

GUIDELINE ANSWERS

INTERMEDIATE EXAMINATION

JUNE 2006

GROUP II



The Institute of
Company Secretaries of India

IN PURSUIT OF PROFESSIONAL EXCELLENCE

Statutory body under an Act of Parliament

ICSI House, 22, Institutional Area, Lodi Road, New Delhi 110 003

Phones : 41504444, 24617321; Fax : 011-24626727

E-mail : info@icsi.edu; Website : www.icsi.edu

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These answers have been written by competent persons and the Institute hopes that the **GUIDELINE ANSWERS** will assist the students in preparing for the Institute's examinations. It is, however, to be noted that the answers are to be treated as model answers and not as exhaustive and the Institute is not in any way responsible for the correctness or otherwise of the answers compiled and published herein.

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

C O N T E N T S

	<i>Page</i>
GROUP II	
1. Company Law ...	1
2. Company Secretarial Practice ...	19
3. Economic, Labour and Industrial Laws ...	36
4. Securities Laws & Regulation of Financial Markets ...	50

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(i)

NOTE : Guideline Answers of the last Five Sessions have been updated with a view to keep the students abreast of new developments. While updating the answers the changes and references to be consulted have been given hereinbelow :

INTERMEDIATE EXAMINATION

UPDATING SLIP

COMPANY LAW

GROUP – II – PAPER 1

<i>Examination Session</i>	<i>Question No.</i>	<i>Updating required in the answer</i>
December 2002	5(c)	SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999 have been amended. The answer be modified accordingly.
-do-	8(a)(i),(ii)	Multi-State Co-operative Societies Act, 2002 has come into force. The answer be modified accordingly.
December 2003	8(a)	Certain industries have been prohibited from appointing sole selling agents for a period of three years. The answer to be modified accordingly.

(ii)

UPDATING SLIP

ECONOMIC, LABOUR & INDUSTRIAL LAWS

GROUP – II – PAPER 3

<i>Examination Session</i>	<i>Question No.</i>	<i>Updating required in the answer</i>
December 2002	4(c)(i)	Section 107A of the Patents Act, 1970 has been amended to include 'imports' by Patents (Amendment) Act, 2005.
June 2003	1(iv)	The provisions relating to Environmental Clearances relating to Industrial Projects to be updated in accordance with Notification S.O. 60E dated 27-01-1994 (as amended in 2004).
	3(b)(v)	Update the answer with Foreign Exchange Management (Transfer or Issue of any Foreign Security) (Amendment) Regulations, 2004.
December 2003	4(c)	Section 50 of the Patents Act, 1970 amended by Patents (Amendment) Act, 2002. Answer to be amended accordingly.
June 2004	1(v)	The provisions relating to Environmental Clearances relating to Industrial Projects to be updated in accordance with Notification S.O. 60E dated 27-01-1994 (as amended in 2004).
	3(a)(ii)	Update the answer with Foreign Exchange Management (Transfer or Issue of any Foreign Security) (Amendment) Regulations, 2004.
	4(b)	Section 107A of the Patents Act, 1970 has been amended to include 'imports' by Patents (Amendment) Act, 2005.
December 2004	3(a)(iii)	Update the answer with Foreign Exchange Management (Transfer or Issue of any Foreign Security) (Amendment) Regulations, 2004.
	4(b)	Section 24A to 24F omitted by the Patents (Amendment) Act, 2005 w.e.f. 1/1/2005.

INTERMEDIATE EXAMINATION

JUNE 2006

COMPANY LAW

Time allowed : 3 hours

Maximum marks : 100

NOTE : 1. Answer **SIX** questions including Question No. 1 which is **COMPULSORY**.

2. All references to section relates to the Companies Act, 1956 unless stated otherwise.

Question 1

Distinguish between any four of the following :

- (i) 'Memorandum of association' and 'articles of association'.
- (ii) 'Trust' and 'bailment'.
- (iii) 'Transfer of securities' and 'transmission of securities'.
- (iv) 'Additional director' and 'alternate director'.
- (v) 'Dividend' and 'interest'.

(5 marks each)

Answer 1(i)

Memorandum of Association and Articles of Association

- Memorandum of Association is a document which sets out the constitution of the company and as such is the foundation on which the structure of the company stands. It defines the scope of the company's activities and its relations with outside world.
However, Articles of Association of a company are its by-laws or rules and regulations that govern the management of its internal affairs and the conduct of its business. They deal with the members of the company inter se and are subordinate to the memorandum of association.
- Memorandum of Association lays down the area beyond which the activities of the company cannot go. Articles however lay down the regulations inside that area. In other words, parameters of articles are laid down by the memorandum of association.
- The alteration of memorandum can be in limited circumstances and in the manner provided in the Act, (normally requiring permission of Central Government, Company Law Board etc.) Alteration of articles is generally permitted by a special resolution of the members.
- Acts done by a company beyond the scope of memorandum are ultra vires and void. Such acts cannot be ratified by the unanimous acts of the shareholders. However, the acts done beyond the articles can be ratified by the shareholders, as long as they are not beyond the memorandum of association.
Thus, whereas the memorandum lays down the scope and powers of the company; the articles govern the ways in which the objects of the company are to be carried out.

Answer 1(ii)**Trust and Bailment**

The definition of 'Bailment' is given in Section 148 of Indian Contract Act, 1872 and the definition of 'Trust' is given in Section 3 of Indian Trust Act, 1882. Trust is defined as an obligation annexed to the ownership of property and arising out of confidence reposed in and accepted by the owner or declared and accepted by him, for the benefit of another or of another and the owner.

On the other hand, bailment is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them.

The following are also the differences between Trust and Bailment.

1. A Trustee becomes the full owner of trust property. A bailee acquires special property only.
2. The obligation of the bailee is legal whereas that of a trustee is equitable.
3. A bailment may be created for movable property only. A trust may be created for both movable and immovable properties.

Answer 1(iii)**Transfer of Securities and Transmission of Securities**

Transmission refers to those cases where a person acquires an interest in property by operation of any provision of law, such as by right of inheritance or succession or by reason of the insolvency or lunacy of the shareholder or by purchase in a Court-sale, while a transfer is effected by act of parties [*Maheshwari Ketan Sugar Mills v. Ishwari Ketan Sugar Mills*, (1963) 2 Comp Cases 1142 (All)]. Thus transmission is the transfer by operation of law or involuntary assignment.

Distinction between Transfer and Transmission of Securities

The distinction between transfer and transmission of securities is as under :

1. Transfer takes place by a voluntary act of the transferor while transmission is the result of the operation of law.
2. An instrument of transfer is required in case of transfer but no instrument of transfer is required in case of transmission.
3. Transfer is a normal course of transferring property whereas transmission takes place on death or insolvency of a shareholder.

Answer 1(iv)**Additional Director**

Section 260 of the Companies Act, 1956 provides that if the articles of association of a company empower its directors to appoint additional directors, the Board of directors may exercise such power. However, such additional director shall hold office only upto the date of the next Annual General Meeting of the Company. Further, the number of

additional directors together with the existing directors shall not exceed the maximum number fixed for the Board by articles.

If the annual general meeting is not held or cannot be held, the person appointed as additional director vacates his office on the last day on which AGM should have been held. He cannot continue in office thereafter on the ground that the meeting was not or could not be called within the time prescribed in the Section.

Alternate Director

The Board of Directors of a Company may if so authorized by its articles or by a resolution passed by the Company in a General Meeting, appoint an Alternate Director in accordance with Section 313 to act for the director during his absence for a period of not less than three months from the state in which meetings of the Board are ordinarily held. An Alternate Director shall not hold office as such for period of longer than that permissible to the original director in whose place he has been appointed and shall vacate office as and when the original director returns to the State in which meetings of the Board are ordinarily held.

The following provisions are not applicable to Alternate Director

- (a) Appointment of an Alternate Director is not considered as an increase in the strength of the Board of Directors.
- (b) Alternate directorship held by a person cannot be counted for maximum number of directorship, which a person can hold.
- (c) An Alternate Director is not required to hold any qualification shares.

Answer 1(v)

Dividend and Interest

Dividend being the return on share capital subscribed for and paid by a company to its shareholders, as per Section 205, may be paid out of the following three sources only viz., current profits, profits for any previous financial year or years and out of moneys provided by the Central or State Government for the payment of dividend. Accordingly, dividends are not allowed to be declared out of capital. However, Section 208, is in effect an exception to this, which provides that where shares are issued to raise money to defray the cost of works or building or of plant, which cannot be made profitable for a long period, the company may pay interest on the amount of capital paid up in respect of such shares, and may charge the same to capital, subject to the conditions specified in Section 208 of the Act.

Dividend is paid on shares in a company whereas interest is paid on debentures and long-term debt and short-term borrowings/ loans including fixed deposits. Interest is a debt, which like all debts is paid out of the company's assets generally. A dividend however becomes a debt only after the Company has declared it. Dividend cannot be paid out of the assets of the Company generally as it can be declared only out of the profit available for the purpose. Interest is a charge on profits while dividend is an appropriation of profits. The power to pay dividend is inherent in a company and is not derived from the Companies Act, 1956 or the Memorandum or Articles of Association although the Act and the Articles generally regulate the manner in which dividends are to be declared.

Question 2

- (a) *The Board of directors of an Indian company passed a resolution for incorporation of a company in Singapore with the initial paid-up capital of \$10,000. Comment whether investment to be made in the Singapore company is exempt from the provisions of Section 372A.*
- (b) *Gold Ltd. is a listed company with paid-up capital of Rs. 125 crore and free reserves of Rs.250 crore. Silver Pvt. Ltd. has approached Gold Ltd. for a loan of Rs. 300 crore to set up a manufacturing plant. Comment whether Gold Ltd. can give aforesaid loan to Silver Pvt. Ltd. keeping in view that Raman is a director in both the companies.*
- (c) *Inspection of profit and loss account of a private limited company is permitted only to the members of the company. Comment.*
- (d) *How will you ascertain the depreciation of assets, which is destroyed before providing for depreciation in full ?* (4 marks each)

Answer 2(a)

Provisions of Section 372A of the Companies Act, 1956 will be attracted as the restrictions contained therein are applicable to investments in a body corporate. As a company incorporated in Singapore will be a body corporate there will be no exemption.

Therefore, investment made by the company for incorporation of a company in Singapore has to be within the prescribed parameters and not exempt as specified under Section 372A(8) of the Companies Act, 1956. However, further investment in Singapore Company, if any, (after making it a wholly owned subsidiary) will be exempted.

Answer 2(b)

As per Section 372A read with Section 295 of the Companies Act, 1956 prior approval of Central Government is required for the giving of loan by a Public Limited Company to a Private Limited Company in which a director of Public Company is a Director or member.

Further, as per Section 372A(1), the loan should not exceed sixty per cent of the lending company's paid up share capital and the reserves or one hundred per cent of its free reserves, whichever is more unless previously authorized by a special resolution passed in a general meeting.

In the given case amount of loan proposed i.e. Rs. 300 crores, is in excess of 60% of the paid up capital and free reserves of the Public Ltd. Company or 100% of the free Reserves of the Company. [60% of 375 crores = Rs. 225 crores; 100% of 250 crores = 250 crores].

Hence Gold Limited has to obtain prior approval of Central Government and approval of its shareholders by passing Special Resolution.

Answer 2(c)

Proviso to Section 220(1) of the Companies Act, 1956 provides that in case of

- (a) a private company which is not a subsidiary of public company;
- (b) a private company whose entire paid up capital is held by one or more bodies corporate incorporate outside India;

no person other than a member of the company concerned shall be entitled to inspect or obtain copies of the profit and loss account of that company under Section 610 of the Act.

If a person seeks inspection of the profit and loss accounts of a private company, the Registrar should make sure that he is a member of the Company by referring to the list of members and demanding to see share scrip duly endorsed in his favour.

Answer 2(d)

Section 350 of the Companies Act, 1956, provides that the amount of depreciation to be deducted is the amount of depreciation on assets as shown by the books of the company at the end of the financial year at the rates specified in Schedule XIV of the Act. Under proviso to Section 350 where any asset is sold, discarded, demolished or destroyed for any reason before depreciation of such asset has been provided for in full, the excess if any, of the written down value of such asset over its sale proceeds or as the case may be, its scrap value shall be written off in the financial year in which the asset is sold, discarded, demolished or destroyed.

Question 3

- (a) Explain 'lifting of corporate veil'.
- (b) Explain powers of the Company Law Board to prevent oppression or mismanagement. (8 marks each)

Answer 3(a)

A company is clothed with a distinct personality by the provisions of law, but in reality it is an association of persons who are in fact, in a way, the beneficial owners of the property of the body corporate. But as the separate personality of the company is a statutory privilege, it must be used for legitimate business purposes only. Where a fraudulent and dishonest use is made of the legal entity, the individuals concerned are not allowed to take shelter behind the corporate personality. The Courts then breakthrough the corporate shell and apply the principle of "lifting or piercing the corporate veil".

Courts have found it necessary to disregard the separate personality of a company in the following situations:

- (a) Where the corporate veil has been used for commission of fraud or improper conduct, Courts have lifted the veil and looked at the realities of the situation e.g. In *Gilford Motor Co. v. Horne*, (1933) 1 Ch. 935. Where a former employee of a company made a covenant not to solicit its customers but formed a company which undertook solicitation the principle was applied.
- (b) Where a corporate facade is really only an agency instrumentality e.g. In *Re. R.G. Films Ltd.* (1953).
- (c) Where the doctrine conflicts with public policy: Courts have lifted the corporate veil for protecting the public policy e.g. In *Connors Bros. v. Connors* (1940) 4 All E.R. 179, the principle was applied against the managing director who made use of his position contrary to public policy and the company was determined to be of enemy character, the native countries being at war.

- (d) For determining the character or status of the company the Court may ignore the separate entity [*Daimler Co. Ltd. v. Continental Tyre & Rubber Co.*, (1916) 2 A.C. 307].
- (e) Where the veil has been used for evasion of taxes and duties, the Court upheld the piercing of the veil to look at the real transaction. (*Commissioner of Income Tax v. Meenakshi Mills Ltd.*, A.I.R. 1967 S.C. 819).
- (f) Where it was found that the sole purpose for which the company was formed was to evade taxes the Courts have ignored the concept of separate entity and made individuals liable to pay taxes [Re *Sir Dinshaw Manakjee Petit*, A.I.R. 1927 Bombay 371].
- (g) Where the company has been formed for the avoidance of welfare legislation such as to reduce the amount to be paid by way of bonus to workmen, the principle of lifting of corporate veil has been upheld.
- (h) In quasi criminal cases also, the Courts have sometimes applied the doctrine.
- (i) Where it is found that a company has abused its corporate personality for an unjust and inequitable purpose, the principle has been applied.

Answer 3(b)

Section 402 defines the powers of the CLB to prevent oppression and mismanagement. This section provides that without prejudice to the generality of the powers of the CLB, any order under Section 397 or, 398 passed by it for prevention of oppression and mismanagement, may provide for:

1. The regulation of the conduct of the company's affairs in future.
2. The purchase of the shares or interest of any member of the company by other members or by the company.
3. In the case of purchase of its shares by the company, the consequent reduction of its share capital.
4. The termination, setting aside or modification of and agreement between the company and managing director, or any other director, and the manager upon such terms and conditions as may, in its opinion, be just and equitable in all the circumstances of the case.
5. The termination, setting aside or modification of any agreement between the company and any person, (other than stated above) provided due notice has been given to him and his consent obtained.
6. Setting aside of any fraudulent preferences made within three months before the date of the application.
7. Any other matter for which, in the opinion of the court, it is just and equitable that provision should be made.

If the Company Law Board pursuant to Section 397 or 398 orders any alteration of the memorandum or articles of the company, the company shall not be at liberty to introduce any provision inconsistent with the order without the leave of CLB [Section 404]. If the order sets aside or modifies any agreement with any management personnel referred to in Section 402, it will not give rise to any claim for damages or compensation for loss of office [Section 407 (1) (a)]. Further any managerial personnel

whose appointment is so set aside shall not be capable of serving the company in any managerial capacity for the period of five years except with the leave of the Company Law Board [Section 407 (1) (b)]. Where the CLB for the purposes of fulfilling the objects of Section 397, orders the company to purchase the shares of the outgoing shareholders, the other provisions of the Act, like those of Section 77A, would not be attracted. [*Gurmit Singh v. Polymer Papers Ltd.* (2003) 45 SCL 251 (CLB-ND)].

Question 4

- (a) *Bright Ltd. desires to raise funds by accepting deposits from the public. Explain the provisions relating to acceptance of deposits.* (10 marks)
- (b) *Explain —*
- (i) *Sweat equity; and*
 - (ii) *Employees' Stock Option Scheme (ESOS).* (3 marks each)

Answer 4(a)

Salient provisions for inviting deposits from the public

According to Section 58A(2) of the Act, if any non-banking, non-financial company wants to invite, or allow any other person to invite or cause to be invited on its behalf, any deposit, it must satisfy the following conditions:

- (a) such deposit is invited or is caused to be invited, in accordance with the rules made under sub-section (1);
- (b) an advertisement, including therein a statement showing the financial position of the company, has been issued by the company in such form and in such manner as may be prescribed; and
- (c) the company is not in default in the repayment of any deposit, or part thereof and any interest thereupon in accordance with the terms and conditions of such deposit.

Accordingly, 'deposit' should be as per explanation to Section 58A and Rule 2(b) of Companies (Acceptance of Deposits) Rules, 1975.

An invitation of deposits from the public at large, or any section of the public will require an advertisement to be published in the newspapers. Therefore:

- (i) A company may invite deposits from the public only after the publication of an advertisement in newspapers. The company must prepare the text of the advertisement containing the particulars laid down in Rule 4(2) of the Deposit Rules and also the highlights and major features of the scheme(s) of deposits.
- (ii) Arrange for the text of the advertisement to be translated into vernacular language, i.e. the main language of the State in which the registered office of the company is situated [Rule 4(1)].
- (iii) Place both the texts of the advertisement before the Board at its meeting and pass a resolution approving the texts.
- (iv) After the text of the advertisement has been approved by the Board and signed by the majority of directors, arrange to file one copy of the text of the advertisement with the Registrar alongwith the requisite filing fee.

- (v) Arrange for publication of the advertisement at least once in a leading English newspaper and once in a vernacular newspaper, circulating in the State in which the registered office of the company is situated.

A non-banking non-financial company, intending to accept deposits without making an invitation to the public by advertisement, must ensure that a statement in lieu of advertisement has been filed in the manner prescribed under the Rules.

No deposit should be taken which is repayable—

- (a) On demand; (b) On notice; (c) Within six months from the date of acceptance/renewal unless it is eligible for the exception under the proviso to Rule 3(l)(a); (d) After thirty-six months from the date of acceptance /renewal.

The rate of interest payable on any deposit should not be more than the rate prescribed under the Deposit Rules. If the company proposes to make repayment of any deposit before the date of expiry of the period for which it was taken, ensure that it is done at a reduced rate of interest in accordance with the provisions of Rule 8. The brokerage payable on deposits should not be more than the rates prescribed under the Deposit Rules. The current rates are as follows:

Deposit for a period up to one year: 1% of the amount of deposit.

Deposit for a period of more than one year but up to two years: 1.5% of the amount of deposit.

Deposit for a period exceeding two years but up to three years: 2% of the amount of deposit.

A company with a net owned fund of less than rupees one crore cannot invite deposits as per the Rules. At no point of time, a company should accept deposits in excess of the limits under Rule 3(2).

If the company has accepted any deposits to which the provisions of the Deposit Rules are applicable, the company must deposit/invest before 30th April of each year, a sum constituting at least 15% of the amount of deposits maturing during the year, ending on the 31st day of March, next following in the methods provided in Rule 3A.

The company must ensure that—

- (a) An application form (to be procured from every depositor, duly filled in and signed by the depositor(s), is accompanied by the text of the advertisement/statement in lieu of advertisement and the terms and conditions subject to which the deposit is accepted;
- (b) The application form also contains a declaration to the effect, that the amount of deposit is not being given out of funds acquired by the depositor, by borrowing or accepting deposits from any other person.
- (c) A receipt of the deposit received, is issued to every depositor within eight weeks from the date, on which money is received or cheque/demand draft is realized (Rule 6).
- (d) The receipt is issued in respect of a fresh deposit, as well as for the renewal of an existing deposit (Rule 7).

- (e) A register of deposits is kept at the registered office of the company in accordance with Rule 7.

If the company has invited/accepted any deposits to which the provisions of the Deposit Rules apply-

- (a) Prepare a return of deposits in the form appended to the Deposits Rules, in relation of the position as on the 31st day of March of that year;
- (b) Get it certified by the auditors of the company and signed by a director or an authorized officer of the company; and
- (c) File the return with the Registrar on or before the 30th day of June every year. [Rule 10].

Answer 4(b)(i)

Section 79A of the Companies Act, 1956 inserted by the Companies (Amendment) Act, 1999 allows companies to issue sweat equity shares of a class of shares already issued.

The expression “sweat equity shares” means equity shares issued by the company to employees or directors at a discount for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

All the limitations, restrictions and provisions relating to equity shares are equally applicable to sweat equity shares issued by the companies.

Answer 4(b)(ii)

The term ‘Employee Stock Option Scheme’ (ESOS) has been defined under Sub-section (15A) of Section 2 of the Companies Act, 1956, according to which ‘employee stock option’ means the option given to the whole-time directors, officers or employees of a company, which gives such directors, officers or employees the benefit or right to purchase or subscribe at a future date, the securities offered by the company at a pre-determined price.

SEBI has issued SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999 according to which Employee Stock Option Scheme means a scheme under which the company grants option to its employees and option means a right but not an obligation granted to an employee in pursuance of ESOS to apply for shares of the company at a pre-determined price.

Question 5

Explain the various aspects relating to —

- (i) *Preferential allotment of shares by a listed company.* (10 marks)
- (ii) *Rights issue of shares by an unlisted company.* (6 marks)

Answer 5(i)

Procedure for Preferential Issue

Board Meeting – Convene a Board meeting to decide about the issue of shares in

terms of Section 81(1A) of the Companies Act, 1956 and to fix up the date, time, place and agenda for calling a general meeting to pass a special resolution.

Intimation to stock exchange – Immediately within 15 minutes of the closure of the Board meeting, intimate to the concerned stock exchange by fax/letter/telegram about the short particulars of such alteration of share capital.

In principle approval from stock exchange - In principle approval for listing from the stock exchange(s) should be taken in respect of proposed preferential issue.

General meeting – Notice of the general meeting together with explanatory statement shall be sent to the eligible members and auditors of the company at least 21 clear days before the date of general meeting.

In case of listed company, 3 copies of the notice of the meeting should be sent to stock exchange. The general meeting should be duly held.

Explanatory statement should cover all the requisite matters set out in SEBI Guidelines. Auditors' Report certifying that the issue is in accordance with SEBI Guidelines should be laid before and kept open for inspection of the shareholders at the meeting.

Pricing to be specified in the resolution – The issue of shares on a preferential basis can be made at a price not less than the higher of the following:

- (i) The average of the weekly high and low of the closing prices of the related shares quoted on the stock exchange during the six months preceding the relevant date;

OR

- (ii) The average of the weekly high and low of the closing prices of the related shares quoted on a stock exchange during the two weeks preceding the relevant date.

The resolution to be passed under Section 81(1A) shall clearly specify the relevant date on the basis of which price of the resultant shares shall be calculated. Relevant date for this purpose shall mean the date thirty days prior to the date, on which the meeting of general body of shareholders is held.

Forwarding copy of proceeding of general meeting to stock exchange - In case of a listed company, send a copy of the proceedings of the general meeting to the stock exchange.

Dematerialisation – A preferential issue of shares shall not be made unless the entire shareholding of such person to the company, if any, is held by him in dematerialized form.

Allotment within 15 days of the passing of the resolution - Allotment pursuant to any resolution passed at a meeting of shareholders of a company granting consent for preferential issues of any financial instrument, shall be completed within a period of 15 days from the date of passing of the resolution.

If allotment of instruments and despatch of certificates is not completed within 15 days from the date of such resolution, a fresh consent of the shareholders shall be obtained and the relevant date referred to above will relate to the new resolution.

Valuation report to be submitted to the stock exchange - In case of preferential allotment of shares to promoters, their relatives, associates and related entities, for

consideration other than cash, valuation of the assets in consideration for which the shares are proposed to be issued shall be done by an independent qualified valuer and the valuation report shall be submitted to the exchanges on which shares of the issuer company are listed.

Return of allotment - A return of allotment in Form No. 2 shall be filed within 30 days of allotment with the concerned Registrar of Companies after paying the requisite fees.

Lock-in period on shares allotted to promoters

The shares allotted on preferential basis to promoters or promoters group shall be subject to lock-in period of three years from the date of allotment. However, not more than 20 per cent of total capital of the company, including capital brought in by way of preferential issue shall be subject to such lock-in period.

The entire pre preferential allotment shareholding of allottees to whom shares etc. are issued on preferential basis, shall be under lock-in from the relevant date upto a period of six months from the date of preferential allotment.

Disclosure in the balance sheet – The details of all monies utilised out of the preferential issue proceeds shall be disclosed under an appropriate head in the balance sheet of the company indicating the purpose for which such monies have been utilized. The details of unutilized monies shall also be disclosed under a separate head in the balance sheet indicating the form in which such unutilized monies have been invested.

Preferential allotments to FIIs – Preferential allotments, if any to be made in case of FIIs shall also be governed by guidelines issued by Government of India/SEBI/RBI etc.

Filing of Form No. 23 – Within 30 days of passing the special resolution Form No. 23 shall be filed ROC after paying the requisite fee.

Listing – File documents for listing of shares with the stock exchange.

Answer 5(ii)

Section 81 of the Companies Act provides for the issue of “Rights Shares” and states that whenever at any time after expiry of two years from the incorporation of a company or after the expiry of one year from the first allotment of shares, whichever is earlier, it is proposed to increase the subscribed capital by allotment of further shares, such shares shall be offered to the existing holders of equity shares in proportion to the capital paid-up on their shares at the time of further issue.

The company must give notice to each of the equity shareholders, giving him option to take the shares offered to him by the company. The shareholder must be informed of the number of shares he has opted to buy giving him at least 15 days to decide. If the shareholder does not convey to the company his acceptance of the company’s offer of further shares he shall be deemed to have declined the offer. Unless the articles of the company otherwise provide, the directors must state in the notice of offer of rights shares the fact that the shareholder has also the right to renounce the offer in whole or in part, in favour of some other persons.

If a shareholder has neither renounced in favour of another person nor accepted the shares himself, the Board of directors may dispose of the shares so declined in such manner as it thinks would be most beneficial to the company.

Section 81(1A) deals with issue of shares to persons other than existing shareholders and provides that a company can issue further shares to persons other than existing shareholders in any manner whatsoever provided —

- (a) if a special resolution to that effect is passed by the company in general meeting, or
- (b) where no such special resolution is passed, if the votes cast (whether on a show of hands, or on a poll, as the case may be) in favour of the proposal contained in the resolution moved in that general meeting (including the casting vote, if any of the Chairman) by members who, being entitled so to do, vote in person, or where proxies are allowed, by proxy, exceed the votes, if any, cast against the proposal by members so entitled and voting and the Central Government is satisfied, on an application made by the Board of directors in this behalf, that the proposal is most beneficial to the company.

The restrictions contained in Section 81 of the Act regarding issue of further shares do not apply to:

- (i) a private company;
- (ii) increase of the subscribed capital of public company caused by the exercise of an option attached on debentures issued or loans raised by the company to convert such debentures or loans into shares of the company or to subscribe for shares in the company [Section 81(3)].

Provided the terms containing such an option:

- (a) have been approved by the Central Government before the issue of debentures or raising of loans is in conformity with the rules made by the Government; and
- (b) have been approved by a special resolution passed in the general meeting before the issue of debentures or raising of loans in cases where the debentures have not issued to or loans raised from the Government or any institutions specified by the Government.
- (c) conversion of part or whole of the debentures issued to or loans raised from the Government in shares of the company in pursuance of a direction issued by the Central Government in public interest on such terms and conditions as appear to be fair and reasonable to the Central Government even if such debentures/loans do not contain a term providing for option for conversion of debentures/loans into shares of the company.

Question 6

- (a) *State the disqualifications of a director.* (6 marks)
- (b) *Debentureholders are widely protected under the Companies Act, 1956 in case of defaults in making their payments by the company. Discuss.* (5 marks)
- (c) *Suresh, a solicitor, is appointed as director on the Board of Sam Organic Ltd. The company has obtained legal opinion from Suresh and paid a fee of Rs. 5 lakh during the financial year 2004-05. Auditor has raised an objection that fee payable to Suresh exceeds the limit prescribed under sections 309 and 198 and hence payment made to him is illegal, as the company has not obtained*

permission from the Central Government. Therefore, the company should take steps to recover the same from Suresh. Keeping in view the provisions of the Companies Act, 1956, give your opinion on the objection raised by the auditor.
(5 marks)

Answer 6(a)

The salient disqualifications of a director are laid down in Section 274 of Companies Act, 1956.

They are as –

Disqualifications of directors.—(1) A person shall not be capable of being appointed director of a company, if—

- (a) he has been found to be of unsound mind by a Court of competent jurisdiction and the finding is in force;
- (b) he is an undischarged insolvent;
- (c) he has applied to be adjudicated as an insolvent and his application is pending;
- (d) he has been convicted by a Court of any offence involving moral turpitude and sentenced in respect thereof to imprisonment for not less than six months, and a period of five years has not elapsed from the date of expiry of the sentence;
- (e) he has not paid any call in respect of shares of the company held by him, whether alone or jointly with others, and six months have elapsed from the last day fixed for the payment of the call; or
- (f) an order disqualifying him for appointment as director has been passed by a Court in pursuance of Section 203 and is in force, unless the leave of the Court has been obtained for his appointment in pursuance of that section;
- (g) such person is already a director of a public company which,—
 - (A) has not filed the annual accounts and annual returns for any continuous three financial years commencing on and after the first day of April, 1999; or
 - (B) has failed to repay its deposit or interest thereon on due date or redeem its debentures on due date or pay dividend and such failure continues for one year or more:

Provided that such person shall not be eligible to be appointed as a director of any other public company for a period of five years from the date on which such public company in which he is a director failed to file annual accounts and annual returns under sub-clause (A) or has failed to repay its deposit or interest or redeem its debentures on due date or pay dividend referred to in clause (B).

However, the Central Government may, by notification in the Official Gazette remove the disqualification by virtue of clause (d) and (e) of Sub-section (1).

Answer 6(b)

Pursuant to Section 117C(3) of the Companies Act, 1956, the company is bound to pay interest and redeem the debentures in accordance with the terms and conditions of their issue.

If the company fails to redeem the debentures on the date of maturity the CLB may on the application made by the debenture holders (singly or jointly) after hearing the parties concerned, direct by order, the company to redeem the debentures forthwith by the payment of principal and interest thereon. [Section 117C(4)].

If defaults are made in complying with the order of the CLB, every officer of the company who is in default, shall be punishable with imprisonment which may extend to three years and shall also be liable to fine of not less than Rs. 500/- for every day during which defaults continues. Also, the defaulter company cannot accept deposits, make loans/investments etc.

This remedy is available whether the debenture holders are secured or unsecured.

Section 274(1)(g) also imposes a disqualification on the directors of a company which has failed to redeem its debentures on due date and such failure continues for one year or more.

The remedies available to a debenture holder vary according to the position i.e. whether he is secured or unsecured.

Answer 6(c)

Pursuant to Section 309(1), the remuneration payable to the directors of a company, including any managing or whole-time director, shall be determined, in accordance with and subject to the provisions of Section 198 and Section 309, either by the articles of the company, or by a resolution or, if the articles so require, by a special resolution, passed by the company in general meeting and the remuneration payable to any such director determined as aforesaid shall be inclusive of the remuneration payable to such director for services rendered by him in any other capacity.

However, any remuneration for services rendered by any such director in any other capacity shall not be so included if—

- (a) the services rendered are of a professional nature, and
- (b) in the opinion of the Central Government, the director possesses the requisite qualifications for the practice of the profession.

In the present case the matter should have been put up before the shareholders at the AGM for their approval. Simultaneously, an application should have been made to the Central Government for obtaining their opinion that Mr. Suresh is competent to render professional services which he rendered to the company. As the same have not been obtained, the contention of the auditor appears to be valid.

Question 7

- (a) Write a short note on 'pledge of shares held in demat mode'.
- (b) What is the meaning of 'specified number' referred to in Section 224(1B) ?
- (c) The Board of directors of Shinewell Ltd. in its meeting held on 24th April, 2005 has declared interim dividend. Subsequently, the Board came to know that accounts were not made properly and hence, interim dividend declared is not justifiable and it is necessary to revoke the interim dividend. What steps will you take to revoke the payment of interim dividend ?

- (d) *What do you understand by 'bonus shares' and what are the advantages of issuing bonus shares ?*
(4 marks each)

Answer 7(a)

Regulation 58 of SEBI (Depository and Participants) Regulations, 1996 deals with the provision relating to manner of creating pledge or hypothecation of securities held in demat mode.

For the purpose of creating pledge the Depository Participant (DP) should ensure that –

- (a) an application is submitted by the client to the depository through the participant;
- (b) note of pledge should be made in the records only after ensuring that sufficient security balances are available for pledge;
- (c) DP should confirm creation of pledge to the Depository within 15 days of receipt of the application;
- (d) DP should inform the pledger as well as pledgee about the creation of pledge;
- (e) if the DP does not create the pledge, an intimation to this effect should be sent to the participants alongwith reasons.

The entry of pledge so made can also be cancelled by the depository on an application made to it by the pledgeor or pledgee through the participant and an intimation to each of them shall be made in this regard by the depository.

Answer 7(b)

For the purpose of Section 224(1B) of the Companies Act, 1956, the term “Specified Number” means:

- (a) in case of a person or firm holding appointment as auditor of a number of companies each of which has a paid up share capital of less than Rs. 25 lacs, twenty such companies.
- (b) In any other case, 20 companies out of which not more than ten shall be companies each of which has a paid up capital of Rs. 25 lacs or more.
[Explanation I of Section 224(1C)].

In computing the specified number, the number of companies in respect of which or any part of which any person or firm has been appointed as an auditor, whether singly or in combination with any other person or firms shall be taken into account.
[Explanation II of Sub-section (1C) of Section 224].

Answer 7(c)

A dividend once declared (including the interim dividend) becomes debt and cannot be revoked except with the consent of the shareholders. But if the declaration is not supported by available profits it is no declaration and hence the decision could be rescinded.

If a dividend is declared and paid to shareholders, the character of the payment cannot be altered by a subsequent resolution.

The following steps should be taken for revocation of interim dividend:

1. The Board of Directors shall consider the reason for revocation and pass the necessary resolutions rescinding the previous resolution declaring interim dividend.
2. The revocation of dividend shall be decided before dispatch of warrants to shareholders.
3. Suitable news inserted in any news paper having wide circulation shall indicate in brief the reasons for revocation of interim dividend and regretting the inconvenience caused to the shareholders.

Answer 7(d)

A Company may issue fully paid up bonus shares by capitalizing its profits provided Articles of Association contains provision in this regard. When a Company is prosperous and accumulates large distributable profits, it converts these accumulated profits into capital and divides the capital among the existing members in proportion to their entitlements. The members do not have to pay any amount for such shares. The bonus shares allotted to the members do not represent taxable income in their hands. The vesting of the rights in the bonus shares takes place when the shares are actually allotted and not from any earlier date.

The advantages of bonus shares are as follows:

1. Fund flow is not affected adversely.
2. Market value of the shares comes down to their nominal value by issue of bonus shares.
3. Market value of the members' shareholding increases with the increase in number of shares in the Company.
4. Bonus shares are not an income. Hence it is not taxable.
5. Paid up share capital increases with the issue of bonus shares.

Question 8

- (a) *State the provisions relating to payment of remuneration to non-executive directors.*
- (b) *Explain the concept of 'producer company'.*
- (c) *Vinay was appointed as an additional director by the Board of directors of Prudent Ltd. in its meeting held on 20th July, 2005. Further, Vinay was appointed as a director by members of the company in its annual general meeting held on 2nd September, 2005. Comment whether Vinay is again required to file consent to act as a director.*
- (d) *State whether a company can appoint more than one Company Secretary keeping in view the increasing compliance requirements. (4 marks each)*

Answer 8(a)

Section 309 (4) of the Companies Act provides that a director who is neither in the whole time employment of the Company nor a Managing Director may be paid remuneration either

- (a) by way of a monthly, quarterly or annual payment with the approval of the Central Government; or
- (b) by way of commission if the Company by special resolution authorize such payment.

However, in either case the remuneration paid to such director or where there are more than one such directors to all of them together shall not exceed

- (i) one percent of the net profits of the Company if the Company has Managing or Whole-time Director or manager
- (ii) three percent of the net profits of the Company in any other case.

The Company in general meeting may with the approval of the Central Government authorize the payment of commission at a rate higher than 1% or 3% of the net profit as the case may be. The special resolution by which payment sanctioned will remain in operation for not more than five years but may be renewed for five years term from time to time provided the renewal is made in the last year of the previous terms. The percentage of 1% and 3% should include sitting fees, if any paid by the company.

Answer 8(b)

A Producer company means a body corporate, having objects or activities specified in Section 581B and registered as Producer Company. Hence, the objectives for which Producer Companies may be formed are laid down in Section 581B. Section 581B provides that —

(1) The objects of the Producer Company shall relate to all or any of the following matters, namely:—

- (a) production, harvesting, procurement, grading, pooling, handling, marketing, selling, export of primary produce of the Members or import of goods or services for their benefit:

Provided that the Producer Company may carry on any of the activities specified in this clause either by itself or through other institution;

- (b) processing including preserving, drying, distilling, brewing, vinting, canning and packaging of produce of its Members;
- (c) manufacture, sale or supply of machinery, equipment or consumables mainly to its Members;
- (d) providing education on the mutual assistance principles to its Members and others;
- (e) rendering technical services, consultancy services, training, research and development and all other activities for the promotion of the interests of its Members;

- (f) generation, transmission and distribution of power, revitalisation of land and water resources, their use, conservation and communications relatable to primary produce;
- (g) insurance of producers or their primary produce;
- (h) promoting techniques of mutuality and mutual assistance;
- (i) welfare measures or facilities for the benefit of Members as may be decided by the Board;
- (j) any other activity, ancillary or incidental to any of the activities referred to in clauses (a) to (i) or other activities which may promote the principles of mutuality and mutual assistance amongst the Members in any other manner;
- (k) financing of procurement, processing, marketing or other activities specified in clauses (a) to (j) which include extending of credit facilities or any other financial services to its Members.

Pursuant to Sub-section (2) every Producer Company shall deal primarily with the produce of its active Members for carrying out any of its objects specified in this section.

Answer 8(c)

Pursuant to Section 264(2)(b), a person other than an additional or alternate director, or a person filling a casual vacancy in the office of a director under Section 262, appointed as a director or re-appointed as an additional or alternate director, immediately on the expiry of his term of office shall not act as a director of the company unless he has within thirty days of his appointment signed and filed with the Registrar his consent in writing to act as such director.

Therefore, as Mr. Vinay already appointed as additional director is re-appointed as a director immediately on the expiry of his term, no fresh consent should be filed.

Answer 8(d)

Section 383A(1) of the Companies Act 1956 makes it obligatory for every company having a prescribed share capital to have a whole time secretary. This shall mean that the Company should have a minimum of one secretary. In practice, there is no bar on appointment of two or more secretaries in a single company. Hence if there are two or more secretaries in a company, it shall not be in violation of the provisions of this section. However, Form no. 32 shall be filed with ROC in respect of every individual appointed as secretary of the Company.

COMPANY SECRETARIAL PRACTICE

Time allowed : 3 hours

Maximum marks : 100

NOTE : Answer SIX questions including Question No. 1 which is **COMPULSORY**.

Question 1

Draft the specimen resolutions with requisite explanatory statement, if necessary, for transacting the following items of business indicating the kind of meeting at which each resolution is to be passed and the type of resolution required for :

- (i) *Changing the registered office of a company from Nariman Point, Mumbai to New Delhi.*
- (ii) *Appointing Abhishek as a director in a vacancy caused by the death of Bhupesh.*
- (iii) *Donating a sum of Rs. 2 lakh to the Navrozji Tata Education Fund.*
- (iv) *Increasing the borrowing limit of a company to Rs. 15 crore.*

(5 marks each)

Answer 1(i)

Type of Resolution = Special Resolution

Kind of Meeting = General Meeting

“RESOLVED THAT—

- (i) pursuant to Section 17(1) and other applicable provisions, if any, of the Companies Act, 1956 and subject to confirmation by the Company Law Board, as prescribed in sub-section (2) of the said section, the memorandum of association of the company be altered so as to change the place of the company's registered office from its present situation at Nariman Point, Mumbai in the State of Maharashtra to New Delhi, by substituting the words 'in the State of Maharashtra' for the words "New Delhi" in Clause II of the memorandum of association of the company.”
- (ii) the Company Secretary, Shri be and is hereby authorised—
 - (i) to make, on behalf of the company, the petition under Sub-section (2) of Section 17 of the Act to the Company Law Board for securing confirmation to the alteration to the memorandum of association of the company so as to change the place of the Registered office of the company from the State of Maharashtra to New Delhi .
 - (ii) to file, along with the petition, his memorandum of appearance before the concerned Bench of the Company Law Board as and when summoned to do so and represent the company in all hearings concerning the petition of the company; and
 - (iii) to appoint, on behalf of the company, Company Secretaries in Practice, advocates, lawyers, counsels and other consultants, if and when required to represent the company and plead on its behalf before the concerned Bench of the Company Law Board and or any other agency in all matters connected with the petition of the company.

Explanatory Statement

When the company was incorporated it was decided that the main manufacturing unit of the company would be located in the Mumbai, State of Maharashtra and in the memorandum of association it was stated that the registered office of the company would be situated in that State.

Subsequently it was found that the location of the main manufacturing unit in New Delhi would be more advantageous to the company. For better management and control, the Head Office of the company has already been shifted to New Delhi. No useful purpose would be served by continuing to keep the company's registered office in the State of Maharashtra. Moreover, 90 % of the members of the company have their registered addresses in the New Delhi. The directors, therefore, consider that the memorandum of association of the company should be altered so as to change the place of its registered office from its present situation at Mumbai in the State of Maharashtra to New Delhi.

After the proposal is approved by the shareholders, a petition is required to be made, under Section 17(2) of the Companies Act, 1956, to the Company Law Board for confirmation of the alteration to the memorandum of association of the company so as to shift the company's registered office from the State of Maharashtra to the New Delhi. Therefore, the proposed resolution also seeks authority to the Company Secretary to make the said petition to the Company Law Board on behalf of the company.

The Board commends the resolution to the members for their consideration and approval.

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

Answer 1(ii)

Type of Resolution = *Board Resolution*

Kind of Meeting = *Board Meeting*

“Resolved that Abhishek be and is hereby appointed as a Director of the Company in the casual vacancy arising out of the untimely demise of Bhupesh, in accordance with Section 262 of the Companies Act, 1956 and Article — of the Company's Articles of Association”.

Answer 1(iii)

Type of Resolution = *Ordinary Resolution*

Kind of Meeting = *General Meeting*

“RESOLVED THAT pursuant to the provisions of Section 293(1)(e) and other applicable provisions, if any, of the Companies Act, 1956, approval be and is hereby accorded to the Board of Directors of the Company for donating a sum of Rs.2,00000 (Rupees two lakhs only) to the Navrozji Tata Education Fund”.

Explanatory Statement:

As part of the Company's social uplift programme, the Board of Directors intend donating a sum of Rs.2,00000/- to the Navrozji Tata Education Fund set up by Tata

Sons Ltd. to promote higher education in the fields of engineering and medical sciences. The Fund has a panel comprising eminent industrialists, scientists, and doctors to select and award merit scholarships to deserving, capable students desiring to pursue advanced studies in engineering and medicine. The Board commends the accompanying resolution for the shareholders' approval. No Director is interested in this item of business.

Answer 1(iv)

Type of Resolution = Ordinary Resolution

Kind of Meeting = General Meeting

“RESOLVED THAT consent be and is hereby accorded, in terms of Section 293(1)(d) and other applicable provisions, if any, of the Companies Act, 1956, to the Board of Directors of the Company for borrowing, from time to time for the purpose of companies business any sum or sums of money, which, together with money already borrowed by the Company, if any, (apart from temporary loans obtained or to be obtained from the Company's Bankers in the ordinary course of business), may 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, provided that, the total sum so borrowed together with moneys already borrowed shall not at any time, exceed the limit of Rs. 15,00,00,000 (rupees fifteen crores only).”

Explanatory Statement:

As per section 293(1)(d) of the Companies Act, 1956, the consent of the Members is required for the Board of Directors to borrow monies (apart from temporary loans obtained or to be obtained from the Company's Bankers in the ordinary course of business) in excess of the aggregate of the Company's paid up capital and free reserves.

The Company requires additional funds for meeting its normal capital expenditure needs. It is, therefore, recommended that the borrowing powers of the Board be raised to Rs.15,00,00,000/- (Rupees fifteen crores only). The Board commends the accompanying resolution for the Members' approval. None of the Directors is interested in this item of business.

Question 2

- (a) *Detail the procedure for conversion of Wholesome Entertainment Ltd. having 70 members (including 25 past and present employees) into a private limited company.*
- (b) *Tejaswi has requested to the Company Secretary of Yogi Ltd. for supply of a list of shareholders along with their names, addresses and shareholdings on a floppy. State the procedure to be followed by the company in this regard.*

(8 marks each)

Answer 2(a)

As the number of members is 70, it is assumed that it is not a listed company. The procedure for conversion of a public company into a private company are:

- (1) Hold a meeting of its Board of Directors to consider and approve the proposal

for conversion of public company into private company. The following resolutions must be passed at the meeting:

- (i) To approve the proposal for conversion of the company into private company.
- (ii) To fix time, date and venue for holding an extra-ordinary general meeting of the company.
- (iii) To approve notice for the general meeting along with the explanatory statement as required under section 173(2) of the Act.
- (iv) To authorize Company Secretary or some competent officer to issue the notice of general meeting on behalf of the Board.

(2) Hold the General Meeting and pass the following resolutions :

- (a) Special resolution for altering the articles of the company, as required under section 31 of the Companies Act, 1956 so as to include therein restrictions, limitations and prohibition specified in section 3(1)(iii) of the Act converting a public company into a private company.
- (b) Special resolution for changing the name of the company as required under proviso to Section 21 of the Act.
- (c) Special resolution for altering the memorandum of association (name clause) of the company in accordance with Section 16 of the Act.
- (v) File Form No. 23 alongwith certified copy of the Special Resolution & Explanatory statement along with filing fees within 30 days of passing of the special resolution with ROC.
- (vi) Get printed the altered copy of the Articles of Association to be filed with Registrar of Companies by addition of the restrictive articles under section 3(1)(iii) i.e.
 - (a) Restriction on Transfer
 - (b) Prohibition for invitation to public for subscription towards shares and debentures
 - (c) Prohibition to accept deposits except from members, directors & their relatives
 - (d) Limiting members to maximum of 50.

Also wherever free transferability of securities is mentioned in the Articles it has to be suitably altered by putting restrictions on free transferability.

- (vii) Get the fresh stationary printed
- (viii) Also the sign Board be changed accordingly
- (ix) Issue public notice for such change.

[Though the present members of the company is 70 it is not required to be reduced to 50 as 25 persons are the employees of the company which are not to be considered for computation of maximum number of members. After such conversion, the company can enjoy all benefits available to a private company].

- (x) Make application to Central Government in form no. 1B along with the following:
 - (a) A copy of Special Resolution

- (b) A printed copy of the unaltered copy of Memorandum & Articles of Associations
- (c) Certified true copy of the Audited Financial Statement of latest year
- (d) Certified true copy of the Minutes of General Meeting at which Special Resolution was passed
- (e) DD/Pay order/Challan evidencing payment of application fees to Central Govt.
- (f) Consent in writing from substantial creditors for conversion
- (g) Consent in writing of all those members of the company who have not voted in favour of the conversion
- (xi) File altered copy of Articles duly approved by Central Government with Registrar of Companies within one month.

Surrender to Registrar, the certificate of incorporation and the Registrar then issued fresh certificate for such conversion.

Answer 2(b)

Every company is required to maintain a register of members, which should indicate the name, address and occupation of the member, date on which he was entered as a member, date on which he ceased to be a member and the details of shares standing in his name.

Under Section 163 of the Companies Act, 1956 register of member shall, except when the register of members or debentureholders is closed under the provisions of the Act, be open during business hours (subject to such reasonable restrictions as the company may impose, so that not less than two hours in each day are allowed for inspection) to inspection of any member or debentureholder, without fee, and to any other person, on payment of such sum as may be prescribed for each inspection.

Further, any member or debentureholder or other person who has taken inspection may require a copy of any such register, Index or copy or any part thereof on payment of prescribed sum i.e. rupee one for every 100 words or part thereof, required to be copied.

Tejaswi assuming he has taken inspection can obtain copies of register of members in floppy by following this procedure :

1. Tejaswi will make a requisition to the company secretary for supply of details of shareholders in floppy.
2. The company secretary shall calculate the fees required including the cost of floppy and computer expenses.
3. The Company Secretary shall ensure that the prescribed fee has been paid.
4. The company will send the copy within ten days of receiving the requisition together with the charges.

Question 3

- (a) *What is 'compounding of offences' under the Companies Act, 1956 and who has got such powers ? state the procedure for compounding of offences.*

- (b) *State the procedure for creation, modification and satisfaction of charges.*
(8 marks each)

Answer 3(a)

As per the provisions of Section 621A of the Companies Act, 1956 three kinds of offences could be compounded, whether committed by a company or its officers. Such offences are :

- (i) An offence punishable with fine only.
- (ii) An offence which is punishable with imprisonment or with fine; and
- (iii) An offence which is punishable with imprisonment or with fine or with both.

This means an offence punishable with imprisonment only and with imprisonment and fine is not compoundable.

The Company Law Board and Regional Directors have authority to make compounding of offences.

The procedure for compounding of offence is as under :

- (a) Every application for the compounding of an offence shall be made to the Registrar who shall forward the same, together with his comments thereon to the Company Law Board or the Regional Director; as the case may be.
- (b) Where any offence is compounded under this section whether before or after the institution of any prosecution, an intimation thereof shall be given by the company to the Registrar within seven days from the date on which the offence is so compounded.
- (c) Where any 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 of the company or by any person authorized by the Central Government against the offender in relation to whom the offence is so compounded.
- (d) Where the composition of any offence is made after the institution of any prosecution, such composition shall be brought by the Registrar in writing, to the notice of the Court in which the prosecution is pending 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.

Answer 3(b)

Section 125 of the Companies Act, 1956 makes it compulsory for the companies to file with the ROC, Form No. 8 containing particulars of every charge created by them along with a certified copy of the document by which the charge has been created. Sub-section (1) of Section 130 makes it compulsory for the ROC to cause to be kept a register containing the particulars of all charges requiring registration.

Section 130(1C) obliges every company to forward to the ROC, Form No. 13 (in triplicate) containing particulars of the charges requiring registration, for being entered in the said register of charges.

Procedure for Modification of Charges

- (1) If any term or condition or the extent of the operation of any charge registered by the company under Section 125 is modified, then particulars of such modification should be sent to the concerned Registrar of Companies in Form No. 8 in triplicate alongwith requisite filing fee, within 30 days of the modification.
- (2) Attach with Form No. 8 a certified true copy of the agreement or other instrument modifying the existing charge and also a certified true copy of the registration certificate of the charge already registered with the Registrar of Companies and now being modified.
- (3) Alongwith Form No. 8 forward to the concerned Registrar of Companies, the particulars of modification of charge in Form No. 13, in triplicate, alongwith a fee of Rs. 50.
- (4) Form No. 8 and Form No. 13 and the instrument modifying the charge shall be signed on behalf of the company and the chargeholder.
- (5) The concerned Registrar of Companies will endorse on all forms and accompanying instruments by rubber stamp with the word “Registered”, under his signature with date.
- (6) A copy of all the forms and instruments will be delivered to the company and a copy of each to the chargeholder. The first copy is retained by the Registrar for his own record.

Procedure for Satisfaction of Charges

- (1) File with the concerned Registrar of Companies an intimation of satisfaction of charge in Form No. 17, within 30 days of making full payment or within 30 days of full satisfaction of the charge, alongwith requisite filing fee.
- (2) Attach with Form No. 17 a certified true copy of the registration certificate of the charge given by Registrar of Companies for which the intimation of satisfaction is now being given and a certified true copy of the document satisfying the charge.
- (3) Form No.13 in triplicate be also filed alongwith Form No. 17.
- (4) Form No. 17, Form No. 13 and the instrument evidencing satisfaction of charge in full shall be signed on behalf of the company and the charge-holder.
- (5) The concerned Registrar of Companies will endorse on all forms and accompanying instruments by rubber stamp with the word “Registered” and his signature and date.
- (6) A copy of all the documents and forms will be delivered to the company and a copy of each to the charge-holder. The first copy is retained by the Registrar for his own record.

Question 4

Prosperous Ltd. had a bumper profit and an all-time high sales turnover for the year ended 31st December, 2005. The directors have decided to reward the shareholders with 35% dividend besides the liberal bonus, more so, since the company is in its 50th year of operations. Draft a report of the Board of directors making appropriate assumptions as to facts and figures.

(16 marks)

Answer 4**DIRECTORS' REPORT**

To,

The Members,

Your Directors have pleasure in presenting their 50th Annual Report together with the audited Accounts for the financial year ended 31st December 2005.

1. *OPERATIONS*

The year witnessed all round improvement in the functioning of the Company with the sales turnover touching a peak of Rs.912 crores, which represented a 25 % growth over the sales recorded in the previous year (Rs.730 crores). Sales in the domestic market as well as the Company's export performance showed much improvement. Exports of machinery, besides exports of machined parts and sub-assemblies, of the order of Rs.350 crores (Rs.170 crores), were made to Bangladesh, Sri Lanka, Taiwan, Indonesia, Malaysia, Japan, the Phillipines and Eastern Europe. The third and final phase of the Company's diversification programme was successfully completed during the year thereby augmenting the manufacturing capacity for larger capacity drilling equipment, vegetable oil refining equipment and chemical equipment.

2. *FINANCIAL RESULTS*

The profit for the year after depreciation was Rs. 185 crores. (Rs. 105 crores). After setting apart a sum of Rs.50 crores for taxation (Rs.40 crores), the net profit is Rs.135 crores (Rs.65 crores). A sum of Rs.25 crores has been transferred to General Reserves which now stand at Rs.100 crores (Rs.81 crores).

3. *DIVIDEND*

The Directors are pleased to recommend a higher dividend of 35% (25 %) on the equity shares. This will entail a pay out of Rs.20 crores (Rs.13 crores).

4. *BONUS ISSUE*

The Company has just completed 50 years. The Board is pleased to announce a Golden Jubilee Bonus in the ratio of 3:2, subject to the approval of the share holders at the ensuing Annual General Meeting.

5. *PROSPECTS*

Business prospects for the current year appear to be better. The Order Book as on date is promising at Rs.500 crores. The company's forays into the export market should get a momentum once full fledged sales offices are established at Moscow and Tokyo.

6. *EMPLOYEES' PARTICULARS*

The particulars of employees under Section 217(2A) are contained in Annexure annexed to this Report.

7. *CONSERVATION OF ENERGY : TECHNOLOGY ABSORPTION AND FOREIGN EXCHANGE EARNINGS AND OUTGO*

The particulars required to be furnished under Section 217 (1)(e) are contained in Annexure ____annexed hereto and forming part of this Report.

8. *DIRECTORS*

Mr. V, was co-opted to the Board on the 15th September, 2005. He holds office till the forthcoming Annual General Meeting.

In accordance with the Companies Act, 1956 and the Company's Articles of Association, Mr. S, Mr. P and Mr. B, Directors, retire by rotation but being eligible offer themselves for re-election at the ensuing Annual General Meeting.

9. *DIRECTORS' RESPONSIBILITY STATEMENT*

In terms of Section 217 (2AA), the Board hereby confirm

- (i) that in the preparation of the Accounts for the financial year ended 31st December 2005, the applicable accounting standards have been followed along with proper explanation relating to material departures;
- (ii) that they have selected such accounting policies and applied them consistently and made judgements and estimates that were reasonable and prudent so as to give a true and fair view of the state of affairs of the Company at the end of the financial year and of the profit of the Company for the year under review;
- (iii) that they have taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of the Companies Act, 1956, for safeguarding the assets of the Company and for preventing and detecting fraud and other irregularities;
- (iv) that they have prepared the Accounts for the financial year ended 31st December, 2005 on a 'going concern' basis.

10. *AUDITORS*

The Auditors, H & K Associates, Chartered Accountants, Pune, hold office till the conclusion of the ensuing Annual General Meeting but have expressed their willingness to continue for a further term on the same remuneration, if re-appointed.

11. *APPRECIATION*

The Board place on record their appreciation of the co-operation and assistance extended/rendered to the Company by various Ministries of the Central and State Governments as well as the Company's Bankers and financiers which enabled the Company to perform creditably in the year under review. The Directors also wholeheartedly thank the employees of the Company for their unstinted support and dedicated service.

For and on behalf of the Board of Directors,

Chairman and Managing Director.

Pune

January 15, 2006

Encls : Annexures "___" & "___".

Question 5

- (a) *Outline the steps to be taken for change of name of a company.* (8 marks)
- (b) *Distinguish between —*
- (i) *'Public limited company' and 'private limited company'.*
 - (ii) *'Certificate of incorporation' and 'certificate of commencement of business'.* (4 marks each)

Answer 5(a)**Procedure for Change of Name of a Company**

A company desiring to change its name may do so in accordance with the provisions of Section 21 of the Companies Act, 1956 by following these procedural steps:

1. Issue notice of the Board Meeting to consider the change of name, as per the provisions of Section 286 of the Act.
2. Hold the Board meeting to —
 - (i) consider and approve the proposed name by passing a resolution. The Board must consider and decide at least three more names in the application for availability of name to be made to the Registrar of Companies in Form No. 1A.
 - (ii) pass another resolution to authorise the Company Secretary/Director to make the required application to the Registrar of Companies in Form 1A and pay the prescribed fees.
3. On receipt of name availability letter, hold Board meeting to fix time, date and venue for holding a general meeting :
 - (a) for passing a special resolution required under Section 21 of the Act for changing the name of the company; and
 - (b) for passing another special resolution under Section 16 of the Act for altering clause I (name clause) in the memorandum of association of the company in accordance with Section 16 of the Act.
4. Issue notice of the general meeting to all the members of the company, its directors and the auditors.
5. In the case of listed companies, send three copies of the notice to each stock exchange where the securities of the company are listed.
6. A general notice of the general meeting may also be published in newspapers.
7. Hold the general meeting and pass the resolutions as contained in the notice.
8. Listed companies shall send six copies to each stock exchange.
9. A copy of the proceedings of the general meeting be sent to each Stock Exchange.
10. File with the ROC Form No. 23 with a certified true copy of each special resolution passed at the general meeting along with the explanatory statement and prescribed filing fee.
11. Make an application to the concerned Registrar of Companies for obtaining Central Government's approval to the change of name of the company.

12. On receipt of the Central Government's approval, the existing Certificate of Incorporation be surrendered to ROC with a request for the issue of a Fresh Certificate of Incorporation.
13. Issue a general notice in newspapers, about the change of name of the company.
14. Inform all concerned persons/authorities about the changed name of the Company.
15. Arrange for a new Common Seal and have the same adopted at a meeting of the Board of Directors and keep both the old and new common seals under lock and key.
16. Get stationery printed with the new name and/or affix rubber stamp of the new name.
17. Get the new name of the Company painted on all the signboards.
18. Correct all records, registers including the Register of Members, share certificates, every copy of Memorandum and Articles of Association.

Answer 5(b)(i)

Public limited company and Private limited company distinguished:

1. A public company requires a minimum of seven promoters, while a private company requires only two persons, for its incorporation.
2. There is no upper limit to the number of members in a public company. In a private company, however, the maximum membership is fifty, excluding past and present employees who may be members.
3. A public company must have at least three Directors whereas a private company must have atleast two.
4. For a public company, any increase in Board strength beyond 12 requires Central Government's approval.
5. The quorum for a General Meeting is five Members personally present in a public company whereas it is just two Members personally present in a private company. However, the Articles of the company may prescribe a larger quorum in both cases.
6. The minimum paid-up capital is Rs.5 lakhs for a public company; whereas it is just Rs. 1 lakh for a private company.
7. A public company may adopt Table A of the Companies Act, 1956 as its Articles, the registration of which is not mandatory. Registration of Articles is, however, mandatory in the case of a private company.
8. A private company has, further, the following characteristics.-
 - (i) it shall not invite any public subscription to its shares or debentures;
 - (ii) it restricts transfer of its shares by its Articles; and
 - (iii) it shall not invite or accept Deposits from persons other than its Members, Directors or their relatives

There is no such restriction for public companies.

Answer 5(b)(ii)**Certificates of Incorporation and Commencement of Business**

Every company shall file with the Registrar of Companies the Memorandum of Association and various documents spelling out the constitution of the company, viz its name, location of registered office, objects, capital and liability. Section 34 of the Companies Act, 1956 provides that on the registration of these documents, in the manner prescribed, the Registrar certifies under his hand that the company is incorporated and, in the case of a limited company, that the company is limited. This certificate is the Certificate of Incorporation. It is conclusive proof that all the requirements of the Companies Act, 1956 have been complied with in respect of registration and matters precedent and incidental thereto and that the association is a company authorized to be registered and duly registered under this Act. A private company is entitled to commence its business operations immediately upon receipt of the incorporation certificate. A public company must, however, obtain a separate certificate from the Registrar for commencement of its business. This is done by filing with the Registrar a Statement in lieu of Prospectus in the form given in Schedule V along with a declaration by one of the Directors or the Secretary, in the prescribed form, that all monies due from the Directors for the shares subscribed for by them have been duly received from them by the company (Section 149). This certificate is called the Certificate of Commencement of Business.

Question 6

As a Company Secretary, how would you deal with the following situations :

- (i) A Board meeting was convened on 25th May, 2006 for approval of the annual accounts for the year ended 31st December, 2005 and also to fix the date of annual general meeting. The CFO has, however, expressed his inability to table the accounts before 10th June, 2006. (6 marks)*
- (ii) The attendance at an annual general meeting of a company is thin on account of torrential rains; but the quorum is, however, available. Both the Chairman and the Secretary are present. The agenda includes important businesses, viz., re-appointment of the managing director, issue of bonus shares and equity investment in a new venture. (5 marks)*
- (iii) A shareholder, who has lost all his share certificates in a flood, approaches the company for issue of duplicate scrips. (5 marks)*

Answer 6(i)

As per Section 210 of the Companies Act, 1956, at every annual general meeting of the company held in pursuance of Section 166, the Board of Directors of the company shall lay before the company:

- (a) a balance sheet as at the end of the period specified in sub-section (3) and
- (b) a profit and loss account for that period.

For the purpose, the maximum period prescribed in sub-section (3) is six months from the date of closing of the relevant financial year. In this case, the last date for holding the Annual General Meeting is 30th June 2006 i.e. Six months from the closing of Financial Year which in this case ends on 31st December 2005.

As CFO has expressed his inability to table the accounts before 10th June 2006, therefore, the Board meeting for approval of the account and for fixing AGM can be held on 10th June 2006. In such case, AGM will be held after 30th June 2006 since as per provisions of Section 171(i), a general meeting may be called by giving not less than 21 days notice in writing. But Section 171(2) provides that an AGM may be called by giving a shorter notice, if it is consented to by all the members entitled to vote at the meeting. The consent for shorter notice may be given either at or before the meeting in Form No. 22A as prescribed in Companies (Central Government) General Rules & Forms, 1956. Thus, if all the member gives their consent, the AGM of this company can be called on or before 30th June 2006.

Alternatively, the company may hold the Annual General Meeting after 30th June if the company obtains the approval for extension of time for holding the Annual General Meeting from the Registrar.

Answer 6(ii)

Quorum is the presence of requisite number of member when a meeting can validly commence its business. Section 174(1) of the Act provides that unless the articles of a company provide for a larger number, five members personally present in the case of public company and two members personally present in the case of a private company shall be quorum for a general meeting of a company.

As long as the requisite quorum is present, it would be perfectly in order for the Chairman to proceed with the Meeting and transact the business thereat, notwithstanding the thin attendance.

Answer 6(iii)

The loss of the share certificates should be notified to the Stock Exchange where the company's shares are listed if the company concerned is a listed company. An affidavit should be taken from the shareholder confirming the loss of the scripts. A Public Notice about the loss of the share certificates should also be published in a newspaper having a wide circulation. Thereafter, the matter should be placed before the Board and a resolution be passed for issue of duplicate share certificates to the shareholder.

Question 7

- (a) *What are the requirements with regard to quorum and frequency of Board meetings ?* (6 marks)
- (b) *Under what `circumstances can a person become a member of a company ?* (5 marks)
- (c) *Can a director of a company act as such immediately on his appointment to the office of a director ?* (5 marks)

Answer 7(a)**Quorum of Board Meetings**

Section 287(2) of the Companies Act, 1956 provides that the quorum of Board meeting shall be one-third of its total strength (any fraction contained in that one-third being rounded off as one) or two directors, whichever is higher. However, where at any

time the number of interested directors exceeds or is equal to two-thirds of total strength, the number of remaining directors, that is to say, the number of the directors who are not interested (present at the meeting being not less than two), shall be the quorum during such time.

Frequency of Board Meetings

As per Section 285 of the Act, in case of every company, a meeting of its 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. However the Central Government, may by notification in Official Gazette direct that provisions of said section shall not apply in relation to any class of companies or shall apply in relation thereto subject to such exceptions, modifications or conditions as may be specified in the notification. As per Clause 49 of listing agreement in case of listed company the Board shall meet at least four times a year with a maximum time gap of three months between any two meetings.

(Students may note that as per revised clause 49 (revised on January 13, 2006, the Board shall meet at least four times a year, with a maximum time gap of four months between any two meetings).

Answer 7(b)

As per Section 41 of the Companies Act, 1956 in the following circumstances a person may become a member :

- (a) By subscribing to the Memorandum of Association.
- (b) By agreeing in writing to become a member :
 - (i) by making an application to the company for allotment of shares, or
 - (ii) by executing an instrument of transfer of shares as transferee, or
 - (iii) by consenting to the transmission of shares of a deceased member in his name, or
 - (iv) by acquiescence or estoppel and on his name being entered in the register of the members of the company.
- (c) By holding equity share capital of a company whose name is entered as beneficial owner in the records of depository.

Answer 7(c)

A person can start functioning as a director immediately on his appointment to the office of Director subject to the following provisions :

1. As per Section 264(2) of the Companies Act, 1956 a person other than those specified in Section 264(2)(a) to (c) shall not act as director of the company unless he has within thirty days of his appointment signed and filed with the Registrar his consent in writing to act as such director. However, this section does not apply to a private company unless it is a subsidiary of a public company.
2. As per Section 270, a director can act as a director for two months without possessing the qualification shares as required by the Articles. If he wants to continue after that period, he must obtain the requisite qualification shares before

the expiry of two months and if he does not do so, he automatically vacate the office.

3. Section 275 provides that a person cannot be a director in more than 15 companies. As per Section 277 of the Act where a person holds the office of director in 15 companies, (excluding certain directorships as provided in Section 278) is appointed, as a director of any other company, the appointment shall not take effect unless such person has, within 15 days, thereof vacated his office as director in any of the companies in which he was already a director and his appointment shall become void immediately on the expiry of the 15th day if he has not, before such expiry, effectively vacated his office as director in any of the other companies aforesaid.

Question 8

Write short notes on the following :

- (i) *Dematerialisation of shares*
- (ii) *Statement on corporate governance in the Board's report*
- (iii) *Interim dividend*
- (iv) *Investor Education and Protection Fund.* (4 marks each)

Answer 8(i)

Dematerialisation of shares

Dematerialisation of securities is a matter connected with Depositories, which are companies formed and registered under the Companies Act, 1956 that hold certificates of registration under Section 12 (1A) of the SEBI Act, 1992, and is regulated by the Depositories Act, 1996.

The company at the outset should enter into an agreement with a Depository. The shareholder of such a company may approach a depository participant for dematerialization of his holdings. The depository participant will write to company and surrender the share certificates for cancellation. The company will substitute in its records, the name of the Depository as the registered owner of the shares and inform the Depository accordingly. The Depository will, in turn, enter the name of the shareholder in its records as the beneficial owner of the shares and inform the company. The company then advises the shareholder that his shares have been dematerialized and that his name has been entered in the Depository's electronic records. This is known as dematerialisation. The physical share certificates are cancelled by the company.

The Depository does not have any voting rights in respect of the shares held by it. These continue to vest in the beneficial owner who is also saddled with the liabilities, if any, on the shares.

Every Depository shall maintain a Register and an Index of Beneficial Owners in the manner provided in Sections 150, 151 and 152 of the Companies Act, 1956.

Section 68B inserted by the Companies (Amendment) Act, 2000 provides that every initial share offer of Rs. 10 crores or more shall be made only in the dematerialized form under the Depositories Act, 1996.

Answer 8(ii)**Statement on Corporate Governance in the Boards Report**

As per Clause 49 of Listing Agreement, there shall be a separate section on Corporate Governance in the Annual Reports of a listed company, having the prescribed equity capital with a detailed compliance report on Corporate Governance. Non-compliance of any mandatory requirement of said Clause with reasons thereof and the extent to which the non-mandatory requirements have been adopted should be specifically highlighted. The requirements of aforesaid Clause 49 are applicable to listed companies. This report should form part of the Directors' Report.

Answer 8(iii)**Interim Dividend**

The Articles of a company generally empower the Board to declare interim dividends. The interim dividend is paid between two annual general meetings of the company. Section 2(14A) defines Dividend to include 'interim dividend'. If the Board contemplate an interim dividend, they should ensure that depreciation is provided for the full year in the provisional accounts of the financial year in which the interim dividend is to be paid. The Stock Exchange in which the company's shares are listed should be intimated about the convening of the Board Meeting for the purpose of declaring the interim dividend. Intimation of the declaration of the dividend should also be given to the Exchange immediately after the Meeting.

Further, a special banking account of the Company for the express purpose of paying the interim dividend should be opened and the amount of the dividend should be transferred to it within 5 days of the declaration. The dividend is to be distributed by means of dividend warrants within 30 days of the declaration. The interim dividend declared by the Board need not be confirmed.

Answer 8(iv)**Investor Education and Protection Fund**

Section 205C of the Companies Act, 1956 empowers the Central Government to establish a Fund to be called the 'Investor Education and Protection Fund'. There shall be credited to the Fund the following amounts, namely :

- (a) amounts in the unpaid dividend accounts of companies;
- (b) the application moneys received by companies for allotment of any securities and due for refund;
- (c) matured deposits with companies;
- (d) matured debentures with companies;
- (e) the interest accrued on the amounts referred to in clauses (a) to (d);
- (f) grants and donations given to the Fund by the Central Government, State Governments, companies or any other institutions for the purposes of the Fund; and

- (g) the interest or other income received out of the investments made from the fund.

Provided that no such amounts referred to in clauses (a) to (d) shall form part of the Fund unless such amounts have remained unclaimed and unpaid for a period of seven years from the date they became due for payment.

The fund should be utilized for promotion of investors' awareness and protection of the investors' interests.

ECONOMIC, LABOUR AND INDUSTRIAL LAWS

Time allowed : 3 hours

Maximum marks : 100

NOTE : Answer SIX questions including Question Nos. 1 and 7 which is **COMPULSORY**.

Question 1

With reference to the relevant legal enactments, write short notes on any five of the following :

- (i) *Anti-competitive agreement*
- (ii) *Industrial undertaking*
- (iii) *Surrender of patents*
- (iv) *Environmental laboratories*
- (v) *Money laundering*
- (vi) *Deemed exports.*

(3 marks each)

Answer 1(i)

Anti Competitive Agreement

Section 3(1) of the Competition Act, 2002 provides that no enterprise or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition. Section 3(2) further provides that any anti competitive agreement within the meaning of section 3(1) shall be void.

Section 3(3) provides that the following kinds of agreement entered into between enterprises or association of enterprises or association of persons or persons including 'cartels', managed in identical or similar goods or services shall be presumed to have an appreciable adverse effect on the competition and onus to prove otherwise lies on the defendant. Such agreements include those which :

- (a) directly or indirectly determines purchase or sale price;
- (b) limits or controls production, supply market, development, investment or provision of services;
- (c) shares the market or source of production or provision of services by way of allocation of geographical area of market, or types of goods or services, or number of customers in the market or any other similar way; and
- (d) directly or indirectly results in bid rigging or collusial bidding.

Section 3(4) provides that any agreement amongst enterprises or persons at different levels or stages of production chain in different markets, in respect of production, supply, distribution, storage, sale or price of or trade in goods or provision of services, including tie in agreement; exclusive supply agreement; exclusive distribution agreement; refusal to deal; resale price maintenance, shall be an agreement in contravention of sub-section (1) if such agreement causes or is likely to cause an appreciable adverse effect on competition in India.

Answer 1(ii)**Industrial undertaking**

Section 3(d) of Industries (Development & Regulation) Act, 1951, defines industrial undertaking to include any undertaking pertaining to a scheduled industry carried on in one or more factories by any person or authority. If the number of workers is less than 50 in power used factory or 100 where no power is used, it will not be a factory or undertaking for the purpose of the Act. The basic feature expected to be present is the existence of factory which carry on some manufacturing process.

Answer 1(iii)**Surrender of patents**

Section 63 of The Patents Act 1970 dealing with surrender of patents, entitles the patentee to surrender the patent at any time by giving notice in the prescribed manner to the Controller. The Controller on receipt of such an offer is under obligation to advertise the offer in the prescribed manner. Any person interested may within the prescribed period after such advertisement give notice to the Controller of Opposition to the surrender and where any such notice is given the Controller shall notify the patentee. If the Controller is satisfied after hearing the patentee and any opponent desirous of being heard that the patent may properly be surrendered, he may accept the offer and by orders, revoke the patent.

Answer 1(iv)**Environmental Laboratories**

Section 12 of the Environment (Protection) Act, 1986 empowers the Central Government to establish by notification in the official Gazette, one or more environmental laboratories or recognise one or more laboratories or institutes as environmental laboratories to carry out certain functions under the Act.

Answer 1(v)**Money Laundering**

Money laundering is the processing of criminal proceeds to disguise its illegal origin. Terrorism, illegal arms sales, financial crimes, smuggling, and the activities of organised crime, including drug trafficking and prostitution rings, generate huge sums. Embezzlement, insider trading, bribery and computer fraud also produce large profits and create an incentive to legitimise the ill-gotten gains through money laundering. When a criminal activity generates substantial profits, the individual or group involved in such activities route the funds to safe heavens by disguising the sources, changing the form, or moving the funds to a place where they are less likely to attract attention. The prevention of Money Laundering Act, 2002 deals with the problem of money laundering in India.

Answer 1(vi)**Deemed Exports**

Deemed Exports mean those transactions in which the goods supplied do not leave the country and the payment for such supplies is received either in Indian rupees or in

free foreign exchange. Deemed exports are eligible to the benefits in respect of manufacture and supply of goods. These include advance licence for intermediate supply, deemed export/DFRC/DFRC for intermediate supply, deemed export drawbacks; and exemption from terminal excise duty in certain cases.

Question 2

- (a) Define the terms 'acquisition', 'competition' and 'cartels'. (6 marks)
- (b) Mention any six functions of Development Councils set-up under the Industries (Development and Regulation) Act, 1951. (3 marks)
- (c) What is 'free trade and warehousing zone' (FTWZ) ? (2 marks)
- (d) State, citing decided cases, whether any restrictive or unfair trade practice has been committed in the following instances :
 - (i) A company engaged in the business of manufacture of cold drinks, stipulates in the franchise agreement with its bottlers that the latter should not bottle the products of other cold drink manufacturers in the same premises as it may cause mixing-up with the company's products.
 - (ii) A company engaged in the business of manufacture of leather items, enters into agreements with small-scale manufacturers for purchase of leather items to be sold by it under its own brand name. The agreement prohibits the small-scale manufacturers from purchasing raw materials and components from parties other than those approved by the company on the ground of quality control. (2 marks each)

Answer 2(a)

Acquisition

Section 2(a) of The Competition Act, 2002 defines the term acquisition as to mean, directly or indirectly, acquiring or agreeing to acquire: (i) shares, voting rights or assets of any enterprise; or (ii) control over management or control over assets of any enterprise.

Competition

The term "Competition" is not defined in the Act. However, in the corporate world, the term is generally understood as a process whereby the economic enterprises compete with each other to secure customers for their product.

Cartels

Section 2(c) of the Competition Act, 2002 defines cartels as to include an association of producers, sellers or 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.

Answer 2(b)

Functions of Development Council

The Industries (Development & Regulation) Act, 1951 assigns following functions to Development Council :

- (i) Recommending targets for production, coordinating production programmes and reviewing progress from time to time.

- (ii) Suggesting norms of efficiency with a view to eliminating waste, obtaining maximum production, improving quality and reducing costs.
- (iii) Recommending measures for securing the fuller utilisation of installed capacity and for improving the working of the industry, particularly of the less efficient units.
- (iv) Promoting arrangements for better marketing and helping in the devising of a system of distribution and sale of the produce of the industry which would be satisfactory to the consumer.
- (v) Promoting standardisation of products.
- (vi) Assisting in the distribution of controlled materials and promoting arrangements for obtaining materials for the industry.

Answer 2(c)

FREE TRADE & WAREHOUSING ZONES

The Free Trade & Warehousing Zones (FTWZ) are a special category of Special Economic Zones with a focus on trading and warehousing. The Government has allowed setting up of FTWZ for creating trade-related infrastructure to facilitate the import and export of goods and services with freedom to carry out trade transactions in free currency. The government has allowed creation of world-class infrastructure for warehousing of various products, state-of-the-art equipment, transportation and handling facilities, commercial office-space, water, power, communications and connectivity, with one-stop clearance of import and export formality, to support the integrated Zones as international trading hubs.

Answer 2(d)

- (i) The very nature of the Agreement seems to be to ensure reputation and goodwill of the franchise. Therefore, restriction in the agreement is reasonable to prevent mix up or contamination in utilization of the same in the bottling of the products. Hence, there is no restrictive trade practice involved in this case, *Mohan Meakins Ltd. & Others* [RTP Enquiry No. 65 of 1984].
- (ii) It is very clear case of restrictive trade practice as was decided by the Commission in the case of *Bata India Ltd.* [RTP Enq. No. 3 of 1974]. But the company can plead gateway u/s 38 of having the restriction in order to ensure quality of the products.

Question 3

- (a) *Discuss the exemptions from the provisions relating to holding, realisation and repatriation of foreign currency under the Foreign Exchange Management Act, 1999.* (4 marks)
- (b) *With reference to the relevant provisions of the Foreign Exchange Management Act, 1999, advise on the following :*
 - (i) *Adarsh Ltd. had export earnings of Rs.15 lakh, Rs.20 lakh and Rs.22 lakh during the years 2003, 2004 and 2005 respectively. It desires to issue advertisements through a foreign TV channel.*

- (ii) *Paritosh Ltd., an Indian company, wishes to donate \$10,000 to a charitable institution in Mauritius.*
- (iii) *Abhay Ltd., an Indian company, which won the bid, has approached the authorised dealer for further remittance towards acquisition of a company in Romania.*
- (iv) *Sumesh, a person resident in India, has acquired foreign securities as qualification shares in a company incorporated in Luxemburg for holding the post of a director in that company.* (2 marks each)
- (c) *Briefly mention the policy initiatives taken by the government to pave way for consumer protection in the country.* (3 marks)

Answer 3(a)

Section 4 of FEMA prohibits a person resident in India from acquiring, holding, owning, possessing or transferring any foreign exchange except as provided in the Act.

Section 8 imposes conditions on the person resident in India to make all reasonable efforts to realize and repatriate foreign exchange due or accrued as per the directions of the Reserve Bank. However, section 9 provides some exemptions from the above provisions under certain circumstances. Accordingly, possession of foreign currency and coin by any person and foreign exchange acquired from employment, business, trade, vocation, services etc. to a certain limit specified by RBI, is permitted.

Answer 3(b)

- (i) Prior approval of RBI is required if remittance for advertisement on foreign television by a person whose export earnings are less than Rs. 10 lakh during each of the preceding two years. In the given case Adarsh Ltd. does not require prior approval of RBI.
- (ii) According to Rule 5 of Foreign Exchange Management (Current Account Transactions) Rules, 2000, no person shall draw foreign exchange for a transaction included in the Schedule III without prior approval of the Reserve Bank. According to item three of Schedule III donations exceeding US \$ 5000 per remitter/donor per annum require approval of Reserve Bank. Hence in view of aforesaid legal position, Paritosh Ltd. is required to take permission from Reserve Bank as the amount involved is more than \$ 5000.
- (iii) The authorised dealer may allow Abhay Ltd. further remittances towards acquisition of the foreign company subject to the specified ceilings and shall submit a Report to RBI within 30 days of making the final remittance.
- (iv) A person resident in India may acquire foreign securities as qualification shares issued by a company incorporated outside India for holding the post of Director. However, he has to satisfy following conditions –
 - (a) The number of shares so acquired shall be the minimum required to be held for holding the post of directors and in any case shall not exceed 1% of the paid up capital of the company.
 - (b) The consideration for purchase does not exceed \$20,000 or its equivalent in any calendar year.

Answer 3(c)

The need to ensure the basic rights to health, safety, etc. of consumers has long been recognised the worldover and various general legislations were enacted in India and abroad in this direction. In India, there are a number of general enactments, other than the law of torts, which ultimately aimed at protection of consumer interests.

However, the Consumer Protection Act, 1986 is a special legislation providing for better protection of the interest of the consumers. This Act provides for simple, quick and easy remedy to consumers under a three-tier quasi-judicial redressal system at the District, State and National levels. To make the Act more effective and meaningful, necessary changes have been brought by Consumer Protection (Amendment) Act, 2002, which came into force w.e.f. March 15, 2003.

Question 4

- (a) *State the grounds under which registration of a trade mark can be refused.*
 - (b) *Mention the inventions which are not patentable under the Patents Act, 1970.*
 - (c) *What amounts to infringement of a copyright under the Copyright Act, 1957 ?*
- (5 marks each)

Answer 4(a)**Grounds for Refusal of Registration of Trade Mark**

Section 9(1) of the Trade Marks Act, 1999 containing provisions relating to absolute grounds for refusal of registration, prohibits the registration of those trade marks which are devoid of any distinctive character or which consist exclusively of marks or indications which may serve in trade to designate the kind, quality, quantity, intended purpose, etc., or which consist exclusively of marks or indications which have become customary in the current language or in the bona fide and established practices of the trade. However, a trademark shall not be refused registration, if the mark has in fact acquired a distinctive character as a result of use or is a well known trade mark before the date of application. In short, a trade mark which has been demonstrated to be distinctive in the market place shall be regarded as distinctive in law as well and be registerable.

Section 11 of The Trade Marks Act, 1999 stipulates that where there exists a likelihood of confusion on the part of the public because of the identity with an earlier trade mark or similarity of goods or services, the trade mark shall not be registered. The registration of a mark which is merely reproduction or imitation of well-known mark is also prohibited. Sub-section (3) prohibits the registration of a trade mark, if or to the extent that, its use will be prevented by law of passing off or under the law of copyright unless the proprietor of earlier trade mark consents to such registration.

Answer 4(b)**Inventions not patentable under The Patents Act, 1970**

Section 3 of the Patents Act, 1970 provides that the following are not inventions and hence not patentable :

- an invention which is frivolous or which claims anything obviously contrary to well established natural laws;

- an invention the primary or intended use or commercial exploitation of which could be contrary to public order or morality or which causes serious prejudice to human, animal or plant life or health or to the environment;
- the mere discovery of a scientific principle or the formulation of an abstract theory or discovery of any living thing or non-living substances occurring in nature;
- the mere discovery of a new form of a known substance which does not result in the enhancement of the known efficacy of that substance or the mere discovery of any property or mere new use for a known substance or of the mere use of a known process, machine or apparatus unless such known process results in a new product or employs at least one new reactant.
- a substance obtained by a mere admixture resulting only in the aggregation of the properties of the components thereof or a process for producing such substance;
- the mere arrangement or re-arrangement or duplication of known devices each functioning independently of one another in a known way;
- a method of agriculture or horticulture;
- any process for the medicinal, surgical, curative, prophylactic diagnostic, therapeutic or other treatment of human beings or any process for a similar treatment of animals to render them free of disease or to increase their economic value or that of their products;
- plants and animals in whole or any part thereof other than micro-organisms but including seeds, varieties and species and essentially biological processes for production or propagation of plants and animals;
- a computer programme *per se* other than its technical application to industry or a combination with hardware;
- a literary, dramatic, musical or artistic work or any other aesthetic creation whatsoever including cinematographic works and television productions;
- a mere scheme or rule or method of performing mental act or method of playing game;
- a presentation of information;
- topography of integrated circuits;
- an invention which in effect, is traditional knowledge or which is an aggregation or duplication of known properties of traditionally known component or components.

Section 4 prohibits the grant of patent in respect of an invention relating to atomic energy falling within Sub-section (1) of Section 20 of the Atomic Energy Act, 1962.

Answer 4(c)

Copyright protection gives exclusive rights to the owners of the work to reproduce the work enabling them to derive financial benefits by exercising such rights. If any person without authorisation from the owner exercises these rights in respect of the work which has copyright protection it constitutes an infringement of the copyright.

However, if the reproduction of the work is carried out after the expiry of the copyright term it will not amount to an infringement.

Section 51 of the Copyright Act, 1957 contemplates situation in which a copyright shall be deemed to be infringed. This Section says that a copyright is infringed when any person without a license granted by the owner of the copyright or the Registrar of Copyright or in contravention of the conditions of a license so granted or of any condition imposed by a competent authority does —

- (1) anything for which the exclusive right is conferred upon the owner of the copyright, or
- (2) permits for profit any place to be used for the communication of the work to public where such a communication constitutes an infringement of the copyright in the work, unless he was not aware and had no reasonable ground for believing that such communication would be an infringement of copyright.
- (3) when any person (i) makes for sale or hire or lets for hire or by way of trade display or offers for sale or hire, or (ii) distributes either for the purpose of trade or to such an extent as to affect prejudicially the owner of the copyright, or (iii) by way of trade, exhibits in public, or (iv) imports into India any infringing copies of the work.

However, import of one copy of any work is allowed for private and domestic use of the importer. Explanation to Section 51 clarifies that the reproduction of literary, dramatic musical or artistic work in the form of cinematograph film shall be deemed to be an infringing copy.

Question 5

- (a) *A CT scan machine is installed in Daya Ram Charitable Trust and Diagnostic Centre. 80% of the patients are required to pay charges for the services rendered by the trust whereas 20% patients are provided free services. On a complaint against the trust for deficiency in service, it contended that the trust did not engage in profit-making activity on a large scale. Will it succeed ?*
- (b) *Aditya, a director of Amex Ltd., visited Germany thrice in 2005 on invitations and free air-tickets, board and lodging extended to Amex Ltd. by the Chamber of Commerce and Industry, Germany. Has Aditya or the company contravened the provisions of the Foreign Contribution (Regulation) Act, 1976 ? Mention relevant provisions.*
- (c) *Kajol purchased 2,000 units from a leading mutual fund in 1999 on monthly income scheme. On maturity, the mutual fund sent account payee cheque dated 1st September, 2005 in favour of Kajol at her address lodged with the mutual fund through registered post. The registered post letter was not returned undelivered and the mutual fund believed that the letter containing the cheque was duly delivered to Kajol. On 19th November, 2005, Kajol asked for payment of the maturity amount and was informed that the cheque was delivered and encashed through a co-operative bank. Kajol files a complaint against the mutual fund for deficiency in service and seeks relief. Will she succeed ?*

(5 marks each)

Answer 5(a)

A complaint can lie against the Daya Ram Charitable Trust and Diagnostic Centre for deficiency of service. Facts of the case are similar to that of *Kalpavruksha Charitable Trust v. Toshnival Brothers (Bombay) Pvt. Ltd.* [1999 (6) Scale 534]. In the present problem Daya Ram Charitable Trust and Diagnostic Centre cannot claim to be consumer u/s 2(d) of Consumer Protection Act, 1986 in view of the fact that machinery was purchased for commercial purposes, every patient who takes advantage of services of CT Scan Machine has to pay for it, services rendered are not free, only 20% patients are provided free service. Thus, machinery has been used for commercial purposes and hence complaint can lie against the trust for deficiency of service.

Answer 5(b)

Foreign Contribution (Regulation) Act, 1976 regulates the acceptance and utilisation of foreign contribution or foreign hospitality by certain categories of persons or associations. Foreign Hospitality has been defined under Section 2(1)(d) of the Act which means any offer, not being a purely casual one, made by a foreign source for providing a person with the costs of travel to any foreign country or territory or with free board, lodging, transport or medical treatment.

Section 9 prohibits acceptance of foreign hospitality by certain persons except with the prior permission of the Central Government. Accordingly no member of a Legislature, office bearer of a political party, Judge, Government servant or employee of a corporation shall, while visiting any country or territory outside India accept, without the prior permission of the Central Government any foreign hospitality. However, it is not necessary to obtain any such permission for an emergent medical aid needed on account of sudden illness contracted during the visit outside India. But, where such hospitality has been received, the person receiving such hospitality is under obligation to intimate, within one month from the date of receipt of such hospitality, to the Central Government as to the receipt of such hospitality and the source from which and the manner in which such hospitality was received by him.

The Central Government has vide notification dated January 3, 1986 granted general exemption to members of delegations sponsored by the Central Government from seeking prior permission for acceptance of foreign hospitality while visiting any country or territory outside India. Similarly, vide notification dated December 30, 1987 Government servants and employees of the Corporation have also been granted exemption from seeking prior permission of the Central Government for acceptance of foreign hospitality while visiting any country or territory outside India, in pursuance of bilateral agreement between the Government of India and the Government of any foreign country, duly approved by the Department of Economic Affairs and/or for attending long- term/short-term training programme duly approved by the Department of Personnel Affairs.

Answer 5(c)

Kajol can claim refund of amount due on maturity for units purchased in a Mutual Fund Scheme as there is failure on the part of Mutual fund to make the payment due to Kajol. Mutual Fund can be held liable for deficiency in service. Hence Kajol will succeed in her action for deficiency of service.

National Commission in *Unit Trust of India v. K Devi and other* [2004(2) CPR (NC)]. held that the applicant is liable to refund maturity value with interest at 12% and cost Rs.1,000. UTI has committed deficiency of service. UTI can retrieve balance from the bank which is their internal matter.

Question 6

- (a) *Mention the conditions under which the report in respect of samples of air or emission from any chimney, flue or duct or any other outlet will be admissible in evidence under the Air (Prevention and Control of Pollution) Act, 1981.*
- (b) *Describe the powers of the National Environment Appellate Authority.*
- (c) *State briefly the principles of sustainable development.* (5 marks each)

Answer 6(a)

The following steps should be observed by competent officer while taking sample of emission :

- (1) Collect the sample in the presence of occupier or agent.
- (2) Cause to place the sample in a container and mark, seal and sign on the label of container.
- (3) The signature of occupier or agent to be obtained, if they refuse to sign, the officer himself take sample, seal and sign and make a note of the refusal of occupier to sign.
- (4) Send the sample to the laboratory recognised by state board without delay.

Answer 6(b)

Powers of the National Environment Appellate Authority

Section 12 of The National Environment Appellate Authority Act, 1997 confers following powers on the National Environment Appellate Authority, namely:

- 1. Summoning and enforcing the attendance of any person and examining him on oath;
- 2. Inquiring the discovery and production of documents;
- 3. Receiving evidence on affidavits;
- 4. Subject to the provisions of the Indian Evidence Act, 1872 requisitioning any public record from any office;
- 5. Issuing summons for the examination of witnesses or documents;
- 6. Reviewing its decisions;
- 7. Dismissing a representation for default or deciding it exparte;
- 8. Setting aside any order;
- 9. Any other matter which may be prescribed by the Central Government.

Answer 6(c)

Sustainable development refers to the interdependence of environmental, social

and economic systems and promotes equality and justice through people empowerment and a sense of global citizenship.

Over a period of time several principles of sustainable development have been evolved. Some of them are illustrated below :

Polluter Pays Principle

One of the core principles of sustainable development is the “Polluter Pays” Principle. This recognises that the polluter should pay for any environmental damage caused, and that the burden of proof in demonstrating that a particular technology, practice or product is safe should lie with the developer, not the general public.

The Precautionary Principle

The Precautionary Principle urges a willingness to take action in advance of scientific proof of evidence of the need for the proposed action on the grounds that further delay could prove ultimately most costly to society and nature, and, in the longer term, selfish and unfair to future generations.

Preferable Futures

Preferable futures principle includes those which we positively hope for and work to create. In the context of sustainable development, a preferable future includes a cleaner environment, a sustained level of economic development but not involving excessive waste and pollution, and the protection of natural resources and biodiversity.

Question 7

(a) *Discuss any two of the following :*

- (i) *Principles governing domestic inquiry.*
- (ii) *Payment of subsistence allowance to a suspended workman under the Industrial Employment (Standing Orders) Act, 1946.*
- (iii) *Social security.* (5 marks each)

(b) *Attempt any five of the following stating the relevant legal provisions and case law, if any :*

- (i) *A development officer of an insurance company used to remain absent from duty without leave. He was asked to show cause why he should not be removed from the service. He sent his reply. Thereupon, he was removed from the service without holding any inquiry. Is the removal justified ?*
- (ii) *There was a dispute between the management of Daisy Mills Ltd. and its workers' union on the issue of wage revision. During the arbitration proceedings, the workers' union decided to go on strike. Is the decision of the workers' union lawful ?*
- (iii) *The workers of a factory gheraoed the factory manager at the factory premises and restrained him for 2 hours. During this period, there was no assault on the manager or any kind of criminal trespass. Will the workers be liable for having committed an offence under the Trade Unions Act, 1926 ?*

- (iv) *The Board of directors of a company appointed its deputy general manager, who controlled the operational activities of the factory, as its 'occupier'. The Chief Inspector of Factories (CIOF) did not approve the appointment. Can the company succeed against the CIOF for having refused to accept its senior functionary's appointment as the 'occupier' ?*
- (v) *While fixing total remuneration, the employer included travelling allowance as part of the remuneration of an employee. The employee claimed that the employer has to include travelling allowance also for the purpose of payment of contribution towards ESI fund. Will he succeed ?*
- (vi) *Ramesh was occupying service quarters of a company at the time of retirement. He did not vacate the house after retirement. The company withheld the payment of gratuity to the retired employee on this ground. Can Ramesh claim the payment of gratuity and succeed against the employer?*
- (vii) *Due to accumulation of stocks, the company declared lay-off for 5 days. The workers' union protested that it was not the legal right of the employer to lay-off the workers and that they should be paid full wages for the period of lay-off. Will they succeed in a court of law, if the employer refuses to concede to their demand ?*
- (viii) *Manmauji, an employee, was suspended for an alleged misconduct. An inquiry was conducted and the charges against him could not be proved. As a result, he was reinstated with full back wages. The employee was, however, not paid bonus for the period of suspension. Can he challenge the employer's action ?* (3 marks each)

Answer 7(a)(i)

Principles governing Domestic Enquiry

- (a) The enquiry should be conducted by an unbiased person.
- (b) He should conduct the enquiry impartially, objectively and fairly.
- (c) The employee should be given a fair opportunity to defend himself.
- (d) If any criminal proceeding is pending against the employee, the Enquiry Officer need not wait for the completion of those proceedings [*DCM v. Kushal Bhim AIR 1960 SC 806*].
- (e) Preliminary enquiry is fact finding and differs from domestic enquiry.
- (f) Proper procedure, rules/regulations, principles of natural justice should be followed while conducting enquiry.
- (g) The enquiry officer should report whether charges are proved or not.

Answer 7(a)(ii)

Payment of Subsistence Allowance

As per Section 10A of the Industrial Employment (Standing Orders) Act, 1946 on suspension, a workmen is entitled to subsistence allowance @ 50 per cent of his last

drawn wages prior to suspension for the first 90 days of suspension and @ 75 % of such wages for the remaining period of suspension if the delay in completion of disciplinary proceedings against such workmen is not directly attributable to the conduct of such workman.

If any dispute arises regarding the subsistence allowance payable to a workman, the workman or the employer concerned may refer the dispute to the Labour Court constituted under the Industrial Disputes Act, 1947 and its decision shall be final and binding on the parties.

Answer 7(a)(iii)

Social Security

Social security is based on the recognition of the rights guaranteed by law to all human beings who live from their own labour and find themselves unable to work temporarily or permanently for reasons beyond their control. The State, as an agent of change, has to develop a system of providing protection to its labour through a legislative, as well as an administrative mechanism, so as to provide responsive, efficient, and long term assistance to its work force.

In India, social security measures draw their strength from the Directive Principles of State Policy under the Constitution (Article 41), which inter-alia, enjoins upon the State, to strive to promote the welfare of the people by securing and protecting, as effectively as it may, a just economic and social order. The principal social security legislations are:

- The Employees' State Insurance Act, 1948
- The Employees' Provident Funds & Miscellaneous Provisions Act, 1952
- The Maternity Benefit Act, 1961
- The Payment of Gratuity Act, 1972
- The Workmen's Compensation Act, 1923

Answer 7(b)

- (i) The removal is not justified without holding an enquiry. In *State of Rajasthan v. Sujata Malhotra*, 2002(93) FLR 616 (SC), the Supreme Court has reiterated that in case of unauthorized absence of an employee for a long period, the termination of services after holding the departmental enquiry is proper.
- (ii) The decision of the workers' union is not lawful as per the provisions of the Section 23(bb) of the Industrial Disputes Act, 1947 which prohibits such strikes. It says that "no workman who is employed in any industrial establishment shall go on strike in breach of contract during the pendency of arbitration proceedings before an arbitrator and two months after the conclusion of such proceedings, where a notification has been issued under sub-section (3-A) of Section 10-A. The underlying reason behind this Section is that where a dispute has been referred to conciliation/arbitration or adjudication, a strike or lock out, in furtherance thereof is both unnecessary and inexpedient.
- (iii) Since there was no assault on the manager or any kind of criminal trespass, the workers have not committed any offence under the Trade Unions Act, 1946.

- (iv) The company cannot succeed. The Supreme Court in *J.K. Industries Ltd. v. Chief Inspector of Factories* (1997) 1 L.L.J. SC 722, has held that only a member of Board of Directors of the Company can be occupier of the factory of the Company. The ultimate control of factory owned by company vests in Board of Directors. Ultimate control which vests in Board of Directors cannot be vested in any one else. Company owning factory cannot nominate its employees or officers except Director of the company as occupier of its factory.
- (v) Travelling allowance paid to employee is to defray special expenses entailed on him by nature of his employment. It does not form part of wages as defined under section 2(22) of the ESI Act, 1948. Therefore, the employer is not liable to pay contribution on traveling allowance.
- (vi) Ramesh can claim gratuity. Gratuity cannot be withheld for non vacation of service quarters by retiring employees. (*Air India v. Authority under the Act*, 1999 CLA 34 Bom.66)
- (vii) In the given problem, the employer is unable to give employment to its employees *due to the accumulation of stocks*. The failure, refusal or inability of an employer to give employment to a workman on account of accumulation of stocks is one of the grounds of lay off under Section 2(kkk) of the Industrial Disputes Act, 1947 which defines "lay-off."

If the employees are laid off in pursuance to the provisions of the Section 2(kkk) of the Industrial Disputes Act, 1947, they are entitled to lay-off compensation in accordance with the provisions of Section 25C of the Industrial Disputes Act, 1947 which inter-alia provides:

"Whenever a workman (other than a *badli* workman or a casual workman) whose name is borne on the muster rolls of an industrial establishment and who has completed not less than one year of continuous service under an employer is laid-off, whether continuously or intermittently, he shall be paid by the employer for all days during which he is so laid-off, except for such weekly holidays as may intervene, compensation which shall be equal to fifty percent (50%) of the total of the basic wages and dearness allowance that would have been payable to him had he not been so laid-off".

In view of the legal provisions mentioned above, the workers' union will not succeed. The workers will get compensation equal to fifty percent of the total of the basic wages and dearness allowance that would have been payable to them. The employer is justified in refusing to concede to their demand.

- (viii) Manmauji can challenge the employer's action. Bonus can be paid to a dismissed employee if he is reinstated with full back wages. It was held in the case of *Project Manager, Ahmadabad Project, ONGC v. Sham Kumar* (1995) 1 LLJ 863 that an employee suspended but subsequently reinstated with full back wages cannot be treated to be ineligible for bonus for the period of suspension.

SECURITIES LAWS AND REGULATION OF FINANCIAL MARKETS

Time allowed : 3 hours

Maximum marks : 100

NOTE : Answer SIX questions including Question No. 1 which is **COMPULSORY**.

Question 1

Write notes on any four of the following :

- (i) *Securities Appellate Tribunal (SAT)*
 - (ii) *Asset management company*
 - (iii) *Promoters quota*
 - (iv) *Market capitalisation*
 - (v) *Depository participants.*
- (5 marks each)*

Answer 1(i)

Securities Appellate Tribunal (SAT)

The Central Government, by any notification may establish an appellate tribunal known as Securities Appellate Tribunal (SAT) to exercise the jurisdiction, powers and authority conferred on such tribunal under the SEBI Act, 1992. SAT shall consist of one person known as presiding officer to be appointed by Central Government. The Central Government shall appoint such staff, as it may deem fit, in the SAT. Any aggrieved person may refer an appeal to a Securities Appellate Tribunal having jurisdiction in the matter. On receipt of an appeal the SAT, after giving the parties opportunities to be heard, may pass such order, as it thinks fit. The SAT is not bound by the Code of Civil Procedure, 1908 but is guided by the principle of natural justice and has the powers to regulate its own proceedings.

Answer 1(ii)

Asset management company

Under SEBI (Mutual Funds) Regulations, every mutual fund is required to have an Asset Management Company (AMC) incorporated under the Companies Act, 1956 to manage the funds of the mutual fund. The AMC should be approved by SEBI and should enter into an agreement with the trustees of the mutual fund to formulate schemes, raise money against units, invest the funds in accrued securities and after meeting the permissible costs as per norms, distribute income to the share holders of the funds. AMC is responsible for operations of Mutual Funds. It has to take all reasonable steps and exercise due diligence to ensure that the investments of the funds or any scheme is not contrary to the provisions of these regulations and trust deed.

Answer 1(iii)

Promoters quota

“Promoters quota” means the shares kept reserved for allotment to promoters in case of issue of shares by listed companies. The SEBI (Disclosure and Investor

Protection) Guidelines 2000 stipulates the minimum promoter's contribution and also the limit upto which the promoters shall participate in the issue of securities. The rationale behind prescribing the lock-in-period on promoters' quota is to restrict the promoters from selling their stake in the company after inducing the public to invest this money and to ensure that the promoters take serious efforts to make the project successful for which public money is raised by issue of shares.

Answer 1(iv)

Market capitalization

Market capitalization is referred to be strength of the stock exchange. It is arrived at by multiplying the current market price with the number of shares issued and outstanding. During post liberalization period, market capitalization of Indian stock exchanges has increased significantly. The market capitalization of NSE and BSE as at the end of March 2005 amounted to Rs. 15,855,853 million and Rs. 16,984,280 million respectively

Answer 1(v)

Depository Participants

SEBI regulations provides various categories of market participants who are eligible to become depository participants. These categories already have a well-established customer interface network and are, therefore, the ideal choice to become the agents of a depository. These categories are : Public Financial Institutions; Scheduled Banks; RBI approved foreign banks operating in India; State Financial Corporations; Certified custodians of securities; Clearing corporations of stock exchanges; Registered stock brokers Non-Banking Financial Companies; Registrars and transfer agents. Depository Participant act as an agent of the depository and its role and functions includes opening and maintaining of demat account of the investor; processing dematerialisation and rematerialisation of securities; to make debit/credit in the demat accounts of the investors/ his clients as per instructions given by the account holder; providing statements of accounts to the investors; and facilitating pledge or hypothecation of securities held in demat account.

Question 2

(a) *Distinguish between any three of the following :*

- (i) *'Open-ended scheme' and 'close-ended scheme' of mutual funds.*
- (ii) *'Money market' and 'capital market'.*
- (iii) *'Advertisement' and 'statement in lieu of advertisement'.*
- (iv) *'Dematerialisation' and 'rematerialisation'. (2 marks each)*

(b) *On 30th October, 2005, Shan Co-operative Bank buys 91-day treasury bill maturing on 24th December, 2005. The rate quoted by the seller is Rs.99.25 per Rs.100 face value. Calculate the yield percentage of the treasury bill. (5 marks)*

(c) *Give full form of any five of the following :*

- (i) NASDAQ

- (ii) *ADR*
- (iii) *SEC*
- (iv) *NAV*
- (v) *NSE*
- (vi) *CDSL*.

(1 mark each)

Answer 2 (a)(i)**Open-ended Schemes and Close-ended Scheme of mutual funds**

Difference between 'Open-ended' and 'Close-ended' investment schemes of mutual funds is as follows

<i>OPEN-ENDED SCHEMES</i>	<i>CLOSE-ENDED SCHEMES</i>
1. Variable corpus due to on going purchase and redemption	Fixed corpus: no new units can be offered beyond the limit
2. No listing on exchange transactions done directly with the fund	Listed on the stock exchange for buying and selling
3. Only one price namely NAV	Two values available namely NAV and the Market Trading Price
4. Highly Liquid	Mostly liquid

Answer 2(a)(ii)**Money Market and Capital Market**

The money market refers to the market where borrowers and lenders exchange short-term funds to solve their liquidity needs. Money market instruments are generally financial claims that have low default risk, maturities under one year and high marketability.

The Capital Market is a market for financial investments that are direct or indirect claims to capital. It is wider than the Securities Market and embraces all form of lending and borrowing. The Capital Market comprises the complex of institutions and mechanisms through which intermediate term funds and long-term funds are pooled and made available to business, government and individuals. The Capital Market also encompasses the process by which securities already outstanding are transferred.

Answer 2(a)(iii)**Advertisement and Statement in lieu of advertisement**

Every miscellaneous non-banking company inviting deposits is required to comply with the provisions relating to advertisement under Non-Banking Financial Companies and Miscellaneous Non-Banking Companies (Advertisement) Rules, 1977

However, where a company intends to accept deposits without inviting or allowing or causing any other person to invite such deposits, it shall before accepting deposits, deliver to the Regional Office of the Department of Supervision of the Reserve Bank, within whose jurisdiction its registered office is situated, for registration, a statement in lieu of advertisement containing all the particulars required to be included in the

advertisement pursuant to the Non-Banking Financial Companies and Miscellaneous Non-Banking Companies (Advertisement) Rules, 1977 duly signed in the manner provided in the aforesaid Rules.

Answer 2(a)(iv)

Dematerialisation and rematerialisation

Dematerialisation is a process of either issue of dematerialized securities or conversion of physical share certificates into distinctive numbers. In process of conversion, the physical share certificates from the investor are taken back by the Company and an equivalent number of securities are credited his account opened with a depository participant in electronic form at the request of the investor.

Holding of shares in Dematerialised form in the hands of investors is optional and an investor can still hold shares in physical form. Therefore the investor who has dematerialized shares with him can send a Rematerialisation Request Form to DP for conversion of his shares to the physical share certificates. This process of such conversion is known as rematerialisation.

Answer 2(b)

Yield percentage of treasury bill :

$$YTM = \frac{(100 - P) \times 365 \times 100}{P \times D}$$

Where P = Price

D = Days to Maturity

P = 99.25

D = 55 days

$$YTM = \frac{(100 - 99.25) \times 365 \times 100}{99.25 \times 55}$$

$$YTM = \frac{(0.75) \times 365 \times 100}{99.25 \times 55} = \frac{27,375}{5458.75}$$

$$= 5.01\%$$

Answer 2(c)

- (i) NASDAQ - National Association of Securities Dealers Automated Quotations.
- (ii) ADR - American Depository Receipt.
- (iii) SEC – US Securities Exchange Commission.
- (iv) NAV – Net asset value.
- (V) NSE – National Stock Exchange of India Ltd.
- (vi) CDSL - The Central Depository Services (India) Limited.

Question 3

- (a) *Discuss the role of securities market in economic growth.* (5 marks)
- (b) *“Buy-back of shares is a corporate financial strategy.” Comment.* (5 marks)
- (c) *Global Systems Ltd., an existing listed company, wants to make a bonus issue of equity shares. As the Company Secretary of Global Systems Ltd., prepare a note on the SEBI guidelines as applicable in this regard.* (6 marks)

Answer 3(a)**Securities Market and Economic Growth**

A well functioning securities market is conducive to sustained economic growth. There have been a number of studies, starting from World Bank and IMF to various scholars, which have established robust relationship not only one way, but also the both ways, between the development in the securities market and the economic growth. The securities market fosters economic growth to the extent that it-(a) augments the quantities of real savings and capital formation from any given level of national income, (b) increases net capital inflow from abroad, (c) raises the productivity of investment by improving allocation of investible funds, and (d) reduces the cost of capital.

Thus, the savings and capital accumulation and formation respond favourably to developments in securities market. The Securities Market provides a bridge between ultimate savers and ultimate investors and creates the opportunity to put the savings at the disposal of enterprising, thus promising to raise the total level of investment and growth.

Answer 3(b)

It is rightly said that buy-back of securities is a corporate financial strategy. Strategy is a competitive plan intended to achieve certain purpose and buy-back is a part of financial plan for dealing with capital restructuring and is prevalent globally with the underlying objective of realigning the capital structure, improving returns to the stakeholders, averting hostile takeovers, increasing EPS as well as market value of shares and net worth of company. In India, buy back of securities is not permitted as a treasury option under which the securities may be reissued later, a company can resort to buy-back to reduce the number of shares issued and return surplus cash to shareholders.

Answer 3(c)

June 15, 2006

From : Company secretary

To : Managing Director

As desired, the Requirements to be complied with while making a Bonus Issue are given hereunder :

1. *Rights of FCD/PCD holders*

The proposed bonus issue should not dilute the value or rights of the fully or partly convertible debentures. If the conversion of FCD/PCD is pending, the reservation of shares out of bonus issue is to be made in proportion to the

convertible part of FCD's or PCD's. The shares so reserved may be issued at the time of conversion of such debentures on the same terms on which the rights or bonus issues were made.

2. *Out of Free Reserves*

The bonus issue is to be made out of free reserves built out of the genuine profits or securities premium collected in cash only.

3. *Revaluation Reserves*

The reserves created by revaluation of fixed assets should not be capitalised.

4. *Bonus Issue not to be in lieu of Dividend*

Bonus issue should not be made in lieu of dividend.

5. *Fully Paid Shares*

If there are any partly paid-up shares, these shares should be made fully paid-up before the bonus issue is made.

6. *No Default in respect of Fixed Deposits/Debentures*

The company should not have defaulted in the payment of any interest or principal in respect of its fixed deposits and interest on debentures or on redemption of debentures.

7. *Statutory Dues of the Employees*

The company should not have defaulted in the payment of its statutory dues to the employees such as contribution to provident fund, gratuity, bonus, minimum wages, workmen's compensation, retrenchment compensation, payments to contract labour, etc.

8. *Implementation of Proposal within Six Months*

The bonus issue should be made within a period of six months from the date of approval of the Board of directors. The company cannot reverse the decision once it has been taken by the Board of directors.

9. *Provision in Articles of Association*

The Articles of Association of the Company should provide for capitalisation of reserves and if not a General Body Meeting of the company is to be held and a special resolution making provisions in the Articles of Association for capitalisation should be passed.

10. *Authorised Capital*

If consequent upon the issue of bonus shares, the subscribed and paid-up capital of the company exceed the authorised share capital, a General Meeting of the company should be held to pass necessary resolution for increasing the authorised capital.

Submitted please.

(XYZ)

Company Secretary

Question 4

- (a) Briefly explain the following credit rating symbols and indicate against each the name of the concerned rating agencies :
- (i) *mfB+*
 - (ii) *PR3*
 - (iii) *C(ind)*
 - (iv) *Cf* (1 mark each)
- (b) What are the contents covered in the offering circular for euro-issue offerings ? (4 marks)
- (c) What is the eligibility criteria for voluntary delisting of securities ? (4 marks)
- (d) State the main recommendations of Narasimhan Committee regarding development of Indian capital market. (4 marks)

Answer 4(a)

- (i) *mfB+* - ICRA Rating symbol for credit risk rating of debt funds indicates poor quality. The investment quality is of lowest grade and is similar to that of fixed income obligations that are risk prone.
- (ii) *PR3* – CARE Rating symbol used for short term instruments. The PR3 indicates that instruments have an adequate capacity for repayment of short term promissory obligations. Variability in earnings and profitability may result in changes in the level of debt protection. The effect of industry characteristics and market composition may be more pronounced.
- (iii) *C(ind)* – Fitch India Rating Symbol used for long term (12 months and above) speculative grade. 'C(ind)' ratings indicate high and imminent default risk. Capacity for meeting financial commitments is solely reliant upon sustained, favourable business or economic developments.
- (iv) *Cf* – CRISIL Bond Fund Rating symbol. Indicates that the fund's portfolio holdings have factors present which make them vulnerable to credit defaults.

Answer 4(b)

The Offering Circular should be very comprehensive to take care of overall interests of the prospective investor. The Offering Circular for Euro-issue offering should typically cover

Background of the company and its promoters including date of incorporation and objects, past performance, production, sales and distribution network, future plans, etc.; Capital structure of the company-existing, proposed and consolidated; Deployment of issue proceeds; Financial data indicating track record of consistent profitability of the company; Group investments and their performance including subsidiaries, joint venture in India and abroad; Investment considerations; Description of shares; Terms and conditions of GDR; Economic and regulatory policies of the Government of India; Details of Indian securities market; Market price of securities; Dividend and capitalization; Securities regulations and exchange control; Tax aspects ; Status of approvals required

to be obtained from Government of India; Summary of significant differences in Indian GAAP, UK GAAP and US GAAP and expert's opinion; Report of statutory auditor; Subscription and sale; Transfer restrictions in respect of instruments; Legal matters etc. and any other general information not forming part of any of the above.

Answer 4(c)

The Securities and Exchange Board of India (Delisting of Securities) Guidelines 2003, issued with the objective to protect the interest of investors in the securities market, deal with Voluntary delisting. As per the Guidelines, Eligibility Criteria for Voluntary Delisting include the following :

1. The securities of the company have been listed for a minimum period of 3 years on any stock exchange.
2. A company, which has a convertible instrument outstanding, shall not be permitted to delist its equity shares, till the exercise of the conversion options.
3. A company may delist one or all of its class of securities. However, if the equity shares of a company are delisted, the fixed income securities may continue to remain listed on the stock exchange.
4. An exit price is required to be determined in accordance with the book building process described in the Delisting Guidelines.

Answer 4(d)

The Government of India had set up a High level Committee to examine all aspects relating to the structure, organization, functions and procedures of the financial system under the chairmanship of Shri M Narasimhan. The Committee observed that the growth of the newer forms of financial institutions is an indication of the growing volume and diversification of the capital market. For the business to grow on sound lines, a framework of regulations is however necessary as a measure of investor protection. The Committee believes that the present measure of control on the capital market requires urgent review. SEBI should be involved in prior sanction of new capital issued in respect of companies whose scrips are listed on the stock exchanges. The Committee also recommended for opening up of the capital market for foreign portfolio investments. The Committee also recommended capital adequacy of 8% for Indian banks.

Question 5

(a) Define and state the functions of any four of the following :

- (i) Lead manager
- (ii) Banker to an issue
- (iii) Share transfer agent
- (iv) Debenture trustee
- (v) Underwriter.

(2 marks each)

(b) You are the Company Secretary of Swift IT Solutions Ltd., which is a newly listed company, and your managing director wants you to prepare a note on the requirements relating to publication of quarterly financial results. Briefly outline the various requirements of clause 41 of the listing agreement in this regard.

(8 marks)

Answer 5(a)

- (i) *Lead Manager* — All public issues are required to be managed by at least one merchant banker functioning as lead manager. Legal Manager undertakes activities relating to management of an issue of capital, investment advice and act as manager, consultant and advisor to the issue.
- (ii) *Bankers to issue* — Bankers to issue carries on the activities relating to acceptance of application and application monies, acceptance of allotment or call monies, refund of application monies and payment of dividend or interest warrants. Banker to an issue is under obligation to maintain records on applications received with date, amount received and name of investors, time taken to forward the applications to issuer/its register. He enters into an agreement with the issuer on matters connected to number of collection centres, time for forwarding prescribed details, daily statement to controlling branches.
- (iii) *Share Transfer Agent* — Share Transfer Agent (STA) maintains the records of holders of securities issued by body corporate and deals with all matters connected with the transfer and redemption of its securities. STA thus carries out activities of maintenance of shareholders/investors database, carries out corporate action from time to time and provide services to investors of the company. Share transfer agent shall exercise adequate care caution and due diligence before dematerialisation of securities by confirming and verifying that the securities to be dematerialized have been granted listing permission by stock exchanges.
- (iv) *Debenture Trustee* — Debenture Trustee is a trustee of a trust deed for securing any issue of debentures of a body corporate. No company can issue a prospectus or letter of offer to the public for subscription of its debentures, unless the company has appointed one or more debenture trustees for such debentures in accordance with the provisions of the Companies Act, 1956.
- (v) *Underwriter* — Underwriter facilitates raising of capital by assuming to take up unsubscribed portion upto a specified limit. Underwriter enters into an arrangement with company to subscribe to the securities of the company when the existing shareholders of the company or the public do not subscribe to the securities offered to them.

Answer 5(b)

From : XYZ, Company Secretary

To : Managing Director, Swift IT Solutions Ltd.

SUB : Requirements of Clause 41 of the Listing Agreement

This is one of the most important requirements of the listing agreement. The stock exchange have from time to time amended clause 41 in the listing agreement pertaining to the publishing of financial result. For the last quarter of the financial year, if the company intimates in advance to the Stock Exchange (s) that it will publish audited results within a period of three months from the end of the last quarter of the financial year, unaudited results for the last quarter need not be published/given to the stock Exchange(s).

In addition to the above, the company must prepare half yearly results in the same proforma and the same must be approved the Board of Directors and must be subject to a limited review by the auditors of the company. The copy of the review report must be submitted to stock exchanges within 2 months after the close of the half year. If the sum total of the first and second quarterly un-audited results of any items given in the same proforma format varies by 20% or more from the respective half yearly results as determined after the limited review by the auditors, the company must send a statement as approved by the board of directors explaining reasons thereof to the stock exchanges along with the review report.

To comply with the requirements of publishing quarterly results, the following action has to be taken:-

- Intimate to Stock Exchanges at least 7 days in advance about the date of Board Meetings
- Along with the intimation, a press release has to be issued immediately in at least one national newspaper and one regional language newspaper about the date of the Board Meeting.
- Send by fax within 15 minutes of the conclusion of the Board Meeting the financial results to the stock exchange.
- Publish within 48 hours of the conclusion of the Board Meeting in at least one English daily newspaper circulating in the whole of India and in one newspaper published in the language of the region, where the registered office of the company is situated.
- After publishing the results, send a copy of the published results to stock exchange(s).

Submitted Please.

Sd/-

XYZ

Company Secretary

Question 6

- (a) What do you understand by 'IDR' ? Explain the eligibility criteria for an IDR. (4 marks)
- (b) What do you understand by any two of the following in relation to venture funds:
 - (i) Incubators
 - (ii) Angel investors
 - (iii) Private equity players ? (2 marks each)
- (c) Why should an investor prefer to invest in government securities ? Discuss the benefits. (4 marks)
- (d) Explain the investment norms applicable to NBFCs. (4 marks)

Answer 6(a)**Indian Depository Receipts**

“Indian Depository Receipt” means any instrument in the form of a depository receipt created by Domestic Depository in India against the underlying equity shares of issuing company.

Eligibility for issue of IDRs

An issuing company can issue IDRs only if it satisfies the following conditions:

- (i) Its pre-issue paid-up capital and free reserves are at least US\$ 100 millions and it has had an average turnover of US\$ 500 million during the 3 financial years preceding the issue.
- (ii) It has been making profits for at least five years preceding the issue and has been declaring dividend of not less than 10% each year for the said period.
- (iii) Its pre-issue debt equity ratio is not more than 2:1.
- (iv) It should fulfill the eligibility criteria laid down by SEBI from time to time.

Answer 6(b)**(i) Incubators**

An incubator is a hardcore technocrat who works with an entrepreneur to develop a business idea, and prepares a Company for subsequent rounds of growth & funding. E-Ventures, Infinity are examples of incubators in India.

(ii) Angel Investors

An angel is an experienced industry-bred individual with high net worth. Typically, an angel investor would invest only his chosen field of technology, take active participation in day-to-day running of the Company, invest small sums in the range of USD 1-3 million and does not insist on detailed business plans sanction.

(iii) Private Equity Players

They are established investment bankers. They typically invest into proven/ established businesses. They have “financial partners” approach and invest between USD 5-100 million.

Answer 6(c)

Government securities (G-secs) are sovereign securities which are issued by the Reserve Bank of India on behalf of Government of India, in lieu of the Central Government's market borrowing programme. The term Government Securities includes. Central Government Securities, State Government Securities and Treasury Bills. Being risk free securities, they set the benchmark for the interest rates of the other money market instruments. Investing in Government Securities provide the following benefits :

- (i) No tax deducted at source; (ii) Additional Income Tax benefit u/s 80L of the Income Tax Act for individuals, (iii) Qualities for SLR purpose (iv) Zero default risk being sovereign paper (v) Highly liquid (v) Transparency in transactions and simplified settlement procedures through CDSL/NSDL.

Answer 6(d)**Investment Norms for NBFCs**

The provisions of the RBI (Amendment) Act, 1997 (section 45B) stipulated the requirement of maintenance of assets in the approved securities whose market value shall not be less than 5 per cent or such higher percentage not exceeding 25 per cent as the RBI may specify the deposits outstanding at the end of the last working day of the second preceding quarter. Every NBFC shall create a reserve fund and transfer therein at least 20 per cent of its net profit every year. NBFCs are required to maintain liquid assets equivalent to 10 per cent of their deposit liabilities in specified approved securities. Similarly norms have been prescribed considering the nature and types of NBFCs including loan and investment companies, leasing and hire-purchase companies, residuary non-banking companies etc.

Question 7

- (a) *What are the requirements for registration of Foreign Institutional Investors (FIIs)?*
(4 marks)
- (b) *Highlight the provisions of revised clause 49 of the listing agreement.* (12 marks)

Answer 7(a)

SEBI may require the applicant making an application for registration as FII, to furnish such further information or clarification as SEBI considers necessary regarding matters relevant to the activities of the applicant for grant of certificate. While granting certificate of Registration as FII, SEBI should take into account the following matters:

- (i) the applicant's track record, professional competence, financial soundness, experience, general reputation of fairness and integrity;
- (ii) whether the applicant is regulated by an appropriate foreign regulatory authority;
- (iii) whether the applicant has been granted permission under FEMA for making investments in India as FII ;
- (iv) whether the applicant is an institution established or incorporated outside India as Pension Fund or Mutual Fund or Investment Trust; or an Asset Management Company or Nominee Company or Bank or Institutional Portfolio Manager, established or incorporated outside India and proposing to make investments in India on behalf of broad based funds and its proprietary funds, if any; or a Trustee or a Power of Attorney holder, incorporated or established outside India, and proposing to make investments in India on behalf of broad based funds and its proprietary funds, if any; university fund, endowments, foundations or charitable trusts or charitable societies and whether the applicant is a fit and proper person.

Answer 7(b)

Clause 49 of the listing agreement deals with good Corporate Governance practices and the salient provisions are as follows:

1. *Board of Directors* : Board should have optimum combination of executive and non-executive directors with not less than 50% of the Board consisting of non-

executive directors. If the Board has a non-executive Chairman then at least 1/3 of the Board should consist of independent directors and in case of an executive Chairman, at least half of the Board should consist of independent directors.

2. *Audit Committee* : A qualified and independent Audit Committee shall be constituted. It shall have minimum three members and two third of members of Audit Committee shall be independent. All members of the audit Committee shall be financially literate and at least one member shall have accounting or related financial management expertise knowledge. The Chairman of the Committee shall be an independent director and he shall be present at the AGM to answer shareholder queries. The Audit Committee shall meet thrice a year. The Audit Committee shall oversee the Company's financial reporting process and disclosure of financial information. It shall review the annual accounts before submission to the Board. Besides performing other functions, it shall also review the internal audit function and internal control systems.
3. *Remuneration of Directors* : All pecuniary relationships or transactions of non-executive directors vis-à-vis the company shall be disclosed in the annual report.
4. *Board Procedure* : This deals with minimum number of four meetings in a year with a maximum gap of four months between any two meetings. Certain minimum information is to be made available to the Board.
5. *Management* : Management discussion and analysis report should form part of the annual report. It should contain details regarding (a) industry structure and developments; (b) opportunities and threats; (c) segment wise or product wise performance; (d) outlook; (e) Risks and concerns; (f) Internal Control Systems and their adequacy; (g) discussion on financial performance with respect to operational performance ; (h) material developments in Human Resources/ individual relations front.
6. *Shareholders* : Information to Shareholders to be given about appointment of new directors, their background, expertise in specific areas, details of directorships and their shareholding. Information on quarterly results and presentations made by the company to analysis should be put on website of company.
7. *Report on Corporate Governance* : The annual report shall contain a separate section on Corporate Governance with a detailed compliance report on Corporate Governance. It should contain information on composition and category of Board of Directors attendance of each Director, Composition of Committees viz. Audit committee, Remuneration Committee, disclosures on materially significant related party transaction, means of communication etc.
8. *Compliance* : The company should also obtain a certificate either from the auditors or practising company secretary of the company regarding the compliance of the conditions of corporate governance and annex it to the directors' report which is sent to all the shareholders of the company. The certificate should be sent to the Stock Exchange alongwith the annual report filed by the company. This certificate is necessary otherwise this will lead to the violation of the requirements of the listing agreement.

Question 8

- (a) Explain any two of the following terms of the secondary market :
- (i) Forward trading
 - (ii) Kerb trading
 - (iii) Odd-lot trading. (2 marks each)
- (b) What is 'escrow account' ? Discuss the provisions of escrow account as per the SEBI Takeover Code. (4 marks)
- (c) What are the common grievances of investors in India ? State investors' grievances redressal authorities in India. (4 marks)
- (d) What do you mean by 'derivatives' ? Name the most commonly traded derivatives. (4 marks)

Answer 8(a)**(i) Forward Trading**

Forward trading relates to carrying over the transactions/settlement to the next settlement period. If an investor sells shares and wants to carry forward, he gets profits when the shares price falls and loose if rises. To carry forward his short position, he has to pay a backwardalism charge or undha badla for borrowing the share certificate. He has to enter into a contract to resell the shares to the lender at the next settlement period and pay interest rate.

(ii) Kerb trading

Transactions are often carried out in the stock exchanges after official trading hours too, even though such trading among the members is not strictly legal. Such unauthorised trading carried out outside the official hours is known as kerb trading.

(iii) Odd-lot trading

Anything less than the standard unit of trading is odd lot. Thus, when the securities are not in marketable lots, they are known as odd lots. Odd lots have limited liquidity and are traded at a discount in the market. However, in case of computerized trading system in demat form, trading lot has lost its relevance.

Answer 8(b)

Escrow account means an account in which money is held until a specified duty is performed. The Regulations 28 of SEBI Takeover Regulations require cash deposit in an Escrow Account before the public announcement and forfeiture thereof if the acquirer fails to discharge his obligations under the offer. The amount is to be calculated as follows :

- (i) For consideration payable under the public offer – upto and including 100 crores – 25%; exceeding Rs. 100 crore – 25% upto Rs.100 crore and 10% thereafter.
- (ii) For the offers which are subject to minimum level of acceptance and the acquirer does not want to acquire a minimum of 20 per cent, then 50% of the consideration

payable under the public offer in cash is required to be deposited in escrow account.

The Escrow Account may consist of cash deposited with a scheduled commercial bank, bank guarantee in favour of merchant banker, deposit of acceptable securities with appropriate margin with the merchant banker and cash deposited with a scheduled commercial bank. The escrow amount deposited with the bank in cash can be released only in the manner provided in the Regulations.

Answer 8(c)

Various common grievances of investors in India are as follows :

1. In case of any public issue, Non-receipt of, Refund order Interest on delayed refund, Allotment advice, Share certificates, Duplicates for all of the above, and revalidations
2. In case of a listed security, Non-receipt of the certificates after Transfer, Transmission, Conversion, Endorsement, Consolidation, Splitting, Duplicates of securities,
3. Regarding listed debentures, non-receipt of Interest due, redemption proceeds, Interest on delayed payment, Regarding bad delivery of shares
4. Grievance relating to share or debentures in unlisted companies
5. Grievance relating to Deposits in collective investment schemes like planations etc. and Units of Mutual Funds; Fixed Deposits in Banks And Finance Companies and manufacturing companies

In respect of the grievances of investor, complaints can be lodged with the Registrar of Companies, Ministry of Company Affairs stock exchanges or SEBI as the case may be and in certain cases, they can be pursued with the Company Law Board also to obtain remedies and relief. Investor Grievance Centres have been set up in every recognized stock exchange which take up all complaints regarding the trades effected in the exchange and the relevant member of the exchange. Moreover, two other avenues are always available to the investors to seek redressal of their complaints i.e Complaints with Consumers Disputes Redressal Forum and Suits in the Court of Law.

Answer 8(d)

Derivatives are contracts which derive their values from the value of one or more of other assets (known as underlying assets). According to Securities Contracts (Regulations) Act, 1956, derivatives include :

- (a) A security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security.
- (b) A contract which derives its value from the prices or index of prices, of underlying securities.

Derivatives thus are meant essentially to facilitate temporarily hedging of price risk of inventory holding or a financial / commercial transaction over a certain period. Every derivative contract has a fixed expiration date.

The most commonly traded derivatives are stock futures.
