

CORPORATE RESTRUCTURING AND INSOLVENCY

Time allowed : 3 hours

Maximum marks : 100

NOTE : All references to sections relate to the Companies Act, 1956 unless stated otherwise.

PART A

(Answer Question No.1 which is compulsory and any three of the rest from this part.)

Question 1

- (a) (i) ABC Ltd. has 700 creditors (in number) representing total value of Rs.100 crore as per its balance sheet. In a creditors meeting called under section 391 for considering proposed scheme of amalgamation with XYZ Ltd., out of total 700 creditors, only 150 creditors representing value of Rs.45 crore were present. Out of said 150 creditors present at the said meeting, only 140 creditors representing value of Rs.40 crore voted in favour of the resolution, while 10 creditors representing value of Rs.5 crore cast their dissenting vote against the scheme. Whether the motion proposing the scheme of amalgamation should be treated as approved or not ? Explain with reference to relevant provisions of law and case law, if any. (5 marks)
- (ii) In a scheme of arrangement made under section 391, a company proposes to transfer one of its undertakings to its subsidiary and also to reduce its share capital. Is the scheme valid ? Explain with relevant provisions of law and relevant cases. (5 marks)
- (b) State whether the following statements are true or false citing briefly relevant provisions of the law :
- (i) There is a bar on a company amalgamating with a newly incorporated company.
- (ii) A non-profit making company licensed under section 25 can be merged with a profit making company.
- (iii) High Court can sanction a scheme of merger of a sick industrial company when a revival scheme is pending before BIFR.
- (iv) An appeal can be preferred to the Supreme Court of India against the order passed under section 391/394 sanctioning a scheme of amalgamation.
- (v) The court can modify 'transfer date' proposed in a scheme of amalgamation. (2 marks each)
- (c) Explain the provisions relating to buy-back of shares through book-building route. (5 marks)

Answer 1(a)(i)

Yes, the motion proposing the scheme of amalgamation shall be treated as passed.

According to Section 391 (2) of the Companies Act, 1956, the resolution relating to the approval of amalgamation has to be approved by a twin majority i.e.

- A simple majority of members or creditors, as the case may be, who are present and voting at the general meeting, whether in person or through proxy; and

- A majority representing three-fourths in value of the votes of or the value of debt of, members or creditors, respectively, present and voting either in person or by proxy.

In the given case, out of 150 creditors who were present and voting, 140 have voted in favour which means that the first of the twin criteria has been satisfactorily met. In terms of value, those who voted in favour were commanding a value of Rs. 40 Crores as against the value of those who voted against who commanded a value of Rs.5 Crores. In other words, more than three-fourths in value of the votes of the creditors present and voting have voted in favour indicating clearly that the second of the twin criteria has also been satisfactorily met. Thus the resolution approving the amalgamation has been duly passed in accordance with the requirements of Section 391(2) of the Companies Act, 1956.

A full bench of the Punjab and Haryana High Court in *Hind Lever Chemicals Limited and Another* [2005] 58 SCL 211 (Punj&Har) held that in our view, the language of Section 391(2) of the Act is totally unambiguous and a plain reading of this provision clearly shows that the majority in number by which a compromise or arrangement is approved should represent three-fourth in value of the creditors/shareholders who are 'present and voting' and not of the total value of the shareholders or creditors of the company.

Similarly, in *Re: Kirloskar Electric Company Ltd.*, [2003] 116 Com Cas 413 (Kar), the Karnataka High Court held that the three-fourth majority required under sub-section (2) of Section 391 of the Act was of the value represented by the members who were not only present but who had also voted. In fact, it went a step further to hold that the creditors who were present and had even voted but whose votes had been found to be invalid, could not be said to have voted because casting an invalid vote is no voting in the eyes of law. Thus, it was held that "the proper construction to be placed in calculating whether any resolution is approved or passed by a three-fourth majority present and voting necessarily mean the value of the valid votes and out of the same whether the resolution has been passed with three-fourth the majority".

Also in *Hindustan General Electric Corporation Ltd. in re.* (1959) 29 Comp Case 46 (Cal.); the Hon'ble Court has held that in determining whether a resolution has been passed by the requisite majority or not, the members remaining neutral or absenting from the voting need not to be counted. The same view has also been upheld in *Kaveri Entertainment Ltd., in re* (2003) 117 Comp. Case 245 (Bom).

Answer 1(a)(ii)

Yes, the scheme is a valid scheme and is well within the scope of Section 391 read with Section 394 of the Act. In *Larsen & Toubro Limited* In re [2004] 60 CLA 335 (Bom) [2004], the Mumbai High Court held that a composite scheme could be made involving de-merger, of one of the undertakings of the transferor company and for the transfer of the demerged undertaking to a subsidiary company and for the reduction in the capital of the transferor-company. The Court ruled that the word arrangement is not specifically defined under the Act. It has a wide range and ambit. It includes restructuring of capital, reduction of capital and demerger. The scheme of arrangement having the ingredients of demerger and reduction of share capital and scheme of arrangements with the concerned companies and trust, cannot be said to be beyond the purview of sections of the Companies Act.

Answer 1(b)(i)

False : The Hon'ble Gujarat High Court in *Re: Apco Industries Ltd.* (1996) 86 Comp Cas 457 (Guj.) has held that there is no bar to a company amalgamating with a fifteen-day old company having no assets and business.

Answer 1(b)(ii)

True, amalgamation of a company licensed under Section 25 of the Companies Act with a commercial, trading or manufacturing company could be sanctioned under Section 391/394. (*Re. Sir Mathurdas Vissanji Foundation* (1992) 8 CLA 170(Bom.) *Re: Walvis Flour Mill Company P. Ltd.* (1996) 23 CLA 104]. There need not be unison or identity between objects of Transferor Company and Transferee Company. Companies carrying entirely dissimilar businesses can amalgamate. *Re: PMP Auto Inds. Ltd.* (1994) 80 Comp. Case 291 (Bom.).

Answer 1(b)(iii)

False, in similar matter of *Tata Motors Ltd. v. Pharmaceuticals Products of India Ltd. and Another* (2008) 144 Comp. Case 178 (SC), it was held High Court cannot sanction scheme proposed under section 391/394 of the Act during the pendency of the revival scheme before BIFR under SICA. In terms of Section 26 of SICA, a company court did not have jurisdiction to entertain any application of a sick industrial company for merger under s.391 to 394 of the Companies Act 1956, while the matter was pending before the BIFR or the AAIFR.

Similarly in *Ashok Organic Industries Ltd v. ARCIL*, [2008]114 Comp Cas 144 (Bom), the Bombay High Court held that once the Industrial Company makes a reference under Section 15 of the SICA, the Company Court would have no jurisdiction for sanctioning the scheme of arrangement of compromise with its creditors and shareholders and neither will it have jurisdiction to take cognisance of such an application during the pendency of the reference.

Answer 1(b)(iv)

True, as per the existing provisions of the Companies Act, 1956, an appeal can be preferred to the Supreme Court of India against the order passed under Section 391/394 sanctioning a scheme of amalgamation.

Answer 1(b)(v)

True, the Hon'ble Supreme Court in *Marshal Sons & Co. (India) Ltd. v. ITO* (1977) 1 Comp LJ P. 1, observed that it is true that while sanctioning the scheme, it is open to the Court to modify the said date. But when the Court does not prescribe any specific date, the date specified in the scheme is "the transfer date".

Answer 1(c)**Buy Back through Book Building Route**

A company can buy back its securities through the book building process as provided

under Securities and Exchange Board of India (Buy Back of Securities) Regulations, 1998 which is as under:

1. (a) The special resolution as in Regulation 5 or 5A, should specify the maximum price at which the buy back will be made.
 - (b) The company should appoint a merchant banker.
 - (c) A public announcement as referred to in Regulation 8 shall be made atleast 7 days prior to the commencement of the buy back.
 - (d) Subject to the provisions of Sub- clauses (i) and (ii), the provisions of Regulation 10 regarding escrow account are applicable –
 - (i) The deposit in the escrow account should be made before the date of the public announcement.
 - (ii) The amount to be deposited in the escrow account should be determined with reference to the maximum price as specified in the public announcement.
 - (e) A copy of the public announcement must be filed with SEBI within two days of the announcement along with the fees specified in Schedule IV to the Regulations. The public announcement shall also contain the detailed methodology of the book building process, manner of acceptance, format of acceptance to be sent by the security holders pursuant to public announcement and details of bidding centers.
 - (f) The book building process should be made through an electronically linked transparent facility.
 - (g) The number of bidding centers should not be less than thirty and there should be atleast one electronically linked computer terminal at all the bidding centers;
 - (h) The offer for buy back should be kept open to the security holders for a period of not less than fifteen days and not exceeding thirty days.
 - (i) The merchant banker and the company should determine the buy back price based on the acceptances received and the final buy back price which should be the highest price accepted should be paid to all the holders whose securities have been accepted for the buy back.
2. The provisions of Regulation 9(5) pertaining to verification of acceptances and the provisions of Regulation 11 pertaining to opening of special account and payment of consideration are applicable mutatis mutandis.

Question 2

- (a) *Reduction of capital is one of the modes of re-organisation of capital structure of the company and to a certain extent it can be done without the sanction of the court. Explain with relevant provisions of the law.* (7 marks)
- (b) *Strategy is the very soul of any action and activity. Briefly define the strategy with 5Ps of Henry Mintzberg.* (4 marks)

- (c) *In a scheme of compromise, arrangement, reconstruction or amalgamation, various types of approvals are required. Describe briefly such approvals.*

(4 marks)

Answer 2(a)

A company may reorganize its capital in different ways which may include: (a) reduction of paid-up capital; (b) conversion of one type of shares into another; (c) conversion of shares into debentures. There may be many other ways and manner of re-organization of capital. Re-organization of share capital may be proposed between the company and its creditors or class of creditors or members or class of members and requires confirmation of CLB under Section 391. Reduction of capital means reduction of issued, subscribed and paid up capital of the company. Section 100 provides for the reduction of share capital, if the articles of the company so authorize with the confirmation of the Court.

However in following cases, reduction of share capital can be made without sanction of court.

(a) *Surrender of Shares*

This means the surrender of shares already issued to the company by the registered holder of shares. Where shares are surrendered to the company, whether by way of settlement of a dispute or for any other reason, it will have the same effect as a transfer in favour of the company and amount to reduction of capital. But if, under any arrangement such shares instead of being surrendered to the company, are transferred to a nominee of the company then there will be no reduction of capital [*Collector of Moradabad v. Equity Insurance Company Limited (1948) 18 Com Cases 309: AIR 1948 Oudh 197*]. Surrender may be accepted by the company under the same circumstances where forfeiture is justified. It has the effect of releasing the shareholder whose surrender is accepted for further liability on shares.

The Companies Act contains no provisions for surrender of shares. Thus surrender of shares is valid only when Articles of Association provide for the same and:

- (i) Where forfeiture of such shares is justified; or
- (ii) When shares are surrendered in exchange for new shares of same nominal value.

Both forfeiture and surrender lead to termination of membership. However, in the case of forfeiture it is at the initiative of the company and in the case of surrender it is at the initiative of member or shareholder.

(b) *Forfeiture of Shares*

A company may if authorized by its articles, forfeit shares for non- payment of calls and the same will not require confirmation of the court.

Where the power is given in the articles, it must be exercised strictly in accordance with the regulations regarding notice, procedure and manner stated therein, otherwise the forfeiture will be void. Forfeiture will be effected by means of Board resolution. The power of forfeiture must be exercised bona fide and in the interest of the company.

(c) *Diminution of Capital*

Where the company cancels shares which have not been taken or agreed to be taken by any person. [Section 94(1)(3)]

- (d) Redemption of redeemable preference shares
- (e) Purchase of shares of a member by the company under Section 402.
- (f) Buy back of its own shares under Section 77A
- (g) Reduction of capital when company is defunct.

Answer 2(b)

Strategy is the very soul of any action and activity and should be omni-present and therefore every executive and owner needs to be a 'strategist'. Henry Mintzberg enunciated 5 Ps of strategy which are as follows namely:

- 1 A Plan i.e. Strategy is consciously intended course of action which a firm chooses to follow after careful deliberations on the various options available to it.
- 2 A Ploy i.e. it is specific maneuver which intends to outwit an opponent or a competition. It is a trick, devise, a scheme or deception to gain advantageous position before engaging into the combat of marketing warfare.
3. A Pattern i.e. it is not one decision and one solitary action; it stands for a stream of decisions and actions to guide and tend the future course of the enterprise until it reaches its predetermined corporate objectives.
4. A Position i.e. it is a means of locating the firm in an environment full of external factors, pulls and pushes.
5. A Perspective i.e. it is an ingrained way of preceding the world around the organization and its business operations.

Answer 2(c)

In a scheme of compromise or arrangement, following types of approvals are required to be obtained by the transferor and transferee companies:

- (i) *Approval of the Boards of each of the Companies* : This is the first step to carry out amalgamation. Approval authorizes the director/company secretary to do everything for this purpose.
- (ii) *Approval of Shareholders/Creditors* : This approval is to be obtained at specially convened meetings as per Court's directions under Section 391(1) of the Companies Act. However, if all members consent in writing, this can be dispensed with. The unsecured / sundry creditors meetings are dispensed with subject to certain conditions.
- (iii) *Approval of Stock Exchange* : In case of companies listed with recognized stock exchange(s), a no-objection certificate under Clause 24(f) of the listing agreement is to be obtained atleast one month prior to filing it with High Court.
- (iv) *Approval from Financial Institutions/Lending Banks/Debenture trustees etc.* : If

the company has borrowed funds from the above lenders, approval is necessary from the lender and debenture trustees.

- (v) *Approval from the land holders* : If the land on which the factory is situated is the lease-hold land and the terms of the lease deed so specifies, the approval from the lessor will be needed.
- (vi) *Approval from Reserve Bank of India* : If amalgamation results to issuance of shares/cash option to the non-resident Indians, the amalgamated company has to obtain permission from Reserve Bank of India under Foreign Exchange Management (Transfer or issue of security by a person Resident outside India) Regulations, 2000.
- (vii) *Approval of Central Government under MRTP Act* : The Monopolies and Restrictive Trade Practices Act, 1969 is on the verge of being phased out with the passing of the Competition Act, 2002. Under the Competition Act, regulation of combinations as provided under Sections 5 and 6 of the Act would also be required to be complied by companies, if applicable. Under the Competition Act, 2002, reference must be made to the Competition Commission of India in certain cases depending upon the post merger size of the assets or business.
- (viii) *Sanction of the respective High Courts* : Both amalgamated/resulting companies and amalgamating companies are required to seek approval from the respective High Court(s) in which their registered offices are situated.

Question 3

- (a) *In a buy-back of securities, a company has to pay stamp duty under the Indian Stamp Act, 1899 for physical shares. Do you agree ? Explain. (5 marks)*
- (b) *In an open offer in terms of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997, what message is conveyed by the SEBI by way of 'disclaimer clause' to the shareholders of the target company ? (5 marks)*
- (c) *What do you mean by 'hostile takeover' ? Why these types of takeovers are resorted to and by whom, and what is the objective of the acquirer ? (5 marks)*

Answer 3(a)

Any transfer of shares is liable for stamp duty under the Indian Stamp Act, 1899 vide entry No.62 in the Schedule I. For completion of transfer of shares, a company is required to register the shares in the name of the transferee. But purchase of own shares by a company cannot be registered in the name of the company. These shares are supposed to be mandatorily extinguished and the capital stands reduced to that extent. They cannot keep the bought back shares as "Treasury Stock" for reissue though such things are permissible in some western countries.

As per provisions of the Companies Act, 1956 and relevant rules, the bought back shares must be extinguished within 7 days from the closure date of said buy back and it should not be treated as "Release" under Article 55 of the Indian Stamp Act. Hence, no registration of such shares takes place in the name of the company.

The names of the members/shareholders from whom the shares are bought back, have to be struck off from the register of members of the company. Therefore, buy-

back cannot be considered as transfer and stamp duty would not be payable in a case where buy-back of shares takes place in physical form even if the shares are accompanied by an application form for transfer of shares in favour of the company.

Answer 3(b)

The message conveyed by SEBI by way of 'disclaimer clause' to the shareholders of the target company are as follows:

- (i) The purpose of the disclosure made in the letter is to facilitate the shareholders to take a decision in an informed way.
- (ii) The disclosures made in letter are generally adequate and are in conformity with the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997.
- (iii) It shall not be deemed or construed that SEBI has approved or cleared or vetted the offer letter.
- (iv) SEBI does not take any responsibility either for the truthfulness or correctness of for any statement, for financial soundness of Acquirer, or of Persons Acting in Concert, or of Target Company, whose shares are proposed to be acquired or for the correctness of the statements made or opinions expressed in the Letter of Offer.
- (v) While the acquirer is primarily responsible for the correctness, adequacy and disclosure of all relevant information in the letter of offer, the Merchant Banker is expected to exercise due diligence to ensure that acquirer(s) duly discharges its responsibility adequately.

Answer 3(c)**Hostile Takeover**

When an acquirer company does not offer the target company the proposal to acquire its undertaking but silently and unilaterally pursues efforts to gain control against the wishes of existing management, such acts of acquirer are known as 'hostile takeover'. Such takeovers are hostile on the management and are thus called hostile takeover.

This type of takeover action preferred by a competitor or a cash rich acquirer to take control over the targeted company against the wish of the existing management and controlling persons of the target company.

This type of takeover is primarily aimed for:

- (i) Elimination of competition or dilution of the degree of competition on the product/service market on the whole.
- (ii) Gaining reign/leadership in prices of the product sold/services rendered.
- (iii) Brand orientation.
- (iv) Building up or broadening the monopolistic or oligopolistic route in product market by the acquiring entity.

However Hostile Takeover is not a prohibited or illegal activity. When shares of a

company are listed in a recognized stock exchange, shares are available for being bought by anybody. Therefore acquisition per se, though hostile, cannot be banned. On the other hand, the regulations incorporate strict rules for regulating such takeover attempts so to make the process transparent and afford opportunity to a competitive process and protects interests of the investors.

Question 4

- (a) *Good Value Ltd. (GVL) is contemplating acquisition of Fair Value Ltd. (FVL). GVL has 3,00,000 equity shares and FVL has 2,00,000 equity shares and the market value of shares are Rs.30 and Rs. 20 and EPS is Rs.4 per share and Rs. 2.25 per share respectively. It is proposed to give one share of GVL to the shareholder of FVL for their two shares in FVL. Based on the above information, you are required to —*
- calculate EPS after the merger/acquisition of the company; and*
 - show the impact on EPS for the shareholders of both the companies.*
- (5 marks)
- (b) *X, an acquirer, fails to fulfil the offer obligation towards shareholders of target company who have lodged their shares with the acquirer. What are the remedies available to a merchant banker for discharge of the obligations especially towards shareholders who have participated in the offer as well as to deal with the escrow account ?*
- (5 marks)
- (c) *State whether any stamp duty is payable on transfer of properties under the order of amalgamation. Briefly comment with relevant case law.*
- (5 marks)

Answer 4(a)

(i) Calculation of EPS after merger/acquisition of the company

Total earnings after merger and acquisition:-

GVL	FVL	Total Earnings
3,00,000 x 4	2,00,000 x 2.25	
= Rs. 12,00,000	Rs. 4,50,000	Rs. 16,50,000

Total number of equity shares after acquisition:-

GVL	3,00,000
FVL (2,00,000 x 1/2)	1,00,000
Total no. of shares after acquisition	<u>4,00,000</u>

$$\begin{aligned}
 \text{EPS after merger} &= \frac{\text{Total earnings after acquisition}}{\text{Total number of shares after acquisition}} \\
 &= \frac{16,50,000}{4,00,000} \\
 &= \text{Rs. 4.125}
 \end{aligned}$$

(ii) Impact of EPS for the shareholders of both the companies

GVL	Rs.
Earnings before acquisition	12,00,000
[3,00,000 x 4]	
Earnings after acquisition	12,37,500
[3,00,000 x 4.125]	
Increase in earnings after acquisition	<u>37,500</u>
Net increase in EPS after merger	= <u>37,500</u>
	3,00,000
	= 0.125
 FVL	 Rs.
Earnings before acquisition	4,50,000
[2,00,000 x 2.25]	
Earnings after acquisition	4,12,500
[*1,00,000 x 4.125]	
Net decrease in earnings	<u>37,500</u>
Net decrease in EPS after merger	= <u>37,500</u>
	1,00,000
	= 0.375

(*being the shares held by shareholders of FVL in GVL after merger)

Therefore, there is an increase of Rs. 37,500 in total earnings of GVL and decrease of Rs. 37,500 in total earnings of FVL after merger.

Answer 4(b)

The Merchant Banker is entitled to ensure realization of Escrow Account by way of foreclosure of deposit, invocation of bank guarantees and sale of the shares (if any) and distribute the proceeds after deduction of expenses, if any, of the merchant banker and the registrars to the offer in following ways:

- (i) One third of amount to the target company.
- (ii) One third to regional stock exchanges where it is listed, for credit of the investor protection fund or any other similar fund for investor education, research, grievance redressal and similar such purposes as may be specified by SEBI.
- (iii) One third to be distributed on pro-rata basis among the shareholders who have accepted the offer.

The Merchant Banker is required to ensure that the rejected documents which are kept in the custody of the Registrar/Merchant Banker are sent back to the shareholder through Registered Post.

Answer 4(c)

Yes, stamp duty is payable on transfer of properties under the order of amalgamation.

In a landmark decision of Hon'ble Bombay High Court in *Li Taka Pharmaceuticals v. State of Maharashtra* (1996) 8 SC 102 (Bom.), it was held that:

- (i) An amalgamation under the order of the Court under Section 394 of the Companies Act, is an instrument under the Bombay Stamp Act;
- (ii) States are well within their jurisdiction when they levy stamp duty on instrument of amalgamation;
- (iii) Stamp duty would be levied not on the gross assets transferred but on the "undertaking", when the transfer is on a going concern basis, i.e. on the assets less liabilities. The value for this purpose would thus be the value of shares allotted. This decision has been accepted in the Act and now stamp duty is leviable on the value of shares allotted plus other consideration paid.

Question 5

- (a) (i) *The court has fixed meeting of equity shareholders of Rim Zim Ltd. on Tuesday, the 9th June, 2009 at Broadway Hotel, 3, Osaka Street, Mumbai for considering the proposed scheme of amalgamation with Jhil Mil Ltd. and appointed Kabir as Chairman and Mrs. Noori as alternate Chairperson of the meeting. As a Company Secretary of Rim Zim Ltd., draft the notice of the meeting.* (7 marks)
- (ii) *After meeting of equity shareholders of Rim Zim Ltd., the proposed scheme of amalgamation of Rim Zim Ltd. with Jhil Mil Ltd. was passed. Draft the Chairman's report for onward submission to the court.* (4 marks)
- (b) *Briefly explain with relevant provisions of the Companies Act, 1956 as to when the scheme of amalgamation would become effective.* (4 marks)

Answer 5(a)(i)**Form No. 36**

IN THE HIGH COURT OF JUDICATURE AT _____
(ORIGINAL JURISDICTION)

In the matter of Companies Act, 1956

And

In the matter of Scheme of Amalgamation of Rim Zim Ltd. with Jhil Mil Ltd. Rim Zim Ltd., an existing company under Companies Act, 1956 and having its registered office at _____

Company Application No. _____ of 200 _____

Rim Zim Ltd., Applicant

Notice Convening Meeting

To

Equity Shareholders

TAKE NOTICE that by an order made on _____ day of _____ 200__, the

Court has directed that a meeting of the equity shareholders of the company be held at Broadway Hotel, 3, Osaka Street, Mumbai on Tuesday, the 9th day of June 2009 at _____AM/PM, for the purpose of considering and, if thought fit, approving with or without modification, the Scheme of Amalgamation proposed to be made between the Applicant Company and Jhil Mil Ltd.

TAKE FURTHER NOTICE that in pursuance of the said order, a meeting of the equity shareholders of the Applicant Company will be held at Broadway Hotel, 3, Osaka Street, Mumbai on Tuesday, the 9th day of June 2009 at _____AM/PM which you are requested to attend.

TAKE FURTHER NOTICE that you may attend and vote at the said meeting in person or by proxy, provided that a proxy in the prescribed form, duly signed by you, is deposited at the registered office of the company at _____ not later than 48 hours before the meeting. The quorum of the meeting shall be five members present in person or by proxy.

The Court has appointed Mr. Kabir as the Chairman of the said meeting and Mrs. Noori as alternate Chairperson of the meeting.

A copy of each of the Scheme of Amalgamation, the statement under Section 393 of the Companies Act, 1956 and a form of proxy and attendance slip are enclosed.

Dated this _____ day of 200 _____

Sd/-

For Rim Zim Ltd.

XYZ

Company Secretary

Note : All alterations made in the form of Proxy should be initialled.

Answer 5(a)(ii)

Form No. 39

IN THE HIGH COURT OF JUDICATURE AT _____

(ORIGINAL JURISDCITION)

In the matter of Companies Act, 1956

And

In the matter of scheme of Amalgamation of Rim Zim Ltd. with Jhil Mil Ltd.

Rim Zim Ltd., an existing company under Companies Act, 1956 and having its registered office at _____

Company Application No. _____ of 200 _____

Rim Zim Ltd., Applicant

Report by Chairman

I, Kabir, Advocate, the person appointed by this Hon'ble Court to act as Chairman of the meeting of the equity shareholders of the above named company, summoned by notice served individually upon them and by advertisement dated theday of..... 200....., and held on the 9th day of June 2009, at Broadway Hotel, 3, Osaka Street, Mumbai, do hereby report to this Hon'ble Court as follows :

1. The said meeting was attended by.....equity shareholders personally holding.....value of shares andequity shareholders holding..... value of shares have attended the said meeting through proxy.
2. The scheme of amalgamation was read out and explained by me to the meeting and questions raised were answered satisfactorily. The equity shareholders of the said company have approved the scheme of amalgamation submitted to the meeting and agreed thereto.
3. The said meeting was unanimously of the opinion that the scheme of amalgamation should be approved and agreed to/or. The result of the voting of the meeting are attached as per annexure A showing names and addresses of the equity shareholders, value of equity shares held by them, number of votes, approved or disapproved.

Dated this_____ day of 200_____

Sd/-

Kabir

Chairman appointed for the meeting

(Annexure A)

Answer 5(b)

According to the provisions of Section 391(3) and 394(3) of the Companies Act, 1956, certified copy of the order passed by the Court shall be filed with the concerned Registrar of Companies. This is required to be filed with e-form 21 which is required to be filed within thirty days of the making of the order. Date of completion of the last of the required approvals shall be treated as effective date for the scheme of amalgamation.

PART B

(Answer ANY TWO questions from this part)

Question 6

- (a) Explain the enforcement of security interest by a secured creditor under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002. (7 marks)
- (b) Define 'securitisation' and explain the objectives of securitisation. (4 marks)
- (c) What do you mean by 'non-performing assets' under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ? (4 marks)

Answer 6(a)

Under section 13 of the Securitization and Reconstruction of Financial assets and Enforcement of Security Interest Act, 2002(hereinafter Securitization Act), secured creditor can enforce his security interest without intervention of the Court, on default in repayment of instalments, and non compliance with the notice of 60 days after the declaration of the loan as a non-performing asset. Secured creditors have been defined to mean any bank or financial institution or any consortium or group of banks or financial institutions and includes debenture trustees appointed by any Bank or Financial Institution or Securitization or reconstruction company or any other trustee holding securities on behalf of bank or financial institution in whose favour security interest is created for due repayment by any borrower of any financial assistance. In case of the default in repayment of installment by the borrower and debts becoming NPA, the secured creditor has two options. It can either transfer the assets to a securitisation or reconstruction company or exercise the powers under the Act.

Section 13(4) of the Act empowers the recourse to one more of the following measures, after giving proper notice, for the recovery of the secured debts, namely:

- Take possession of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realizing the secured asset;
- Take over the management of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale and realize the secured asset;
- Appoint any person (hereafter referred to as the manager), to manage the secured assets the possession of which has been taken over by the secured creditor;
- Require at any time by notice in writing, any person who has acquired any of the secured assets from the borrower and from whom any money is due or may become due to the borrower, to pay the secured creditor, so much of the money as is sufficient to pay the secured debt.

In cases of joint financing under consortium or multiple lending arrangements if 75% of the secured creditors in the value agree to initiate recovery action the same is binding on all secured creditors.

In case of a company under liquidation, the amount realized from the sale of the secured assets is to be distributed in accordance with the provisions of Section 529A of the Companies Act, 1956. If the company is being wound up after the commencement of this Act, the secured creditor of such company, who opts to realize its security instead of relinquishing its security and proving its debts under proviso to Sub-section (1) of Section 529 of the Companies Act, may retain the sale proceeds of its secured assets after depositing the workmen's dues with the liquidator in accordance with the provisions of Section 529A of that Act. In case, dues of the secured creditors could not be satisfied in full, secured creditor may file application before DRT for recovery of balance amount. Secured creditor is also entitled to proceed against the guarantor or sell the pledged assets for its recovery.

Answer 6(b)

According to Section 2(1) (z) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, "Securitisation" means acquisition

of financial assets by any securitisation company or reconstruction company from any originator, whether by raising of funds by such securitisation company or reconstruction company from qualified institutional buyers by issue of security receipts representing undivided interest in such financial assets or otherwise. "Securitisation company" means any company formed and registered under the Companies Act, 1956 for the purpose of securitization [Section 2(1)(za)].

Securitisation is the issuance of marketable securities backed not by the expected capacity to repay of a private corporation or public sector entity, but by the expected cash flows from specific assets.

Simply stated securitisation is the process by which the 'originators' of assets like loans which are illiquid, are able to transfer such assets to a 'special purpose vehicle' (SPV), which, in turn, issues tradable liquid securities to the investors. These transactions can be structured with a wide variety of 'credit enhancement' to make the deals attractive for investors. The most important, however, is the 'guarantees of credit quality'.

There are two motives for Securitisation. One, the securitised assets go off the balance sheet of the originator and so the asset base is pruned down to that extent, thereby reducing the regulatory capital requirements to support the assets. Second, the asset portfolio is liquidated; releasing cash, which in turn reduces the need for demand and time liabilities that are subject to statutory reserves.

Answer 6(c)

According to Section 2 (1) (o) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 "Non-Performing Asset" means an asset or account of a borrower, which has been classified by a bank or financial institution as sub-standard, doubtful or loss asset—

- (a) in case such bank or financial institution is administered or regulated by an authority or body established, constituted or appointed by any law for the time being in force, in accordance with the directions or guidelines relating to assets classifications issued by such authority or body;
- (b) in any other case, in accordance with the directions or guidelines relating to assets classifications issued by the Reserve Bank.

In *Srinivas Rice & Floor Mill v. Authorized Officer, State Bank of India*, [2008] 81 SCL 66 (AP), the AP High Court held that there is no statutory format, express or by necessary implication, that require the Banks to follow a particular or formal procedure or require a formal declaration as a condition precedent to classification of debt as "NPA". What section 13(2) r/w Section 2(1)(o) requires is a classification of a debt by a bank as 'NPA' within the legislative guidelines spelt out in the definition of NPA.

Question 7

- (a) *What do you understand by 'sick industrial company' ? Explain the immunities provided to a sick industrial company under the Sick Industrial Companies (Special Provisions) Act, 1985. (7 marks)*
- (b) *Though, UNCITRAL Model Law is not a substantive law, yet it recommends protection to creditors and other interested persons. Briefly describe what are the protections provided under the UNCITRAL Model Law. (4 marks)*

- (c) *The main objective of asset reconstruction company (ARC) is to act as an agent for banks and financial institutions. Briefly explain with the relevant provisions of law. (4 marks)*

Answer 7(a)

According to Section 3(1)(o) of the Sick Industrial Companies (Special Provisions) Act, 1985, "sick industrial company" means an industrial company (being a company registered for not less than five years), which has at the end of any financial year accumulated losses equal to or exceeding its entire net worth.

Explanation : For the removal of doubts, it is hereby declared that an industrial company existing immediately before the commencement of the Sick Industrial Companies (Special Provisions) Amendment Act, 1993 registered for not less than five years and having at the end of any financial year accumulated losses equal to or exceeding its entire net worth, shall be deemed to be a sick industrial company.

Immunities to a sick industrial company has been granted under the provisions of Section 22 of the SICA, 1985. This Section provides that in certain circumstances, no proceedings for the winding up of the industrial company or for execution, distress or the like against any of the properties of the industrial company or for the appointment of a receiver in respect thereof and no suit for the recovery money or for the enforcement of any security against the industrial company or of any guarantee in respect of any loans or advance granted to the industrial company shall lie or be proceeded with further, except with the consent of BIFR or, as the case may be, the Appellate Authority.

Section 22 of SICA has two limbs. The first part enacts that "no proceeding for the winding up of the industrial company or for execution, distress or the like against any of the properties of the industrial company or for the appointment of a receiver in respect thereof ... shall lie or be proceeded with further, except with the consent of the Board or, as the case may be, the Appellate Authority." The second part which is independent of the first part declares that "no suit for the recovery of money or for the enforcement of any security against the industrial company or of any guarantee in respect of any loans or advance granted to the industrial company shall lie or be proceeded with further, except with the consent of the Board or, as the case may be, the Appellate Authority."

The protection under Section 22 of SICA is a superior protection as it operates notwithstanding anything contained in the Companies Act, 1956, or any other law or the memorandum and articles of association of the industrial company or any other instrument having effect under the said Act or other law.

The above protection is available in respect of an industrial company when an inquiry under Section 16 is pending in relation to the said industrial company or when any scheme referred to under Section 17 is under preparation or consideration or a sanctioned scheme is under implementation or where an appeal under Section 25 relating to an industrial company is pending.

BIFR may by order declare with respect to the sick industrial company concerned that the operation of all or any of the contracts, assurances of property, agreements, settlements, awards, standing orders or other instruments in force, applicable to the sick industrial company in question shall remain suspended or that all or any of the rights, privileges, obligations, and liabilities accruing or arising thereunder before the

said date, shall remain suspended or shall be enforceable with such adaptations and in such manner as may be specified by BIFR. Provided that such declaration shall not be made for a period exceeding two years which may be extended by one year at a time so, however, that the total period shall not exceed seven years in the aggregate. Any such declaration is valid and is protected notwithstanding anything contained in the Companies Act, 1956, or any other law or agreement or instrument or any decree or order of a court, Tribunal, officer or other authority or of any submission, settlement or standing order.

Section 22 does not grant immunity against the criminal proceedings against the company or its directors.

The apex court in *Maharashtra Tubes Limited v. State Industrial and Investment Corporation of Maharashtra Limited* [1993] 78 Comp Cas 803 (SC) held that the idea underlying Section 22(1) of SICA is that every such action (against the company or its guarantors for recovery of money or enforcement of security) should be frozen unless expressly permitted by the specified authority until the investigation for the revival of the industrial undertaking is finally determined. The apex court in *Patheja Bros. Forgings and Stamping v. ICICI Limited* AIR 2000 CLC 1492: (2000) 4 Comp LJ 9 (SC) held that the words Section 22 are clear and unambiguous and that they provide that no suit for the enforcement of a guarantee in respect of any loan or advance granted to the concerned industrial company will lie or can be proceeded with without the consent of BIFR or the appellate authority. When the words of a legislation are clear, the court must give effect to them as they stand and cannot demur on the ground that the legislature must have intended otherwise.

Answer 7(b)

Under the UNCITRAL Model Law, foreign creditors have the same rights regarding the commencement of and participation in a proceeding under the laws of the enacting state relating to insolvency as creditors in the state. The Model Law contains following provisions for protection of the creditors (in particular local creditors), the debtors and other affected persons:

1. availability of temporary relief upon application for recognition of a foreign proceeding or upon recognition is subject to the discretion of the court; it is expressly stated that in granting such relief the court must be satisfied that the interests of the creditors and other interested persons, including the debtor, are adequately protected (Article 22, paragraph 1);
2. the court may subject the relief it grants to conditions it considers appropriate; and
3. the court may modify or terminate the relief granted, if so requested by a person affected thereby (Article 22, paragraphs 2 and 3).

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

Further, the Model Law states that the courts that recognize Foreign Proceeding may, where relief is urgently needed to protect the assets of the debtor or the interests of the creditors, grant necessary interim or other relief as stipulated thereunder.

Answer 7(c)

Assets Reconstruction Company (ARC) means a company incorporated under the provisions of Companies Act, 1956 for the purpose of assets reconstruction. The problem of non-performing loans created due to systematic banking crisis world over has become acute. Focused measures to help the banking systems to realise its NPAs has resulted into creation of specialised bodies called asset management companies which in India have been named asset reconstruction companies ('ARCs'). The buying of impaired assets from banks or financial institutions by ARCs will make their balance sheets cleaner and they will be able to use their time, energy and funds for development of their business. ARCs may be able to mix up their assets, both good and bad, in such a manner to make them saleable.

The main objective of the ARC is to work as an agent of the banks and or financial institutions for the purpose of recovering their dues from the borrowers on payment of fees or charges, to act as manager of the borrowers' assets taken over by the banks or financial institution, to act as receiver of properties of any bank or financial institution or to carry on such ancillary or incidental business with the prior approval of RBI whenever necessary. If an ARC carries on any business other than the business of asset reconstruction or securitisation or the business mentioned above, it shall cease to carry on any such business within one year of doing such other business.

Question 8

- (a) *State the World Bank principles for effective insolvency and creditor rights systems. (7 marks)*
- (b) *On 2nd December, 1983, winding-up order was passed in respect of Heaven Ltd. On 1st December, 1989, official liquidator of Heaven Ltd. (in liquidation) initiated misfeasance proceedings against the promoter directors of the company. Directors pleaded that proceedings should be quashed being time barred. Briefly explain with support of relevant case laws, period of limitation for initiating misfeasance proceedings under the Companies Act, 1956. (4 marks)*
- (c) *Can an Indian court pass an order of amalgamation that has the winding-up effect in respect of the foreign company? Support your answer with relevant case law. (4 marks)*

Answer 8(a)

The World Bank Principles for effective insolvency and creditor rights system have been designed as a broad-spectrum assessment tool to assist countries in their efforts to evaluate and improve core aspects of their commercial law systems that are fundamental to a sound investment climate, and to promote commerce and economic growth. Efficient, reliable and transparent creditor rights and insolvency systems are of key importance for reallocation of productive resources in the corporate sector, for investor confidence and forward looking corporate restructuring. These systems also play a pivotal role in times of crisis to enable a country and stakeholders to promptly respond to and resolve matters of corporate financial distress on systemic scales.

The Principles emphasize contextual, integrated solutions and the policy choices involved in developing those solutions. The Principles highlight the relationship between

the cost and flow of credit (including secured credit) and the laws and institutions that recognize and enforce credit agreements (Part A). The Principles also outline key features and policy choices relating to the legal framework for risk management and informal corporate workout systems (Part B), formal commercial insolvency law frameworks (Part C) and the implementation of these systems through sound institutional and regulatory frameworks (Part D).

The principles have broader application beyond corporate insolvency regimes and creditor rights. The Principles are designed to be flexible in their application, and do not offer detailed prescriptions for national systems. The Principles embrace practices that have been widely recognized and accepted as good practices internationally. As legal systems and business and commerce are evolutionary in nature, so too are the Principles, and it is anticipated that these will continue to be reviewed going forward to take account of significant changes and developments.

Answer 8(b)

No, proceedings are not time barred. In a similar case of *Ajay G Podar V. Official Liquidator Of JS & WM & Ors.* (2008) 85 CLA 398 (SC), Hon'ble SC has held that section 543(2) of the Companies Act, 1956 deals with the limitation of applications/claims including misfeasance proceedings and prescribes five (5) years period of limitation from the date of the winding up order for filing an application under section 543 (1). However, section 458A of the Companies Act, 1956 provides for the concept of computation of the limitation period. Section 458A being a non obstante clause exclude the period starting from commencement of winding up proceedings till the date on which winding up order is passed and a period of one (1) year thereafter. In view of the above, misfeasance proceedings filed by the Official Liquidator are well within limitation period.

Answer 8(c)

Yes, Indian Court can pass an order of amalgamation that has the winding up effect in respect of the foreign company. Section 390 of the Companies Act, 1956 provides definition and interpretation aid for sections 391 to 393 of the Act. In the case of *Bombay Gas Co. Pvt. Ltd. v. Regional Director* (1996) 21 CLA 269 (Bom.), it was held that Section 390(a) is applicable to a company incorporated outside India. If court has jurisdiction to wind up such a company on any of the grounds specified in the Act, court has jurisdiction to sanction scheme of amalgamation if a company incorporated outside India is a transferor-company.
