

PAPER – 4 : CORPORATE LAWS AND SECRETARIAL PRACTICE

QUESTIONS

Companies Act, 1956

1. A Public Company sought extension of time from the ROC for holding AGM upto a period of 3 months and it was granted. However, when the AGM was held and the accounts were presented, it was found that the annual accounts were upto a period beyond which it is permissible. The Company contended that since ROC granted extension of time for holding AGM upto a period of 3 months, the same would also be applicable for presentation of accounts as well. Referring to the relevant provisions of the Companies Act, 1956, whether the contention of the company shall/may hold good?
2. According to the Companies Act, 1956, an individual cannot be auditor of more than twenty companies at a time. Further, out of these twenty companies, not more than ten should be companies having a paid-up capital of Rs.25 lakhs or more. Mr. Excellent is an individual auditor wants to compute the specified number of audits and for this purpose, a list has been drawn out of which identify, the company which shall be/not be taken into account for the purpose of calculating specified number of audits:
 - (i) Audit of Private Company
 - (ii) Guarantee companies not having share capital
 - (iii) Audit of non-profit companies
 - (iv) Special Audits
 - (v) Audits- of Foreign Companies
 - (vi) Branch Audits
 - (vii) Company audit where he is appointed as a joint auditorBesides, he wants to know that as a member of the ICAI, is there any other restriction on him as a matter of self-regulation in the matter of inclusion/exclusion of audit of private companies for the purpose of calculating specified number of audit assignments. Advise.
3. The Articles of Association of a private company incorporated appointed X as Managing Director for life on 1st June, 2000. The articles also empowered X to appoint successor. X appointed by will Y to succeed him after his death. Answer with reference to the relevant provision of the Companies Act, 1956 and decided Supreme Court judgement, whether Y can succeed X as Managing Director after the death of X?
4. The articles of a public company provides for appointment of directors by the principle of proportional representation. Referring to the relevant provisions, if any contained in the Companies Act, 1956, advise the company to the methods which it may adopt for the purpose and the procedure for the same. Illustrate your answer.
5. In a public company the total number of directors are 9 and 2 office of the directors have fallen vacant. Referring to the relevant provisions of the Companies Act, 1956.
 - (a) What would be the quorum for the Board meeting?
 - (b) Can the articles of a company fix the quorum (higher or lower) for the Board meeting?
 - (c) Assuming if there are 15 directors in the company and of which 13 happen to be interested directors, what would be the quorum?
 - (d) How do you resolve the situation if all the directors are interested in a particular transaction?
6. Mr. X is serving in a company in the dual capacity of a director and an employee? Referring to the provisions of the Companies Act, 1956. State:
 - (a) Whether there is any prohibition/restriction serving in the dual capacity?

- (b) If so whether a director serving as an employee would amount to holding an office or place of profit?
 - (c) Whether the remuneration drawn by the director as an employee of the company would be governed by the provisions relating to managerial remuneration?
 - (d) What would be your answer if the said director is rendering services of a professional nature?
7. A public company is contemplating setting up an Audit Committee as a part of good corporate governance. Advise the company on the Constitution, Composition, Terms of Reference and the Role of Audit Committee. In your opinion, whether setting up of such an Audit Committee is supplementary or complimentary to the Board.
 8. The Directors of X & Co desire to authorise the MD to enter into the following transactions namely- (a) invest from time to time surplus funds in the purchase of shares of other companies; (b) borrow from banks money required for the purpose; (c) give loans to person, including firms in which directors or their relatives are partners; (d) give donations to charitable trusts in which any of the directors may be interested as trustees. Discuss.
 9. Examine the possibilities of the following with reference to relevant provisions of the Companies Act, 1956:
 - (i) Filing of Unaudited balance sheet with the ROC.
 - (ii) Filing of non-adopted balance sheet with the ROC and preparation of subsequent year's accounts with the balances taken from such balance-sheet.
 10. RM Limited went for a public issue of Equity Shares (Rs. 10 Crores) of Rs.10 each. The shares were subscribed to an extent of 95% of the total issue. The shares of the company were accepted for listing by Bombay Stock Exchange but subsequently the permission was cancelled on certain grounds. On an appeal to the Central Government by the company, the decision of the Stock Exchange was held to be valid. As a result, the application money had become refundable to the allottees. The company, had no prospects of doing any business and there was a complete deadlock among the Directors. Looking at the circumstances, certain creditors filed a petition in the court for winding up of the company on the ground that the company had become commercially insolvent. The shareholders of the company object to the petition of the creditors. Decide giving reasons :
 - (a) Whether the objections of the shareholders will sustain and the court can dismiss the petition of creditors for winding up of the company?
 - (b) State the provisions of the Companies Act, 1956 in this regard.
 11. Decide on the following :
 - (a) A Managing Director who has completed 70 years of age is to be re-appointed for 5 years. The remuneration will be the limits prescribed under Schedule-XIII.
 - (b) X the Managing Director of Y Limited is also the Managing Director of Z Limited wants to draw remuneration from both the companies.
 - (c) The Directors' wish to increase the sitting fees payable for attending board meetings from Rs.2,000/- to Rs.20,000/- by passing the resolution in the Board Meeting.
 - (d) The Board of XYZ Ltd., has received an attractive offer for sale for one of the sugar mills owned by the company. The transaction should be completed within a month.
 12. State whether the acts done by the Board meeting be invalid if it was found afterwards that there was some defect in the appointment of directors or any person acting as a director?
 13. Advise:
 - (a) XYZ Ltd. wants to maintain its books of account on cash basis;
 - (b) It has a branch office outside India and wants to maintain accounts over there;

- (c) A shareholder of a company wants to inspect books of account. Would your answer be different if he is acting as an agent of the director of the company?
14. A director of a public company has taken a loan of Rs.10 lakhs from the company without the approval of the Central Government. He seeks your opinion on the following matters:
- Is it possible to avoid prosecution by applying to the government for approval or by refunding the loan?
 - Whether the offence is compoundable before or after Institution of prosecution and the authority who can compound the offence.
15. When is a company called a foreign company and a foreign controlled company? What legal requirements under the Companies Act, 1956 is a foreign company wishing to establish a place of business in India required to comply with relating to delivery of documents to the Registrar of Companies?
16. Whether a composite and simultaneous petition for relief against oppression or mismanagement and for binding up is maintainable.
17. What is meant by 'oppression'? State whether the aggrieved party would succeed in obtaining relief from company law board on the ground of oppression in the following cases:
- The majority of the Board of Directors overrides the minority directors and the minority directors apply to Company Law Board complaining oppression by majority directors.
 - A petition by majority shareholders complaining oppression by minority shareholders.
18. The Board of Directors of Very Well Ltd., are contributing every year to a charitable organization a sum of Rs.60, 000/-. In a particular year, the company suffered losses and the directors are contemplating to contribute the said amount in spite of the losses. In this connection, state whether the directors can do so?
19. The Board of Directors of 'X Ltd' having a paid-up share capital of Rs.40 lakhs appointed 'Y Ltd.' as sole selling agent for a period of 5 years with effect from 1st April, 2003 and the said appointment was approved by the company in the next Annual General Meeting held on 30th September, 2003. The Directors of 'Y Ltd.' were holding fully paid up shares of face value of Rs.3 lakhs in 'X' Ltd. Answer the following explaining the relevant provisions of the Companies Act, 1956:
- Is the appointment of the sole selling agent in order?
 - Would your answer be different if both are private companies or if the director of Y Ltd., acquired the aforesaid shares in X Ltd on 1st September 2003.
20. The Board meeting of Governance Ltd. has the following schedules:
- | | | |
|-------------------------|---|----------------------------------|
| 1 st Meeting | - | 1 st January, 2005 |
| 2 nd Meeting | - | 30 th June, 2005 |
| 3 rd Meeting | - | 1 st July, 2005. |
| 4 th Meeting | - | 31 st December, 2005. |
- State whether the Board Meetings are as per order/compliance with the provisions of the Companies Act, 1956. What would be your views if the meeting to be held on 30th June, 2005 is adjourned due to lack of quorum?

Competition Act, 2002

21. The Association of Truck Operators of India by agreement insisted that members of the association shall not deal with the non-members in transportation of goods. The Association claims that this agreement is entered for the welfare of trade and not for any other purpose. In your opinion whether the agreement would be under the purview of the Competition Act, 2002. Whether your answer would be different if the association attempts to control the provisioning of services rendered by its members?

FEMA, 1999

22. Mr. Bharat, born and brought up in India, goes to USA on 10.4.2005 to look after his son, Amit, who is suffering from chronic disease, with the intention to stay over there till his son, Amit recovers completely. Determine his residential status under the Act for the financial year 2005-2006 and 2006-2007.
23. Mr. Patel, who was resident of USA for many years, now permanently returns to India. He continues to hold some immovable property, foreign security and other foreign exchange assets in USA. Can he hold such assets outside India?
24. What is the procedure for compounding of offences under the FEMA, 1999?
25. The following are various types of capital account transactions of which specify, the nature of transaction as whether it is permissible or where restrictions cannot be imposed or transactions are altogether prohibited:
 - (a) For amortisation of loan.
 - (b) A person resident outside India for making investments in chit fund.
 - (c) Investment by a person resident in India in foreign securities.
 - (d) Maintenance of foreign currency accounts in India and outside India by a person resident in India.
 - (e) Trading in transferable Development Rights (TDR's) by a person resident outside India.

SCRA, 1956

26. Kutch Stock Exchange is an Association of Persons, registered and recognized under the Securities Contracts (Regulation) Act, 1956. The Central Government wants that persons should manage the stock exchange that does not have role that of a trading or a clearing member and that the stock exchange should be corporatised and de-mutualised. Advise the stock exchange as to how it should reorganize as per the latest amendments in the Securities Contracts (Regulation) Act, 1956.

SEBI ACT, 1992

27. What are the penalties prescribed in respect of the following:
 - (a) For failure to furnish information, return, etc.,
 - (b) For failure by any person to enter into agreement with clients.
 - (c) For failure to redress Investors' Grievances.

SUGGESTED ANSWERS/HINTS

1. While a company may hold its AGM in a year within the time limit of 15 months as provided by Section 166(1), it may still contravene Section 210. A company and its director may commit offences if it does not fulfil the three requirements and failure to comply with any of them constitute an offence unless an extension of time has been granted for holding the meeting by the ROC. However, the extension of time for holding the AGM is only with reference to the meeting and not to that of submission of accounts.
2. In computing the specified number of audits for the purpose of Section 224(1B), the following audit shall not be taken into account:
 - (a) Audit of private company.
 - (b) Audit of Guarantee Companies not having share capital.
 - (c) Special Audits.
 - (d) Audit of Foreign Companies.
 - (e) Branch Audits.

Though the audit of private companies has been excluded for the purpose of calculating the specified number of audits, as a member of ICAI, the Audit of Private Companies will come under the purview of calculating the ceiling limit as a matter of self-regulation.

3. Assignment of office by director: Any assignment of office made after the commencement of the Act by any director is void [Section 312].

It was held in *Oriental Metal Pressing Works Private Ltd. vs. B.K. Thakoor* (A.I.R.) 1960 Bom. 167 that the appointment of one as managing director by the will of one D was void in view of the provisions contained in Section 312, since, according to the High Court, the words 'any assignment' were comprehensive enough to include every assignment to transfer of a director or of the appointment by a director of a person to the office of a director in his place, whether by a deed inter vivos or by will. But this ruling has been reversed by the Supreme Court (vide A.I.R. 1961 S.C. 573). The Court considers that the word 'assignment' in Section 312 does not mean or include appointment. From its every nature transfer inevitably imports the passing of a thing from one person to another. A transfer without the passage of the thing, even when that is an office is inconceivable. On the other hand, an 'appointment' has nothing to do with passing from one person to another; it connotes the putting in of someone in a vacancy. So transfer and appointment are dissimilar. It would be an unusual statute, which by using a single word intended to prohibit at the same time, two wholly different acts. A construction leading to such a result cannot be permitted.

4. Appointment by proportional representation: But the articles of a public company or a private company which is subsidiary of a public company may adopt the principle of proportional representation for appointing not less than $\frac{2}{3}$ rd if the total number of the directors, whether by a single transferable vote or by a system of cumulative voting or otherwise. In such a case, appointments will be so made once in every three years and interim casual vacancies will be filled in conformity with the provisions of Sections 262 and 265. Cumulative voting denotes that if there are five candidates or distributes his five votes. He can cast all the five votes in favour of one candidate or distribute his five votes among different candidates. This system of voting ensures that the Board will have fair representation of the minority interest.
5. Where total number of directors are 9 and 2 offices of the directors have fallen vacant, we find: $\frac{1}{3}$ of $(9-2) = \frac{1}{3}$ of $7 = \frac{7}{3}$ directors. If the fraction of $\frac{7}{3}$ were to be rounded off as one then 3, i.e. $2+1$ directors would constitute the quorum for the Board meetings. If at any time the number of the remaining directors exceeds or is equal to two thirds of the total strength, the number of the remaining directors who are non-interested but present at the meeting, not being less than two shall constitute the quorum. For example, there are in all 15 directors and the Board meeting commences with all the 15 directors. During the currency of the meeting, an item comes up for discussion in respect of which 13 happen to be "interested" directors. In this case, in spite of the excess of the interested directors being more than two-thirds, the prescribed minimum number of non-interested directors constituting the quorum, namely, 2 present at the meeting are to transact the particular item of business.
6. There is no prohibition is contained in the Companies Act for a director acting in the dual capacity of a director and an employee. However, Section 314 puts a restriction for a director while accepting office or place of profit in the company. For this purpose, the director appointment in the office or place of profit need to be approved by the shareholders in the general meeting. A director however, without recourse to Section 314 can render services to the company in his professional capacity on one time basis.
7. Section 292A of the Companies Act, 1956 relating to Audit Committee provides for the following in relation to constitution, composition etc.
 - (1) Every public company having paid-up capital of not less than five crores of rupees shall constitute a committee of the Board known as "Audit Committee" which shall consist of not less than three directors and such number of other directors as the Board may determine of which two-thirds of the total number of members shall be directors, other than managing or whole-time directors.

- (2) Every Audit Committee constituted under sub-section (1) shall act in accordance with terms of reference to be specified in writing by the Board.
 - (3) The members of the Audit Committee shall elect a chairman from amongst themselves.
 - (4) The annual report of the company shall disclose the composition of the Audit Committee.
 - (5) The auditors, the internal auditor, if any, and the director-in-charge of finance shall attend and participate at meetings of the Audit Committee but shall not have the right to vote.
 - (6) The Audit Committee should have discussions with the auditors periodically about internal control systems, the scope of audit including the observations of the auditors and review the half-yearly and annual financial statements before submission to the Board and also ensure compliance of internal control systems.
 - (7) The Audit Committee shall have authority to investigate into any matter in relation to the items specified in this section or referred to it by the Board and for this purpose, shall have full access to information contained in the records of the company and external professional advice, if necessary.
 - (8) The recommendations of the Audit Committee on any matter relating to financial management, including the audit report, shall be binding on the Board.
 - (9) If the Board does not accept the recommendations of the Audit Committee, it shall record the reasons therefore and communicate such reasons to the shareholders.
 - (10) The chairman of the Audit Committee shall attend the annual general meetings of the company to provide any clarification on matters relating to audit.
 - (11) If a default is made in complying with the provisions of this section, the company, and every officer who is in default, shall be punishable with imprisonment for a term which may extend to one year, or with fine which may extend to fifty thousand rupees, or with both."
- 8. (a)** Although Section 292 empowers the Board of Directors of a company to delegate to the Managing Directors the power to invest, in general terms, the funds of the company, nevertheless because of the overriding provisions of Section 372(5) (which Section we shall discuss in detail in Study Paper 3), the transaction in the instant case would be invalid. Section 372(5) provides that no investment in shares of a company can be made by the Board of Directors of an investing company in pursuance of sub-section (2), unless it is sanctioned by a resolution passed at a meeting of the Board with the consent of all the directors present at the meeting except those not entitled to vote thereat, and unless further notice of the resolution to be moved at the meeting has been given to every director in the manner specified in Section 286. Since Section 372 does not provide for delegation of the power, the proposed delegation to be Managing Director in question, notwithstanding the general provision of Section 292, cannot be made.
- (b)** In terms of Section 292 the Board of Directors may also delegate to the Managing Director the power to borrow money otherwise than on debentures which it can exercise only by means of resolutions passed at Board meetings. As per Explanation to Section 292(1), it is the arrangement for an overdraft or cash credit that constitutes the exercise of the borrowing power and not the actual utilisation of the arrangement. In other words, an arrangement for an overdraft or cash credit to the tune of say Rs.5 lakhs constitutes the exercise of the borrowing power and not the actual drawing of this amount on the basis of the overdraft or cash credit. Consequently, the transaction in the instant case shall be valid. But before implementation of the proposal, the Board must pass a resolution at its meeting authorising the Managing Directors to borrow from banks money required for the purpose of the company's business. Also the resolution delegating this power shall specify the total amount outstanding at any one time up to which the delegate may borrow money.
- If, however, the moneys to be borrowed together with the money already borrowed by the company (apart from temporary loans obtained from the Company's bankers in the ordinary course of business) will exceed the aggregate of the paid up capital of the company and its

free reserves, [that is to say, reserves not set apart for any specific purpose] the Board of Directors of the company in question must obtain the consent of the company in its general meeting. Consequently, care should be taken to ensure that while delegating the power to the managing director the aforesaid provision has not been violated; also it should be ensured that the memorandum of association permits borrowing.

- (c) Since according to Section 295(1), without obtaining prior approval of the Central Government in that behalf, a company cannot directly or indirectly lend money to persons including firms, in which directors or their relatives are partners, the company in question must in the first instance seek the Central Government's approval. Secondly, since the power to make loans may be delegated under Section 292(1)(e), the Board of Directors of the company in question must pass a resolution therefore and every resolution delegating this power to the Managing Director shall specify the total amount up to which loans may be made by the delegate, the purpose for which loans may be made and the maximum amount of loans which may be made for each such purpose in individual cases. Thirdly, by virtue of Section 291(1), the Board must see with reference to the memorandum and articles whether the company is authorised to exercise the power.
- (d) Under Section 293(1)(e), the Board of Directors of a public company can contribute or donate to charitable and other funds not directly related to the business of the company or the welfare of its employees any amount the aggregate of which will not, in any financial year exceed Rs.50, 000 or 5% of its average net profits during the three financial years preceding whichever is greater. If this power of the company is not ultra virus the memorandum of the company, then only the Board can act in pursuance of the above-mentioned resolution of the company and in so acting, it can authorise the Managing Director to exercise the power on behalf of the Board.

It may be noted that the power of the Board to donate to general charities is not conditional to the existence of any profits. In such case, they may contribute up to the limit given in Section 293(1)(e)

9. (i) Unaudited Balance sheet : Section 220(1) requires that the balance sheet and profit and loss account shall be filed with the 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. If any copy of the balance sheet is issued, circulated or published without there being annexed or attached thereto, as the case may be, a copy 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.500. (Section 218). But, in view of requirements of sections 216, 218 unaudited balance sheet and profit and loss account cannot be filed with the Registrar of Companies.(ICAI Compendium of Opinions, Vol.III).
 - (ii) Non-adoption of annual accounts: If the accounts placed before the annual general meeting in accordance with section 210 are not adopted, it would be treated as vote of no confidence against the Board of Directors. What the law requires is consideration of accounts. Therefore, there is no bar against in which the opening balances are those appearing to the balance sheet of the previous year, which was not adopted by the AGM. Section 220(3) stipulates that if the AGM does not adopt the balance sheet, a statement of the fact and of the reasons thereof shall be annexed to the copies of the balance sheet to be filed with the ROC.
10. (a) Commercial Insolvency of RM Ltd.:
In this case three facts are given i.e.:
 1. RM Limited went for a public issue and subsequently it was required to refund the amount received on application.

2. As a result, the company has no prospects of doing any business.
3. There was a complete dead lock among the directors.

These three circumstances may be construed as indicators of commercial insolvency of the company.

Section 433 (e) read together with Section 434 provides that a Court may order for winding up of a company if it is unable to pay its debts or deemed to be unable to pay its debts and it is proved to the satisfaction of the Court after taking into account all the liabilities including the contingent and prospective liabilities of the company.

Moreover, Section 439 gives powers to the creditors for filing an application for its petition for winding up. There are no chances for the sustenance of shareholder's objection. *Deccan Farms & Distilleries Ltd. v. Velabai Laxmidas Bhaji* (1979).

The Court has got wide discretionary powers regarding winding up. It may or may not dismiss the petition of creditors for winding up. Even if a winding up petition is a proper remedy against a company which is unable to pay its debts, the Court may in its discretion refuse to put an end to the life of the company [*Jugalkishore Banarsidas v. South India Saw Mills P. Ltd.* (1975)].

(b) The Provisions of the Companies Act, 1956, which will apply in this case are:

- (a) A company may be wound up by the Court, if the company is unable to pay its debts. [Section 433(e)].
- (b) A company shall be deemed to be unable to pay its debts, if it is proved to the satisfaction of the Court that the company is unable to pay its debts, and in determining whether a company is unable to pay its debts, the Court shall take into account the contingent and prospective liabilities of the company. [Section 434(c)].
- (c) An application to the Court for the winding up of a company shall be by petition presented, subject to the provisions of this section, by any creditor or creditors, including any contingent or prospective creditor or creditors. [Section 439(b)].

11. (a) As per the notification dated 12th September, 1996, a person who is otherwise qualified but has attained the age of 70 years can be appointed as Managing Director without Central Government's approval if his appointment is approved by a special resolution passed by the company in general meeting. So Mr. Y can be reappointed for a period of five years if the approval of the shareholders is obtained by special resolution.

(b) As per the notification dated 12th September, 1996, if the appointee is managerial person of more than one company, he shall draw remuneration from one or both companies provided that the total remuneration drawn from both the companies does not exceed the higher maximum limit admissible from any one of the companies of which he is the Managing Director. Accordingly, Mr. X can draw remuneration from both the companies provided the same is within the overall ceiling mentioned in the notification as stated above.

(c) Rule 10B of Companies (Central Government's) General Rules and Forms, 1956, permits sitting fees to be paid upto Rs. 20,000 to Directors if paid-up share capital and free reserves of Rs.10 crore and above or turnover of Rs.50 crores and above. For others not to exceed Rs.10,000/-.

In the instant case, increase in sitting fees is within the ceiling of Rule 10B, no approval of the Central Government is required. However, the company has to see the limits prescribed.

(d) As per Section 293(1)(a) of the Companies Act, 1956, Board has to obtain the approval of shareholders for sale or disposal of any undertaking of the company. Any decision by the Board to sell the sugar mill will not be valid unless it is approved by the shareholders in general meeting. In the instance case the Board cannot accept the offer even if it is attractive. The acceptance is *ultra vires* the Board. Section 293 speaks about "Consent" of the shareholders. The consent implies only prior consent. Directors cannot sell the undertaking with the hope that it will be ratified by members.

12. All Acts done by the Board meeting by its committee meeting or by any person acting as a director shall be as valid as if every such director or such person had been duly appointed and was qualified to be a director. The validity of all such acts done is not affected even if it discovered later on that there was some defect in the appointment of any one or more of such directors or of any person acting as a director. The said acts will also remain unaffected even the directors are later on discovered to be disqualified (Article 80). This provision has been intended to prevent the validity of transactions from being questioned where there has been a slip in the appointment of a director. But the provision cannot be utilized to ignore or override the substantive provisions pertaining to such appointment. It is applicable only to acts of directors whose appointment or qualification is later on discovered to be faulty. Where, however, their appointments have not taken place at all but they merely choose to act on the company's behalf, the protection prescribed by either Article 80 or Section 290 cannot be invoked [*Morris vs. Danssen (1964) 1, A.E.R. 586 (H, L.)*] This is because the said subsequent discovery must be a discovery of the defect; it must not be discovery of facts which go to constitute the defect [*British Asbestos Co. vs. Body (1903) 2 Ch. 439*].

Suppose a regulation like Articles 80 is included in the Article of association of a company. What would be the possible impact of this? The impact has been summed up in Halsbury's Laws of England (*vide p. 277, 3rd Edition, Vol. VI*) thus: "An Article validating the acts of persons acting as directors, though it is afterwards discovered that there was a defect in their appointment or qualification, operates not only between the company and outsiders but also as between the company and its members; as where *defecto* directors make a call, summon meetings of the company, elect other directors or allot shares, A *defecto* director may be ordered to furnish a statement of affairs in winding up. Directors can not take advantage of any infirmity in their proceedings in which they have themselves participated; they are stopped as between themselves and the company; they are also stopped from saying they have been improperly appointed if, they have acted after appointment, persons dealing with them who know of the invalidity are likewise stopped."

It should also be noted that Section 290 applies to act of an individual director, whereas Article 80 covers Act of the Board and of its committee.

13. (a) In the absence of any express provision in the Act, hitherto it was open to a company to maintain its accounts on 'cash basis' or 'accrual basis' or on hybrid basis i.e. partly on cash and partly on accrual basis. Under the Income-tax Act, an assessee can, even now, maintain its books of account by adopting any of the aforesaid methods. The controversy in so far as maintenance of accounts pursuant to the provisions of Companies Act, has now been set at rest by the amendment of sub-section (3) of section 209. Every company is now required to keep its books of account on accrual basis and according to the double entry system of accounting, popularly known as mercantile system of accounting which alone discloses a true and fair view of the state of affairs of a company.' The responsibility for the preparation of accounts giving a true and fair view of the company's financial statement is placed fairly and squarely on the shoulders of the directors' (*Caparo Industries plc v. Dickman, (1990)*).
- (b) *Maintenance of books of account*:. Books of account shall be maintained at the company's registered office unless the Board of directors decides to keep them at another place in India [Proviso to section 209(1)]. It will be the duty of the company to inform the Registrar of Companies within 7 days of the decision in case the Board decides to maintain books at a place other than the registered office. This has to be done by filing Form No. 23AA.
- Where a company has a branch office whether in or outside India, it may maintain books of account with respect to the transactions effected at such branch, at that branch itself. However, in such a case, proper summarised return made up at an interval of not more than three months should be sent to the registered office or to the other place where the Board has decided to keep the books of account.
- (c) The clear cut answer shall be 'no' except where he represents a director and the inspection is not mala fide or for some ulterior motive or against the interest of the company. In

Sugrabai Alibhain v. Amtee Properties (P) Ltd. [1984] 55 Comp Cas. 734 (Bom.), the Bombay High Court observed that a director is entitled to ask for inspection of books either personally or through an agent subject to the condition that the agent must give an undertaking to the company that he shall not pass on any information to any person other than the director who had appointed him to carry out the inspection.

14. (i) According to Section 295 of the Companies Act, no public company shall make any loan to any of its directors either directly or indirectly without obtaining the previous approval of the Central Government. As the Act envisages prior approval, Central Government will not entertain any application from the company seeking approval for a loan already given to its directors.

The company has, therefore, contravened the provisions of Section 295(1) and for this offence every person who is knowingly a party to this contravention including the person to whom the loan is made shall be punishable either with fine which may extend to Rs.5,000 or with simple imprisonment for a term which may extend to six months [Section 255(4)]. Where any such loan has been repaid in full, no punishment by way of imprisonment shall be imposed and where the loan has been repaid in part, the maximum punishment that may be imposed by way of imprisonment shall be proportionately reduced. So, by refunding the loan in full, it is possible to avoid punishment in the form of imprisonment, but it is not possible to avoid prosecution and punishment in the form of fine.

- (ii) All offences other than an offence which is punishable under the Companies Act with imprisonment only or with imprisonment and also with fine are compoundable under Section 621A. As the offence under Section 295 is punishable with fine or imprisonment, it is compoundable but with the permission of the court [Section 621A(2)]. The offence may be compounded either before or after the institution of prosecution. If the offence is compounded before the institution of any prosecution, no prosecution shall be instituted in relation to such offence, either by the Registrar or by any shareholder or by any person authorised by the Central Government. Where the composition of any offence is made after the institution of any prosecution, such composition shall be brought to the notice of the court by the Registrar in writing and on such notice of the composition of the offence being given, the company or its officer in relation to whom the offence is so compounded shall be discharged [Section 621A(4)].

The offence may be compounded by the Regional Director where the maximum amount of fine which may be imposed for such offence does not exceed Rs.5,000 and in other cases by the Company Law Board. In this case, the offence may be compounded by Regional Director, as the maximum fine is only Rs.5,000. On receipt of applications from the persons liable for penalty under Section 295(4) along with the comments of the Registrar, the Regional Director may specify the amount not exceeding the maximum fine which shall be paid to the Central Government for compounding of the offence.

15. Foreign Company: A foreign company means a company incorporated outside India and having a place of business in India; whatever be the pattern, of their holding. However where not less than 50% paid up capital of foreign company is held by one or more citizens of India or by one or more bodies corporate incorporate in India, whether singly or in aggregate, such company shall comply with the provisions of the Companies Act, 1956, as if it were a company incorporated in India. A 'foreign controlled company' however, means a company in which the majority shareholding and voting power is in the hands of foreign individuals and/or bodies corporate.

Filing of Returns and Documents (Sections 592 & 593) : Foreign companies which establish a place of business in India must within one month from that date file with the Registrar,

- (a) a certified copy of the charter, statutes or memorandum and articles of the company or other instrument defaming its constitution with a certified translation of the documents in the English language if they are not in that language. Rule 16 of the Central Government's General Rules, 1956 specifies the persons who are to certify the documents,
- (b) the full address of the registered or principal office of the company,

- (c) a list of directors giving with respect to each of the directors who are individuals, his name and surname, former name and surname, usual residential address and nationality.
- (d) the present name and surname, former name and surname and usual residential address of the secretary if he is an individual and if a body corporate its corporate name and its registered or principal office and if a firm the partners of which are joint secretaries, the name and principal office of the firm.
- (e) the names, addresses of persons resident in India and authorised to accept service of documents, notices and processes on behalf of the company, and
- (f) the address of the principal place of business in India (Section 592).

The other category of foreign companies, namely, companies which have already established a place of business in India, have to file the documents and particulars in accordance with the provisions of Section 277(1) of the Indian Companies Act, 1913, if they have not already done so. [Section 592(4)].

A foreign company should deliver to the Registrar within the prescribed time a return containing particulars of any changes or alterations in any of the particulars mentioned above (Section 593). Rule 17 of the Central Government's General Rules, 1956 prescribes the time within which the particulars of alterations are to be filed.

16. The Madhya Pradesh High Court in *Kilpest (P) Ltd. v. Shekhar Mehra* held that the petition, if initially made under Sections 397 and 398, cannot be converted into a winding up petition under section 433(f) and even no composite petition can be filed.

The aforesaid decision of the Madhya Pradesh High Court was overruled by the Supreme Court in *Worldwide Agencies (P) Ltd. v. Mrs. Margaret T. Desor* [1990] 67 The Comp.Cas. 607 (SC). The Supreme Court in this case observed that "though there may be some differences in the procedure to be adopted, it is not such which is irreconcilable and cannot simultaneously be gone into. The Supreme Court held that "a composite petition under sections 397, 398 and 433(f) of the Act is maintainable."

17. **Oppression:** The term 'oppression' is not defined in the Companies Act. Oppression, according to the Dictionary meaning of the word, is any act exercised in a manner burdensome, harsh and wrongful. The meaning of the term 'oppression' was explained by Lord Cooper in the Scottish case of *Elder v. Elder and Watson Ltd.* As given below:

"The conduct complained of should be at the lowest involve or visible departure from the standards of fair dealing and a violation of the conditions of fair play or which every shareholder who entrusts his money to a company is entitled to rely.

- (i) *Oppression of a member as a director:* The oppression dealt with by section 397 is only oppression of members in their character as such; and it is only in that character they can involve section 397. The harsh treatment, for instance, of a member who is a director or other officer or employee, by the Board of Directors or management does not come within (section 397). It has been held in '*Re. Bellador Silk Ltd.* That if the majority of the Board of Directors override the minority directors the latter cannot resort to section 397 and hence the minority directors will not succeed in getting relief from CLB on the ground of oppression.
- (ii) *Right not confined to minority:* According to section 399, the right to apply for relief under section 397/398 is given to 100 members or 1/10th of the total number of members or any member or members holding not less than 1/10th of the issued share capital of the company. There is nothing in this section which suggests even indirectly that unless the application is made by minority shareholders it is not maintainable. The right to apply is, therefore, not confined to oppressed minority of the shareholders along. It was held by *Calcutta High Court in Re. Sindhri Iron Foundry (P) Ltd.*, that the oppressed majority also might apply for relief under section 397. Therefore, the petitioners are likely to succeed in getting relief provided the other condition laid down in section 397 (i.e. that to wind up the company would unfairly prejudice such members, but that otherwise the facts would justify the making of a winding-up order on just and equitable ground) is satisfied, even though the Delhi High Court

held a contrary view in *Suresh Kumar Sanghi v. Supreme Motors Ltd.*

18. The power of the to donate to general charities is not conditional to existence of any profit. In such a case they may contribute up to the limit given in sec. 293(1) (e), even though the company may be working at a loss. Under the section the section a public company can contribute in any financial year not exceeding Rs 50,000 or 5% of its average net profits during the three preceding financial years whichever is greater.
19. The appointment of sole-selling agent is not in order since approval of central Govt. as per sec. 294 AA (2) has not been obtained. The approval of the Central Govt. shall be necessary even if both the companies and private companies Section 294AA applies to private companies also. If Y Ltd has acquired shares in X Ltd as on 1, September 1985; he provisions of section 294AA shall not apply.
20. As per Section 285, in the case of every company, a meeting of the Board of Directors shall be held at least once in every three months and at least four such meetings shall be held in every year. The section does not state the gap between two board meetings. In the present case four meetings have been scheduled for the year 2005 even though the gap between two board meetings is more than 3 months. However, as per the section there appear to be no contravention.

If the Board meeting to be held on 30th June, is adjourned due to lack of quorum, again a meeting is held on some other date, the company shall not be deemed to have contravened the provisions of Section 285. If the said meeting is held on 30th June, 2005 and was adjourned for want of quorum, the meeting automatically stand adjourned by virtue of Section 288 (1) till the same day in the next week, at the same time and place. And if the same day is a public holiday, then the meeting stands adjourned till the next succeeding day which is not a public holiday.

21. "Cartel" includes an association of producers, sellers, distributors, traders or service providers who, by agreement amongst themselves, limit, control or attempt to control the production, distribution, sale or price of, or, trade in goods or provision of services;

The term cartel like agreement has been given an inclusive meaning. Thus an association for the welfare of the trade or formed for any other purpose not mentioned in the aforesaid definition will not be a cartel. It is only when an association, by agreement amongst themselves, limits control or attempts to control the production, distribution, sale or price of, or, trade in goods or provision of services, that it will be a cartel.

22. Mr. Bharat is going to USA neither for employment nor for business nor for any purposes which indicate his intention to stay there for an uncertain period. Thus, his physical presence in India during the preceding F.Y., i.e., 2004-2005 shall have to be considered and as he was in India for 365 days during the F.Y. 2004-2005 he would be treated Residential of India for the financial year 2004-2005.

If he continues to stay in USA, say, till 31-3-2006, his stay in India during the preceding financial year; i.e., 2005-2006 shall be less than 183 days and hence he would be treated Non-Residential for the financial year 2006-2007.

23. Yes, section 6(4) of the Act gives general permissions to Residents to hold such immovable property, foreign security and foreign exchange outside India if they were acquired when he was Resident outside India. No special permission is required from the RBI but the current income on such assets say, rent, dividend or interest etc., shall have to be repatriated to India within the prescribed time limit as specified in regulation 5(i) of Notification No.9 viz: FEMA (Realisation, Repatriation & Surrender of Foreign Exchange), 2000.

24. Process and Procedure for Compounding

(a) An application for compounding of a contravention under the FEMA may be submitted to the compounding authority (CA) either on being advised of a contravention under FEMA either through a memorandum or suo motu on being made or becoming aware of the contravention or suo motu on being made or becoming aware of the contravention. The application should be as per format given in the Foreign Exchange (Compounding Proceedings) Rules.

- (b) Application for compounding any contravention in prescribed form together with a copy of the memorandum, wherever applicable, with the prescribed fee has to be submitted with the relevant facts and supporting documents to the Compounding Authority [Cell for Effective Implementation of FEMA (CEFA)], Foreign Exchange Department, 11th Floor, Central Office Building, S.B.Singh Road, Fort, Mumbai 400 001.
- (c) The compounding authority may call for any information, record or any other documents relevant to the compounding proceedings.
- (d) Where additional information/document is called for, such additional information/document shall be submitted within 30 days or such additional period as may be given by the compounding authority from the date of the said letter. In case the contravener fails to submit the additional information/documents called for within the specified period, the application for compounding will be liable for rejection.
- (e) On receipt of the application for compounding, the proceedings would be concluded and order issued by the CA within 180 days from the date of the receipt of application for compounding.
- (f) The sum for which the contravention has been compounded shall be paid within fifteen days from the date of order of compounding.

The payment towards application fee and the sum for which contravention has been compounded shall be paid by demand draft in favour of the Compounding Authority i.e. Reserve Bank of India and payable at Mumbai.

25. Transactions under FEMA. 1999

With no restriction:

For amortisation of loan

Prohibited transaction

In the business of chit fund

Trading in Transferable Development Rights (TDR's)

Permissible transaction

Maintenance of foreign currency accounts in India and outside by a person resident in India

Investment by a person in India in foreign securities

26. Corporatisation & Demutualisation

The Corporatisation intends to make a stock exchange as a corporate entity limited by shares. In the new legislation under Section 2 (aa) the term corporatisation has been defined as "the succession of a recognised stock exchange, being a body of individuals or a society registered under the Societies Registration Act, 1860, by another stock exchange, being a company incorporated for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities carried on by such individuals or society".

Further, Demutualisation is the process of separating ownership, trading and management in a stock exchange. This process shall prevent conflict of interests, which may arise when stockbrokers involved in the management of the stock exchanges. It is defined under section 2(ab) as "the segregation of ownership and management from the trading rights of the members of a recognised stock exchange in accordance with a scheme approved by the Securities and Exchange Board of India". Until the legislation came into effect only two exchanges i.e., National Stock Exchange and OTCEI in our country were in demutualised structure. Very recently the Bombay Stock Exchange (BSE) got the approval of SEBI for its corporatisation and demutualisation.

Procedure for corporatisation and demutualisation.(Section 4B)

It provides

- (1) All recognised stock exchanges referred to in section 4A shall, within such time as may be specified by the Securities and Exchange Board of India, submit a scheme for corporatisation and demutualisation for its approval:

Provided that the Securities and Exchange Board of India may, by notification in the Official Gazette, specify name of the recognised stock exchange, which had already been corporatised and demutualised, and such stock exchange, shall not be required to submit the scheme under this section.

- (2) On receipt of the scheme referred to in sub-section (1), the Securities and Exchange Board of India may, after making such enquiry as may be necessary in this behalf and obtaining such further information, if any, as it may require and if it is satisfied that it would be in the interest of the trade and also in the public interest, approve the scheme with or without modification.
- (3) No scheme under sub-section (2) shall be approved by the Securities and Exchange Board of India if the issue of shares for a lawful consideration or provision of trading rights in lieu of membership card of the members of a recognised stock exchange or payment of dividends to members have been proposed out of any reserves or assets of that stock exchange.
- (4) Where the scheme is approved under sub-section (2), the scheme so approved shall be published immediately by –
 - (a) the Securities and Exchange Board of India in the Official Gazette;
 - (b) the recognised stock exchange in such two daily newspapers circulating in India, as may be specified by the Securities and Exchange Board of India,

and upon such publication, notwithstanding anything to the contrary contained in this Act or any other law for the time being in force or any agreement, award, judgment, decree or other instrument for the time being in force, the scheme shall have effect and be binding on all persons and authorities including all members, creditors, depositors and employees of the recognised stock exchange and on all persons having any contract, right, power, obligation or liability with, against, over, to, or in connection with, the recognised stock exchange or its members.

- (5) Where the Securities and Exchange Board of India is satisfied that it would not be in the interest of the trade and also in the public interest to approve the scheme under sub-section (2), it may, by an order, reject the scheme and such order of rejection shall be published by it in the Official Gazette:

Provided that the Securities and Exchange Board of India shall give a reasonable opportunity of being heard to all the persons concerned and the recognised stock exchange concerned before passing an order rejecting the scheme.

- (6) The Securities and Exchange Board of India may, while approving the scheme under sub-section (2), by an order in writing, restrict-
 - (a) the voting rights of the shareholders who are also stock brokers of the recognised stock exchange;
 - (b) the right of shareholders or a stock broker of the recognised stock exchange to appoint the representatives on the governing board of the stock exchange;
 - (c) the maximum number of representatives of the stock brokers of the recognised stock exchange to be appointed on the governing board of the recognised stock exchange, which shall not exceed one-fourth of the total strength of the governing board.
- (7) The order made under sub-section (6) shall be published in the Official Gazette and on the publication thereof, the order shall, notwithstanding anything to the contrary contained in the Companies Act, 1956, or any other law for the time being in force, have full effect.

- (8) Every recognised stock exchange, in respect of which the scheme for corporatisation or demutualisation has been approved under sub-section (2), shall, either by fresh issue of equity shares to the public or in any other manner as may be specified by the regulations made by the Securities and Exchange Board of India, ensure that at least fifty-one per cent. of its equity share capital is held, within twelve months from the date of publication of the order under sub-section (7), by the public other than shareholders having trading rights:

Provided that the Securities and Exchange Board of India may, on sufficient cause being shown to it and in the public interest, extend the said period by another twelve months.'

27. (a) Penalty for failure to furnish information, return, etc. (Section 15A) : If any person who, is required under this Act or any rules or regulations made thereunder.

- (i) to furnish any document, return or report to the Board, fails to furnish the same, he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.
- (ii) to file any return or furnish any information, books or other documents within the time specified therefor in the regulations, fails to file return or furnish the same, he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.
- (iii) to maintain books of accounts or records, fails to maintain the same, he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

(b) Penalty for failure by any person to enter into agreement with clients (Section 15B): If any person who, is registered as an intermediary and is required under this Act or any rules or regulations made thereunder, to enter into an agreement with his client, fails to enter into such agreement, he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

(c) Penalty for failure to redress investors' grievances (Section 15C): If any listed company or any person who is registered as an intermediary, after having been called upon by the Board in writing, to redress the grievances of investors, fails to redress such grievances within the time specified by the Board, such company or intermediary shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

PRE-EXAMINATION NOTES

AMENDMENTS TO SEBI (DIP) GUIDELINES

Securities and Exchange Board of India (SEBI)'s DIP (Disclosure Investor Protection) Guidelines have been amended vide circular dated 19th September 2005 issued to all registered Merchant Bankers/Stock Exchanges. The highlights of the amendments are:

1. Specific allocation of 5% for mutual funds within the category of qualified institutional buyers (Q1Bs)
2. Eligible bids by mutual funds to be considered in the said 5% and also in the balance available for allocation to Q1B Category.
3. 10% margin to be collected from Q1Bs.
4. Allocation to Q1Bs to be made on proportionate basis as is presently being done for retail individual investors and non-institutional investors.

These amendments are applicable to the public issues through book building route, draft offer documents in respect of which, are filed with SEBI on or after the date of this circular (given below).

[Press Release No. PR 119/2005, issued by Securities and Exchange Board of India, dated 19th September, 2005]