

PAPER – 4 : CORPORATE LAWS AND SECRETARIAL PRACTICE

Question No. 1 is compulsory.

Answer any **five** questions from the remaining **six** questions.

Question 1

- (a) It is apprehended by the Directors of a Public Company that they are likely to be prosecuted for an offence under the Companies Act, 1956 which is not compoundable. Explain the provisions of the Companies Act, 1956 under which the Directors can seek relief from the liability for offence. What will be the position in case prosecution has already been launched? (5 Marks)
- (b) The Securities and Exchange Board of India issued an order against ABC Limited for redressal of grievance of one of its members. On failure on the part of the company the Board imposed penalty upon the company under Section 15 C of the Securities and Exchange Board of India Act, 1992. The company seeks your advice whether it has any remedy against the order of the said Board. (5 Marks)
- (c) The governing body of Jaipur Stock Exchange desires to establish an additional trading floor at Bikaner. Advise, whether additional trading floor can be established by the said stock exchange under the provisions of the Securities Contracts (Regulation) Act, 1956. (5 Marks)
- (d) Mr. M was a member of the Competition Commission of India. On the basis of information that he had acquired such financial interest as was likely to affect prejudicially his functions as a member of the Commission, the Central Government appointed an officer to hold an inquiry. On the basis of report of the said officer the Central Government issued an order of removal of Mr. M. Decide whether the action of the Central Government is in order under the provisions of the Competition Act, 2002? (5 Marks)

Answer

- (a) **Relief under Section 633:** Section 633 of the Companies Act, 1956 seeks to grant relief to the company directors and offences from liability in respect of offences under the Companies Act.

The relief under Section 633 can be sought on any proceeding for negligence default, breach of duty, misfeasance or breach of trust. The relief may be granted by the Court either wholly or partly. For getting relief under this section it must be proved to the satisfaction of the Court by the person concerned (1) that he acted honestly, (2) that he acted reasonably and (3) that having regard to all the circumstances of the case, he ought fairly to be excused.

In a case where proceeding is only apprehended, the application for relief should be made to the High Court having jurisdiction in the matter [Section 633 (2)]

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In a case where the proceedings of a prosecution against an officer have already commenced, the application for relief should be made to the Court before which the proceedings are pending e.g. the Criminal Court.

Hence, the application seeking relief can be made either after proceedings are started against the person concerned or by way of preventive action.

(b) Remedy against order of SEBI:

ABC Limited was penalized by the SEBI. The following remedies are available to the Company:

- (1) **Appeal to the Securities Appellate Tribunal:** Section 15T of the SEBI Act, 1992 provides that any person aggrieved by an order of the Board may prefer an appeal to the Securities Appellate Tribunal. Such appeal shall be filed within 45 days from the date on which a copy of the order of the Board was received. However, the Tribunal may entertain an appeal after the expiry of the said period if it is satisfied that there was sufficient cause for not filing it within the said period of limitation.
- (2) **Appeal to the Supreme Court:** Section 15Z of the SEBI Act, 1992 provides that any person aggrieved by the decision or order of the SAT may file an appeal to the Supreme Court within 60 days from the date of communication of the decision or order on any question of law arising out of such order. The Supreme Court may entertain such appeal even after the expiry of said period of limitation if there was reasonable cause for such delay.

(c) Additional Trading Floor:

According to Section 13A of the Securities Contracts (Regulation) Act, 1956 a stock exchange may establish additional trading floor with the prior approval of the Securities Exchange Board of India (SEBI) with the terms and conditions stipulated by the said Board.

Additional Trading Floor means a trading facility offered by a recognized stock exchange outside its area of operation to enable the investors to buy and sell securities through such trading floor under the regulatory frame work of that stock exchange.

In view of the above, Jaipur Stock Exchange may establish an additional trading floor at Bikaner with prior approval of the SEBI.

- (d) **Removal of Member of Competition Commission:** Section 11(2)(d) of the Competition Act, 2002 empowers the Central Government to remove, by an order, a member of the Competition Commission of India from his office if such member has acquired such financial interest as is likely to affect prejudicially his functions as a member of the Competition Commission. However, provisions of Section 11(3) of the said Act put some restrictions on such power of the Central Government. According to this Section, the Central Government has to make a reference to the Supreme Court of India.

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The Supreme Court shall hold an enquiry in accordance with the procedure formulated by it and then report that the member in question ought to be removed from his office on such ground.

Thus, the Central Government can remove a member of the Competition Commission of India only after following the procedure established by Section 11 of the Competition Act, 2002.

In view of the above the action of the Central Government is not in order and removal of Mr. M is not valid.

Question 2

- (a) *Modern Technologies Limited, an unlisted company, proposes to finance its expansion programme by issuing equity shares to public. The company has been making good profits every year from the commencement of business on 1st April, 2003, but it has not declared dividend so far. The company was started with initial equity share capital of Rs. 3 crores in January, 2003. The paid-up equity share capital and free reserves as per the latest audited Balance Sheet as at 31st March, 2010 amounted to Rs. 5 crores and Rs. 10 crores respectively.*

State the conditions which are required to be fulfilled by an unlisted company under the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009 in order to be eligible to make an initial public offer and also examine whether Modern Technologies Limited is eligible to make the proposed public issue.

(8 Marks)

- (b) *The Managing Director of BM Technologies Limited, a listed company having a large number of shareholders and employees, has confessed at the board meeting of the company that he has indulged in large scale manipulation of accounts during the last three years on account of which the financial position of the company has been adversely affected. The Central Government proposes to appoint its nominees as Directors of BM Technologies Limited to safeguard the interests of the company. Examine with reference to the provisions of the Companies Act, 1956 whether the Central Government has any 'Suo Motu' power in this regard. Explain the powers which can be exercised by the Central Government with regard to the affairs of the company when its nominees are appointed as directors of the company.*

(8 Marks)

Answer

- (a) **Initial Public offer by Unlisted Company:** An unlisted company can make an Initial Public Offer (IPO) of equity shares, or any other security convertible into equity shares, only if it meets all the conditions listed in Regulation 26 of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009. The conditions are given below:
- (1) The Company has net tangible assets of at least Rs. 3 crores in each of the preceding 3 full years (of 12 months each), of which not more than 50% is held in monetary assets. If more than 50% is so held in monetary assets, the company

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should have made firm commitments to deploy such monetary assets in its business/project.

- (2) The Company has a track record of distributable profits in terms of section 205 of the Companies Act, 1956 for atleast 3 out of immediately preceding 5 years. Extraordinary items shall not be considered for calculating the distributable profits.
- (3) The Company has a net worth of at least Rs. 1 crore in each of the preceding 3 full years (of 12 months each).
- (4) If the Company has changed its name within the last one year, at least 50% of the revenue for the preceding 1 full year is earned by the company from the activity suggested by the new name.
- (5) The aggregate of proposed issue and all previous issues made in the same financial year in terms of issue size does not exceed 5 times its pre-issue net worth as per the audited balance sheet of the preceding financial year. (Regulation 26(1))

An unlisted Company not complying with any of the conditions listed in Regulation 26(1) explained above may make I.P.O. of equity shares by complying with alternative conditions specified in Regulation 26(2).

In this case, Modern Technologies Ltd. was making good profit since 1st April, 2003. It is not necessary that the Company should declare dividend. It is enough if the company has distributable profits for at least 3 out of 5 immediately preceding 5 years.

As the Company had initial capital of Rs. 3 crores and continuously made good profits, condition No. 3 relating to minimum net worth of Rs. 1 crore is also satisfied.

The Company has not changed its name. Hence the conditions No. 4 is not applicable.

As the Company was started with initial capital of Rs. 3 cores and it was making good profits every year, it is presumed that condition No. 1 relating to net tangible asset of Rs. 3 crores in each of 3 preceding financial year is also satisfied.

The net worth as per latest audited balance sheet is Rs. 15 crores. Hence the proposed issue of Rs. 40 crores does not exceed 5 times the pre-issue net worth. Hence condition No. 5 is also satisfied.

Hence all the conditions listed in Regulation 26(1) have been fulfilled. But the company is also required to obtain grading for the initial public offer from at least one credit relating agency registered with SEBI (Regulation 26(7) before making the proposed I.P.O of Rs. 40 crores.

- (b) **Power of Central Government to prevent oppression or mismanagement:** The Central Government is empowered to appoint its nominees as directors of a Company to effectively safeguard the interest of the Company or its shareholders or the public interest. But such power cannot be exercised by the Central Government on its own. The Central Government has to make a reference to the Company Law Board and if the Company Law Board is satisfied that the affairs of the Company have been conducted in a manner oppressive to any member of the Company or in a manner prejudicial to the

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interests of the Company or to public interest, it may pass an order asking the Central Government to appoint to nominees or directors for a period not exceeding three years. There is no limit as to the number of directors that can be appointed. The Company Law Board may also pass similar orders on an application not less than 100 numbers or members holding with less than one tenth of the total voting price. Hence as Central Government has no suo motu power to appoint additional directors in B.M. Technologies Ltd. and it can do so only on an order passed by CLB in this regard.

Notwithstanding anything contained in the Companies Act or in any other law for the time facing in force, where any person is appointed by the Central Government to hold office as director, Section 408 (6) empowers the Central Government to issue such directions to the company as it may consider appropriate in regard to its affairs. Such directions may include directions to remove an auditor already appointed and to appoint another auditor in his place or to alter the articles of the company. When such directions are given the appointment, removal or alteration, as the case may be shall be deemed to have come into effect as if the provisions of the Companies Act in this behalf have been complied without requiring any further act or thing to be done. Though these powers are substantial, yet the same do not empower the Central Government to interfere in the day to day management of the company.

Further, Section 408(7) empowers the Central Government to require the persons appointed as directors to report to the Central Government from time to time with regard to affairs of the company.

Question 3

- (a) *Examine with reference to the provisions of the Foreign Exchange Management Act, 1999 whether there are any restrictions in respect of the following:-*
- (i) *Drawal of Foreign Exchange for payments due on account of Amortization of loans in the ordinary course of business.*
 - (ii) *A person, who has resident of U.S.A. for several years, is planning to return to India permanently. Can he continue to hold the investment made by him in the securities issued by the companies in U.S.A.?*
 - (iii) *A person resident outside India proposes to invest in the shares of an Indian company engaged in plantation activities. (8 marks)*
- (b) *PQR Limited is being wound up by the Court. All the assets of the company have been charged to the company's bankers to whom the company owes Rs. 1 crore. The company owes the following amounts to others:*
- | | |
|---|----------------------|
| (i) <i>Dues to workers</i> | <i>Rs. 25,00,000</i> |
| (ii) <i>Taxes payable to Government</i> | <i>Rs. 5,00,000</i> |
| (iii) <i>Unsecured creditors</i> | <i>Rs. 10,00,000</i> |

You are required to compute with reference to the provisions of the Companies Act, 1956 the amount each kind of creditors is likely to get if the amount realized by the official

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liquidator from the secured assets and available for distribution among the creditors is only Rs. 80 lakhs. (8 Marks)

Answer

(a) Capital Account Transactions:

All the transactions referred to in the question are capital account transactions.

Section 6(2) of FEMA, 1999 provides that the Reserve Bank may in consultation with the Central Government specify the permissible capital account transactions and the limit upto which foreign exchange will be allowed for such transactions.

Amortization of Loan: According to proviso to section 6(2), the Reserve bank shall not impose any transaction on the drawal of foreign exchange for certain transactions. One such transaction is drawal of foreign exchange for payment due on account of amortization of loans in the ordinary course of business. Hence this transaction is permissible without any restrictions.

Person resident in USA returning permanently to India: When the person returns to India permanently, he becomes a resident in India. Section 6(4) provides that a person resident in India may hold, own transfer or invest in foreign currency, foreign security, etc. if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India. In view of this, the person who returned to India permanently can continue to hold the foreign security acquired by him when he was resident in U.S.A.

Investment in shares of Indian company by non-resident: Reserve Bank issued Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000. Regulation 4(6) of the said Regulations prohibits a person resident outside India from making investment in India, in any form, in any Company or partnership firm or proprietary concern or any entity, whether incorporated or not, which is engaged or proposes to engage in agricultural or plantation activities. Hence it is not possible for a person resident outside India to invest in the shares of a plantation company as such investment is prohibited.

- (b) Overriding preferential payments:** The amount realized from assets is to be distributed to various kinds of creditors in accordance with the provisions of sections 529, 529A and 530 of the Companies Act, 1956. According to the proviso to Section 529(1)(c) the security of every secured creditor shall be deemed to be subject to a pari passu change in favour of the workmen to the extent of the workmen's portion therein. The workmen's portion is to be worked out as per section 529(3)(c).

Workmen's dues

$$\text{Workmen's portion of the security} = \frac{\text{Workmen's dues}}{\text{Workmen's dues} + \text{Amount due to secured creditors}}$$

Section 529A provides for overriding preferential payment. According to the said section the workmen's dues and that part of the secured debt which cannot be realized because

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it has been appropriated towards workmen's dues shall be paid in preference to all other debts. Section 529A overrides the preferential claim under section 530 (taxes payable to Government in this case).

In this case, all the assets of the company in liquidation have been charged to the secured creditor. Unless the property by which the debt is secured realizes an amount equal at least to the total of workmen's dues and the secured debts, other creditors will not get any amount. In this case the amount realized from the security is Rs. 80 lakhs, while the amount due to the workmen and secured creditors (i.e. bankers) aggregate to Rs. 125 lakhs.

Amount available for distribution of workmen's dues	$\frac{25,00,000}{1,00,000 + 25,00,000} \times 80 \text{ lacs}$ $\frac{1}{5} \times 80 \text{ lac}$ Rs. 16 lacs.
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Amount available to secured creditor} Rs. 80 lacs – 16 lacs
Rs. 64 lakhs.

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

Question 4

- (a) Mr. Suresh resided in India during the Financial Year 2008-09. He left India on 15th July, 2009 for Switzerland for pursuing higher studies in Biotechnology for 2 years. What would be his residential status under the Foreign Exchange Management Act, 1999 during the Financial Years 2009-10 and 2010-11?

Mr. Suresh requires every year USD 25,000 towards tuition fees and USD 30,000 for incidental and stay expenses for studying abroad. Is it possible for Mr. Suresh to get the required Foreign Exchange and, if so, under what conditions? (8 marks)

- (b) (i) A meeting of members of ABC Limited was convened under the orders of the Court to consider a scheme of compromise and arrangement. Notice of the meeting was sent in the prescribed manner to all the 700 members holding in the aggregate 20,00,000 shares. The meeting was attended by 400 members holding 13,00,000 shares. 160 members holding 10,00,000 shares voted in favour of the scheme. 150 members holding 2,40,000 shares voted against the scheme. The remaining members abstained from voting. Examine with reference to the relevant provisions of the Companies Act, 1956 whether the scheme is approved by the requisite majority.
- (ii) Does the scheme of compromise or arrangement require approval of preference shareholders? (8 Marks)

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Answer

(a) Residential Status

According to Section 2(v) of Foreign Exchange Management Act, 1999, 'person resident in India' means a person residing in India for more than 182 days during the course of preceding financial year (Section 2(v(i))). However, it does not include a person who has gone out of India or who stays outside India for employment outside India or for any other purpose in such circumstances as would indicate his intention to stay outside India for an uncertain period.

Generally, a student goes out of India for a certain period. In this case, Mr. Suresh who resided in India during the financial year 2008-09 left on 15.7.2009 for Switzerland for pursuing higher studies in Biotechnology for 2 years, he will be resident for 2009-10, as he has gone to stay outside India for a 'certain period' (If he goes abroad with intention to stay outside India for an 'uncertain period' he will not be resident with effect from 15-7-2009).

Mr. Suresh will not be resident during the Financial Year 2010-2011 as he did not stay in India during the relevant previous financial year i.e. 2009-10.

Foreign Exchange for studies abroad

According to Schedule III read with Rule 5 of Foreign Exchange Management (Current Account Transactions) Rules, 2000 release of foreign exchange for studies abroad exceeding the estimates from the institution abroad or USD 1,00,000 per academic year, whichever is higher requires prior approval of Reserve Bank of India. In this case the foreign exchange required is only USD 55,000 per academic year and hence approval of RBI is not required.

(b) Compromise or Arrangement

The scheme must be approved by a resolution passed with the special majority stipulated in Section 391(2) of the Companies Act, 1956, namely a majority in number representing three-fourths in value of the creditors, or members, or class of members, as the case may be, present and voting either in person or, by proxy.

The majority is dual, in number and in value. A simple majority of those voting is sufficient. Whereas the 'three-fourths' requirement relates to value. The three-fourths value is to be computed with reference to paid-up capital held by members present and voting at the meeting.

In this case out of 700 members, 400 members attended the meeting, but only 310 members voted at the meeting. As 160 members voted in favour of the scheme the requirement relating to majority in number (i.e. 156) is satisfied 310 members who participated in the meeting held 12,40,000, three-fourth of which works out to 9,30,000 while 160 members who voted for the scheme held 10,00,000 shares. As both the requirements are fulfilled, the scheme is approved by the requisite majority. (It is presumed that all the shares are fully paid-up).

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Preference shareholders

The term 'member' includes preference shareholders also. Further, preference shareholders are a class of members and their rights may be affected differently in the proposed scheme of arrangement. Hence their approval is also required.

If the Court directs separate meeting of preference shareholders and equity shareholders, then the scheme should be approved by requisite majority in both such meetings held as per directions of the Court.

Question 5.

- (a) A producer company was incorporated on 1st September, 2009. At present the paid-up share capital of the company is Rs. 10 lakhs consisting of 1,00,000 equity shares of Rs. 10 each fully paid-up held by 200 individuals and 20 producers institutions. You are required to answer the following with reference to the provisions of the Companies Act, 1956:-
- (i) What is the time limit for holding the First Annual General Meeting and the subsequent Annual General Meetings?
 - (ii) What is the Quorum for the Annual General Meeting?
 - (iii) State the manner in which the voting rights of the members are determined.
 - (iv) Is it possible to remove a member? (8 Marks)
- (b) Explain the rule of "Ejusdem Generis" with reference to the interpretation of statutes. State the cases in which this rule is no applicable. (8 Marks)

Answer

(a) Producer Companies

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

Quorum Unless the articles of association of the producer company provide for a larger number, 1/4th of the total number of members of the producer company shall be the quorum for its annual general meeting. In this case the company has got 220 members. Hence the quorum is 55 (Sec. 581ZA(8))

Voting rights of members: It depends on the type of membership. Where the membership consists of individuals and producer institutions, (as in this case) voting rights should be computed on the basis of a single vote for every member (Section 581D(i))

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Removal of member: No person, who has any business interest which is in conflict with business of the producer company, shall become a member of that company (Section 581D(4)). A person who has become a member of the producer company acquires any business interest which is on conflict with the business of the producer company, shall cease to be a member of that company and be removed as a member in accordance with the articles (Sec. 581D(5)).

(b) Rule of Eiusdem Generis

The term ejusdem generic means of the same kind or species. Simply stated the rule means where any Act enumerates different subjects, general words following specific words are to be construed with reference to the words that precede them. The general words are to be taken as applying to things of the same kind as the specific words previously mentioned unless there is something to show that a wider sense was intended. Thus the rule of 'ejusdem generis' means that where specific words are used and after these specific words, some general words are used, the general words would take their colour from the specific words used earlier (eg) where an Act permitted keeping of dogs, cats, cows, buffaloes and other animals, the expression 'other animals' would not include wide animals like lions and tigers, but would only mean domesticated animals like horses, etc.

However, there are certain cases/circumstances on which this rule cannot be applied in the interpretation of statutes. The general principle of 'ejusdem generis' applies only where the specific words are all of the same nature. When they are of different categories, then the meaning of general words following these specific words remain unaffected. These general words would not take colour from the earlier specific words.

Again if the particular words used exhaust the whole genus (category), then the general words are to be construed as covering a larger genus.

Further, the Courts have a discretion whether to apply the 'ejusdem generis' doctrine in a particular case or not. For instance, the 'just and equitable' clause in the winding up, powers of the Court is held to be not restricted by the first five situations in which the Court may wind up a Company.

Question 6

- (a) *Examine the validity of the following with reference to the provisions of the Companies Act, 1956:-*
- (i) *EF Limited re-appointed Naresh & Company, Chartered Accountants, as Auditors of the company at the Annual General Meeting held on 30th September, 2010. Mrs. Kamala, wife of one of the partners of Naresh & Company, invested Rs. 1 lakh in the equity shares of EF Limited on 15th October, 2010. But Naresh & Company continues to function as statutory auditors of the company.*

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- (ii) Mr. Suresh, a Chartered Accountant, was appointed by the Board of Directors of AB Limited as the First Auditor. The company in General Meeting removed Mr. Suresh without seeking the approval of the Central Government and appointed Mr. Gupta as Auditor in his place. (8 Marks)
- (b) A group of shareholders of Green Wheels Limited is of opinion that the management of the company is not carrying out its functions in accordance with the prudent commercial practice and if the affairs of the company are allowed to run in future in the same manner, the company's financial position would be in danger. They want that a special audit be conducted to find out the actual nature of the transactions.
- (i) State with reference to the provisions of the Companies Act, 1956, as to when a special audit can be directed and by whom.
- (ii) Draft an application to be submitted to the appropriate authority in this respect. (8 Marks)

Answer

(a) (i) **Disqualification of auditor:** According to section 226(3)(e) of the Companies Act, 1956, a person who holds any security of the company, which carries voting rights, cannot be appointed as auditor of the company. In the case of a firm of chartered accountants, all the partners should not hold any such security. Further Section 226(5) provides that if an auditor becomes subject, after his appointment, to any of the disqualifications specified in sub-section 3 of section 226, he shall be deemed to have vacated his office of auditor. However section 226 (3)(e) is not applicable if the security is held in the name of wife or other relative. Hence Naresh and Company can continue to function as auditors of the Company even after 15th October 2010 is after the investment made by wife of a partner in the equity shares of EF Limited.

(ii) Removal of first auditor

Section 224(7) stipulates that any auditor appointed under section 224 may be removed from office before the expiry of his term only by the Company in general meeting, after obtaining the previous approval of the Central Government in that behalf. But no such approval of the Central Government is required in the case of first auditor. The first auditors appointed by Board of Directors can be removed in first general meeting and any other person may be appointed in his place if notice for his nomination is given by any member at least 14 days before the general meeting (Section 224(5)). Hence the removal of the first auditor appointed by the Board without seeking approval of the Central Government is valid.

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(b) **Special Audit :** Section 233A of the Companies Act, 1956 deals with the matter relating to special Audit. The special audit can be ordered by the Central Government if the Central Government is of the opinion:

- (i) that the affairs of the company are not being managed in accordance with the sound business principles or prudent commercial practices, or
- (ii) that any company is being managed in a manner likely to cause serious injury or damage to the interest of the trade, industry or business to which it pertains; or
- (iii) that the financial position of my company is such as to endanger its solvency.

Thus, a complaint can be submitted by the shareholders requesting for conducting the special audit.

Draft Application:

To,

Date:

The Secretary,

Department of Company Affairs,

Government of India

(Address) New Delhi.

Sub. : _____

Sir,

We, the undersigned, the shareholders of Green Wheels Limited would like to bring to your kind notice that for a long time the affairs of the said company are not being managed in accordance with the sound business principles and prudent commercial practices. Certain expenditures incurred by the company are not related to the business of the company. Moreover, we have the apprehension that there are certain business transactions which are entered into by the directors with the concerns which are owned by the relative of the directors and the prices charged for such transactions are not comparable with the prices charged by other parties for similar transactions.

(Students may state any other circumstances also)

If such a state of affairs is allowed to be carried on for long, the financial position of the company will reach a stage where it will endanger its solvency. The modus operandi of the transactions is such that it may be difficult for the regular statutory auditor to detect them in course of normal audit.

It is, therefore, prayed that the Central Government be pleased to appoint, pursuant to section 233A of the Companies Act, 1956, a special audit to properly audit the

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accounts of the company and find the real nature of the transactions and determine the losses so far sustained and being sustained by the company of this account.

Yours Faithfully,

1.

2.

3.

4.

5.

(Shareholders)

Question 7

Answer any **four** of the following

- (a) *Examine with reference to the provisions of the Securities Contracts (Regulation) Act, 1956 whether it is possible for City Stock Exchange Limited, a company incorporated under the Companies Act, 1956 and a recognized Stock Exchange, to insist that its members should appoint only other members as their proxies to attend and vote at the meeting of the Stock Exchange. (4 Marks)*
- (b) *The Articles of Association of AB Limited provide for a maximum of 15 directors but the company has only 10 directors. The Board Meeting held on 16th August, 2010 was attended by 6 directors out of which 3 directors were interested in an item which was considered and approved by 3 non-interested directors. Examine the validity of the resolution passed at the Board Meeting explaining the relevant provisions of the Companies Act, 1956. (4 Marks)*
- (c) *The management of Rampur Stock Exchange desires to transfer its duties and functions to a clearing corporation. Advise the management of the said stock exchange about the extent of control which may be exercised by the clearing corporation under the Securities Contracts (Regulation) Act, 1956. (4 Marks)*
- (d) *A dispute between PQR Limited and ABC Limited is pending in the Competition Commission of India. During the course of hearing, PQR Limited submitted an application that services of experts may be obtained for deciding an issue. ABC Limited raised objection that services of experts can not be obtained. Decide whether the Commission can obtain the services of experts under the provisions of the Competition Act, 2002. (4 Marks)*
- (e) *Gujarat Textiles Limited is having a foreign subsidiary company. The said Indian holding company failed to furnish particulars of its foreign subsidiary company in its Balance Sheet. Decide the liability of Gujarat Textiles Limited under the Companies Act, 1956. (4 Marks)*

Answer

(a) Proxies in the case of stock exchange

Section 7A of Securities contracts (Regulation) Act, 1956, permits a recognised stock exchange to make rules or amend any rules made by it to provide for all or any of the matters listed in section 7A(1) including the restriction on the right of a member to appoint another person as his proxy to attend and vote at a meeting of the stock exchange. If the rules of City Stock Exchange Ltd permit its members to appoint only another member as his proxy, then members can not appoint non-members as proxies.

If the rules of City Stock Exchange Ltd do not have any such provision, then it is possible to amend the rules providing for such restriction. But the rules can be amended only with approval of Central Government/SEBI. These should be published on the Official Gazette. Such rules will be valid notwithstanding anything to the contrary contained on the Companies Act, 1956 [Section 7A(2)].

According to section 176(1) of the Companies Act, 1956, a member can appoint another person (whether a member or not) is a company as his proxy. Though City Stock Exchange Ltd. is a company; it is possible to provide for restriction relating to appointment of proxies taking advantage of Section 7A of SCRA, 1956.

(b) Board Meeting: According to Section 287(2) of the Companies Act, 1956, quorum for a board meeting shall be one-third of total strength of the Board, or two directors, whichever is higher.

Directors whose place is vacant, should not be considered for the purpose of deciding 'total strength' of the Board [Section 287(1)(a)].

Further, fraction of one-third should be rounded off as one [Section 287(2)].

In this case articles of AB Ltd. provide for a maximum of 15 directors, but the company has only 10 directors i.e. the total strength is 10. $\frac{1}{3}$ rd of total strength is 3.33, fraction being rounded off as one. Hence the quorum for the Board Meeting is 4.

However, there is an exception. If the number of interested directors exceeds or is equal to two thirds of total strength, the number of remaining directors who are not interested present at the meeting being not less than 2 shall be the quorum during such meeting. [proviso to section 297(2)]

Proviso to section 287(2) is not applicable in this case as number of interested directors is only less than two third of total strength.

The Board Meeting held on 16.8.2010 was attended by 6 directors out of which 3 directors are interested and hence they cannot be counted for the purpose of forming a quorum (section 287(1)(b)). The number of non-interested directors is only 3 which is

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less than the quorum. Hence the resolution passed at the Board Meeting in respect of an item where 3 directors are interested is not valid.

- (c) (1) A recognized stock exchange may, with the prior approval of the Securities and Exchange Board of India, transfer the duties and functions of a clearing house to a clearing corporation being a company incorporated under the Companies Act, 1956, for the purpose of-
- (a) the periodical settlement of contracts and differences there under;
 - (b) the delivery of, and payment for, securities;
 - (c) any other matter incidental to, or connected with, such transfer.
- (2) Every clearing corporation shall, for the purpose of transfer of the duties and functions of a clearing house to a clearing corporation referred to in sub-section(1) make by-laws and submit the same to the Securities and Exchange Board of India for its approval.
- (3) The securities and Exchange Board of India may, on being satisfied the is in the interest of the trade and also in the public interest to transfer the duties and functions of a clearing house to a clearing corporation, grant approval to the by-laws submitted to it under sub-section(2) and approve transfer of the duties and functions of a clearing house to a clearing corporation referred to in sub-section(1)
- (4) The provision of section 4,5,6,7,8,9,10,11 and 12 shall, as far as may be, apply to a clearing corporation referred to in sub-section (1) as they apply in relation to a recognized stock exchange.

(d) **Competition Commission of India**

As per provisions of Section 36(4) of the Competition Act, 2002 the Competition Commission may call upon such experts from the fields of economics, commerce, accountancy, international trade or other disciplines as it deems necessary, to assist the Commission in the conduct of any inquiry or proceeding before it. As per Regulation 54 of the competition Commission (General) Regulations', 2004 made by the commission under Section 64 of the Competition Act 2002, it may draw up a panel of such experts.

In view of the above stated specific powers given to the competition Commission it can call upon the services of an expert to determine the truth of allegation or issue under consideration.

(e) **Attachment of documents in relation to an overseas subsidiary company:**

Section 212 of the Companies Act, 1956, does not make any distinction between a local subsidiary company and an overseas subsidiary company. Under section 4(4), a company shall be deemed to be the holding company of another, if, but only, if that other is its subsidiary. Under section 4(5), the expression company includes any body corporate and the definition of body corporate in section 2(7) includes a company incorporated outside India. In view of the aforesaid position, the Indian holding company is legally bound to attach to its balance-sheet the

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documents mentioned under section 212 prepared in accordance with the requirements of the Companies Act. However, there may be some practical difficulty in attaching the documents of foreign subsidiary, in which case the Board of Directors of the Indian holding company may apply to the Central Government under section 212(8) either to waive the requirement or to modify the same. Hence, the company has violated the provisions of section 212 in not furnishing the particulars of the foreign subsidiary.

