

PAPER – 4 : CORPORATE AND ALLIED LAWS

Question Nos. 1, is compulsory. Out of remaining questions in Section A,
Answer any six questions.

Question 1

Answer any two of the following:

- (a) P, son of A, who is the Managing Director of ABC Limited, proposes to give his flat on lease to the company. The paid-up share capital of ABC Limited is Rs.10 crores. Advise the company explaining the restrictions, if any, under the Companies Act, 1956. (5 Marks)
- (b) A Government company holds 49% of the subscribed share capital in Smart & Co. Ltd. Mr. R has been appointed as the auditor at the Annual General Meeting of Smart & Co. Ltd through an ordinary resolution. Certain members of the company object to this appointment on the ground that the appointment of auditors is violative of the provisions of the Companies Act, 1956. Examine the legal position with reference to the relevant provisions of the Companies Act, 1956. (5 Marks)
- (c) Audit Accounts of a public company are not available. Examine the possibility of filing unaudited accounts with the Registrar of companies with reference to the relevant provisions of the Companies Act, 1956. (5 Marks)

Answer

- (a) Lease of flat: Section 297 of the Companies Act, 1956 requires certain contracts on which the directors of a company are interested to be sanctioned by the Board of Directors of the Company and in certain cases (i.e. where the paid up share capital of the company is Rs.1 crore or more) it is also required to be approved with the previous approval of Central Government. Section 297 applies only to contracts of sale, purchase or supply of goods, materials and services or for underwriting the subscription of any shares in, or debentures of the company. Providing premises on a rental or lease basis by a director or his relative to company is not covered by Section 297. Since this Section does not apply to transactions in immovable properties, hence the proposed lease does not require either board resolution or approval of the Central Government.

However, it is an arrangement in which the Managing Director is interested and as such he is required to make a disclosure under Section 299 of the said act and he should not participate or vote in the Board's proceedings (Section 300) and the lease arrangement must be entered in the Register of Contract maintained under Section 301 of the said act.
- (b) Appointment of Auditors: According to Section 224A(1) of the Companies Act, 1956, the appointment or reappointment at each Annual General Meeting of an auditor or auditors shall be made by a special resolution in case of a Company in which not less than 25% of the subscribed share capital is held, whether singly or in any combination, by-

- (a) a public financial institution or a Government Company of Central Government or any State Government, or
- (b) any financial or other institution established by any Provincial or State Act in which a State Government holds not less than fifty one percent of the subscribed share capital, or
- (c) a nationalized bank or an insurance company carrying on general insurance business,

CONSEQUENCES: If any company fails to pass at its Annual General Meeting any special resolution for appointment of an auditor or auditors, it shall be deemed that no auditor or auditors had been appointed by the company at the Annual General Meeting and thereupon the provisions of sub-section (3) of Section 224 of the said Act shall become applicable in relation to such company, i.e. the Central Government is to be informed and it will exercise its power of appointing the auditor/s.

Hence in the given problem, it shall be deemed that Mr. R had not been appointed as Auditor of Smart & Co. Ltd. because the company had not passed special resolution in the Annual General Meeting for appointment of Mr. R as auditor of the company.

- (c) Filing of unaudited Balance Sheet with Registrar Of Companies: Section 220(1) of the Companies Act, 1956 requires that the Balance Sheet and Profit and Loss Account shall be filed with Registrar of Companies together with all documents which are required by the Companies Act to be attached/annexed thereto. Section 216 stipulates that the Auditor's Report (including the auditor's separate or supplementary report, if any) shall be attached to the Balance Sheet. According to Section 218, if any copy of Balance Sheet is issued, circulated or published without there being annexed or attached thereto as the case may be a copy each of (i) the Profit and Loss Account, (ii) any accounts, reports, or statements which, by virtue of Section 212, are required to be attached to the Balance Sheet: (iii) the Auditor's report and (iv) the Board's report. The company and every officer of the company, who is in default, shall be punishable with fine which may extend to Rs.5000. In view of the requirements of Section 216,218 and 220, unaudited Balance Sheet and Profit and Loss Account cannot be filed with Registrar of Companies.

Question 2

- (a) Examine the validity of the resolution passed at the Annual General Meeting of a public company for payment of dividend at a rate higher than that recommended by the board of directors. Is it possible for the board of directors of the company to revoke the dividend declared at the Annual General Meeting? (5 Marks)
- (b) The board of directors of XYZ Limited having paid-up share capital of Rs. 6 crores and free reserves of Rs.3 crores proposes to increase the sitting fee which is at present Rs.5,000. They seek your advice about the maximum amount upto which the sitting fee may be increased without seeking the approval of the Central Government. Advise explaining the relevant provisions of the Companies Act, 1956. (5 Marks)

Answer

- (a) Dividend: According to Regulation 85 of Table A of the Companies Act, 1956, a company in general meeting may declare dividends, but no dividend shall exceed the amount recommended by the Board of Directors of the company. The shareholders at an Annual General Meeting may reduce the amount of dividend recommended by the Board of Directors of the company, but they cannot increase it. Hence the resolution passed at the Annual General Meeting for payment of dividend at a rate higher than that recommended by the Board of Directors is not valid.

Revocation of declared dividend

Ordinarily, a dividend once declared at Annual General Meeting, cannot be revoked, except, with the consent of the shareholders, for a declaration of dividend creates a debt to the shareholders in whose favour it is declared. If a dividend is declared and the amount is paid or credited to the shareholders as dividend, the character of the credit or payment as dividend cannot be altered by a subsequent resolution (Kishanchand Chellaram VCIT (1962) 32 Company cases 1046,105C (SC).

But where a dividend has been illegally declared, or where, due to events intervening — after the declaration, such as fire destroying the company's property, or the out break of a war, or the imposition of new heavy tax burden or other causes diminishing the assets of the company makes it advisable to conserve the remaining assets, the Board of Directors will be justified in revoking the declaration of dividend.

- (b) Sitting fees: The Company proposes to increase the Sitting fees payable to directors for attending Board meetings without seeking the approval of the Central Government for such increase. According to the first provision to Section 310 of the Companies Act, 1956, any increase in sitting fees up to prescribed limit will not require approval of the Central Government. As per rule 10b of Companies (Central Governments) General Rules & Forms, 1956 maximum sitting fees payable per meeting of Board of Directors or its committee is as follows-
- (a) Rs.20,000 per meeting if paid up capital plus free reserves are Rs.10 crore or more or turnover is Rs.50 crore or more (since word used is "or", it is so sufficient if one of the conditions is satisfied).
- (b) Rs. 10,000 per meeting in other cases (i.e. company whose paid up capital plus free reserves is less than Rs.10 crore and turnover is less than Rs.50 crore).

The paid up capital plus free reserves of XYZ Ltd is less than Rs. 10 crore and information regarding turnover is not available. If the turnover of the company is also less than Rs.50 crore, the Sitting fees can be increased only up to Rs.10,000 per meeting ,without seeking approval of the Central Government. If the turnover is Rs.50 crore or above Sitting fees can be increased up to Rs.20,000 without approval of the Central Government.

Question 3

- (a) The board meeting of MNO Ltd. was held on 10th May, 2008 at Chennai at 11a.m. At the time of starting the board meeting the number of directors present were 7. The total number of directors were 10. The board transacted ten items in the board meeting. At 12 noon after the completion of four items in the agenda 4 directors left the meeting. Examine the validity of these transactions explaining the relevant provisions of the Companies Act, 1956. (5 Marks)
- (b) An inspector was appointed under Section 235 of the Companies Act, 1956 to investigate the affairs of a public company. Mr. WM, the works manager of the company, who is aware of certain misdeeds of the management, desires to know whether he is entitled to any protection against dismissal by the company, if he discloses the misdeeds during the course of examination by the inspector. Advise him explaining the relevant provisions of the Companies Act, 1956. (5 Marks)

Answer

- (a) QUORUM: Section 287 of the Companies Act, 1956 provides for the quorum for meeting. The quorum for a meeting of the Board of Directors of a company shall be one third of its total strength (any fraction contained in the said one third being rounded off as one), or two directors, whichever is higher. Where at any time the number of interested directors exceeds or it's equal to two thirds of the total strength, the number of remaining directors, that is to say, the number of directors who are not interested present at the meeting being not less than two shall be the quorum during such time. In this case, the quorum is 4 (i.e. $\frac{1}{3}$ rd of 10 = 3 $\frac{1}{3}$ rounded off as 4). Hence the quorum was present at the time of commencement of meeting.

As a rule, in the case of a meeting of the Board of Directors, the meeting cannot transact any business, unless a quorum is present at the time of transacting the business. It is not enough that a quorum was present at the commencement of the business.

The quorum of the Board is required at every stage of the meeting and unless a quorum is present at every stage, the business transacted is void. (Balakrishna V. Balu Subudhi AIR 1949 pat 184).

In the given situation four items were transacted with the quorum and thus they are valid. Six items were transacted after 4 Directors left the meeting resulting in the reduction of quorum as only 3 Directors were present as against the required quorum of 4 Directors. Such six transactions are void.

- (b) Protection of employees during investigation: Section 635B of the Companies Act, 1956 protects against dismissal, discharge, removal etc. of the employees of the company under investigation who makes disclosure during the course of investigation. The Section provides that if during the course of investigation under Section 235, 237 etc, the Company proposes to discharge any employee from service or punish him by way of dismissal removal or reduction in rank, then the Company must send to Company Law Board/Tribunal a previous intimation in writing of the action proposed to be taken against the employee. If the Company Law Board has any objection to the proposed

action, it must send a notice thereof to the employer. The Company Law Board is not bound to hear the company or any other person before issuing the notice (Ashoka Marketing Ltd Vs CLB (1968) 38 Com Cases 5/9 Calcutta) If the company does not receive any notice of objection from the Company Law Board within 30 days of sending of the intimation when the company may proceed to take the proposed action against the employee.

If the company is dissatisfied with the objection raised by Company Law Board, it may, within 30 days of the receipt of notice of the objections prefer an appeal to the Court/Appellate Tribunal in the prescribed manner. The decision of the Court on such appeal shall be final and binding on the Company Law Board and on the company. The works manager in this case is entitled to this protection under Section 635B.

Question 4

- (a) A scheme of amalgamation was approved by overwhelming majority of members of both the merging companies. The exchange ratio was fixed by a firm of reputed Chartered Accountants. When the scheme of amalgamation was awaiting sanction of the court, a small group of members of one of the merging companies raised objection on the ground that the exchange ratio was unfair. Examine with reference to decided case law whether the objection is likely to be sustained. What would be your answer in case similar objection was raised by the Central Government? (5 Marks)
- (b) The issued, subscribed and paid up capital of OPM Limited is Rs.5 crores consisting of 50,00,000 equity shares of Rs.10 each. The company has 700 members. A petition was made to the appropriate authority duly signed by 80 members holding 2,50,000 equity shares of the company seeking relief against oppression and mismanagement. Subsequently 20 of them withdrew their consent. Examine with reference to the relevant provisions of the Companies Act, 1956 and decided case law whether the petition is maintainable. (5 Marks)

Answer

- (a) Exchange Ratio: Courts leave the aspect of share valuation to expert valuers and shareholders. Unless the person who challenges the valuation satisfies the court that the valuation is grossly unfair, the court will not disturb the scheme (Piramal Spg Vs Weaving Mills Ltd). In this case the valuation is confirmed to be fair by eminent firm of auditors and is also confirmed by majority of members. The objection of the some by small group of shareholders cannot be sustained as held in Hindustan Lever Employees. Union Vs Hindustan Lever Ltd.

Section 394A of the Companies Act, 1956 requires the Court (Tribunal) to give notice of every application made to it under Section 391 or 394 to the Central Government. The Court (tribunal) should take into consideration the representations if any made to it by that Government before passing any order. The role played by the Central Government is that of an impartial observer who acts in public interest and advises the Court (tribunal) whether it is or it is not feasible for the two companies to amalgamate (Ucal Fuel Systems Ltd Sure). But the court is not bound to accept the views of the Central

Government. Thus objection of the Central Government as regards valuation of shares was rejected by the Court (Tribunal), in the face of views expressed by two independent chartered accountants (M.G Investments & Industrial Co. Ltd Vs New Shorrock spinning & Mgf Co. Ltd). Hence even in the case of representation by Central Government, unless that Government establishes that the exchange ratio was unfair and not in public interest, the court will refuse to interfere.

- (b) Members eligible to make petition seeking relief under Section 397 and 398: The requisite number of members who must sign the application under Sections 397 and 398 is given in Section 399 of the Companies Act, 1956. In the case of a company having a share capital, the application must be signed by, (i) atleast 100 members or, (ii) by at least $1/10^{\text{th}}$ of total number of members, whichever is less. In the alternative valid application may be made by any members holding not less than $1/10^{\text{th}}$ of the issued share capital of the company.

In this case, the application was made by 80 members and it is more than $1/10^{\text{th}}$ of total number of members. Hence the application is valid at the time of presentation. The number of members required for the purpose of making a petition is 70. Subsequently 20 members withdrew their consent and the number of members continuing to give their consent is reduced to 60.

It was held in *Rajahmundry Electric Supply Corporation Ltd. Vs A. Nageswara Rao* that the validity of a petition must be judged on the facts as they were at the time of its presentation and where a petition was valid when it was presented, it could not cease to be voidable by reason of events subsequent to its presentation. In view of this Supreme Court decision, it can be said that withdrawal of consent by 20 members subsequent to the presentation of application would not affect the validity of the petition.

Question 5

- (a) Under what circumstances shall it be deemed that the substratum of a company has gone? A company has ceased to carry on two of the ten business stated as the main objects of the company. Examine whether the company can be wound up on the ground that substratum of the company is gone. (5 Marks)
- (b) What is meant by a "Sick industrial company" under the Companies Act, 1956? Whether the provisions of the Companies Act, 1956 relating to "Sick industrial company" are applicable to Government companies. (5 Marks)

Answer

- (a) **LOSS OF SUBSTRARUM OF A COMPANY AND THE WINDING UP:** A company's substratum is the purpose or the main object, for which the company was formed. If the company has abandoned all of its main objects and not merely some of them, or if it cannot achieve any of its main objects, its substratum has gone and will be wound up by the Tribunal.

In *Re German Date Coffee Co.*, Where a company was formed for the purpose of coffee from dates under a patent which was to be granted by the Government of Germany. The

German patent was never granted. On a petition of a shareholder it was held that the substratum of the company had failed and it was impossible to carry on the object for which it was formed. Therefore, it was just and equitable that the company be wound up.

In other words the substratum of a company is deemed to have disappeared or gone, if the main objects for which the company was formed has become impracticable, i.e. permanently impracticable. Usual tests for determining whether the substratum of the company has disappeared are whether:

- the subject matter of the company is gone, or
- the object for which it was formed has substantially failed, or
- it is impossible to carry on the business of the company except at a loss, which means there is no reasonable hope that the object of trading at a profit can be attained, or
- the existing and probable assets are insufficient to meet the existing liabilities. (In re Kaithal & General Mills Co. Ltd., 1951, 31, Comp. Cas.461.)

Therefore, applying the above to the given situation in the question it can be said that in this case the substratum of the company cannot be said to have gone, since there are other businesses authorized by the Memorandum which can be carried out successfully. A company, therefore, cannot be wound up on the ground that it has ceased to carry on two of the 10 business authorized by the Memorandum of Association. [Re Amalgamated Syndicate (1897)].

- (b) SICK INDUSTRIAL COMPANY: "Sick Industrial Company means an Industrial Company which has (i) the accumulated losses in any financial year equal to fifty percent or more of its average net worth during four years immediately preceding such financial year or (ii) failed to repay its debts within any three consecutive quarters on demand made in writing for its repayment by a creditor or creditors of such company (Section 2(46AA) of the Companies Act, 1956). The term used is creditor and hence if any creditor (secured or unsecured) is not paid for 9 months despite demand made by him, the company will be a sick industrial company.

Section 424A (1) of the said Act which provides for making a reference to Tribunal shall not apply to a Government Company. However a Government Company may, with the prior approval of the Central/State Government, make a reference to Tribunal and thereafter all the provisions of the Act shall apply to such Government Company.

Question 6

- (a) A producer company wants to amend its Memorandum and Articles of Association. The director of the company approaches you for advice in this regard. Advise the director about the procedure to be followed for amending the Memorandum and Articles of Association of the company. (5 Marks)
- (b) Indian citizens incorporated a company in U.K. for the purpose of carrying on business there. Examine with reference to the relevant provisions of the Companies Act, 1956

whether it is a "Foreign Company". What would be your answer in case the U.K. company was incorporated by a company registered in India? (5 Marks)

Answer

- (a) Amendment of Memorandum of a producer company (Section 581H): A producer company shall not alter the conditions contained in its memorandum except in the cases by the mode and to the extent for which express provision is made in the Act. However, a producer company, may, by special resolution, not inconsistent with Section 581B alter its objects specified in its memorandum. A copy of the amended memorandum, together with a copy of the special resolution duly certified by two directors shall be filed with the Registrar within thirty days from the date of adoption of resolution. Where as in case of transfer of the registered office of a producer company from the jurisdiction of one Registrar to another, certified copies of the special resolution certified by two directors shall be filed with both the Registrars within thirty days, and each Registrar shall record the same, and thereupon the Registrar from whose jurisdiction the office is transferred, shall forthwith forward to the other Registrar from whose jurisdiction the office is transferred, shall forthwith forward to the other Registrar all documents relating to the producer company. The alteration of the provisions of memorandum relating to the change of the place of the registered office from one state to another shall not take effect unless it is confirmed by the Company Law Board on petition.

Amendment of Articles (Section 581-I): Any amendment to the articles should be proposed by not less than two third of the elected directors or by not less than one third of the members of the producer company and adopted by the members by a special resolution.

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

- (b) Foreign Company: Foreign company as per Section 591 of the Companies Act, 1956 means a Company incorporated outside India but having a place of business in India. Accordingly, to qualify as foreign company a company must have both the following features:

- it should be a company incorporated outside India
- it should have a place of business in India

In view of the provisions of Section 591 explained above, the company incorporated in U.K. for the purpose of carrying on business in U.K. is not a foreign company. Its incorporation by Indian citizens is immaterial. In order to be a "Foreign Company" the U.K. company must have a place of business in India. The answer would be the same, even if the U.K. company was incorporated by a company registered in India.

Question 7

- (a) Mr. X a Director of XYZ Limited received a show-cause notice from the Registrar of Companies for an offence under Section 297 (1) of the Companies Act, 1956 in respect

of certain contracts entered into with the company without the approval of the Central Government. The offence is punishable with fine only under Section 629A of the Act. He seeks your advice whether he can take steps for getting the offence compounded either before or after the prosecution is launched. Advise him explaining the effect of compounding of offence either before or after institution of prosecution. (5 Marks)

- (b) Mr. X applied to the Central Government for allotment of Director Identification Number. What are the obligations of Mr. X and the companies in which he is appointed as a director, after "DIN" is allotted to him, under the Companies Act, 1956 and the rules made thereunder? (5 Marks)

Answer

- (a) Compounding of offence: The offence under Section 297(1) of the Companies Act, 1956 is punishable with fine only and as such it is compoundable under Section 621A of the said Act. An offence may be compounded either before or after the institution of prosecution in the court. The compounding of offence will act as a bar to the prosecution where the compounding was done before the institution of the prosecution. However, if an offence is compounded after the institution of any prosecution in respect of that offence, the Registrar of companies must give intimation thereof in writing to the court in which the prosecution has been instituted and upon such intimation being given the company or the officer against whom the prosecution has been launched and which offence has been compounded shall be discharged on the prosecution and the prosecution dropped. The court has no power to refuse to grant the discharge. The effect of the compounding of an offence is thus condonation from prosecution for an offence.

Hence, Mr. X in this case can take steps for getting the offence compounded either before or after the prosecution is launched, provided a similar offence was not compounded earlier within a period of 3 years.

- (b) Director Identification Number: The obligations of the person who has been allotted DIN and the company provided in Section 266D, 266E and 266F of the Companies Act, 1956 is explained below:

Every existing director shall within one month of the receipt of DIN from the Central Government intimate his DIN to the company or all companies wherein he is a director. Intimation to companies from Director shall be in Form DIN-2 [Section 266D read with the Companies (Director Identification) Rules]. Intimation to companies by directors in form DIN-2 may be given in physical /paper form.

Companies, in turn are required to file Form DIN-3 for sending intimation of DIN to the Registrar of Companies (online through MCA 21 portal) within one week of receipt of intimation from directors. Form No. DIN-3 is required to be verified by Managing Director or Director or Manager of the company and certified by the company secretary in full time employment of the company or company secretary in whole time practice [Section 266 E read with companies (Director Identification) Rules].

It is obligatory on the part of the company to quote DIN in any return or information furnished under the Act, if such return contains any information relating to a director (Section 266F).

Changes in the personal particulars of a director must be intimated by the concerned director to the Central Government within 30 days of the change in Form DIN-4.

Question 8

- (a) Mr. Suresh, an additional director appointed by the board of directors of a public company, is proposed to be appointed as a regular director in the Annual General Meeting. Explain the requirements under the Companies Act, 1956 to give effect to the proposed appointment. (5 Marks)
- (b) Shri J is already the managing director of two companies viz., M/s ABC Ltd. and M/s CBA Ltd. M/s DEF Ltd. wants to appoint Shri J as the managing director of their company for a period of five years from 1.12.2008. You are required to prepare a draft board resolution for the appointment of Shri J as managing director of M/s DEF Ltd., taking into consideration the requirements under the Companies Act, 1956. (5 Marks)

Answer

- (a) When the additional director, Mr. Suresh is to be appointed as a regular director in general meeting a notice in writing of his candidature as director has to be received from him or from any member under Section 257 of the Companies Act, 1956, at least 14 days before the meeting. The candidate or the member proposing a person as director, is also required to pay Rs. 500 as refundable deposit. This is because the additional director who is retiring is not a director retiring by rotation and hence exemption from Section 257 (1) is not available to him.

The members must be duly informed of the candidature (individually) at least 7 days before the meeting or the candidature is duly advertised. Normally the notice is received well in advance and in such a case the contents of the notice are included in notice of the meeting under "special business" with an explanatory statement.

These are the main requirements relating to the proposed appointment of Mr. Suresh as a regular director in the general meeting.

- (b) Board Resolution for appointment of Managing Director who is already Managing Director in another two companies:

"RESOLVED that subject to the approval of the Central Government under sub Section (4) of Section 316 of the Companies Act, 1956, Mr. J, who is already the Managing Director of two companies, namely M/s ABC Ltd, and M/s CBA Limited, be and is hereby appointed as Managing Director of the company for a period of five years commencing from 1st December 2008, with the consent of all the Directors present at the meeting of which meeting and the resolution to be moved there at specific notice was given to all the Directors then in India, on the terms and conditions in the draft agreement tabled before the meeting and initialed by the Chairman for purposes of identification and that Shri

MG, the Secretary of the Company be and is hereby authorized to apply to the Central Government for seeking approval.

RESOLVED further that Smt. VR, Director and Shri MG the Secretary of the company be and are hereby authorized to execute the said agreement subject to such modifications/alternations made by the Central Government while giving their approval and to affix the common seal of the company therein”.

Note :- In the above question, Mr. J cannot be appointed as Managing Director of M/s DEF Ltd. because he is already holding the position of Managing Director in two public companies. The appointment can be made only when the Central Government may, by order, permit any person to be appointed as a managing director of more than two companies if the Central Government is satisfied that it is necessary that the companies should, for their proper working, function as a single unit and have a common managing director. But in the question it is not mentioned that all the companies are working as a single unit. If we take the assumption that these are working as a single unit then the appointment can be made.

SECTION-B

Question No. 9 is compulsory. Out of remaining questions in Section B, answer any four questions.

Question 9

Answer any one of the following:

- (a) A company proposes to make a public issue of equity shares for financing its project through book building process. It proposes to fix the floor price of the share at Rs.500 for a share of Rs. 10. Answer the following with reference to SEBI (Disclosure and Investor Protection) guidelines:

What is the price band that may be indicated in the red herring prospectus?

If the company wants to lower the floor price during the bidding period in order to increase the response to the issue, state the conditions subject to which such revision can be made. (6 Marks)

- (b) Explain clearly the meaning of the term “Green shoe option” in relation to a public company going for public offer of equity shares. What disclosures is such a company required to make in the draft red herring prospectus in accordance with SEBI (Disclosure and Investor Protection) guidelines? (6 Marks)

Answer

- (a) SEBI (Disclosure and Investor Protection) Guidelines, 2000 relating to price band: The price band is the range within which the price can move. The cap of the price band shall not be more than 20% of the floor price. If the floor price is Rs.500 the cap of the

price shall be Rs.600 and the company may indicate a price band of Rs.500 to 600 in the red herring prospectus (para 11.3.1 (viii) (b) of SEBI (DIP) Guidelines).

The price band can be revised during the bidding period in which case the maximum revision on either side shall not exceed 20% i.e. floor of the price band can move up or down to the extent of 20% of the floor price. Hence the revised price band may be Rs. 400 (Rs. 500 less 20%) to 480 (120% of Rs.400).

Any revision in the price band shall be widely disseminated by informing the stock exchange, by issuing press releases and also indicating the change on the relevant website and terminals of syndicate members.

The bidding period shall be extended for a further period of 3 days subject to the total bidding period not exceeding 13 days.

The manner in which the shortfall, if any in the project financing arising on account of lowering of price band will be met shall be disclosed in the red-herring prospectus. It shall also be disclosed that the allotment shall not be made unless the financing is tied up. These are the conditions subject to which the price band may be lowered.

- (b) GREEN SHOE OPTION: Green shoe option in relation to a public company going for public issue of equity shares means an option of allocating shares in excess of the shares included in the public issue and operating a post-listing price stabilizing mechanism in accordance with the provisions of Chapter VIII-A of SEBI (Guidelines), which is granted to a company to be exercised through a stabilizing Agent.

DISCLOSURES TO BE MADE IN THE RED HERRING PROSPECTUS:

An issuer company going for a public offer of equity shares is required to make the following disclosures in the Red Herring Prospectus:

- (1) Details of agreement between the company and the stabilizing agent stating all the terms and conditions relating to the Green Shoe Option.
- (2) Details of agreement with the promoter(s) or pre-issue shareholders who will lend their shares, which shall not be in excess of 15% of the total issue size.
- (3) Maximum number of shares proposed to be over- allotted by the company.
- (4) The period for which the company proposed to avail of the stabilization mechanism.
- (5) The maximum increase in the capital of the company and the shareholding pattern post issue in case the company is required to allot further shares to the extent of over-allotment in the issue.
- (6) The maximum amount of funds to be received by the company in case of further allotment and the use of these additional funds in final document to be filed with the ROC.
- (7) Details of the agreement/ arrangement entered in to by Stabilizing Agent with the promoters to borrow shares from the latter which inter-alia shall include name of the promoters, their existing shareholding, number & percentage of shares to be lent by

them and other important terms and conditions including the rights and obligations of each party.

- (8) The final prospectus shall additionally disclose the exact number of shares to be allotted pursuant to the public issue, stating separately therein the number of shares to be borrowed from the promoters and over allotted by the SA and the percentage of such shares in relation to the total issue size.

Question 10

Mr. Basu desires to draw foreign exchange for the following purposes:

- (i) Payment related to "Call back services" of telephones
- (ii) USD 1,20,000 for studies abroad on the basis of estimates given by the foreign university.
- (iii) USD 25,000 for sending a cultural troupe on a tour of Europe.

Advise him, whether he can get foreign exchange and, if so, under what conditions (6 Marks)

Answer

Current Account Transactions: The Central Government in consultation with RBI framed regulation known as Foreign Exchange Management (Current Account Transaction) Regulation, 2000. Under these Regulations certain transactions are prohibited, certain transactions require Central Government approval and certain transactions require RBI approval.

- (i) Payment related to 'call back services' of telephone is totally prohibited under Schedule I of Foreign Exchange Management (Current Account Transaction) regulations.
- (ii) Remittance of Foreign Exchange for studies abroad:
This is a Schedule III transaction. Foreign Exchange may be released for studies abroad up to a limit of USD 1,00,000 or the estimates from the institution abroad, whichever is higher. Above this limit RBI's approval is required. In this case USD 1,20,000 is required on the basis of estimates of the institution abroad. Hence no permission from RBI is required.
- (iii) Cultural troupe: This is a Schedule II transaction. Irrespective of the amount involved prior approval of Central Government, Ministry of HRD (Dept. of Education and Culture) is required. However no permission is required in case of remittance out Of Resident Foreign Currency (RFC) Account or EEFC Account (Exchange Earner's Foreign Currency).

Question 11

The Competition Act, 2002 deals with the agreement. Differentiate between Horizontal Agreement and Vertical Agreement. (6 Marks)

Answer

Section 2(b) of Competition Act, 2002 defines the term “agreement” which includes any arrangement or understanding or action in concert:

- (i) Whether or not, such arrangement, understanding or action is formal or in writing; or
- (ii) Whether or not such agreement, understanding or action is intended to be enforceable by legal proceedings;

Agreements may be horizontal agreements and vertical agreements.

Horizontal agreements referred to agreements among competitors and vertical agreements to an actual or potential relationship buying or selling to each other.

Horizontal agreements relating to prices quantities, bids and market sharing are particularly anti- competitive. Vertical agreements like tie in arrangements; exclusive supply/distribution agreements and refusal to deal are also generally anti-competitive.

Horizontal agreements are those agreements among competitors operating at the same level in the economic process i.e., enterprises engaged in the same activity. For example the agreements between the producers or between whole sellers or between retailers, dealing in similar kind of products.

Vertical agreements are those agreements between non competing undertakings operating at different levels of manufacturing and distribution process. For example, the agreements between manufacturers of components, manufacturers of products, between producers and whole-sellers or between producers, whole-sellers and retailers.

Horizontal agreements or agreement between two or more enterprises that are at the same stage of the production chain and in the same market. Horizontal agreements and membership of cartels lead to unreasonable restrictions of competition and may be presumed to have an appreciable adverse effect on competition.

Vertical agreements are agreements between enterprises that are at different stages or levels of the production chain and therefore in different markets. An example of this would be an agreement between a producer and a distributor. This includes tie in arrangements, exclusive supply arrangements, exclusive distribution arrangements, refusal to deal and resale price maintenance.

Question 12

In what way does the Reserve Bank of India regulate the determination of loans and advances which can be made by a Banking Company under the Banking Regulation Act, 1949? Explain.

Answer

POWERS OF RBI TO REGULATE DETERMINATION OF LOANS AND ADVANCES BY BANKING COMPANIES:

By virtue of provisions of Banking Regulations Act, 1949, as contained in Section 21 the RBI is empowered to issue directives to a banking company to determine the policy in relation to loans and advances. Such directions may relate to:

- (1) Purpose for which loan may or may not be made.
- (2) Margin stipulation.
- (3) Maximum amount of advances to any company, firm individual or association of persons (at present 15% for individual borrower without infrastructure project, if infrastructure project go by additional 10%, 40% for group borrower and for infrastructure project of group borrower it may be up to 50% of bank's capital and reserve (presently tier-I and tier-II capital from capital adequacy point of view).
- (4) Maximum amount of guarantee liability on behalf of any individual firm /company.
- (5) The rate of interest and other terms and conditions on which such advances are made or guarantee given.

It may further be mentioned that in accordance with the provisions of Section 21A, rate of interest charged by banking company on the basis of loan contract between the bank and debtor is not to be subject to scrutiny by the court.

Question 13

Enumerate the obligations of banking companies under the Prevention of Money Laundering Act, 2002. (6 Marks)

Answer

Section 12 of Prevention of Money Laundering Act, 2002 provides for the obligation of Banking Companies, Financial Institutions and Intermediaries of securities market. Every banking company, financial institution and intermediary shall:

- (a) Maintain a record of all transactions, the nature and value of which may be prescribed, whether such transactions comprise of a single transaction or a series of transactions integrally connected to each other, and where such series of transactions take place within a month. Such records shall be maintained for a period of ten years from the date of cessation of the transactions between the clients and the banking company or financial institution or intermediary, as the case may be:
- (b) Furnish information of the above transactions to the Director appointed for the purpose of this Act within the prescribed time;
- (c) Verify and maintain the records of the identity of all its clients, in the prescribed manner.

If the principal officer of a banking company or financial institution or intermediary has reason to believe that a single transaction or series of transactions integrally connected to each other have been valued below the prescribed value so as to defeat the provisions of this section, such officer shall furnish information in respect of such transactions to the Director within the prescribed time.

Question 14

Explain the 'Rule of reasonable construction' as may be applied in determining whether a particular act of a director of a company is 'ultra vires' or 'intra vires' of the objects of the company. (6 Marks)

Answer

As per the Rule of Reasonable Construction, the words of a statute must be construed 'ut us maquis valeat quampareat' meaning thereby that words of statute must be construed so as to lead to a sensible meaning. Generally the words or phrases of a statute are to be given their ordinary meaning. For example, in the case of *Dr. A.L. Mudiliar v. LIC of India* (1963) 33 Comp. Cas. 420 (SC), it was held that the Memorandum of Association of a company must be read fairly and its importance derived from a reasonable interpretation of the language which it employs. Further, in order to determine whether a transaction is intra vires the objects of a company, the objects clause should be reasonably construed: neither with rigidity nor with laxity (*Waman Lal Chotanlal Parekh v. Scindia Steam Navigation Co. Ltd.* (1944) 14 Comp. Cas. 69 (Bom)).

Thus, if the Court finds that giving a plain meaning to the words will not be fair or reasonable construction, it becomes the duty of the court to depart from the dictionary meaning and adopt the construction which will advance the remedy suppress the mischief provided the Court does not have to resort to conjecture or surmise. A reasonable construction will be adopted in accordance with the policy and object of the statute.