

# **GUIDELINE ANSWERS**

## **PROFESSIONAL PROGRAMME (New Syllabus)**

**JUNE 2019**

**MODULE 2**



**THE INSTITUTE OF  
Company Secretaries of India**

**भारतीय कम्पनी सचिव संस्थान**

**IN PURSUIT OF PROFESSIONAL EXCELLENCE**

Statutory body under an Act of Parliament

(Under the jurisdiction of Ministry of Corporate Affairs)

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

Phones : 41504444, 45341000; Fax : 011-24626727

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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.

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**PROFESSIONAL PROGRAMME EXAMINATION**  
JUNE 2019  
**SECRETARIAL AUDIT, COMPLIANCE MANAGEMENT  
AND DUE DILIGENCE**

*Time allowed : 3 hours*

*Maximum marks : 100*

**NOTE:** Answer **ALL** Questions.

**PART I**

**Question 1**

- (a) *XYZ Ltd. has not filed Annual return for the financial year 2017-18. Write a note on the consequences of non-filing of Annual Return by the company in relation to a Director of the company, as per provisions laid under the Companies Act, 2013.*
- (b) *“Good Corporate Governance demands compliances level that match the intentions of Legislature, expectations of Stakeholders and requirements of Regulators”. Explain.*
- (c) *Describe the role of a Company Secretary as an Insolvency Professional.*
- (d) *You are appointed as Compliance Officer in a listed company. An Independent Director asks you to describe the scope of Corporate Compliance. Prepare a brief note. (5 marks each)*

**Answer 1(a)**

**Consequences on the Director of XYZ Ltd. for Non filing of Annual Return**

As per section 92 of the Companies Act, 2013, XYZ Ltd. is required to file a copy of annual return with the Registrar, within sixty days from the date on which the annual general meeting of the company was held for the financial year 2017-18.

If the company has not filed its Annual Return from the date by which it should have been filed with fee and additional fees, every officer including director of the company, who is in default shall be liable to a penalty of fifty thousand rupees and in case of continuing failure, with further penalty of one hundred rupees for each day during which such failure continues, subject to a maximum of five lakh rupees. (Section 92).

If the company has not filed its financial statement or Annual Return for continuous period of three financial years, then every person who is or has been director of that company shall not be eligible for reappointment as Director of that company or appointed in any other company for a period of five years from the date on which the said company fails to do so.(Section 164(2)).

**Answer 1(b)**

Good Corporate Governance demands compliances level that match the intentions of legislature, expectations of stakeholders and requirements of regulators. The

compliances, however, generally found to fall in three categories, i.e. Apparent Compliances, Adequate Compliances and Absolute Compliances.

Apparent compliance is a disguise form of non-compliance, which is worse than a non-compliance. The classic example for Apparent Compliances are generating documents such as notice, agenda, minutes on paper for board and general meeting which are not actually held.

Adequate compliance is compliance in letters. The aspects specified in law are complied in letters, without getting into the spirit of the law, e.g. box ticking practices.

Absolute compliances are those which are in line with the spirit and intent of the law. A typical example in this regard is demonstrating shareholder democracy as prescribed by law.

When a company complies with law in spirit it gains public confidence as well. Experts view annual report as self-appraisal report of the company. The shift from shareholder concept to stakeholder concept has necessitated the corporates to provide a transparent report which is viewed by all stakeholders such as shareholders, creditors, lenders, strategic investors etc. as a potential source of information. In order to attain corporate sustainability and to ensure a level playing field with international market, corporates has to necessarily increase their level of compliance from apparent to adequate leading to level of absolute compliance.

### **Answer 1(c)**

#### **Company Secretary as Insolvency Professional**

Company Secretaries having passed necessary examination, possessing prescribed number of years of experience, enrolled with an insolvency professional agency and registered with Insolvency and Bankruptcy Board of India (IBBI) as an insolvency professional, can take up matters relating to corporate insolvency resolution process as Interim Resolution /Resolution Professionals, and also take up voluntary liquidation cases. They can also act as authorized representatives for a class of creditors in a meeting of Committee of Creditors in a resolution process.

As per the Insolvency and Bankruptcy Board of India Regulations, a member of the Institute of Company Secretaries of India having ten years' of experience and have other requisite qualifications is eligible for registration as insolvency professional.

### **Answer 1(d)**

**From:**

**Compliance officer**  
\_\_\_\_\_ Limited

**To:**

**Mr. \_\_\_\_\_**  
**Independent Director**

*Sub: Scope of Corporate Compliance*

Dear Sir,

As desired, the note on the Corporate Compliance is as under:

Corporate compliances broadly include compliance of Corporate & Economic Laws,

Securities Laws, Commercial Laws including Intellectual Property Rights Laws, Labour Laws, Tax Laws, Cyber Laws which is also known as the Information Technology Law, Pollution Control Laws, Industry Specified laws and all other laws affecting the company concerned depending upon the type of industry/activity. The broad coverage of laws includes the compliances of the following laws:

- Companies Act, 2013 and the Rules and Regulations framed thereunder, MCA-21 requirements and procedures
- Secretarial Standards/Accounting Standards/Cost Accounting Standards issued by ICSI/ICAI/ICMAI, respectively
- Foreign Exchange Management Act, 1999 and the various Notifications, Rules and Regulations framed thereunder
- Competition Act, 2002
- SEBI Act, 1992
- Securities (Contracts) Regulation Act, 1956 and rules made thereunder
- SEBI (Listing obligations and Disclosure Requirements) Regulations, 2015
- Depositories Act, 1996
- Intellectual Property Rights Laws
- Income Tax Act, 1961
- Customs Act, 1962
- GST Laws
- Labour Laws
- Environment Laws
- Industry Specific Laws
- Local Laws include Municipal and Civic Administration Laws, Shops and Establishments etc.

Regards,

\_\_\_\_\_  
**Compliance Officer**

\_\_\_\_\_ **Ltd.**

***Attempt all parts of either Q. No. 2 or Q. No. 2A***

**Question 2**

- (a) *How does Enhanced Due Diligence (EDD) in KYC differ from Customer Due Diligence (CDD) in KYC ?* (5 marks)
- (b) *Explain the procedure for search Report under IPR Laws.* (5 marks)

- (c) *What are the disadvantages of Electronic records ?* (5 marks)
- (d) *Explain the compliances under Securities Exchange Board of India (Listing Obligations and Disclosure Requirements) [SEBI (LODR)] Regulations, 2015 relevant to the common obligations to any listed entity indicating the time period and event of each.* (5 marks)

**OR (Alternate Question to Q. No. 2)**

**Question 2A**

- (i) *Z Ltd. seeks your opinion on the role of the various levels of management for compliance ownership. Explain the role.*
- (ii) *You are appointed as Compliance Officer of the company. One of the foreign investor in the company is hesitating to provide personal data during the KYC saying that KYC is a risky process and data can be misused by someone. Prepare the list of risks involved in the KYC process.*
- (iii) *What is peer review and describe its contents ?*
- (iv) *XYZ Bank Ltd. has sanctioned a term loan for ₹5,000 crore to CXT Ltd. The purpose of the loan is to develop the townships in 5 Smart Cities including Mumbai. The 30% of the loan amount is to be used for Mumbai only. However, during the verification of the records of the company, it was found that certain land area in Mumbai is a disputed area where the Hon'ble High Court has granted stay till next hearing. You are appointed by the Bank as Secretarial Auditor for making a search report. What are the documents to be inspected by the Secretarial Auditor in the instant case ?* (5 marks each)

**Answer 2(a)**

**Customer Due Diligence (CDD)** refer to identifying and verifying the customer and the beneficial owner, CDD refers to the monitoring of clients and their activities to see if the client does not change its status over time. For example changes in the signatory of the account, changes in the partners, changes in the object, changes in the source of income, revenue etc. hence without CDD the services provider would not know that there is changes in the ownership.

Whereas the **Enhanced Due Diligence (EDD)** refers to a rigorous and robust process of investigation over and above (KYC) procedures, that seeks with reasonable assurance to verify and validate the customers identity; understand and test the customers profile, business and account activity; identify relevant adverse information and risk assess the potential for money laundering and / or terrorist financing to support actionable decisions to mitigate against financial, regulatory and reputational risk and ensure regulatory compliance.

**Answer 2(b)**

**Procedure for Search Report under IPR Laws**

1. *Preparing checklist*: The checklist should contain a list of information required to understand the company's business and its existing protected and protectable IP rights.

2. *Segregating the IP assets relevant for the transaction from irrelevant ones* : This activity should be done as soon as the preliminary perusal of the target's business assets is done. It is important to connect additional IP rights with the main IP rights for the transaction.
3. *Analysing all documents carefully* : This activity includes analysing documents, relating to registration or agreements in the nature of licensing and franchising agreements, consultancy agreements, technology transfer agreements, other contracts where IP clauses are included.
4. *Verifying facts and confirm that the information is correct* : This activity is important to verify the legality of documents. It is not prudent to merely rely on all details without cross-checking the same from other available sources.
5. *Analyzing protected and protectable IP rights* : After receiving full information/ documents, IP rights, already subsisting or potential ones is required to be analyzed. Status check, validity check, ownership check, claim check and conflict check should be conducted in a proper manner.
6. *Drafting of status and search report* : The final report should contain all the observations in relation to IP rights that would be the part of the transaction, before the prospective buyer / investor.

The IPR Search Report should also contain all the associated risks and liabilities along with strategies to deal with such issues which will help the prospective buyer / investor understand the pros and cons of the transaction.

### **Answer 2(c)**

The followings are the disadvantages of Electronic records:

- *Software risk* : Storing records in an electronic document management system, have a risk that since the system being no longer supported by the software company the company will cease to exist.
- *Format risk* : When storing the records as an electronic record, a person run the risk of not being able to read them at some point.
- *Media compatibility* : Maintaining images on media which the person can access at a later date is a big challenge. For example, the documents are also stored in floppy disks. But the floppy disk drive is no longer available.
- *Reliability* : It's a good idea to have most vital documents imaged, but keeping a paper copy assures that the person have access to them anytime.
- *Portability* : The portability is an advantage for digital images. It's very easy to misplace or accidentally delete large amounts of data or to duplicated and transported outside of any organization.
- *Conversion expense* : It's very expensive to convert paper documents to digital images. The amount of labour it takes to prepare documents and analyze them so that they can be identified and indexed correctly is very large.

**Answer 2(d)**

Regulations 5 to 14 of Chapter III of the SEBI (Listing Obligations and Disclosure Requirements), 2015 provides for the following Common Obligations of Listed Entities which require compliance:

<i>S.No.</i>	<i>Compliance</i>	<i>Time Period</i>	<i>Event</i>
1	Submission of Compliance Certificate to the Exchange <b>Regulation 7(3)</b>	Within one month of end of each half of the financial year	Submission of Compliance Certificate to Stock Exchange certifying that all activities in relation to both physical and electronic share transfer facility are maintained either in house or by Registrar to an issue and share transfer agent registered with the Board.
2	Appointment/change of Share Transfer Agent <b>Regulation 7(5)</b>	Intimate to the Stock Exchange such appointment or change within 7 days of entering into agreement.	Company can manage in house Share Transfer Facility. But as and when the total number of holders of securities of the listed entity exceeds one lac, the listed entity shall appoint Share Transfer Agent.
3	Grievance Redressal Mechanism <b>Regulation (13)</b>	Within 21 days of the end of the each quarter.	The listed entity shall file with the recognized stock exchange(s) a statement giving <ul style="list-style-type: none"> <li>• The number of investor complaints pending at the beginning of the quarter,</li> <li>• Those received during the quarter,</li> <li>• Disposed of during the quarter and</li> <li>• Those remaining unresolved at the end of the quarter.</li> </ul>

However, the other requirements under this chapter are continuous in nature such as appointment of a qualified company secretary as the compliance officer, policy for preservation of documents, electronic mode of payment facility for payment of dividend or interest or redemption or repayment. These requirements do not provide for any timelines and the compliance of such obligations are required on a continuous basis.

**Answer 2A(i)**

The ownership of the various compliances has to be described function wise and individual wise. Clear description of primary and secondary ownership is also very important. While the primary owner is mainly responsible for the compliance the secondary owner (usually the supervisor of the primary owner) has to supervise the compliance. The role of the various level of management for compliance ownership can be illustrated as under:

**(a) Top Management**

- Understanding the compliance obligations and recent changes.



- Approval of Policy and Procedures.
- Motivating employees to ensuring compliance on time.

**(b) Legal Cell**

- Identification of new and changed relevant local laws, regulations and standards.
- Communication in Writing to compliance owner/ executor.
- Review of systems, policies and Procedures.
- Resolution of Doubts and Clarity in Directions.
- Periodical Review and Assessment.

**(c) Senior Management & functional Heads**

- Analysis and research on the Regulatory changes.
- Formation of Policy and procedure.
- Motivating Compliance officer to ensure timely compliance.
- Guiding compliance officer in executing compliance.
- Tracking the Compliance chart.
- Risk Escalation.
- Conflict Resolution.

**(d) Compliance Officer / Subordinate staff**

- Performing Compliance Obligations.
- Updating Compliance obligations into the Compliance Chart.
- Risk Identification and intimation.
- Conflict intimation.

**Answer 2A(ii)**

The objectives of conducting KYC is to prevent the corporate vehicles from being used intentionally or unintentionally, by criminal elements for illicit purposes such as money laundering activities, fraud, bribery and corruption, shielding assets from creditors, illicit tax practices, market fraud, terrorist funding and avoiding future risk. The KYC related procedures also enable an institution to better understand their customers and their financial dealings. This helps in managing associated risks prudently.

There are different types of risk involved in the proper implementation of KYC

1. **Reputational Risk** like entering into fraudulent transaction and later on the public come to know about it, this would create a sense of insecurity among the public.
2. **Operational Risk** is a risk of loss due to failed internal processes, poor documentation, litigation, disputes and due diligence, people and systems or also from external events.

3. **The Risk that arises legally** in case where any client gets involved with any illegal activity, it will also attract penalties and adjudications on the professional.
4. **Financial Risks** If any professional without complying with KYC norms, provides its services relating to certification or declarations and the financial institution gives loan to a customer and later the bank fails to identify the customer, then it will be hard for the bank to retrieve its money.

**Answer 2A(iii)**

Peer Review is a process for examining the work performed by one's equals (peers) and to understand the systems, practices and procedures followed by the Practice Unit and to give suggestions, if any, for further improvement.

The Institute of Company Secretaries of India provides a mechanism of Peer Review of their Members in Practice to enhance the quality of attestation services, to enhance credibility and provide competitive advantage and provide a forum for Guidance and knowledge sharing. The peer review includes the following services by the company secretaries in practice:

- (i) Certification/ Signing of Annual Return pursuant to section 92 of the Companies Act, 2013.
- (ii) Issuance of Secretarial Audit Report in terms of Section 204 of the Companies Act, 2013
- (iii) Issuance of Certificate of Securities Transfers in Compliance with the LODR with Stock Exchanges.
- (iv) Certificate of reconciliation of capital, updation of Register of Members, etc. as per the Securities & Exchange Board of India's Circular D & CC/Cir-16/2002 dated December 31, 2002.
- (v) Conduct of Internal Audit of Operations of the Depository Participants.
- (vi) Compliance Certification under LODR.
- (vii) Attestation services of Form AOC-4, MGT-7, DIR-12, SH-7 and PAS-3 filed with the ROC.
- (viii) Such other services as decided by the Council of ICSI under the scope of peer review from time to time.

**Answer 2A(iv)**

In the instant case, it is necessary to inspect and retrieve the history of a property right from the original owner of the property to the current owner over a period of time. It provides documents which help determine relevant interests in property of the owner and other individuals, if any, along with the title certificate, 'agreement to sell' with the intended purchaser containing details of the existing mortgage, litigation, condition or claim, which likely to affect the project.

In case of the property title Search report, the following documents are considered:

- Ownership: Status of ownership- sole or joint and the documents stating the same.

- *Deed Copy* : Recent deeds in respect to the property.
- *Legal Description* : Description of the property in legal parlance.
- *Chain documents* : Previous owner of the property.
- *Possession* : Actual Possession of the property.
- *Right of way* : Easementary Right - the Right of way given to the owner.
- *Leases* : Leases on the property which can affect the property status.
- *Mortgage* : Whether the property has been mortgaged or not?
- *Tax Payment* : Details of tax payment in relation to the property.
- *Bankruptcy Search* : Report of bankruptcy of the owner of the property.
- *Municipal Service Lien* : Report of unpaid municipal dues like water, sewer, trash etc.
- *Property Restriction* : Restriction on sale of property like sale in case of unsound owner.
- *Plot Map* : Official copy of Map of the plot.
- *Property Zoning* : Property lying under which zone like Ecological Zone, Flood Zone, Earthquake Zone etc.
- *Civil Court Record* : Any order of the Civil Court against the property.

and other things like Spousal Support Lien Search, Child Support Lien search, Power of Attorney, Special Assessment etc.

In case of Company Search report, the professional should go through the various documents maintained by the company which are required for the purpose of the report, some the documents which may require are as under:

- Various clauses of Memorandum and Articles of Association
- Forms filed with the Registrar of Companies with receipts.
- All statutory registers.
- Verification of financial statement along with notes to accounts and Auditor Report.
- Report of Internal Auditor.
- Copies of contracts made between the company and any of the related parties
- Transfer and Transmission of Share.
- Instruments creating, modifying or satisfying charges.
- Various Disclosures from Directors
- Related Party Transactions.
- Corporate Social Responsibility (CSR)
- Directors and Key Managerial Personnel (KMP)

**PART II****Question 3**

- (a) Differentiate between Audit Plan and Audit Programme.
- (b) Prepare a note on Illustrative checkpoint on the Cyber Security Audit.
- (c) “A Corporate Social Responsibility (CSR) Audit aims at identifying environmental, social or governance risks faced by the organization and evaluating managerial performance in respect of those”. Explain the purpose of CSR Audit.  
(5 marks each)

**Answer 3(a)**

Difference between Audit plan and Audit Programme can be tabulated as under:

<i>Audit Plan</i>	<i>Audit Programme</i>
Audit Plan lays down the audit strategies to be followed for conducting an audit such as identifying the areas where special audit consideration and skills may be necessary, obtain the knowledge of business etc.	Audit Programme is an outline of how the audit is to be done, who is to do what work and within what time
Plans should be made to cover the following among other things:	It lays down the following audit procedure to be followed :
(i) Acquiring knowledge of accounting systems, policies and internal control procedures	(i) Evaluation process
(ii) Establishing the expected degree of reliance to be placed on the internal control	(ii) Ascertaining accuracy
(iii) Determining the nature, timing and extent of the audit procedures to be performed	(iii) Verification of Document
(iv) Co-ordinating the work to be done.	(iv) Scrutiny of supporting Documents
	(v) Checking of overall disclosure and presentation of all items in the audit completion.
	(vi) Preparation and submission of audit report.

**Answer 3(b)**

Cyber security is an attempt to minimising any risk of financial loss, disruption or damage to the reputation of an organisation that may arise from the failure of its information technology systems. The objective of the cyber audit is to provide an assessment of the operating effectiveness of cyber security policies and procedures, identify, protect, detect, respond and recover processes and activities to the board.

The following can be the illustrative check point on the Cyber Securities Audit:

- Check points relating to the Personnel Security
- Check points relating Physical access to electronic information systems
- Account and Password Management

- Confidentiality of Data
- Compliance and Audit of policies, standards, procedures, and guidelines.

### Answer 3(c)

Corporate Social Responsibility (“CSR”) is a broad term. However, for the purpose of addressing the scope of a CSR Audit, CSR is about managing and taking into consideration organization’s operational, processes and behavioural impact on society and stakeholders from a broad perspective. Contrary to common belief, CSR is more than basic legal compliance and is highly connected with and affects organization’s bottom line.

The followings are the purpose of CSR Audit:

- To ensure compliance with the provisions of Companies Act, 2013 with respect to constitution of the Committee, adoption of policy and appropriate spending towards CSR activities.
- To facilitate transparent monitoring mechanism and Act as a mentor for the Company’s CSR activities and implementation of CSR policy.
- To evaluate internal control and governance framework.
- To assess the project life cycle.
- To conduct financial review of projects to confirm the utilization of budgets for achieving desired outcomes.

### Question 4

- X & Co. Practicing Company Secretary, was appointed as Secretarial Auditor of a Company. During the audit certain irregularities were found. However, before the finalisation of the Report, the Company Secretary of the Company suggested a communication on the subject. Brief the stages involved for communication and discussion to finalise the Final Report of Secretarial Auditor.*
- Prepare a note on provisions with respect to punishment under Section 392 of the Companies Act, 2013 for contravention of the provisions by a foreign company.*
- If the amount of a fraud detected by a Secretarial Auditor during the course of his work in a company is ₹ 50 lakh, explain his duties to report.*
- What are the guiding criteria for identifying the applicable laws while conducting the Secretarial Audit ?*
- A firm of Company Secretaries is to be engaged as professional experts in due diligence process. What are the preconditions of accepting the professional engagement by the firm to maintain the quality ? (3 marks each)*

### Answer 4(a)

The stages involved for communication and discussion to finalise the Secretarial Audit report are as under:

- Submission of the Preliminary Draft* : At the conclusion of fieldwork, the auditor

should draft the report and present it to the entity's management for auditee's comments.

- (ii) *Exit Meeting* : The auditor should discuss with the management the findings, observations, recommendations, and text of draft and obtain their comment on the draft, achieve consensus and reach an agreement on the audit findings.
- (iii) *Formal Draft* : The auditor should prepare a formal draft, in view of the outcome of the exit meeting and other discussions. Upon review of such changes by the auditor and the management, the final report should be issued.
- (iv) *Final Report* : The report should be submitted to the appointing authority or such members of management, as directed.

#### **Answer 4(b)**

#### **Section 392: Punishment for Contravention**

Without prejudice to the provisions of section 391 of the Companies Act, 2013, if a foreign company contravenes the provisions of Chapter XXII - Companies Incorporated Outside India, the foreign company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees and in the case of a continuing offence, with an additional fine which may extend to fifty thousand rupees for every day after the first during which the contravention continues and every officer of the foreign company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty five thousand rupees but which may extend to five lakh rupees, or with both.

#### **Answer 4(c)**

#### **Reporting of frauds by auditor involving amount less than ₹1 crore**

As per the Sub-rule (3) of Rule 13 of the Companies (Audit and Auditors) Rules, 2014 in case of fraud involving an amount less than ₹1 Crore, the auditor shall report the matter of fraud to the Audit Committee or to the Board within 2 days of his knowledge of the fraud. The report should specify the nature of the fraud with description, approximate amount of the fraud and parties involved in the fraud.

In such case, as per Sub-rule (4), the Board shall disclose in its report (Board's Report) the nature of fraud with description, approximate amount of the fraud, parties involved in the fraud and remedial action taken. Name of parties should be disclosed only when the Board or Audit Committee has not taken any remedial action against the fraud.

In the given instance, the Secretarial Auditor shall report the same to the Audit Committee or to the Board of the company within 2 days of his knowledge of fraud.

#### **Answer 4(d)**

#### **Guiding Criteria for Segregation of Specific Laws and General Laws**

Segregation of laws applicable on the Company into the industry specific and general is essential for Secretarial Audit. After considering the following factors, the auditor should make the segregation of the same based on the laws applicable on the Company:

- Key financial parameters such as Turnover, Paid-up share capital, Net worth, Borrowings, etc.
- Geographic location of registered office, units/divisions/plants/branches, etc.
- Status of company such as listed/unlisted
- Type/Class of company such as Private, Public, Holding, Subsidiary, Foreign, Nidhi, Producer, Section 8 Company, etc.
- Registration with various authorities such as SEZ, Sectorial Regulators, etc.
- Segment such as Manufacturing/Trading/Service/e-commerce and Industry classification thereof
- Agreements governing rights, obligations of shareholders such as Joint venture, shareholders' agreements.
- Number, class and category of employees/workers such as women, contractual employees, etc.

The auditor should comprehensively verify all laws, rules, regulations made for regulation of specific Industry and should assess the adequacy of systems and process for other General laws applicable to the Company other than Industry Specific Laws and laws specifically covered under Form MR-3.

#### **Answer 4(e)**

#### **Pre-conditions of accepting professional engagement by a firm of Company Secretaries**

Prior to acceptance of any engagement, the firm, in order to establish whether the preconditions for a professional assignment are present, shall:

- (a) Determine whether the reporting framework to be applied in the preparation, audit, review of the secretarial/ non-financial statements is acceptable; and
- (b) Obtain the agreement of management that it acknowledges and understands its responsibility:
  - i. For the preparation of the secretarial/ non-financial statements in accordance with the applicable reporting framework, including where relevant their fair presentation;
  - ii. For such internal control/systems/procedure as management determines is necessary to enable the preparation of secretarial/ non- financial statements that are free from material misstatement, whether due to fraud or error; and
  - iii. To provide the firm with:
    - a) Access to all information of which management is aware that is relevant to the preparation/audit/review etc. of the secretarial/ non- financial statements such as records, documentation and other matters;

- b) Additional information that the firm may request from management for the relevant purpose; and
- c) Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

**Question 5**

- (a) *As a Company Secretary, prepare a note differentiating between concept of Ethics and Values.*
- (b) *ABC Ltd. has got the licence for setting up of a Rubber enterprise in State of Tamil Nadu. While providing the environmental clearance, Ministry of Environment, Forest and Climate Change imposes the condition for audit to check the compliances of norms issued with respect to environment. The company engages C & Co. Practicing Company Secretary (PCS) for this specific purpose. Prepare a note on Environmental Due Diligence as the PCS.*
- (c) *During the Secretarial Audit of the Company, auditors found various reports of expert. Some reports comprise technical details about the plant and project including assessment. Write the note on the reliability of the said reports.*  
(5 marks each)

**Answer 5(a)**

Ethics are consistently applied over the period, and remains same for all the human beings. Values have an individualistic approach, i.e. it varies from person to person but remains stable, relatively unchanging, but they can be changed over time due to a significant emotional event.

The fundamental differences between ethics and value are described in the given below points:

- Ethics refers to the guidelines for conduct, that address question about morality. Value is defined as the principles and ideals, which helps them in making the judgement of what is more important.
- Ethics is a system of moral principles in contrast to values, which is the stimuli of our thinking.
- Values strongly influence the emotional state of mind. Therefore it acts as a motivator. On the other hand, ethics compels us to follow a particular course of action.
- Ethics are consistent, whereas values are different for different persons, i.e. what is important for one person, may not be important for another person.
- Values tell us what we want to do or achieve in our life, whereas ethics helps us in deciding what is morally correct or incorrect, in the given situation.
- Ethics determines to what extent our options are right or wrong. Values define our priorities for life.



**Answer 5(b)**

**From:** C & Co.  
**Company Secretary in Practice**

**To:** ABC Ltd.

*Subject: Environment Due Diligence for setting up of a Rubber enterprises in the State of Tamil Nadu.*

**Dear Sir,**

We need your kind attention that audit of the compliance of environment norms and the environmental due diligence is scheduled on \_\_\_\_\_. In this regard, we request you to please avail the following documents and records for audit on the schedule dates:

- List of environmental permits and licenses and validities of the same
- All correspondence and notices with Environment Protection Agencies, state, or local regulatory agencies
- Whether the company's disposal methods of various by products are in sync with the regulatory guidelines.
- Whether there are any contingent environmental liabilities or continuing indemnification obligations.

We further inform you that as a part of the Environmental due diligence process, we will also review and prepare the detailed assessment report based on the historic, current and potential future environmental risks associated with the proposed locations at Tamil Nadu and for its operations. The process involve the risk identification and assessment with respect to:

- Environmental setting and history of the site
- Assessment of the site conditions
- Operations and management of sites
- Confirmation of legal compliance and pollution checks from regulatory authorities etc.

Accordingly, We request you to please provide the records and available for the Audit on the scheduled dates.

Regards,

CS \_\_\_\_\_

C & Co.

Company Secretary in Practice

**Answer 5(c)****Dependence on the Report of Other Expert by the Secretarial Auditor**

Where the secretarial auditor is planning to use the work of an expert, the auditor should evaluate the professional competence of the expert. This will involve considering

the expert's professional certification or licensing by, or membership in, an appropriate professional body and experience and reputation in the field in which the auditor is seeking audit evidence. For example, for building structure related compliance, a civil engineer is considered as the expert; for aviation related compliance, the aeronautical engineer is considered as expert and so on.

The auditor should evaluate the objectivity of the expert. The risk that an expert's objectivity will be impaired increases when the expert is employed by the entity; or is related in some other manner to the entity.

**Attempt all parts of either Q. No. 6 or Q. No. 6A**

**Question 6**

- (a) *A fraud is punishable offence whereas the non-compliance also attracts the penalties. Differentiate between the two concepts i.e. Fraud and Non-Compliance. (5 marks)*
- (b) *Internal audit is applicable to every company. Comment. (5 marks)*
- (c) *FKZ Ltd. is a public limited company carrying business of manufacturing the electric products having a paid up capital of ₹75 crore and turnover of ₹250 crore as per latest audited financial statement. Answer the following :*
- (i) *Explain the applicability of Secretarial Audit to this company.*
  - (ii) *Define 'Turnover' as per section 2(91) of the Companies Act, 2013.*
  - (iii) *Explain the provision regarding appointment of the Secretarial Auditor.*
  - (iv) *In case, 'S' a Secretarial Auditor, is found involved in the fraud amounting of ₹3 lakh (does not involve any public interest), then state the penalty for such action. (2+1+1+1=5 marks)*

**OR (Alternate Question to Q. No. 6)**

**Question 6A**

- (i) *There are various heads under which due diligence of Competition Law can be carried out. Explain.*
- (ii) *Why is there a need of external experts' opinion on various technical matters to auditors ?*
- (iii) *XYZ Ltd. a public limited company appointed R, a practicing professional, as an Internal Auditor of the company. During its audit procedure, he came to know some material information of the company which was revealed, due to incompetency of his audit staff, to the outsiders. The company filed a suit against him stating that due to his unprofessional and irresponsible behaviour, the company has to bear a huge loss. Explain the auditor's responsibility & duties in respect of the information acquired while performing the audit assignment. (5 marks each)*

**Answer 6(a)**

Any person who is found to be guilty of fraud shall be punishable with imprisonment and shall also be liable to fine as prescribed under section 447 of the Companies Act, 2013.

The term fraud can be defined as an act or course of deception, an intentional concealment, omission, or perversion of truth, to

- o Gain unlawful or unfair advantage,
- o Induce another to part with some valuable item or surrender a legal right, or
- o Inflict injury in some manner.

**Non Compliance** : The term non-compliance refers to failure to comply with the laws, rules regulations etc. The term non-compliance is commonly used in regard to a failure to meet the compliance requirements, be it the failure in following procedures, filing of information, eligibility conditions, reporting etc.

The relationship between fraud and the Non –compliance can be constructed as the Non- compliance in the company may lead to a fraud. However the fraud can also be made in the compliant company.

#### **Answer 6(b)**

#### **Applicability of Internal Audit**

The concept of the Internal Audit has been recognized as a statutory requirement under Section 138 of the Companies Act, 2013 read with Rule 13 of Companies (Accounts) Rule, 2014, and has been made mandatory on the following class of companies:

- (a) every listed company;
- (b) every unlisted public company having-
  - i. paid up share capital of fifty crore rupees or more during the preceding financial year; or
  - ii. turnover of two hundred crore rupees or more during the preceding financial year; or
  - iii. outstanding loans or borrowings from banks or public financial institutions exceeding one hundred crore rupees or more at any point of time during the preceding financial year; or
  - iv. outstanding deposits of twenty five crore rupees or more at any point of time during the preceding financial year; and
- (c) every private company having-
  - i. turnover of two hundred crore rupees or more during the preceding financial year; or
  - ii. outstanding loans or borrowings from banks or public financial institutions exceeding one hundred crore rupees or more at any point of time during the preceding financial year.

These companies are required to appoint an internal auditor which may be either an individual or a partnership firm or a body corporate.

**Answer 6(c)(i)**

Section 204(1) of the Companies Act, 2013 read with rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 provides that-

1. every listed company;
2. every public company having a paid-up share capital of fifty crore rupees or more; or
3. every public company having a turnover of two hundred fifty crore rupees or more

shall annex with its Board's Report made in terms of sub-section (3) of section 134, a Secretarial Audit Report, given by a Company Secretary in practice, in form MR- 3.

In the instant case FKZ Ltd. meets the criteria of paid up capital and the Turnover, hence the company is required to annex secretarial Audit report with its Boards Report.

**Answer 6(c)(ii)**

As per section 2(91) of the Companies Act, 2013, "Turnover" mean the gross amount of revenue recognised in the profit and loss account from the sale, supply, or distribution of goods or on account of services rendered, or both, by a company during a financial year.

**Answer 6(c)(iii)**

As per Rule 8 of the Companies (Meetings of Board and its powers) Rules, 2014, read with Section 179 of the Companies Act, 2013, secretarial auditor / company secretary in practice is required to be appointed by means of resolution at a duly convened board meeting.

**Answer 6(c)(iv)**

In the instant case since the fraud is of Rupees 3 Lakh which is less than Rupees 10 Lakh and does not involve public interest, the Secretarial Auditor 'S' shall be punishable with imprisonment for a term which may extend to five years or with fine which may extend to Rupees 50 Lakh or with both.

**Answer 6A(i)**

Due diligence of competition law may be made under the following heads:

1. Due diligence of various agreements (both existing and proposed)
  2. Due diligence on dominance and its likely abuse, if any (existing)
  3. Due diligence on combinations (i.e. effect of proposed mergers & Acquisition)
1. Due Diligence of various agreements includes:
    - Agreements relating to production, supply and distribution of goods or services.
    - Agreement if any with competitor relating to production, marketing or bidding, price etc.

- Agreements with customers and distributors.
  - Purchase agreements.
  - Non-compete covenants.
  - Technology transfer/technical know-how agreements.
  - Concession agreements
- 2. Due diligence on abuse of dominance if any includes:**
- Examination as to the existence of dominance
  - Examination of relevant market, whether product or geographical Areas.
  - Cases of abuse if any.
- 3. Due diligence on regulation of combinations:** The following aspects are to be analysed during due diligence process:
- Nature of combination.
  - acquisition of share, voting rights, assets or control or merger/amalgamation etc.
  - Examination of total value of Assets or Turnover and the valuation methodology.
  - Status of merger notification to be filed with Competition Commission of India.
  - Status of dominance after merger.

**Answer 6A(ii)**

An auditor may take external expert's opinion on various technical matters which forms the audit evidence. The auditor has to place reliance on the opinion expressed by the external expert considering his reliability, competency, consistency with data & information and independence.

In case of an external expert it shall be ensured that the interests and relationship of the external expert does not constitute a threat to that expert's objectivity. The auditor shall evaluate adequacy of expert's work having regard to the following:

1. Relevance and reasonableness of expert's findings /conclusions and consistency thereof with other audit evidence.
2. Relevance and reasonableness of assumptions and methods used in the expert's work.
3. Relevance, reasonableness, accuracy and completeness of source data (if any) used in the expert's work provided such data are significant for the expert's Work.
4. Agreement with the expert on the nature and extent of further work by the expert in case expert's work is found to be inadequate for audit purpose.

5. Performance of additional, appropriate audit procedures in case expert's work is found to be inadequate for audit purpose.

**Answer 6A(iii)**

The Auditors of a company while performing the audit assignment accesses various confidential information of the company and it is essential for the auditors to maintain the confidentiality of the auditee information. The principle of confidentiality imposes an obligation on the auditor to refrain from:

- Disclosing information acquired as a result of professional relationships without proper and specific authority or unless there is a legal or professional right or duty to disclose;
- Using information acquired as a result of professional relationships to their personal advantage or the advantage of third parties.
- An auditor should maintain confidentiality even in a social environment. The auditor should be alert to the possibility of inadvertent disclosure, particularly in circumstances involving long association with a business associate or a relative.
- He should also maintain confidentiality of information disclosed by a prospective client or employer.
- An auditor should also consider the need to maintain confidentiality of information within the firm or employing organization.
- An auditor should take all reasonable steps to ensure that staff under the auditor's control and persons from whom advice and assistance is obtained respect the auditor's duty of confidentiality.

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## **CORPORATE RESTRUCTURING, INSOLVENCY, LIQUIDATION & WINDING-UP**

Time allowed : 3 hours

Maximum marks : 100

**NOTE :** 1. Answer ALL Questions.

2. All references to sections relate to the Companies Act, 2013 unless stated otherwise.

### **PART – I**

#### **Question 1**

- (a) XYZ Ltd. is going for reduction of capital, but the Board of directors of the company expects objection from some of the creditors of the company. The Board seeks your opinion as a company secretary with respect to this matter. Express your opinion in light of the provisions of Companies Act, 2013.
- (b) The Board of directors of MNM Ltd., a small company is considering to merge with BRQ Ltd., another small company. The Board wants the merger to be fast and seeks your opinion about the conditions to be complied in this respect. Render your opinion based on the provisions of Companies Act, 2013.
- (c) “Circumstances or reasons that prompt or motivate Management to resort to Corporate Restructuring” — Briefly analyse the phrase giving or citing certain noted mergers or demergers during the last couple of years.
- (d) Mergers and acquisitions have one common goal of creating synergy that makes the value of the combined companies greater than the sum of the parts — Analyse briefly to focus on the visible benefits of such combinations.

(5 marks each)

#### **Answer 1(a)**

After passing the special resolution for the reduction of capital, XYZ Ltd. has to apply to the National Company Law Tribunal (NCLT) for the confirmation of resolution under section 66 of the Companies Act, 2013. Where the proposed reduction of share capital involves either (i) diminution of liability in respect of unpaid share capital, or (ii) the payment to any shareholder of any paid-up share capital, or (iii) in any other case, if the Tribunal so directs, the following provisions shall have effect:

The creditors having a debt or claim admissible in winding-up are entitled to object. To enable them to do so, the Tribunal will settle a list of creditors entitled to object. If any creditor objects, then either his consent to the proposed reduction should be obtained or he should be paid off or his payment be secured. The Tribunal, in deciding whether or not to confirm the reduction will take into consideration the rights of the creditors.

The Tribunal shall give notice of every application made to it to the Central Government, Registrar of Companies and to the Securities and Exchange Board of India, in the case of listed companies, and the creditors of the company and shall take

into consideration the representations, if any, made to it by Central Government, Registrar, the Securities and Exchange Board and the creditors within a period of three months from the date of receipt of the notice.

If no representation has been received from them within the said period, it shall be presumed that they have no objection to the reduction.

Provided that no application for reduction of share capital shall be sanctioned by the Tribunal unless the accounting treatment, proposed by the company for such reduction is in conformity with the accounting standards specified in section 133 of the Companies Act, 2013 or any other provision of the Act and a certificate to that effect by the company's auditor has been filed with the Tribunal.

There is no limitation on the power of the Tribunal to confirm the reduction except that it must first be satisfied that all the creditors entitled to object to the reduction have either consented or been paid or secured [*British and American Trustee and Finance Corporation v. Couper (1894)*].

When exercising its discretion, the Tribunal must ensure that the reduction is fair and equitable.

#### **Answer 1(b)**

In a Fast Track Merger under section 233 of the Companies Act, 2013 and rules made thereunder, broadly the steps followed are as under:

1. Both the companies need to check their Articles of Association and ensure that they have the requisite authority under them to enter into a merger. If no, the Articles of Association should be amended before the merger can take place.
2. Convene the Board meeting and prepare a draft scheme of merger or amalgamation.
3. Prepare the financial statement of assets and liabilities and get an Auditor's Report prepared.
4. Get the draft scheme approved in the Board meeting.
5. Both the companies need to send a notice to the Registrar of Companies (ROC) and Official Liquidator (OL) of their respective regions inviting suggestions/objections to the scheme, if any, within 30 days of issuing the notice.
6. Notice to the ROC shall be in Form CAA-9.
7. Both the companies are required to file a declaration of solvency with their respective ROCs. The declaration of solvency shall be accompanied by (a) Board Resolution (b) Statement of Assets and Liabilities and (c) Audit Report.
8. Sending notice for holding shareholders meeting and creditors meeting.
9. Conducting the shareholders meeting and creditors meeting and getting the scheme approved.
10. Filing the results of such meeting with the Regional Director and Official Liquidator by the transferee company.



**Answer 1(c)**

Broadly speaking, management is prompted to resort to corporate restructuring either for financial or other reasons. Financial reasons could be to reduce risk; increase operating efficiency; improve access to financial market; or to avail tax benefits. Other reasons could be to expand marketing and management capabilities; explore new products for development; avail synergistic benefits; or revive a sick company. Insolvency and Bankruptcy Code, 2016 has created one more window to submit resolution plan in a Corporate Insolvency Resolution Process.

Restructuring aims at improving the competitive position of an individual business and maximizing its contribution to corporate objectives. It also aims at exploiting the strategic assets accumulated by a business i.e., monopolies, goodwill, exclusivity through licensing, etc. to enhance the competitiveness advantages. Thus, restructuring helps in bringing an edge over competitors.

Prominent mergers/ demergers or acquisitions that took place recently are Flipkart acquiring Myntra, Asian Paints acquiring Ess Ess Bathroom products, RIL acquiring Network 18, Merck acquiring Sigma, Sun Pharma absorbing Ranbaxy; Tata Power acquiring PT Arutimin Indonesia, Reliance Industries demerger, Whitbread plc. demerged Costa Coffee and Sintex demerger.

**Answer 1(d)**

All mergers and acquisitions (M&A) have one common goal, i.e., they are all meant to create synergy that makes the value of the combined companies greater than the sum of the two parts. The success of a merger or acquisition depends on whether this synergy is achieved or not. Synergy may be in the form of revenue enhancement and cost savings. By merger, the companies expect to reap the following benefits:

1. *Becoming bigger*: Many companies use M&A to grow in size and leapfrog their rivals. While it can take years or decades to double the size of a company through organic growth, this can be achieved much more rapidly through mergers or acquisitions, i.e., through inorganic growth.
2. *Domination*: Companies also engage in M&A to dominate their respective sector/ industry. However, since a combination of two behemoths may result in a potential monopoly, such a transaction may have to face regulatory challenges.
3. *Tax benefits*: Companies also use M&A for tax purposes, although this may be an implicit rather than an explicit motive.
4. *Economies of scale*: Mergers also translate into improved economies of scale which refers to reduced costs per unit that arise from increased total output of a product.
5. *Acquiring new technology*: To stay competitive, companies need to stay on top of technological developments and their business applications. By buying a smaller company with unique technologies, a large company can maintain or develop a competitive edge.
6. *Improved market reach and industry visibility*: Companies buy other companies to reach new markets and increase their revenues and earnings. A merger may

expand two companies' marketing and distribution channels thereby giving new sales opportunities. A merger can also improve a company's standing in the investment community, i.e., bigger firms often have an easier time raising capital than smaller ones.

**Attempt all parts of either Q. No. 2 or Q. No. 2A**

**Question 2**

- (a) GKL Ltd., an Indian company intends to amalgamate with PS International Ltd., a foreign company. Examine the legal provisions that have to be complied with for such an amalgamation.
- (b) Whatever may be the degree of complexity and method of satisfaction, valuation is always an estimate — explain citing principles to be kept in mind for valuation.
- (c) “Under Companies Act, 1956 small companies were deterred from entering into mergers owing to the lengthy process and the Companies Act, 2013 provided a solution”. Comment. (5 marks each)

**OR (Alternate question to Q. No. 2)**

**Question 2A**

- (i) Sun Ltd. (listed company) has paid dividend of ₹10 per share in the current year. The estimated annual growth rate of the dividend is 5% per annum and share price is ₹120. Moon Private Ltd. (unlisted company), has paid dividend of ₹2 per share. The annual growth rate of the company is estimated to be 10% per annum. Calculate the rate of return of the listed company, Sun Ltd. and apply the same to unlisted company to compute the value of the share of the unlisted company Moon Private Ltd. (Assuming annual growth rate will continue for the future also.) (5 marks)
- (ii) Draft balance sheet of Mentos Ltd. as on 31st March, 2019 :

(₹ in '000)

Liabilities	Amount	Assets	Amount
Share Capital		Land & Building	7,500
Equity shares (₹10 each)	10,000	Plant & Machinery	3,700
16% Preference shares (₹100 each)	3,000	Furniture	730
General Reserve	1,050	Investments	1,620
18% debenture	600	Inventory	550
Other current liabilities	350	Trade receivables	750
		Cash at bank	150
	15,000		15,000

*Additional information :*

- (i) *Zeus Ltd. will take over Mentos Ltd. on 10th May, 2019.*
- (ii) *Debentureholder of Mentos Ltd. are discharged by issuing 12% debenture of Zeus Ltd. at a premium of 15%.*
- (iii) *Intrinsic value per share of Mentos Ltd. is ₹40 and that of Zeus Ltd. ₹50. Zeus Ltd. will issue shares on basis of intrinsic value to satisfy the equity shareholder of Mentos Ltd. However the entry should be made at par value only. The nominal value of each equity share of Zeus Ltd. is ₹10.*
- (iv) *16% preference shareholder of Mentos Ltd. are discharged at a premium of 20% by issuing necessary number of 10% preference share of Zeus Ltd. (Face value ₹100 each).*

*Compute the purchase consideration.*

*(5 marks)*

- (iii) *Brakes Ltd., a small company manufacturing brakes proposes to merge with Lubricants Ltd., another small company. Registrar of Companies (ROC) objected the scheme on the ground that it is not in the interest of the creditors. Comment on further steps as per Companies Act, 2013.*

*(5 marks)*

### **Answer 2(a)**

'Outbound merger' means a cross border merger where the resultant company is a foreign company. In terms of the Foreign Exchange Management (Cross Border Merger) Regulations, 2018, GKL Ltd. and PS International Ltd. have to take care of the following provisions in this regard:

- (i) A person resident in India may acquire or hold securities of the resultant company in accordance with the Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2004.
- (ii) A resident individual may acquire securities outside India provided that the fair market value of such securities is within the limits prescribed under the Liberalized Remittance Scheme laid down in the Act or rules or regulations framed thereunder.
- (iii) An office in India of the Indian company, pursuant to sanction of the Scheme of cross border merger, may be deemed to be a branch office in India of the resultant company in accordance with the Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016. Accordingly, the resultant company may undertake any transaction as permitted to a branch office under the aforesaid Regulations.
- (iv) The guarantees or outstanding borrowings of the Indian company which become the liabilities of the resultant company shall be repaid as per the Scheme sanctioned by the National Company Law Tribunal (NCLT) in terms of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

The resultant company shall not acquire any liability payable towards a lender in India in Rupees which is not in conformity with the FEMA or rules or regulations

framed thereunder. A no-objection certificate to this effect should be obtained from the lenders in India of the Indian company.

- (v) The resultant company may acquire and hold any asset in India which a foreign company is permitted to acquire under the provisions of the Foreign Exchange Management Act, 1999, rules or regulations framed thereunder. Such assets can be transferred in any manner for undertaking a transaction permissible under the said Act or rules or regulations thereunder.
- (vi) Where the asset or security in India cannot be acquired or held by the resultant company under the Foreign Exchange Management Act, 1999, rules or regulations made thereunder, the resultant company shall sell such asset or security within a period of two years from the date of sanction of the Scheme by NCLT and the sale proceeds shall be repatriated outside India immediately through banking channels. Repayment of Indian liabilities from sale proceeds of such assets or securities within the period of two years shall be permissible.
- (vii) The resultant company may open a Special Non-Resident Rupee Account (SNRR Account) in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016 for the purpose of putting through transactions under these regulations. The account shall run for a maximum period of two years from the date of sanction of the Scheme by NCLT.

### Answer 2(b)

Valuation is guessing with tact and intelligence. Different methods are adopted to record the price as near as possible on actual disposal. Certain principles need to be borne in mind before finalising Valuation Report. Report may be required for specific assets or may be for whole business or undertaking. In case of whole business or undertaking the past data on segment performance is required to be commented and taken into consideration. Valuation as per the report is taken as successful when the fair market value is arrived at the satisfaction of the seller company and the buyer company is willing to pay if it is beneficial to owners.

Broadly following principles are to be kept in mind for valuation:

**Principle of Time Value of Money** : This principle suggests that the value can be measured by calculating the present value of future cash flows discounted at the appropriate discount rate.

**Principle of Risk and Return** : This principle believes that the investors are basically risk averse and on the other hand expects higher amount of wealth. Higher the risk, higher may be possibility of return and *vice versa*.

**Principle of Substitution** : This principle believes that understanding the market with competitive forces is very important in order to decide the price consideration. The risk averse investor will not pay more than that of the substitute available in the market.

**Principle of Alternatives** : This principle suggests that one should explore the various alternatives available in the market and should not rest only on one option. The benefits of vetting of various alternatives will give a comparative valuation and a prudent investor will choose the most beneficial alternative to his portfolio.

**Principle of Expectation** : Cash flows are based on the expectations about the

performance in future and not the past. In the case of mature companies, we may assume that the growth from today or after some certain period would be constant.

**Principle of Reasonableness :** In valuation the principle of reasonableness is most important. It takes into consideration various aspects viz. nature of business, historical background, brand image, book value of the stock, earning capacity, dividend track record, etc.

### Answer 2(c)

The legal provisions pertaining to merger process stipulated in sections 391-394 of the Companies Act, 1956 was not considered as a simple procedure and there was no special provision for small companies. The process involved, *inter alia*, drafting a merger scheme, taking judicial approval for the scheme, getting Board and shareholders authorization, etc.

Section 233 of the Companies Act, 2013 has introduced the concept of fast track mergers. It carved out an exception from the regular merger procedure. It exempted small companies and holding and subsidiary companies entering into merger arrangements from the regular merger procedure as stipulated under sections 230-232 of the Companies Act, 2013. Section 233 of the Companies Act, 2013 along with Rule 25 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 lay down the entire legal framework of fast track mergers.

Fast track merges provide the following benefits:

- Simplified procedure for merger
- No judicial approval is required
- Separate procedures for small companies to enable them to expand without any roadblocks
- Form filings required also significantly reduced
- Fast track mergers have dispensed with Tribunal approval for mergers. Regional Directors, Registrar of Companies (ROC) and Official Liquidator are the authorities whose approval is required. The process has been simplified to a great extent.

A provision allowing the government to notify any other company in this regard has also been made.

### Answer 2A(i)

Gordon Growth model provides as under:

$$P_0 = D_0(1 + g) / (r_e - g)$$

Where:

$P_0$  = share price

$D_0$  = current dividend

$g$  = rate of growth of dividend

$r_e$  = rate of return required by the equity shareholders (student may also use  $k_e$  instead of  $r_e$ )

**Computation of Rate of return required by shareholder of Sun Ltd. (listed company)**

By using the following formula rearranged as:

$$r_e = D_0(1+g)/P_0 + g$$

$$\text{Rate of return } (r_e) = 10(1+5\%)/120 + 5\%$$

$$= 10(1+0.05)/120 + 0.05 = 0.1375 = 13.75\%$$

**Computation of value of share of Moon Pvt. Ltd.**

$$P_0 = D_0(1+g)/(r_e - g)$$

$$\text{Value of share } (P_0) = 2(1+10\%)/(13.75\% - 10\%)$$

$$= 2(1+0.1)/(0.1375 - 0.1) = 2.2/0.0375 = \text{Rs.58.67 per share}$$

**Answer 2A(ii)****Computation of purchase consideration**

The conversion ratio for equity share holders is 40:50 and for preference shares is 5:6

<i>(Rs. in '000)</i>		
<i>Issued to</i>	<i>From Zeus Ltd.</i>	<i>Amount</i>
Equity shareholder of Mentos Ltd. (10,00,000 shares x 10 x 40/50)	8,00,000 equity shares of Zeus Ltd. of Rs.10 each	8,000
Preference shareholder of Mentos Ltd.	36,000, 10% preference shares of Zeus Ltd. of Rs.100 each	3,600
<b>Total</b>		<b>11,600</b>

*Note* : Consideration to debenture holders not included in computation of purchase consideration as per AS-14. The same will be taken over by Zeus Ltd. and then discharged.

**Alternate Answer 2A(ii)**

<i>Calculation</i>	<i>Amount to be paid by transferee company i.e. Zeus Ltd. (Rs.)</i>	<i>No. of shares to be issued by transferee company i.e. Zeus Ltd.</i>

**A. Payment to preference shareholder of Mentos Ltd:**

*(Rs.)*

Preference share capital of Mentos Ltd.	30,00,000
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Premium to be paid (20% of 30,00,000)	6,00,000		
<b>Total amount to be paid to preference shareholders</b>	36,00,000	36,00,000	
No. of 10% preference shares (Rs.100 each) to be issued	36,00,000/ 100	—	36,000
<b>B. Payment to equity shareholders of Mentos Ltd:</b>			
1. No. of equity share of Mentos Ltd.	10,00,000		
2. Intrinsic value of one share of Mentos Ltd.	Rs. 40		
3. Total intrinsic value of equity shares of Mentos Ltd. (10,00,000*40)	400,00,000		
4. No. of equity shares to be issued on the basis of intrinsic value (400,00,000/50) of Rs.10 each (as per terms shares are to be issued at par)			8,00,000
<b>Total amount to be paid to equity shareholders</b>		80,00,000	
<b>Total</b>		<b>116,00,000</b>	

*Note* : Consideration to debenture holders not included in computation of purchase consideration as per AS-14. The same will be taken over by Zeus Ltd. and then discharged.

### Answer 2A(iii)

Section 233 of the Companies Act, 2013 provides the conditions which small companies have to follow for the merger (fast track merger). As per the said section further steps in the matter are as follows:

- (i) The Registrar will communicate the objections or suggestions to the scheme to the Central government within a period of thirty days. In the absence of any such communication, it would be presumed that no objections were raised.
- (ii) If the Central Government after receiving the objections or suggestions or for any other reason forms the opinion that the said scheme is not in public interest or in the interest of the creditors, it can file an application before the Tribunal within a period of sixty days.
- (iii) After filing of such application, the Tribunal has to render its judgment. If it is of the opinion (with reasons recorded in writing) that the scheme should be considered as per the procedure laid down in section 232 of Companies Act, 2013, it may give directions accordingly.

Provided that if the Central Government does not have any objection to the scheme or it does not file any application under this section before the Tribunal, it shall be deemed that it has no objection to the scheme.

### Question 3

- (a) *Certain ambiguities are cleared with the notification of Competition Commission of India (Procedure in regard to transactions of business relating to Combinations) Amendment Regulations, 2018 on 9th October 2018 — Briefly comment.*
- (b) *Distinguish between merger and an acquisition (any three points).*
- (c) *Write a short note on Leveraged buyout.*
- (d) *“Small Companies can only opt for Fast Track Mergers” — Elucidate briefly for identifying small companies.*
- (e) *“Cross Border Mergers not only bring benefits but also assume risks”. — Briefly comment with specific provision under Companies Act, 2013. (3 marks each)*

### Answer 3(a)

Certain ambiguities are cleared on notification of the CCI (Procedure in regard to transactions of business relating to combinations) Amendment Regulations, 2018 on 9th October, 2018. There is a clarity in computing 210 days for a notified transaction that could be extendable on the number of requests by the Commission. Applicant has liberty to offer voluntary modifications. Regulation 27 of the said regulations has made provision for appointing agencies to oversee the implementation of modifications directed by the Commission. Regulation 25 of the said regulations affords parties not to wait for the Commission to order modification after a long Drawn Phase II review process. This would result in speedier resolution of the Competition Commission of India's concern according quicker approvals in line with international practices.

### Answer 3(b)

<i>Merger</i>	<i>Acquisition</i>
A merger occurs when two separate entities combine forces to create a new joint organization in which both are equal partners.	An acquisition refers to the purchase of one entity by another.
Old company cease to exist and a new company emerges.	A new company does not emerge.
It requires two companies to consolidate into a new entity with a new ownership and management structure.	It occurs when one company takes over all of the operational management decisions of another.
A transaction legally structured as a merger may give each party's shareholders partial ownership and control of combined enterprise.	A transaction legally structured as an acquisition may have the effect of placing one party's business under the indirect ownership of the other party's shareholders.



**Answer 3(c)****Leveraged buyout**

When one refers to something (a company, a property or an investment) as 'highly leveraged' it means that item has more debt than equity.

A leveraged buyout (LBO) is the acquisition of a company in which the buyer puts-up only a small amount of money and borrows the rest. The buyer can achieve this desirable result because the targeted acquisition is profitable and may provide ample cash that can be used to repay the debt. The expectation with leveraged buyout is that the return generated on the acquisition will more than outweigh the interest paid on the debt, hence making it a very good way to experience high returns whilst only risking a small amount of capital.

**Answer 3(d)**

Section 233 of the Companies Act, 2013 has introduced the concept of fast track mergers. It exempted small companies and holding and subsidiary companies entering into merger arrangements from the regular merger procedure as stipulated under sections 230-232 of the Companies Act, 2013. Section 233 of the Companies Act, 2013 along with Rule 25 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 lay down the entire legal framework of fast track mergers.

'Small Company' under section 2(85) of the Companies Act, 2013 means a company, other than a public company -

- (i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees; and
- (ii) turnover of which as per profit and loss account for the immediately preceding financial year does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than one hundred crore rupees:

Provided that nothing in this clause shall apply to, (a) a holding company or a subsidiary company; (b) a company registered under section 8 of the Companies Act, 2013; or (c) a company or body corporate governed by any special Act.

**Answer 3(e)**

As per section 234(1) of the Companies Act, 2013, the provisions of cross border merger are subject to every other law specifically providing for any restriction.

A company may merge with a foreign company incorporated in any of the jurisdictions specified in Annexure B under Rule 25A of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 after obtaining prior approval of the Reserve Bank of India and after complying with provisions of sections 230 to 232 of the Companies Act, 2013 and these rules. It is to be ensured that while entering into an outbound merger, it is with a company from one of the specified jurisdictions.

Some of the risks associated with cross border mergers are:

1. **Taxation** : Despite Double Tax Avoidance Agreements, the tax implications in

the host countries may prove to be complex and tedious. This may increase the costs as a local professional is required to be hired.

2. **Regulatory landscape** : The laws and regulations in the host country would be different and may be difficult to comply. An unsuitable regulatory landscape may pose risks to a cross border merger.
3. **Political scenario** : It is essential to assess the political situation of the country before one enters into a merger with an entity belonging to that country. Unstable political situation may lead to difficulties in carrying out business.
4. **Valuation** : Valuation is one factor which changes with countries due to changes in exchange rate, stock market transactions and other macroeconomic developments.

## PART - II

### Question 4

- (a) *Global Finance Bank Ltd. has extended ₹100 crore to GEO Ltd. against mortgage of 50 acre of landed property with building. GEO Ltd. is being liquidated. Global Finance Bank Ltd. seeks to realise the mortgaged property given as security. Advise Global Finance Bank Ltd. about realising its security (5 marks)*
- (b) *Terms “Insolvency” and “Bankruptcy” are synonymous in result but practically refer to different situations and consequences — Briefly explain. (5 marks)*
- (c) *“Any security interest created in favour of any secured creditor may be enforced, without the intervention of the court or tribunal, by such creditor”. Explain the procedure for enforcement of security interest under Securitisation and Reconstruction of Financial Asset and Enforcement of Security Interest Act, 2002 (SARFAESI). (5 marks)*
- (d) *While adjudication was available for each kind of insolvency and bankruptcy, do you feel the necessity of a single code in the name of Insolvency and Bankruptcy Code, 2016 — Discuss with relevant background. (5 marks)*

### Answer 4(a)

Regulation 37 of the IBBI (Liquidation Process) Regulations, 2016 deals with realisation of security interest by a secured creditor (Global Finance Bank Ltd.).

- (i) Global Finance Bank Ltd. who seeks to realize its security interest shall intimate the liquidator of the price at which he proposes to realise its secured asset.
- (ii) The liquidator shall inform the Global Finance Bank Ltd. within twenty one days of receipt of the intimation, if a person is willing to buy the secured asset before the expiry of thirty days from the date of intimation at a price higher than the price intimated.
- (iii) Where the liquidator informs the Global Finance Bank Ltd. of a person willing to buy the secured asset, Global Finance Bank Ltd. shall sell the asset to such person.

- (iv) If the liquidator does not inform Global Finance Bank Ltd. or the person does not buy the secured asset, Global Finance Bank Ltd. may realise the secured asset in the manner it deems fit, but at least at the price intimated.
- (v) Where the secured asset is realised under (iii) above, Global Finance Bank Ltd. shall bear the cost of identification of the buyer.
- (vi) Where the secured asset is realised under (iv) above, the liquidator shall bear the cost incurred to identify the buyer.
- (vii) The provisions of this Regulation shall not apply if Global Finance Bank Ltd. enforces its security interest under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 or the Recovery of Debts and Bankruptcy Act, 1993.

**Answer 4(b)**

The terms 'Insolvency' and 'Bankruptcy' are generally used interchangeably in common parlance but there is a marked distinction between the two. Insolvency and bankruptcy are not synonymous.

The term 'insolvency' denotes the state of one whose assets are insufficient to pay his debts; or his general inability to pay his debts. The term 'insolvency' is used in a restricted sense to express the inability of a person or an entity to pay his debts as they become due in the ordinary course of business.

'Bankruptcy' is a legal status of a person or an entity who cannot repay debts to creditors. The bankruptcy process begins with filing of a petition in a court or before an appropriate authority designated for this purpose. The debtor's assets are then evaluated and used to pay the creditors in accordance with law.

Thus insolvency is a state and bankruptcy is the conclusion. The term insolvency is used for individuals as well as organisations/ corporates. If insolvency is not resolved, it leads to bankruptcy in case of individuals and liquidation in case of corporates.

**Answer 4(c)**

Section 13 of SARFAESI Act, 2002 deals with enforcement of security interest by a creditor which provides as under:

- (a) Where any borrower, who is under a liability to a secured creditor under a security agreement, makes any default in repayment of secured debt or any installment thereof, and his account in respect of such debt is classified by the secured creditor as non-performing asset, then, the secured creditor may require the borrower by notice in writing to discharge in full his liabilities to the secured creditor within sixty days from the date of notice failing which the secured creditor shall be entitled to exercise all or any of the rights under section 13(4) of the Act.
- (b) If on receipt of the notice, the borrower makes any representation or raises any objection, the secured creditor shall consider such representation or objection and if the secured creditor comes to the conclusion that such representation or objection is not acceptable or tenable, he shall communicate within fifteen days of receipt of such representation or objection the reasons for non-acceptance of the representation or objection to the borrower.

In case the borrower fails to discharge his liability in full within the period specified above, the secured creditor may take recourse to one or more of the following measures to recover his secured debt, namely:

- (i) take possession of the secured assets of the borrower
- (ii) takeover the management of the business of the borrower
- (iii) appoint any person (hereafter referred to as the manager)
- (iv) 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.

#### **Answer 4(d)**

Before the enactment of the Insolvency and Bankruptcy Code, there were multiple overlapping laws and adjudicating forums dealing with financial failure and insolvency of companies and individuals in India. The framework for insolvency and bankruptcy was inadequate, ineffective and resulted in undue delays in resolution. The legal and institutional framework did not aid lenders in effective and timely recovery or restructuring of defaulted assets and causes undue strain on the Indian credit system.

Prior to the enactment of the Insolvency and Bankruptcy Code, the provisions relating to insolvency and bankruptcy for companies were made in the Sick Industrial Companies (Special Provisions) Act, 1985, the Recovery of Debt Due to Banks and Financial Institutions Act, 1993, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 and the Companies Act, 2013. These statutes provided for creation of multiple fora such as Board of Industrial and Financial Reconstruction (BIFR), Debt Recovery Tribunal (DRT) and their respective Appellate Tribunals. Liquidation of companies was handled by the High Courts. Individual bankruptcy and insolvency was dealt with under the Presidency Towns Insolvency Act, 1909, and the Provincial Insolvency Act, 1920.

The liquidation of companies was handled under various laws and different authorities such as High Court and Debt Recovery Tribunal had overlapping jurisdiction which was adversely affecting the debt recovery process.

The objective of the Insolvency and Bankruptcy Code is to consolidate and amend the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner. An effective legal framework for timely resolution of insolvency and bankruptcy will not only encourage entrepreneurship but will also improve Ease of Doing Business, and facilitate more investments leading to higher economic growth and development.

#### **Question 5**

- (a) *On or after promulgation of Insolvency and Bankruptcy Code, 2016 only the qualified person can be appointed as a Resolution Professional or a Liquidator of a Corporate Body — Discuss briefly. (3 marks)*
- (b) *Debt for Equity swaps can be used as a tool not only for 230-231 of Companies*

*Act, 2013 but for resolution plans formulated under Insolvency and Bankruptcy Code, 2016 — Present your views briefly. (3 marks)*

- (c) *Define “bankrupt” under Insolvency and Bankruptcy Code, 2016. (3 marks)*
- (d) *In a case of Individual Insolvency, creditors resolved to replace the Resolution Professional and approached you for an advice. Offer your views for replacing the Resolution Professional. (3 marks)*
- (e) *Central Government has power to examine the books and papers, financial reports even after sanction of the scheme by National Company Law Tribunal—Elaborate the issue in relation to preservation of records of amalgamated companies. (3 marks)*

#### **Answer 5(a)**

As per section 206 of the Insolvency and Bankruptcy Code, 2016 no one can render services of an Insolvency Professional (IP) without being enrolled as a member of an Insolvency Professional Agency (IPA) and registered with Insolvency and Bankruptcy Board of India (IBBI). Thus, only persons with requisite qualifications and registered as Insolvency Professional can take-up the roles of Resolution Professional or Liquidator including Voluntary Liquidation. IBBI (Insolvency Professionals) Regulations, 2016 require a person to complete a pre-registration educational course, as may be required by the Board, from an insolvency professional agency after his enrolment as a professional member. Section 207(2) of the Code empowers the IBBI to state eligibility criteria for the persons having exposure in finance, law, management, insolvency or such other field, as it deems fit.

#### **Answer 5(b)**

Regulation 37 of Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 provides that a resolution plan shall provide for the measures for maximisation of value of assets. Thus, one of the best methods of corporate debt restructuring is debt-equity swap where specified shareholders shall have right to exchange stock for a predetermined amount of debt in the same company. In debt-equity swap debt/bonds are exchanged with shares/stock of the company. However, the resolution plan needs to be placed before Committee of Creditors for approval before the same is placed for sanction by the NCLT.

#### **Answer 5(c)**

Section 79(4) of the Insolvency and Bankruptcy Code, 2016 defines the term ‘bankruptcy’ as the state of being bankrupt.

According to section 79(3) of the Insolvency and Bankruptcy Code, 2016 ‘bankrupt’ means:

- (a) a debtor who has been adjudged as bankrupt by a bankruptcy order under section 126;
- (b) each of the partners of a firm, where a bankruptcy order under section 126 has been made against a firm; or
- (c) any person adjudged as an undischarged insolvent.

**Answer 5(d)**

Section 98 of the Insolvency and Bankruptcy Code 2016 provides for the grounds and the manner in which a resolution professional can be replaced with another resolution professional in an insolvency resolution process initiated under section 94 of the Code on an application by the debtor or under section 95 of the Code if applied for by a creditor. The debtor or creditor may apply to Adjudicating Authority for such replacement. Within seven days, the Adjudicating Authority shall make a reference to Insolvency and Bankruptcy Board of India (IBBI) for replacement. IBBI in turn within ten days shall recommend the name of Resolution Professional against whom no disciplinary proceedings are pending.

**Answer 5(e)**

In terms of section 239 of the Companies Act, 2013 that corresponds to Section 396A of Companies Act, 1956, the books and papers of a company that has been amalgamated with or whose shares have been acquired by another company shall not be disposed of without obtaining prior permission of Central Government. Before granting such approval the Government is empowered to appoint a person to examine the books and papers or any of them for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion, formation or the management of the affairs of the transferor company or its amalgamation, or the acquisition of its shares.

**Attempt all parts of either Q. No. 6 or Q. No. 6A****Question 6**

- (a) *A model Law is a legislative text that needs legislative guide to outline the core issues to be incorporated in the substantive law — Discuss the relevance in having Legislative Guide by United Nations Commission for International Trade Law (UNCITRAL) to supplement UNCITRAL Model Law on cross border insolvency.*
- (b) *A resolution plan has been submitted in respect of the company PQR Ltd. and the resolution plan is yet to be confirmed. The committee of creditors resolved to liquidate PQR Ltd. approved by not less than sixty-five percent of the voting share. Can liquidation be ordered ?*
- (c) *“The Insolvency and Bankruptcy Code makes significant changes in the priority of claims for distribution of liquidation proceeds”. Comment. (5 marks each)*

**OR (Alternate question to Q. No. 6)****Question 6A**

- (i) *EST Ltd. is aggrieved by the order of National Company Law Tribunal (NCLT) and seeks your advice for further steps in the matter.*
- (ii) *The National Company Law Tribunal (NCLT) has confirmed the reduction of share capital of MGF Ltd. Explain when the reduction of share capital will take place as per the Companies Act, 2013*

- (iii) Explain the major amendments introduced in SEBI (Substantial Acquisition of Shares Takeovers) Regulations, 2011 notified on September 21, 2011.

(5 marks each)

**Answer 6(a)**

A model law is generally used differently than a legislative guide. Specifically, a model law is a legislative text recommended to States to enact as part of National Law, with or without modification. As such, model laws generally propose a comprehensive set of legislative solutions to address a particular topic and the language employed supports direct incorporation of the provisions of the model law into a national law.

On the other hand, legislative guide focuses upon providing guidance to legislators and other users and for that reason guides generally include a substantial commentary discussing and analysing relevant issues. It is not intended that the recommendations of a legislative guide be enacted as part of law as such. Rather, they outline the core issues that it would be desirable to address in that law, with some recommendations providing specific guidance on how certain legislative provisions might be drafted.

The purpose of the Legislative Guide on Insolvency Law is to assist the establishment of an efficient and effective legal framework to address the financial difficulty of debtors. The Legislative Guide provides a comprehensive statement of the key objectives and principles that should be reflected in a State's insolvency laws.

**Answer 6(b)**

Section 33(2) of the Insolvency and Bankruptcy Code, 2016 provides that where the resolution professional, at any time during the corporate insolvency resolution process but before confirmation of resolution plan, intimates the Adjudicating Authority of the decision of the committee of creditors approved by not less than sixty-six per cent of the voting share to liquidate the corporate debtor, the Adjudicating Authority shall pass a liquidation order.

In the instant question the approval of the resolution to liquidate PQR Ltd. by the creditors having sixty-five percent of the voting share is not sufficient. The decision of the committee of creditors should be approved by not less than sixty-six percent of the voting share. Hence, the liquidation of PQR Ltd. cannot be ordered.

**Answer 6(c)**

Section 53 of the Insolvency and Bankruptcy Code 2016 deals with distribution of assets in liquidation. The Insolvency and Bankruptcy Code, 2016 makes significant changes in the priority of claims for distribution of liquidation proceeds.

In case of liquidation, the assets will be distributed in the following order:

- (i) fees of insolvency professional and costs related to the resolution process;
- (ii) workmen's dues for the preceding 24 months and secured creditors;
- (iii) employee wages;
- (iv) unsecured creditors;
- (v) government dues and remaining secured creditors (any remaining debt if they enforce their collateral);

- (vi) any remaining debts and dues
- (vii) preference shareholders, if any; and
- (viii) equity shareholders or partners, as the case may be.

Before the enactment of the Code, the government dues were immediately below the claims of secured creditors and workmen in order of priority. Now, the Central and State Government's dues stand below the claims of secured creditors, workmen dues, employee dues and other unsecured financial creditors.

#### **Answer 6A(i)**

As per section 421 of the Companies Act, 2013, EST Ltd. can prefer appeal to the National Company Law Appellate Tribunal (NCLAT). The appeal shall be filed within a period of forty-five days from the date on which a copy of the order of the National Company Law Tribunal (NCLT) is made available to EST Ltd. and shall be in such form, and accompanied by such fees, as may be prescribed.

The NCLAT may entertain an appeal after the expiry of the said period of forty-five days from the date aforesaid, but within a further period not exceeding forty-five days, if it is satisfied that the appellant EST Ltd. was prevented by sufficient cause from filing the appeal within that period.

On the receipt of an appeal the NCLAT shall, after giving the parties to the appeal a reasonable opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or setting aside the order appealed against. The NCLAT shall send a copy of every order made by it to the NCLT and the parties to appeal.

As per section 423 of the Companies Act, 2013, if EST Ltd. is further aggrieved by the order of the NCLAT, it may file an appeal to the Supreme Court within sixty days from the date of receipt of the order of the NCLAT on any question of law arising out of such order.

#### **Answer 6A(ii)**

As per section 66(5) of the Companies Act, 2013, MGF Ltd. shall deliver a certified copy of the order of the Tribunal and of a Minute approved by the Tribunal showing —

- (a) the amount of share capital;
- (b) the number of shares into which it is to be divided;
- (c) the amount of each share; and
- (d) the amount, if any, at the date of registration deemed to be paid-up on each share, to the Registrar of Companies (RoC) within thirty days of the receipt of the copy of the order, who shall register the same and issue a certificate to that effect.

The reduction of share capital takes effect only on registration of the order and Minutes and not before. The RoC will then issue a certificate of registration which will be conclusive evidence that the requirements of the Companies Act, 2013 have been complied with and that the share capital is now as set out in the Minutes. The Memorandum has to be altered accordingly.



**Answer 6A(iii)**

The major changes/ amendments introduced *vide* the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 notified on 23rd September, 2011 were as under:

1. increase in trigger limit for open offer from 15% to 25%.
2. increase in statutory open offer size from 20% of share capital to 26% of total share capital of the company.
3. overhaul of exemptions from open offer.

Exemptions have been further categorized into the following broad heads:

- (a) transactions, which trigger a statutory open offer due to substantial acquisition of shares/ voting rights, or due to change in control.
  - (b) transactions which trigger a statutory open offer due to acquisition of shares/ voting rights exceeding prescribed thresholds, provided that there is no change in control.
4. Offer pricing: These regulations brought in the concept of Volume Weighted Average Market Price.
  5. Creeping acquisition: These regulations provided that an acquirer could make a creeping acquisition of 5% annually (between April 1 to March 31 of next year) to reach 75% stake such that the minimum public shareholding of 25% is maintained. The manner of computation of the 5% creeping acquisition limit has also been clarified.
  6. Non-compete fee: The provision of payment of non-compete was done away with.
  7. Recommendation of independent directors on the open offer to be published in the newspapers in which the detailed public statement was given.

The Regulations, further sought to include the various SAT judgments, informal guidance given and the experience gained from implementing the Takeover Regulations since 1994. They further sought to align itself with the Takeover Regulations as they exist in the rest of the world.

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## **RESOLUTION OF CORPORATE DISPUTES, NON-COMPLIANCES AND REMEDIES**

*Time allowed : 3 hours*

*Maximum marks : 100*

**NOTE:** Answer **ALL** Questions.

### **Question 1**

- (a) *A is a minority shareholder who brought an action for damages against the Company and its directors on the ground that they have been negligent in selling a plant owned by the Company for ₹25 Lakh. A alleged that the real value of plant was about ₹70 Lakh. Evaluate based on decided case law(s), whether action taken by A will be maintainable in the Court.*
- (b) *“Breach of trust may be held to be a civil wrong but when mens-rea is involved, it gives rise to criminal liability also”. Comment on this statement with supporting judicial pronouncements.*
- (c) *“Person once convicted or acquitted not to be tried for same offence again”. Comment on the statement in the light of decided case law(s).*
- (d) *The current regulatory scenario demands the Company Secretary to be more vigilant and diligent specifically about the applicability of multiple laws and timely compliances. Briefly comment on the statement. (5 marks each)*

### **Answer 1(a)**

No, the action taken by "A" will not be maintainable in court on the mentioned ground. The management of company is based on the majority rule. Almost every question relating to the affairs of the company is required to be decided upon either by an ordinary Resolution or by a Special Resolution of shareholders.

In *Pavrides v. Jensen* (1956) Ch. 565, a minority shareholder brought an action for damages against three directors and against the company itself on the ground that they have been negligent in selling a mine owned by the company for £ 82,000, whereas its real value was about £ 10,00,000. It was held that the action was not maintainable. The judge observed, " It was open to the company, on the resolution of a majority of the shareholders to sell the mine at a price decided by the company in that manner, and it was open to the company by a vote of majority to decide that if the directors by their negligence or error of judgement has sold the company's mine at an undervalue, proceedings should not be taken against the directors".

### **Answer 1(b)**

The essential elements of the offence of criminal breach of trust are:

1. The accused must be entrusted with the property or with dominion over it,
2. The person so entrusted must use that property, or;

3. The accused must dishonestly use or dispose of that property or wilfully suffer any other person to do so in violation,
  - (i) of any direction of law prescribing the mode in which such trust is to be discharged, or;
  - (ii) of any legal contract made touching the discharge of such trust.

The Supreme Court of India in *VR. Dalal v. Yugendra Naranji Thakkar*, 2008 (15) SCC 625, has held that the first ingredient of criminal breach of trust is entrustment and where it is missing, the same would not constitute a criminal breach of trust. Breach of trust may be held to be a civil wrong but when mens-rea is involved it gives rise to criminal liability also.

In a judgment of *Pratibha Rani v. Suraj Kumar*, AIR 1985 SC 628, the appellant alleged that her stridhan property was entrusted to her in-laws which they dishonestly misappropriated for their own use. She made out a clear, specific and unambiguous case against in-laws. The accused were held guilty of this offence and she was held entitled to prove her case and no court would be justified in quashing her complaint.

#### **Answer 1(c)**

Section 300 of Code of Criminal Procedure, 1973 (CrPC) protects a person from being prosecuted for the same offence again. Section 300 of CrPC cannot be definitely interpreted to mean that if a person steals a property and gets convicted of the offence of theft, he should not be prosecuted for the same offence if it arises out of another theft. Section 300 of CrPC is unique in the sense that it requires either a conviction or acquittal as a pre-requisite for the protection to be available.

In the case of Kerala High Court in *Bharat Plywood and Timber Products Private Limited and Onr. v. Registrar of Companies and Another*. [2002] 108 Comp Cas 601 (Ker) held that "Section 300 of the CrPC provides that so long as an order of acquittal or conviction handed down by a court of competent jurisdiction stands in respect of a person charged with committing an offence, that person cannot again be tried on the same facts for the offence for which he was earlier tried or for any other offence arising therefrom. Section 300 of CrPC becomes applicable when a court of competent jurisdiction had already tried the accused and that he is either acquitted or convicted. It is also necessary to note that for the first part of sub-section (1) of Section 300 to apply, the prior prosecution and subsequent prosecution should be for the same offence."

#### **Answer 1(d)**

The Company Secretary has a vital role to play in the event of invocation of any action under the Act. The current regulatory scenario demands the Company Secretary to be more vigilant and diligent specifically about the applicability of multiple laws and timely compliances thereunder as he being a Key Managerial Person is jointly liable for any non-compliances under the applicable legislation. The role which a Company Secretary can play includes:

1. To ensure timely compliances of the provisions of the Act to avoid any action for default or failure
2. To represent the Company before the ROC, RD or NCLT, in the event of any action for default or failure

3. To develop a robust internal compliance system which generates the details of compliances undertaken and any compliance lapses in a timely manner
4. To initiate the compounding procedure in the event of any non-compliance(s) coming to light and to avoid recurrence of such non-compliances in future
5. To ensure timely and appropriate disclosure pertaining to penalties or compounding offences or action by any authorities.

Further, since the Practicing Company Secretaries are also covered under section 447 of the Companies Act, 2013, they should ensure that they are not certifying any returns or issuing any report which contains any false certification or information or omits any material information or facts, as such a failure to ensure proper verification of compliances may lead to the Practicing Company Secretary being liable to penalties under the above referred provisions as well as disciplinary proceedings under the guidelines issued by ICSI.

**Attempt all parts of either Q. No. 2 or Q. No. 2A**

**Question 2**

- (a) *Super Source Limited has filed Form AOC-4 with Registrar of Companies after 85 days of its Annual General Meeting along with additional fee. State whether the Company can be penalized again under section 403 of the Companies Act, 2013.*
- (b) *A crime is alleged to have been committed in a particular State. The Central Government has referred the case to Central Bureau of Investigation Agency (CBI) for investigation. Can CBI conduct such investigation on the direction of Central Government ? Would your answer be different if such direction was given by the Supreme court of India ?*
- (c) *X, a director of PQR Private Limited, is authorised by Board of directors to prepare and file returns, reports or other documents to Registrar of Companies (ROC) on behalf of the Company. He files all the required documents with ROC, despite being aware of material discrepancies in them. Subsequently, it was found that the documents filed with ROC contained materially false details. Explain the penal provisions under the Companies Act, 2013 for this offence.*
- (d) *Distinguish between General Liability Insurance and Professional Liability Insurance. (4 marks each)*

**OR (Alternate question to Q. No. 2)**

**Question 2A**

- (i) *ABC & Co., Chartered Accountants, are the Statutory Auditors, as well as the Internal Auditors of Super Sky Limited. Evaluate whether the same is permitted under the Companies Act, 2013. If not, what are the penal provisions under the Companies Act, 2013 ? (4 marks)*
- (ii) *P is the Managing Director of AMR Limited who committed a fraud against the Company. A judicial proceeding has been initiated against P for fraud committed by him. Now P wants to settle the case through mediation or conciliation. Can P's case be referred to mediation or conciliation ? (4 marks)*

- (iii) *ABC Exports Limited aggrieved by an order of Adjudication Authority under Foreign Exchange Management Act, 1999, wants to file an appeal against the order in Civil Court. As a Company Secretary, advise ABC Exports Limited whether the civil court has jurisdiction to entertain such a suit ? If not, suggest an alternate remedy. (4 marks)*
- (iv) *“Directors and Officers (D & O) insurance has become closely associated with broader management liabilities insurance, which covers liabilities of the corporate itself as well as the personal liabilities for the directors and officers of the company”. Enumerate the reasons to buy D & O policy. (4 marks)*

**Answer 2(a)**

Yes, the additional fee does not absolve the Company from the liability of penalty or any other action under the Act for such default or failure.

One of the significant changes brought in by the Companies (Amendment) Act, 2017 is the amendment in section 403 of the Companies Act, 2013. Pursuant to the said amendment, the non-offence period of 270 days has been omitted from the Companies Act, 2013 and the filing of forms, returns or documents within the time prescribed under the relevant provision has been made mandatory. Accordingly, the non-filing of forms, returns or documents within the time prescribed under relevant provision (for e.g., Form AOC-4 within 30 days of date of AGM) is now considered as a default or failure and the payment of additional fees does not absolve the company from the liability of penalty or any other action under the Act for such default or failure.

**Answer 2(b)**

No, The Central Bureau of Investigation (CBI) cannot directly investigate based on the directions of Central Government. The functioning of CBI is governed by section 6 of Delhi Special Police Establishment Act, 1946. The Act prohibits the agency from investigating the case outside Delhi and other Union Territories without permission from the respective state government. The Central Government can authorize CBI to investigate such a crime in a State but only with the consent of the concerned State Government.

Yes, The Supreme Court and High Courts can order CBI to investigate such a crime anywhere in the country without the consent of the State.

**Answer 2(c)**

According to section 448 of the Companies Act, 2013, if any person makes a statement which is false in any material particulars, knowing it to be false or omits any material facts, knowing it to be material, such person shall be liable under section 447 of the Companies Act, 2013.

As per Section 447, any person who is found to be guilty under this section shall be punishable with imprisonment for a term which shall not be less than 6 months but which may extend to 10 years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to 3 times the amount involved in the fraud. Provided that, where the fraud involves public interest, the term of imprisonment shall not be less than 3 years.

Hence, X, director of PQR Private Limited shall be punishable with imprisonment and fine as mentioned above.

**Answer 2(d)**

General Liability Insurance covers business from a few "general" lawsuits that any business could face. It triggers when a third party (i.e., anyone who doesn't work for the company) sues the business over:

- Bodily injuries they incurred on the commercial premises,
- Damage caused to their property,
- Advertising injuries (e.g. slander, libel, misappropriation, and copyright infringement).

General Liability Insurance pays for the legal expenses (lawyers' fees, court costs, and settlements or judgments). Any small-business owner, no matter their industry or the size of their business, can face these claims. That's why many consider this policy to be the keystone of a business protection plan.

Professional Liability Insurance is also known as "Errors and Omissions Insurance" or "Malpractice Insurance". Its coverage focuses specifically on the lawsuits that stem from the professional services rendered.

Though this policy is especially important for service providers to carry, most small-business owners can benefit from its coverage. It shields the insured from third-party lawsuits alleging:

- Negligent professional services.
- Failure to uphold contractual promises.
- Incomplete or shoddy work.
- Mistakes or omissions.

These torts are among the most expensive a business owner can face. One need not be at fault to be sued, an unhappy client may name the business in a lawsuit to recoup the "losses" they incurred because of the work carried out.

**Answer 2A(i)**

As per provisions of Section 144 of the Companies Act, 2013, the statutory auditor of a Company shall not provide internal audit services. The internal audit services provided by ABC & Co., Chartered Accountants to Super Sky Limited, is not permissible under the Companies Act, 2013

As per section 147(2) of the Companies Act, 2013, if an auditor of a company contravenes any of the provisions of section 139, section 143, section 144 or section 145, the auditor shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees or four times the remuneration of the auditor, whichever is less.

Provided that if an auditor has contravened such provisions knowingly or wilfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with imprisonment for a term which may extend to one year and with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees.

ABC & Co. is liable to penalties as mentioned above and it cannot file an application for Compounding, as the offence committed under section 144 of the Companies Act, 2013 is a non-compoundable offence, if the auditor has contravened knowingly or wilfully.

**Answer 2A(ii)**

The crime of fraud comes under non-compoundable offence and these types of crime shall not be referred to mediation or conciliation for settlement. Hence the crime committed by P, cannot be referred to mediation and conciliation.

As per rule 30 of Companies (Mediation and Conciliation), Rule 2016, following matters shall not be referred to mediation or conciliation, namely: -

- (a) the matters relating to proceedings in respect of inspection or investigation under Chapter XIV of the Companies Act, 2013; or the matters which relate to defaults or offences for which applications for compounding have been made by one or more parties.
- (b) Cases involving serious and specific allegations of fraud, fabrication of documents forgery, impersonation, coercion etc.
- (c) Cases involving prosecution for criminal and non-compoundable offences.
- (d) Cases which involve public interest or interest of numerous persons who are not parties before the Central Government or the Tribunal or the Appellate Tribunal as the case may be.

**Answer 2A(iii)**

Civil court cannot entertain such suits as civil court has no jurisdiction.

As per section 34 of Foreign Exchange Management Act, 1999, no civil court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which an Adjudicating Authority or the Appellate Tribunal or the Special Director (Appeals) is empowered by or under this Act to determine and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under this Act.

In the given case, ABC Exports Limited can appeal to:

**(A) Appeal to Special Director (Appeals)**

As per section 17(1) of Foreign Exchange Management Act, 1999, the Central Government shall, by notification, appoint one or more Special Directors (Appeals) to hear appeals against the orders of the Adjudicating Authorities under this section and shall also specify in the said notification the matter and places in relation to which the Special Director (Appeals) may exercise jurisdiction.

As per section 17(2) of Foreign Exchange Management Act, 1999, any person aggrieved by an order made by the Adjudicating Authority, being an Assistant Director of Enforcement or a Deputy Director of Enforcement may prefer an appeal to the Special Director (Appeals).

**(B) Appeal to Appellate Tribunal (Section 19)**

As per section 19(1) of Foreign Exchange Management Act, 1999, save as

provided in sub-section (2), the Central Government or any person aggrieved by an order made by an Adjudicating Authority, other than those referred to in section 17(1), or the Special Director (Appeals), may prefer an appeal to the Appellate Tribunal.

### **Answer 2A(iv)**

Directors and officers insurance affords protection to directors and officers from liability arising from actions connected to their corporate responsibilities. The policy provides indemnity to the directors and officers in respect of Legal costs in defending proceedings brought against them alleging wrongful acts.

Key reasons to buy D&O insurance are:

- *Personal assets of directors are at risk* : If a director has been accused of breaching duties, their personal assets are at risk in case they don't have any D & O insurance.
- *Defending a legal action is an expensive affair*: The legal costs and expenses in litigations involving directors are usually complex and costly.
- *Investors can file a case* : If investors believe that they have incurred losses due to mismanagement of the company, they could approach the court to seek compensation.
- *Employees can sue* : It is not only shareholders who can file a case against the directors as even employees reach the court to challenge the decision of the directors. It is a hard reality that in today's corporate world, there has been a rise in the number of cases filed by employees, related to sexual harassment or wrongful dismissal.
- *Customers can take legal actions* : In some cases, customers also reach the court against misrepresentations made in the advertisement materials and deceptive trade practices.
- *Enquiry initiated by regulatory authorities* : Regulatory bodies like SEBI, Revenue Department, etc, can initiate enquiry against directors.
- *In case of bankruptcy or insolvency* : If faced with bankruptcy, creditors can pursue legal action against directors if they think that they have not acted in their best interest.
- *Helps in attracting/retaining talent* : Not having a comprehensive D&O may discourage talented employees from joining the company as they know will not be guarded against any legal case if arise in future.

D&O claims are not covered under any other policy: Most of the people believe that D&O claims are also covered under other liability insurance plans like professional indemnity.

### **Attempt all parts of either Q.NO. 3 or Q. No. 3A**

#### **Question 3**

- (a) X, a Police Officer comes to know from reliable sources that four persons are staying in a house and are planning to kidnap and murder Mohan. He also has



information that they possess automatic weapons. The Police Officer apprehends that they will commit the crime at any moment. He directly goes to that house and without any warrant or order from the Metropolitan Magistrate, arrests all the four persons along with weapons in their possession. Is the arrest of all the four persons valid ?  
(4 marks)

- (b) ABC Technologies Limited was incorporated under the Companies Act, 2013 as a closely held Public Company. The paid-up capital of Company is ₹15 Crore. The Company suo-motuo filed a petition for compounding of violation under Section 203 of the Companies Act, 2013 read with Rule 8 of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014. The Company pleaded that it had tried, but was unable to find and appoint a full time Company Secretary as required under the Act. What would be the consequences for Company, its Directors and KMP in this case ?  
(4 marks)
- (c) PQR Express Limited is aggrieved by an order of National Company Law Appellate Tribunal (NCLAT). As a Company Secretary, advise the Company as to where an appeal can be filed against the order of NCLAT and also comment on limitation period of appeal against the order.  
(4 marks)
- (d) Sundry creditors of MNO Trading Limited filed a complaint with the Registrar of Companies (ROC), Delhi & Haryana alleging that the management of the company is indulging in destruction and falsification of the accounting records of the company. The complainants request the ROC to take immediate steps to seize the books of accounts & records of the company so that the management may not be allowed to tamper with the books of accounts & records. The complaint was received at 11 A.M on 10th January 2019 and the ROC entered the premises at 11.30 A.M., for a search without obtaining an order from the Special Court. Comment on the action of ROC vis-a-vis his powers under the Companies Act, 2013.  
(4 marks)

**OR (Alternate question to Q. No. 3)**

**Question 3A**

- (i) Explain in brief the grounds on which the Central Government may order for investigation into affairs of company.
- (ii) A group of shareholders of ABC Developers Limited consisting of 24 members decided to file a petition before the Tribunal for relief against oppression and mismanagement by the Board of Directors. The company has a total of 250 members and the group of 24 members holds one-tenth of the total paid-up share capital accounting for one-fifteenth of the issued share capital. The main grievance of the group is that due to mismanagement by the Board of directors, the company is incurring losses and the company has not declared any dividends even when profits were available in the past years for declaration of dividend. In the light of the provisions of the Companies Act, 2013, advise the group of shareholders regarding the chances of success for :
- (i) getting the petition admitted
- (ii) obtaining relief from the Tribunal.

- (iii) *S is a newly qualified Company Secretary. He wants to know whether there is any dress code approved by the Council of ICSI as professional dress code, for Company Secretaries to appear before judicial/quasi-judicial bodies and Tribunal? Advise S.*
- (iv) *Mrs. Geeta is Managing Director of HEL Limited. She has been arrested for an offence covered under Section 447 of the Companies Act, 2013 on a complaint made by the Director, Serious Fraud Investigation Office. Geeta seeks your legal advice to know the conditions under which she can be released on bail. Advise Geeta. (4 marks each)*

### Answer 3(a)

Section 2(c) of the Criminal Procedure Code, 1973 defines cognizable offences. Cognizable offence means a case in which, a police officer may arrest without warrant, as per the First Schedule of the Criminal Procedure Code, 1973 or under any other law for the time being in force. Cognizable offences are usually offences which are serious in nature like, Murder, Rape, Dowry, Kidnapping etc.

In the given case, all four persons are planning to kidnap and murder Mohan, which is in nature of cognizable offence, hence arrest of all four persons is valid according to section 2 (c) of the Criminal Procedure Code, 1973.

As per section 156 of Criminal Procedure Code 1973, a police officer may, without an order of the Magistrate, investigate any cognizable case. Thus on the basis of the first information report and other materials placed before the Police, if there is a suspicion that a cognizable offence has been committed, the Police Officer may arrest without any warrant.

### Answer 3(b)

As per Section 203(5) of the Companies Act, 2013, if a company contravenes the provisions of this section, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees and every director and key managerial personnel of the company who is in default shall be punishable with fine which may extend to fifty thousand rupees and where the contravention is a continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the contravention continues.

The NCLT may levy maximum fine as:

<i>Particulars</i>	<i>Violation under Section 203</i>	<i>Fine for continuing of contravention</i>
Penalty on Company	Rupees five lakh	Rupees one thousand per day of delay
Penalty on Director and KMP	Rupees fifty thousand	Rupees one thousand per day of delay

Hence, ABC Technologies Limited, its directors & KMP are subjected to penal provisions of Companies Act, 2013 as mentioned above.

**Answer 3(c)**

As per section 423 of the Companies Act, 2013, any person aggrieved by any order of the Appellate Tribunal may file an appeal to the Supreme Court within sixty days from the date of receipt of the order of the Appellate Tribunal to him on any question of law arising out of such order.

The Supreme Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.

In the given case, PQR Express Limited can file an appeal to Supreme Court of India against order of National Company Law Appellate Tribunal (NCLAT) within 60 days from the date of receipt of order of the Appellate Tribunal.

**Answer 3(d)**

Section 209 of the Companies Act, 2013 provides that where upon information in his possession or otherwise, the Registrar or inspector has reasonable ground to believe that the books and papers of-

- i. a company, or
- ii. relating to the key managerial personnel, or
- iii. any director, or
- iv. auditor, or
- v. company secretary in practice if the company has not appointed a company secretary,

are likely to be destroyed, mutilated, altered, falsified or secreted, he may, after obtaining an order from the Special Court for the seizure of such books and papers,-

1. enter, with such assistance as may be required, and search, the place or places where such books or papers are kept; and
2. seize such books and papers as he considers necessary after allowing the company to take copies of or extracts from, such books or papers at its cost.

According to the above provisions, ROC may enter and search the place where such books or papers are kept and seize them only after obtaining an order from the Special Court.

Since in the given question, ROC entered the premises for the search and seizure of books of the company without obtaining an order from the Special Court, he is not authorised to seize the books of the PQR Trading Limited.

**Answer 3A(i)**

Investigation into the affairs of the company may be ordered by the Central Government on grounds given in Section 210(1) of the Companies Act, 2013. The investigation shall be ordered by Central government, where an order of investigation was made by a court or the tribunal.

Where the Central Government is of the opinion, that it is necessary to investigate into the affairs of a company-

- a) on the receipt of a report of the Registrar or inspector;
- b) on intimation of a special resolution passed by a company that the affairs of the company ought to be investigated; or
- c) in public interest,

it may order an investigation into the affairs of the company.

Where an order is passed by a court or the Tribunal in any proceedings before it that the affairs of a company ought to be investigated, the Central Government shall order an investigation into the affairs of that company.

For the purpose of investigation, the Central Government may appoint one or more inspectors to investigate the affairs of the company. These inspectors shall report on the affairs of the company in such manner as the central government may direct.

### **Answer 3A(ii)**

Section 244 of the Companies Act, 2013 provides the right to apply to the Tribunal for relief against oppression and mismanagement. This right is available only when the petitioners hold the prescribed limit of shares as indicated below:

- (i) In the case of company having a share capital, not less than 100 members of the Company or not less than one tenth of the total number of its members whichever is less or any member or members holding not less than one tenth of the issued share capital of the company, provided that the applicant(s) have paid all calls and other dues on the shares.
- (ii) In the case of company not having share capital, not less than one-fifth of the total number of its members.

Since the group of shareholders do not number to 100 or hold 1/10th of the issued share capital or constitute 1/10th of the total number of members, they have no right to approach the Tribunal for relief.

However, pursuant to Section 244 of the Act, the Tribunal may, on an application made to it waive all or any of the requirements specified in (i) or (ii) so as to enable the members to apply under section 241.

As regards obtaining relief from Tribunal, continuous losses cannot, by itself, be regarded as oppression (*Ashok Betelnut Co. P. Ltd. vs. M.K. Chandrakanth*).

Similarly, failure to declare dividends or payment of low dividends also does not amount to oppression. (*Thomas Veddon V.J. (v) Kuttanad Robber Co. Ltd*). Thus, the shareholders may not succeed in getting any relief from Tribunal.

### **Answer 3A(iii)**

The professional dress prescribed under the code of conduct for the professional is required to be worn by the authorised representative while appearing before the authorities.

The Council of ICSI has approved the following Guidelines for Professional Dress Code for Company Secretaries to appear before judicial/quasi-judicial bodies and tribunals:

1. For Male Members:
  - a. Navy Blue Suit (Coat & Trouser), with CS logo, Insignia or Navy Blue Blazer over a sober colored Trouser
  - b. Neck Tie (ICSI)
  - c. White full sleeve Shirt
  - d. Formal Black Leather Shoes (Shined)
2. For Female Members:
  - a. Navy Blue corporate suit (Coat & Trouser), could be with a neck tie Insignia or
  - b. Saree / any other dress of sober colour with Navy Blue Blazer with CS logo
  - c. A sober footwear like Shoes/Bellies/Wedges, etc. (shined)

The Members in employment have also been prescribed the same dress code.

#### **Answer 3A(iv)**

According to Section 212(6) of the Companies Act, 2013, notwithstanding anything contained in the Code of Criminal Procedure, 1973, offence covered under section 447 shall be cognizable and no person accused of any offence under those sections shall be released on bail or on his own bond unless:

- (i) the Public Prosecutor has been given an opportunity to oppose the application for such release; and
- (ii) where the Public Prosecutor opposes the application, the court is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while on bail. A person, who, is under the age of sixteen years or is a woman or is sick or infirm, may be released on bail, if the Special Court so directs. The Special Court shall not take cognizance of any offence referred to this sub-section except upon a complaint in writing made by-
  - i. the Director, Serious Fraud Investigation Office; or
  - ii. any officer of the Central Government authorised, by a general or special order in writing in this behalf by that Government.

Hence, in the instant case, Geeta has been arrested for an offence covered under section 447 of the Act on a complaint made by the Director, SFIO.

Geeta may be released (on the grounds of being a woman) on bail if the Special Court so directs.

#### **Question 4**

- (a) *P is an employee of ABC Limited and he is being investigated under the provisions of Companies Act, 2013. The Company wants to terminate P on the ground that*

*an investigation is going on against him. They have filed the application to Tribunal for approval of termination. Company has not received any reply from the Tribunal within 30 days of filling the application. The Company considers it as a deemed approval and terminates him. Is the contention of Company valid in law ?*

- (b) *Enumerate the Compounding Authorities under Companies Act, 2013. Write the procedure for compounding in brief.*
- (c) *Can Registrar of Companies order adjudication proceedings under Section 454 of Companies Act, 2013 ? In what cases can the Central Government appoint him as the Adjudicating Officer ?*
- (d) *An investigation has been initiated against PR Limited under Section 210 of the Companies Act, 2013. M, the Managing Director of PR Limited, refused to produce books of accounts before the Inspector and disobeyed the direction issued by the Inspector. What would be the penal provisions for such an action under the Companies Act, 2013 ?* (4 marks each)

#### **Answer 4(a)**

Yes, the termination of P made by the company is totally valid in law and company can do so by considering deemed approval of tribunal.

The provision of Section 218 of the Companies Act, 2013 states that the company is required to take approval of the tribunal before taking action against the employee if there is any pendency of any proceedings against any person concerned in the conduct and management of the affairs company. The company shall require approval in the following circumstances:

- discharge or suspension of an employee or
- punishment to an employee by dismissal, removal, reduction in rank or otherwise or
- change in the terms of employment to the disadvantage of employee(s) The Tribunal shall notify its objection to the action proposed in writing.

In case, the company other body corporate or person concerned does not receive the approval of the Tribunal within 30 days of making the application, it may proceed to take the action proposed against the employee. That means it can be consider as a deemed approval by the tribunal.

#### **Answer 4(b)**

In terms of Section 441 of the Act, there are two compounding authorities:

- *Regional Director* : The Regional Director (RD) appointed by the Central Government as a Regional Director for the purposes of the Companies Act, 2013, and
- National Company Law Tribunal (NCLT)

#### **Procedure for Compounding of offence**

- Call for a board meeting to decide on compounding as per the Companies Act, 2013.

- Arrive at the amount of the fine involved as per the relevant section(s).
- Hold the Board Meeting and pass resolution(s) to compound and provide for preparation and providing necessary authorization for compounding.
- 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 Tribunal or the Regional Director or any officer authorised by the Central Government, as the case may be.
- The filing with Registrar of Companies (ROC) is done in the e-form GNL-1 prescribed for this purpose. Also deliver sufficient number of hard copies of the compounding application to ROC for him to forward it to RD/Tribunal based on the quantum of fee involved.
- There will be a personal hearing before the Regional Director or Tribunal which will decide the amount to be paid for compounding.
- Get the order passed by the RD/Tribunal and pay the amount stipulated within the time fixed.
- File Order of RD/NCLT with ROC in form INC-28 and ROC will take note of the same.

#### **Answer 4(c)**

The Registrar of Companies may note the non-compliance of the provisions of Companies Act as arrived at under section 206(4) of the Companies Act, 2013 either:

- by himself on a scrutiny of documents filed with him and on his satisfaction or
- based on any report on inspection or investigation, if any, under the relevant provisions of the Companies Act, 2013, or
- on the qualifications of the statutory auditors in the Annual Report or by the secretarial auditors in their Secretarial Audit Report whereby he can ascertain and identify the nature of non-compliance or default.

In all these cases, he himself cannot initiate any adjudicating proceedings if he is the adjudicating officer even as he may be clothed with a power of adjudication. Therefore, if adjudicating powers are under his jurisdiction, any other officer who is independent of his office has to identify the existence of violation as otherwise the adjudicating officer, being the head of his office may be biased. This is a grey area to be addressed by the Central Government as otherwise the adjudicating officer will be sitting on a judgement of the findings of his own office.

It is pertinent to note that it would, therefore, be only logical, prudent and wise for the concerned Regional Director not to appoint as the adjudicating officer pursuant section 454(2) of the Companies Act, 2013, the same jurisdictional Registrar of Companies whose office has identified the violation.

#### **Answer 4(d)**

As per section 217(6) of the Companies Act, 2013, if any director or officer of the

company disobeys the direction issued by the Registrar or the inspector, the director or the officer shall be punishable with imprisonment which may extend to one year and with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

If a director or an officer has been convicted of an offence, the director or the officer shall on and from the date of conviction shall be deemed to have vacated his office and shall also be disqualified from holding an office in any company.

As per section 217(8) of the Companies Act, 2013, if any person fails without reasonable cause or refuse-

- a. To produce to an inspector or authorised person any book or paper which is his duty
- b. To furnish any information which is his duty to furnish
- c. To appear before the inspector personally when required to do so or to answer any question which is put to him by the inspector
- d. To sign the notes of any examination,

he shall be punishable with imprisonment for a term which may extend to six months and with fine which shall not be less than twenty five thousand rupees but may extend to one lakh rupees and also with a further fine which may extend to two thousand rupees for every day after the first during which the failure or refusal continues.

#### Question 5

- (a) *During the Statutory audit of MOP Limited, the auditors found that a fraud has been committed against the Company by its officers amounting to more than ₹10 Crore. What are the duties of statutory auditors in the given case under the Companies Act, 2013 ?*
- (b) *“Crisis Management is not necessarily the same thing as risk management”. What is Crisis Management and how is it different from risk management. Explain in detail guidelines/recommendations for establishing a good crisis management plan. (8 marks each)*

#### Answer 5(a)

If an auditor of a company, in the course of the performance of his duties as statutory auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of rupees one crore or above, is being or has been committed against the company by its officers or employees, the auditor shall report the matter to the Central Government. Section 143 of the Companies Act, 2013 confers certain powers on the auditors of the company as well it casts certain duties on them.

The auditor shall report the matter to the Central Government as under:-

- the auditor shall report the matter to the Board or the Audit Committee, as the case may be, immediately but not later than two days of his knowledge of the fraud, seeking their reply or observations within forty-five days.
- on receipt of such reply or observations, the auditor shall forward his report and



the reply or observations of the Board or the Audit Committee along with his comments to the Central Government within fifteen days from the date of receipt of such reply or observations.

- In case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of forty-five days, he shall forward his report to the Central Government along with a note containing the details of his report that was earlier forwarded to the Board or the Audit Committee for which he has not received any reply or observations.
- the report shall be sent to the Secretary, Ministry of Corporate Affairs in a sealed cover by Registered Post with Acknowledgement Due or by Speed Post followed by an e- mail in confirmation of the same.

### **Answer 5(b)**

Crisis management is the identification of threats to an organization and its stakeholders, and the methods used by the Organization to deal with these threats. An organization may face various types of crisis like natural crisis, technological crisis, confrontation crisis, etc.

Crisis management involves dealing with crises in a manner that minimizes damage and allows the affected organization to recover quickly. Dealing properly with a crisis can be especially important for a company's public relations.

Businesses that effectively put a continuity plan in place in case of unforeseen contingencies can mitigate the effects of any negative event that occurs. The process of having a continuity plan in place in the event of a crisis is known as crisis management.

Crisis management is different from risk management. Unlike risk management, which involves planning for events that might occur in future, crisis management involves reacting to negative events during and after they have occurred. For example, an oil company may have a plan in place to deal with the possibility of an oil spill, but if such a disaster actually occurs, the magnitude of the spill, the backlash of public opinion, and the cost of clean-up can vary greatly and may exceed expectations.

As Crisis may come in several forms and it is recommended in all cases that a company be prepared ahead of time with a crisis management plan.

The following guidelines are recommended for establishing good crisis management plans:

- Employ a professional crisis manager who can help in planning crisis management processes.
- Initiate frequent training and refresher courses on handling crises. Drills and fake operations must frequently take place to keep refreshing stakeholders on emergency responses to crises.
- Form a crisis team to work under the leadership of a crisis manager.
- Planning responses and crisis management processes for various potential crises is highly recommended. It takes several approaches and processes to address different crises.

- Initiate systems that can effectively monitor or detect foreseeable crises signals early enough in order to tackle the situation before it gets out of hand.
- Provide a list of key persons in case of a crisis and their contacts. The contact information must be displayed where anyone can see and easily access them.
- Identify the ground person to be notified immediately when a crisis occurs. Apart from a crisis manager, there must be a coordinating person among employees who possess first-hand news on a looming crisis. It should be the same person who can be trusted by his colleagues with vital information on any suspected crisis.
- Identify a central point where the employees can assemble and the exit points to use in case of a crisis. Emergency exit doors with ease of opening them must be labelled well and an emergency central place identified and properly labelled as well.
- Regular testing of the crisis management process and emergency equipment and updating them frequently or as needed.

#### Question 6

- (a) *POB Limited wants to design and implement an effective Enterprise Risk Management (ERM) system. Evaluate the challenges likely to be faced by the Company during implementation of ERM system.*
- (b) *G is the General Manager (HR) of XYZ Limited. He wrongfully withholds the flat of the Company and also lets it out on rent to someone. XYZ Limited has filed a complaint against G. What are the penalties for such a conduct under the Companies Act, 2013.*
- (c) *“Class action suit is a new mechanism in India to claim the loss caused to the specified stakeholders of the Company not only from the Company but also from other entities”. Analyse the statement in brief.*
- (d) *“The minority shareholders are empowered under the Companies Act, 2013 to bring action with a view to prevent the majority from oppression and mis-management”. Justify the statement with rights available to minority shareholders under the Act.* (4 marks each)

#### Answer 6(a)

Risk management also known as Enterprise Risk Management ('ERM'), is a systematic and holistic approach for firms to address all their risks, whether operational, strategic or financial, comprehensively. ERM focuses on identifying risks, developing and monitoring risk management system and reacting to risk events, when they occur.

POB Limited may face the following challenges in designing and implementing an effective ERM system, including:

1. *Effectively linking risk and strategy*: Integrating risk management into the overall corporate strategy is a challenge for many Indian firms. The challenge is to have an ERM system that encompasses a process capable of being applied in strategy setting across the enterprise.

2. *Implementing cost-effective risk management for small and medium-sized enterprises* : While the costs of risk management failures can be high, designing and implementing efficient ERM can also be quite costly, especially for small and medium-sized firms.
3. *Addressing all major areas of risk* : ERM requires a firm to take a portfolio view of risk; boards must consider how various risks inter-relate, rather than treating each business and risk individually. This is a significant challenge for many boards.
4. *Mitigating new risks* : In India, many complex areas of risks have emerged in the last decade or so, which has made risk management particularly challenging. For example, some traditional areas of risk, such as political instability and strikes and unrest, appear to have subsided while others, such as information and cyber security as well as terrorism and insurgency, have increased in prominence. Companies operating in various industries have experienced the theft of data and sensitive information. For companies in major cities, the threat of terror attacks has become a growing cause for concern, which can be hard to manage by the company itself.

**Answer 6(b)**

The Company is entitled to take following actions against "G" in accordance with section 452 of the Companies Act, 2013, it provides that:

- (1) If any officer or employee of a company -
  - a. Wrongfully obtains possession of any property, including cash of the company or
  - b. having any such property including cash in his possession, wrongfully withholds it or knowingly applies it for the purposes other than those expressed or directed in the articles and authorised by this Act, he shall, on the complaint of the company or of any member or creditor or contributory thereof be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.
- (2) The Court trying an offence under sub-section (1) of Section 452 of the Companies Act, 2013 may also order such officer or employee to deliver up or refund, within a time to be fixed by it, any such property or cash wrongfully obtained or wrongfully withheld or knowingly misapplied, the benefits that have been derived from such property or cash or in default, to undergo imprisonment for a term which may extend to two years.

**Answer 6(c)**

A class action suit is a new mechanism to claim the loss caused to the specified stakeholders of the company not only from the company but also from other entities. Various persons/ entities against whom such actions can be taken are:

- i. A company or its directors for any fraudulent, unlawful or wrongful act or omission.
- ii. An auditor including audit firm of a company for any improper or misleading

statement of particulars made in the audit report or for any unlawful or fraudulent conduct.

- iii. An expert or advisor or consultant for an incorrect or misleading statement made to the company.

It is pertinent to note that the definition of the expert is wide under the Companies Act, 2013 which includes an engineer, a valuer, a chartered accountant, a company secretary, a cost accountant and any other person who has the power or authority to issue a certificate in pursuance of any law for the time being in force. However the advisors or consultants are not provided, thus the definitions of the same will be derived from judicial precedence and use of the same in common parlance.

#### **Answer 6(d)**

The various rights are available to the minority shareholders under the Companies Act, 2013 to bring action with a view to prevent oppression and mismanagement:

1. *Right to appoint Small Shareholders' Directors* : The small shareholders or minority shareholders as often construed, of a listed company have a right to appoint a shareholder of their choice on the board and such shareholder may be called as a 'Small Shareholders' Director' under section 151 of the Companies Act, 2013.
2. *Right to apply to NCLT for Oppression and Mismanagement* : The minority shareholders can approach the National Company Law Tribunal (NCLT) under the provisions of the Companies Act, 2013. Section 241, 242 and 244 of the Companies Act, 2013 under Chapter XIV lays down the remedies that minority shareholders can resort to in cases of oppression and mismanagement.
3. *Right to file a Class Action Suit under section 245(1) of the Companies Act, 2013* : It is another type of protection given to minority shareholders. A class action suit usually means a legal suit wherein a group of persons sharing a common interest can go to NCLT if they are of the view that the affairs of the company are conducted in manner that is prejudicial to the interests of the company or members or depositors.

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