (in particular local creditors), the debtor and other affected persons:

— availability of temporary relief upon application for recognition of a foreign

proceeding or upon recognition is subject to the discretion of the court; it is expressly stated that in granting such relief the court must be satisfied that the interests of the creditors and other interested persons, including the debtor, are adequately protected (Article 22, paragraph 1);

— the court may subject the relief it grants to conditions it considers appropriate; and

— the court may modify or terminate the relief granted, if so requested by a person affected thereby(Article 22, paragraphs 2 and 3).

In addition to those specific provisions, the Model Law in a general way provides that the court may refuse to take an action governed by the Model Law if the action would be manifestly contrary to the public policy of the enacting State (Article 6).

Answer 6(e)

Recovery Officer on receipt of certificate from DRT recover the amount in following modes -

— Attachment and sale of immovable (or) movable property of defendant.

— Appointing a receiver for the management of immovable (or) movable properties of defendant

Answer 6A(i)

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

Once foreign proceeding is recognized which is a foreign main proceeding, 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 6A(ii)

In the cases of *Pravin Gada* v. *Central Bank of India* [2013] 176 Comp Cas 101(SC), *Allahabad Bank* v. *Canara Bank* [2000] 101 Comp Cas 64(SC) and *Rajsthan Financial Corporation* v. *Official Liquidator* [2005] Com Cas 387(SC), Supreme Court held that anyone who is aggrieved by any act done by the Recovery Officer can prefer an appeal. The Debts Recovery Tribunal has the powers under the 1993 Act to make an enquiry as it deems fit and confirm, modify or set aside the order made by the Recovery Officer in exercise of powers under sections 25 to 28 of the 1993 Act. Thus, the auction, sale and challenge are completely codified under the 1993 Act, regard being had to the special nature of the legislation.

The official liquidator has a role under the 1956 Act. He protects the interests of the workmen and the creditors and, hence his association at the time of auction and sale is appropriate. He has been conferred locus to put forth his stand in these matters. Since it is the Debts Recovery Tribunal which would have the exclusive jurisdiction when a matter is agitated before the Debts Recovery Tribunal, the official liquidator does not have a choice either to approach the Debts Recovery Tribunal or the company court. The language of the 1993 Act, being clear, provides that any person aggrieved can prefer an appeal. The official liquidator whose association is mandatorily required is indubitably a person aggrieved relating to the action taken by the Recovery Officer which would include the manner in which the auction is conducted or the sale is confirmed. Under these circumstances, the official liquidator cannot have recourse to the doctrine of election. He has only one remedy, i.e., to challenge the order passed by the Recovery Officer before the Debts Recovery Tribunal and further appeal under the 1993 Act and not approach the company court to set aside the auction or confirmation of sale when a sale has been confirmed by the Recovery Officer under the 1993 Act.

Answer 6A(iii)

The provisions of the Act shall not apply to—

(a) a lien on any goods, money or security given by or under the Indian Contract Act, 1872 or the Sale of Goods Act, 1930 or any other law for the time being in force;

(b) a pledge of movables within the meaning of Section 172 of the Indian Contract Act, 1872;

(c) creation of any security in any aircraft as defined in clause (1) of Section 2 of the Aircraft Act, 1934;

(d) creation of security interest in any vessel as defined in clause (55) of Section 3 of the Merchant Shipping Act, 1958;

(e) any conditional sale, hire-purchase or lease or any other contract in which no security interest has been created;

(f) any rights of unpaid seller under Section 47 of the Sale of Goods Act, 1930;

(g) any properties not liable to attachment (excluding the properties specifically charged with the debt recoverable under this Act)] or sale under the first proviso to Sub-section (1) of Section 60 of the Code of Civil Procedure, 1908;

(h) any security interest for securing repayment of any financial asset not exceeding one lakh rupees;

(i) any security interest created in agricultural land;

(j) any case in which the amount due is less than twenty per cent of the principal amount and interest thereon.

Answer 6A(iv)

Salient Features of Chapter 11

— Chapter 11 is not a declaration of insolvency.

— Companies don't file Chapter 11 to liquidate; they do so in order to continue

operating and to take the necessary steps to emerge as a financially stronger business, reorganizing their operations or balance sheet or in some cases by selling substantially all its assets.

— Management remains in control of the business during the chapter 11 rehabilitative process.

— Trustees, administrators and monitors typically are not appointed.

— Chapter 11 normally does not cause interruption to business operations.

— The company is given breathing room during the process - an “automatic stay” generally prevents parties from taking legal action against the company or taking the company’s assets.

— Most publicly-held companies prefer to file under Chapter 11 rather than Chapter 7 because they can still run their business and control the bankruptcy process. Chapter 11 provides a process for rehabilitating the business of the company.

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