

Thus, meeting of board of director can be held at factory premises and it is not necessary that it should be held at registered office of the company.

As per Section 174(4), where a meeting of the Board could not be held for want of quorum, then, unless the articles of the company otherwise provide, the meeting shall automatically stand adjourned to the *same day at the same time and place* in the *next week* or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place.

Thus, contention of Chairman that meeting is dissolved due to want of quorum is not correct. If quorum is not present the meeting shall automatically stand adjourned to the *same day at the same time and place* in the *next week* or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place.

Que. No. 51] In a private limited company, there are only two directors on the board. A Board meeting convened was adjourned for want of quorum. At the adjourned meeting, inspite of quorum not being present, the resolutions were passed as per the agenda. Discuss the validity of resolutions so passed. CS (Inter) – Dec 2003 (4 Marks)

Ans.: As per Section 174(1), the quorum for a meeting of the Board of Directors of a company shall be higher of the following two:

- 1/3rd of its total strength or (*fraction rounded up to next*)
- Two directors

In case of board meeting quorum must be present even at adjourned meeting and any business transacted for want of quorum is not valid.

Que. No. 52] A meeting of the board of directors of a company was convened on 31st December, 2015 to discuss some important matters. 5 Directors out of 7 directors write to the chairman that they would like to attend the meeting but could not do so due to other pre-occupations. The last meeting was held on 29th September, 2015. Advise the chairman. CS (Inter) – June 2003, Dec 2007 (4 Marks)

Ans.: As per Section 173(1), every company shall hold a minimum 4 meetings of its Board of Directors every year. The gap between two board meetings should not be more than 120 days.

As per Section 174(1), the quorum for a meeting of the Board of Directors of a company shall be higher of the following two:

- 1/3rd of its total strength (*fraction rounded up to next*) or
- Two directors

1/3rd of 7 comes to 3(2.33 rounded up to 3). Thus, meeting cannot be held with two directors on 31.12.2015.

As per Section 173(4), where a meeting of the Board could not be held for want of quorum, then, unless the articles of the company otherwise provide, the meeting shall automatically stand adjourned to the *same day at the same time and place* in the *next week* or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place. Even at such adjourned meeting, 'quorum' is essential.

However, if at adjourned meeting required quorum is present then such adjourned meeting will be deemed to be held on 31.12.2015 as adjourned meeting is nothing but the mere continuance of original meeting and it cannot be said that company has contravened Section 173(1).

Que. No. 52A] As the Company Secretary of Joy Ltd., what steps would you take in case the scheduled Board meeting could not complete the agenda slated thereat. The items of business left un-transacted are of extreme importance for the company's growth and the same cannot be deferred until the next Board meeting because of urgency. Advise the Board about the steps to be taken to get the un-transacted items passed.

CS (Executive) – Dec 2015 (4 Marks)

Ans.: If items of business left un-transacted in board meeting are extreme importance for the company, then as Company Secretary following actions can be taken:

- Meeting can be adjourned by the Chairman and such adjourned meeting can be held on next day or some other day to complete the items left un-transacted.
- Company can also pass the resolution by circulation for the items left un-transacted if passing by circular resolution on a subject is not specifically prohibited under the Companies Act, 2013.
- The company can also avail the option of holding of Board Meeting through video conferencing as provided u/s 173(2) of the Companies Act, 2013.

Que. No. 53] Explain the provisions relating to passing of resolution by circulation.

CS (Inter) – Dec 1999 (4 Marks), June 2003 (5 Marks)

CS (Inter) – Dec 2011 (5 Marks)

State the matters which cannot be decided through resolution by circulation.

CS (Executive) – Dec 2012 (4 Marks)

Ans.: Passing of resolution by circulation [Section 175]: Resolution shall be deemed to have been duly passed by the Board or by a committee by circulation if –

- The resolution has been circulated in draft, together with the necessary papers, if any
- The resolution should be circulated to all the directors, or members of the committee, as the case may be
- It shall be circulated at their addresses registered with the company in India by hand delivery or by post or by courier, or through electronic means
- Such circular resolution shall be approved by a majority of the directors or members, who are entitled to vote on the resolution.

Noting and inclusion in minutes: A resolution passed by circulation shall be noted at a subsequent meeting of the Board or the committee thereof, and made part of the minutes of meeting.

Demand for decision at board meeting: If not less than 1/3rd of the total number of directors of the company require that any resolution under circulation must be decided at a meeting, the chairperson shall put the resolution to be decided at a meeting of the Board.

Matters which cannot be decided by circular resolution:

- (a) To fill a casual vacancy occurred in the Board. [Section 161(4)]
- (b) Power to make calls on shareholders in respect of money unpaid on shares. [Section 179(3)]
- (c) To authorize buy-back of securities up to 10% of the total paid-up equity capital and free reserves [Section 68]
- (d) Power to issue debentures [Section 179(1)(c)]
- (e) Power to borrow moneys otherwise than on debentures. [Section 179(1)(d)]
- (f) Power to invest the funds of the company. [Section 179(1)(e)]

- (g) Power to make loans [Section 179(1)(f)]
- (h) Power to delegate to any committee of directors, managing director, manager or any other principal officer of the company or in the case of branch office of the company, a principal officer of the branch office, the powers specified in clauses (d) to (f) [Proviso to Section 179(3)]
- (i) Decision to make any political contribution [Section 182]
- (j) To give general notice of interest specifying firms or bodies corporate in which the director may be deemed to be concerned or interested. [Section 184(1)]
- (k) To accord consent to a contract in which a director or other specified persons are interested. [Section 188]
- (l) In the case of a public company or a private company, if it is a subsidiary of a public company, to appoint a person as a managing director, if he is already a managing director or manager of any other company, by an unanimous resolution. [Section 203]
- (m) In the case of a public company or a private company, if it is a subsidiary of a public company, to appoint a person as a manager, if he is already a manager or managing director of any other company, by an unanimous resolution. [Section 203]
- (n) To make a declaration of solvency where it is proposed to wind up the company voluntarily. [Section 305]

Que. No. 54] Write a short note on: Time and place of board meetings

CS (Inter) - Dec 2011 (5 Marks)

Ans.: As per Section 96(2), an annual general meeting can be called during business hours, that is, between 9 a.m. and 6 p.m. on any day that is not a National Holiday.

There is no similar provision for holding board meeting. Thus, the meetings of the board of directors may be held at *any place* convenient to the directors even outside the business hours and even on a national holiday unless the articles provide otherwise.

As per Section 173(4), where a meeting of the Board could not be held for want of quorum, then, unless the articles of the company otherwise provide, the meeting shall automatically stand adjourned to the *same day at the same time and place in the next week* or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place. Thus, it is evident that adjourned meeting cannot be held on national holiday. However in following two cases adjourned meeting can be held on national holiday:

- (1) Where board voluntarily adjourns a duly convened board meeting for a day which is a national holiday
- (2) If it is so provided in article of the company.

Que. No. 55] The Board of Directors of Infotech Consultant Ltd., registered in Kolkata, proposes to hold next board meeting in the month of December, 2014. They seek your advise in respect of the following matters:

- (1) Can the board meeting be held in Chennai, where all the directors of the company reside?
- (2) Whether the board meeting can be called on a national holiday and that too after business hours as the majority of directors have gone on vacation.
- (3) Is it necessary that the notice of the board meeting should specify the nature of business to be transacted?

CA (Final) - May 2000 (6 Marks)

Ans.: The answers to given problem is as follows:

- (1) The meetings of the board of directors may be held at *any place* convenient to the directors even outside the business hours and even on a national holiday unless the articles provide otherwise. Thus, board meeting can be held in Chennai.
- (2) The board meeting can be on a national holiday.
- (3) There is no provision under the Companies Act, 2013 which requires to specify the nature of business to be transacted. Therefore, the notices of board meeting need not to specify the nature of business to be transacted.

Que. No. 55A] Board of directors of Ash Ltd. having its registered office at New Delhi decides to hold its next meeting at New York, USA since all the directors of the company are going to attend a sales exhibition to be held at New York. Examining the provisions of the Companies Act, 2013, advise the Board about the validity of its decision to hold the Board meeting at New York.
CS (Executive) - June 2016 (4 Marks)

Ans.: As per Section 96(2), an annual general meeting can be called during business hours, that is, between 9 a.m. and 6 p.m. on any day that is not a National Holiday.

There is no similar provision for holding board meeting. Thus, the meetings of the board of directors may be held at *any place* even at abroad convenient to the directors; outside the business hours and even on a national holiday unless the articles provide otherwise.

Thus, board of directors of Ash Ltd. can held board meeting outside India.

Que. No. 56] Which companies are required to constitute a 'Nomination & Remuneration Committee'? What is the composition of the above committee?

CS (Executive) - June 2016 (4 Marks)

CA (Final) - May 2015 (4 Marks)

Ans.: Constitution of Nomination & Remuneration Committee [Section 178(1)]: The Board of Directors of every listed company and other prescribed classes of companies, shall constitute the Nomination & Remuneration Committee consisting of 3 or more non-executive directors out of which not less than one-half shall be independent directors.

The Chairperson of the company may be appointed as a member of the Nomination & Remuneration Committee but shall not Chair such Committee.

As per Rule 4 of the Companies (Meeting of Board & its Powers) Rules, 2014, following classes of companies shall constitute an 'Audit Committee' and Nomination and Remuneration Committee of the Board :

- (i) Public company having paid-up share capital of ₹ 10 Crore or more
- (ii) Public company having turnover of ₹ 100 Crore or more
- (iii) Public company which have in aggregate, outstanding loans, debentures and deposits exceeding ₹ 50 Crore.

Duties of Nomination & Remuneration Committee [Section 178(2) to (5)]: The Nomination & Remuneration Committee shall identify persons who are qualified to become directors and who may be appointed in senior management in accordance with the criteria laid down, recommend to the Board their appointment and removal and shall specify the manner for effective evaluation of performance of Board, its committee and individual director to be carried out either by Board, by the committee or by independent external agency and review its implementation and compliance.

The Nomination & Remuneration Committee shall formulate the criteria for determining qualifications, positive attributes and independence of a director and recommend to the Board a policy, relating to the remuneration for the directors, KMP and other employees.

The Nomination and Remuneration Committee shall, while formulating the policy ensure that –

- (a) The level and composition of remuneration is reasonable and sufficient to attract, retain and motivate directors of the quality required to run the company successfully;
- (b) Relationship of remuneration to performance is clear and meets appropriate performance benchmarks; and
- (c) Remuneration to directors, KMP and senior management involves a balance between fixed and incentive pay reflecting short and long-term performance objectives appropriate to the working of the company and its goals. Such policy shall be disclosed in the Board's report and website of company.

Constitution of Stakeholders Relationship Committee [Section 178(1)]: The Board of Directors of a company which consists of more than 1,000 shareholders, debenture-holders, deposit-holders and any other security holders at any time during a financial year shall constitute a Stakeholders Relationship Committee consisting of a chairperson who shall be a non-executive director and such other members as may be decided by the Board.

Duties of Stakeholders Relationship Committee [Section 178(6)]: The Stakeholders Relationship Committee shall consider and resolve the grievances of security holders of the company.

Attendance at general meetings [Section 178(7)]: The Chairperson of Nomination & Remuneration Committee and Stakeholders Relationship Committee, in his absence, any other member of the committee authorized by him in this behalf shall attend the general meetings of the company.

Que. No. 56A] Examining the provisions of the Companies Act, 2013, relating to the constitution of 'Nomination and Remuneration Committee' and 'Stakeholders Relationship Committee', answer the following:

- (i) Is it mandatory for a listed company to constitute such committees? Also state whether it is mandatory for a non-listed public company having paid-up share capital of ₹ 5 Crore to constitute such committees?
- (ii) What shall be the composition of the committees in case the company is required to constitute such committees?

CS (Executive) - Dec 2015 (4 Marks)

Ans.: Keeping in view above provisions of Section 178 of the Companies Act, 2013, answer to given problem is as follows:

- (i) It is mandatory for a listed company to constitute such committees. In case of a non-listed public company having paid-up share capital of ₹ 5 Crore it is not necessary to constitute such committees.
- (ii) Nomination & Remuneration Committee shall consist of 3 or more non-executive directors out of which not less than one-half shall be independent directors.

Stakeholders Relationship Committee shall consist of a chairperson who shall be a non-executive director and such other members as may be decided by the Board.

Que. No. 57] Discuss briefly the duties of directors under Section 166 of the Companies Act, 2013?

Ans.: Duties of directors [Section 166]:

- (1) A director of a company shall act in accordance with the articles of the company.
- (2) A director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment.

- (3) A director of a company shall exercise his duties with due and reasonable care, skill and diligence and shall exercise independent judgment.
- (4) A director of a company shall not involve in a situation in which he may have a direct or indirect interest that conflicts, or possibly may conflict, with the interest of the company.
- (5) A director of a company shall not achieve or attempt to achieve any undue gain or advantage either to himself or to his relatives, partners, or associates and if such director is found guilty of making any undue gain, he shall be liable to pay an amount equal to that gain to the company.
- (6) A director of a company shall not assign his office and any assignment so made shall be void.
- (7) If a director of the company contravenes the provisions of this section such director shall be punishable with fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 5,00,000.

Que. No. 58] Write a short note on: Agenda of Board Meeting

Ans.: The Companies Act, 2013 do not have any provision relating to agenda of board meeting. However, good governance envisages such requirement.

The SS-1 issued by ICSI requires circulating agenda, setting out the business to be transacted at the meeting and notes on agenda to directors at least 7 days before the date of meeting unless article provides longer period.

Que. No. 59] A whole-time director of a company made an invention during the course of his employment with the company. He patented the invention in his own name and appropriated the benefits to himself. Can he do so? Cite case law, if any.

CS (Executive) - June 2009 (5 Marks)

Ans.: The directors are liable to the company for all personal profits or gain made by them taking advantage of their position as directors.

A director was held liable when a director patented and exploited in his own name an invention made during the course of his employment with the company. [*Cranleigh Precision Engineering Ltd. vs. Bryan* (1964) All ER 289].

Que. No. 60] Whether secretarial standard relating to general and board meeting is required to be complied by the companies under the Companies Act, 2013.

Ans.: Compliance with Secretarial Standard relating to general and board meeting [Section 118(10)]: Every company shall observe secretarial standards with respect to general and Board meetings specified by the Institute of Company Secretaries of India constituted under section 3 of the Company Secretaries Act, 1980, and approved as such by the Central Government.

In the context of this provision, observance of Secretarial Standard issued by the ICSI assumes special relevance and companies will have to ensure that there is compliance with these standards on their part. The ICSI has already issued the Secretarial Standard relating to Board and General Meeting.

Note: SS-1 & SS-2 are given at the end of the book.

CHAPTER 17

APPOINTMENT & REMUNERATION OF KEY MANAGERIAL PERSONNEL

This Chapter Covers:

- Key managerial personnel
- Appointment of key managerial personnel
- Appointment with the approval of Central Government
- Disqualifications of Managing Director, Whole time director & Manager
- Remuneration of Managing Director, Whole time director & Manager
- Remuneration of non-executive directors

KEY MANAGERIAL PERSONNEL

Que. No. 1] Explain the meaning of the term 'Key Managerial Personnel' in relation to company as introduced by the Companies Act, 2013.

CS (Executive) - June 2015, Dec 2015 (2 Marks)

Ans.: Key Managerial Personnel [Section 2(51)]: Key managerial personnel means -

- (i) The Chief Executive Officer or the Managing Director or the Manager
- (ii) The Company Secretary
- (iii) The whole-time director
- (iv) The Chief Financial Officer
- (v) Such other officer, not more than one level below the directors who is in whole-time employment, designated as key managerial personnel by the Board
- (vi) Other prescribed officers.

Que. No. 2] Define the following terms as defined in Companies Act, 2013.

- (1) Manager
- (2) Managing Director
- (3) Whole-time director
- (4) Chief Executive Officer
- (5) Chief Financial Officer

Ans.:

(1) **Manager** [Section 2(53)]: Manager means an individual who, subject to the superintendence, control and direction of the Board of Directors, has the management of the whole, or substantially the whole, of the affairs of a company, and includes a director or any other person occupying the position of a manager, by whatever name called, whether under a contract of service or not.

(2) **Managing Director** [Section 2(54)]: Managing director means a director who, by virtue of the articles of a company or an agreement with the company or a resolution passed in its general meeting, or by its Board of Directors, is entrusted with substantial powers of management of the affairs of the company and includes a director occupying the position of managing director, by whatever name called.

Explanation: The power to do administrative acts of a routine nature when so authorized by the Board such as the power to affix the common seal of the company to any document or to draw and endorse any cheque on the account of the company in any bank or to draw and endorse any negotiable instrument or to sign any certificate of share or to direct registration of transfer of any share, shall not be deemed to be included within the substantial powers of management

(3) **Whole-time director** [Section 2(94)]: Whole-time director includes a director in the whole-time employment of the company.

(4) **Chief Executive Officer** [Section 2(18)]: Chief Executive Officer means an officer of a company, who has been designated as such by it.

(5) **Chief Financial Officer** [Section 2(19)]: Chief Financial Officer means a person appointed as the Chief Financial Officer of a company.

A company, instead of appointing MD or WTD, can appoint CEO or Manager. The distinction is that MD or WTD should be on board of directors, while the CEO or Manager need not be director on the board.

Que. No. 3] Distinguish between: Managing Director and Whole Time Director

CS (Inter) - Dec 2007 (4 Marks)

CS (Executive) - June 2013 (4 Marks)

Ans.: Following are the main points of distinction between managing director & whole time director:

| Points | Managing Director | Whole Time Director |
|--------------------------|--|---|
| Meaning | According to Section 2(54), Managing Director means a director who is entrusted with substantial powers of management. | According to Section 2(94), Whole-time director includes a director in the whole-time employment of the company |
| No. of companies | A person can be managing director in one, and of not more than one, other company. [Section 202(3)] | A person cannot be whole time director in more than one company. |
| Appointment with Manager | A managing director and manager cannot be appointed simultaneously. | A whole time director and manager can be appointed simultaneously. |

Que. No. 3A] Distinguish between: Whole time chairman and Part time chairman

CS (Executive) – June 2010 (4 Marks)

Ans.: In India, we have Boards, which are chaired by managing directors, who are known as chairman-cum-managing director (CMD). We have also Boards, which are chaired by directors, who are not whole-time directors. A chairman-cum-managing director (CMD) is sometimes called a whole-time chairman whereas a director, who is not a whole-time director of the company, is called a part-time chairman. Even if a managing director is chairman-cum-managing director of the company, he acts as chairman of the meetings of the Board of directors only when they are held. During the intervals, he occupies the chair of the managing director. Strictly speaking therefore, a chairman is never a whole-time chairman. He is always a part-time chairman. The term whole-time chairman thus seems to be a misnomer.

Que. No. 4] Whether a person initially appointed as additional director could continue as managing/whole-time director?

CS (Inter) – Dec 2000 (8 Marks)

Ans.: The terms "director" and "managing director" are defined in the Act. On the face of it, a managing director has first to be a director. So long as he is a director and is also appointed as managing director, he continues as managing director.

An additional director can be appointed by the board of directors of a company u/s 161(1). Such a person continues to be the additional director till the next AGM. As soon as the AGM is held, he ceases to be the additional director. If such a person while he was the additional director of a company had been appointed as managing director ceases to be a director, he also ceases to be the managing director, the latter appointment also ceases simultaneously with his ceasing of directorship at the commencement of the AGM. However, if such a person is re-elected as a full-fledged director at the AGM and thereby he continues as a director of the company, he shall continue as a managing director also for the period for which he is so elected by the AGM.

Que. No. 5] Can company appoint at the same time a Managing Director and a Manager?

Ans.: As per Section 196(1), a company shall not appoint or employ at the same time a Managing Director and a Manager.

Que. No. 6] For what period a company can appoint the Managing Director and the Manager?

Ans.: As per Section 196(2), a company shall not appoint or re-appoint any person as its Managing Director, Whole-time Director or Manager for a term not exceeding 5 years at a time.

Reappointment: Re-appointment of the Managing Director, Whole-time Director and a Manager shall not be made earlier than 1 year before the expiry of his term.

Que. No. 6A] The Managing Director of a company filed a suit on behalf of the company against the tenants and the trial court granted decree directing the tenants to vacate and deliver possession of the tenanted premises. The tenants filed an application and contended that in the instant case, the managing director, who had filed suit, had no proper authorization from the board of directors. Discuss with reference to decided case whether contention of tenant is correct?

Ans.: The facts of the given case are similar to *Wasava Tyres vs. Printers (Mysore) Ltd.* (2008) 86 SCL 171 (Kar). In this case the managing director of a company filed a suit on behalf of the company against the tenants and the trial court granted decree directing the tenants to vacate and deliver possession of the tenanted premises. The court also directed payment of damages

and, in default, to pay interest. The tenants filed an application and contended that in the instant case, the managing director, who had filed suit, had no proper authorization from the board of directors. The Court dismissed the application of the tenants and held that the words 'substantial powers of management' specifically excludes certain acts from its purview.

Therefore, except the excluded acts, the managing director has power and privilege of conducting the business of the company in accordance with the memorandum and articles of association of the company. The institution of the suit on behalf of the company by the managing director is deemed to be within the meaning of 'substantial powers of management', since such a power is necessary and incidental to manage the day-to-day affairs and business of the company. Therefore, the suit instituted by the managing director is deemed to be within his power and authority. The suit was obviously filed for the benefit of the company. In that view of the matter, the contention that the managing director had no authority to file a suit is untenable.

Que. No. 7] Write a short note on: Disqualification of Managing Director, Whole-time Director & Manager

Ans.: **Disqualification of Managing Director and Manager [Section 196(3)]:** A company shall not appoint or continue the employment of following person as Managing Director, Whole-time Director or Manager –

- A person who is below the age of 21 years or has attained the age of 75 years. However, the appointment of a person who has attained the age of 70 years may be made by passing a *special resolution* in which case the explanatory statement annexed to the notice for such motion shall indicate the justification for appointing such person.
- A person who is an un-discharged insolvent or has at any time been adjudged as an insolvent.
- A person who has at any time suspended payment to his creditors or makes, or has at any time made a composition with them.
- A person who has at any time been convicted by a Court of an offence and sentenced for a period of more than 6 months.

Que. No. 8] State the provisions of Section 197 of the Companies Act, 2013 relating to "Overall maximum managerial remuneration and managerial remuneration in case of absence or inadequacy of profits".

Write short notes on: Remuneration to directors CS (Inter) – Dec 2000 (5 Marks)

CS (Executive) – June 2009 (4 Marks)

Ans.: Section 197 is amended by the Companies (Amendment) Act, 2017 and the requirement as to previous approval of Central Government for payment of managerial remuneration has been done away. Thus, companies can pay remuneration to managerial personnel as per limit laid down in section and in case above limit, remuneration is payable by complying with the conditions laid down in this Section and Schedule V. For paying excess remuneration henceforth no prior approval of Central Government is necessary.

Overall maximum managerial remuneration [Section 197(1)]: Total managerial remuneration payable by a public company, to its directors in respect of any financial year shall not exceed 11% of the net profits. Net profit for this purpose will be calculated as per Section 198.

However, the company in general meeting may authorize the payment of remuneration exceeding 11% of the net profits, subject to the provisions of Schedule V.

Limit of 11% of net profit for remuneration is applicable for public companies only. Thus, private company and OPC can pay any remuneration without any limit.

Maximum remuneration to managing director or whole-time director or manager: Except with the approval of the company in general meeting by a special resolution the remuneration payable to any one managing director; or whole-time director or manager shall not exceed 5% of the net profits and if there is more than one such director remuneration shall not exceed 10% of the net profits to all such directors and manager taken together.

However, where any term loan of any bank or public financial institution is subsisting or the company has defaulted in payment of dues to non-convertible debenture holders or any other secured creditor, the prior approval of the bank or public financial institution concerned or the non-convertible debenture holders or other secured creditor, as the case may be, shall be obtained by the company before obtaining the approval in the general meeting.

Maximum remuneration to part-time director (non-executive director): Except with the approval of the company in general meeting the remuneration payable to part-time director (non-executive director) shall not exceed -

- (a) 1% of the net profits, if there is a managing or whole-time director or manager
- (b) 3% of the net profits in any other case.

Summary of different limits based on net profits of the company is given below:

| Managerial personnel | % of net profits |
|--|------------------|
| Overall (excluding fees for attending meetings) | 11% |
| If there is one managerial personnel | 5% |
| If there are more than one managerial personnel | 10% |
| Remuneration to part-time directors: | |
| (a) If there is no managing director, whole-time director or manager | 3% |
| (b) If there is a managing director or whole-time director | 1% |

Sitting fee not to be included in remuneration [Section 197(2)]: The percentages aforesaid shall be exclusive of any sitting fees payable to directors for attending the board meetings.

Remuneration in case the company has no profits or its profits are inadequate [Section 197(3)]: If in any financial year, a company has no profits or its profits are inadequate, the company can pay remuneration to managing or whole-time director or manager in accordance with the provisions of Schedule V only.

Remuneration for other services not to be included in remuneration of directors [Section 197(4)]: The remuneration payable to the directors of a company in any other capacity shall also be included in 'remuneration payable to directors' under the provisions of Section 197(1).

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

- (a) The services rendered are of a professional nature
- (b) If company is required to form the Nomination & Remuneration Committee, then such committee is of the opinion that the director possesses the requisite qualification for the practice of the profession for which additional remuneration is payable.

Judicial View:

Guarantee Commission received by the director is for personal liability which the director undertakes. Therefore, guarantee commission is not remuneration within the meaning of Section 309. [Suessen Textile Bearings Ltd. v. Union of India, [1984] 55 Comp. Cas. 492 (Delhi)]

Mode of payment of remuneration [Section 197(6)]: A director or manager may be paid remuneration either by way of a monthly payment or at a specified percentage of the net profits of the company or partly by one way and partly by the other.

Remuneration to an independent director [Section 197(7)]: An independent director may receive remuneration by way of -

- (a) Sitting fees
- (b) Reimbursement of expenses for participation in the board and other meetings
- (c) Profit related commission approved by the members.

However, an independent director shall not be entitled to any stock option.

Computation of net profit for the purpose of managerial remuneration [Section 197(8)]: The net profits for the purposes of managerial remuneration shall be computed as per Section 198.

Refund of excess remuneration [Section 197(9)]: If any director draws or receives, directly or indirectly, by way of remuneration any such sums in excess of the limit prescribed by this section or without approval required under this section, he shall refund such sums to the company, within 2 years of such lesser period as may be allowed by the company, and until such sum is refunded, hold it in trust for the company.

Company cannot waive the excess remuneration paid to managerial person [Section 197(10)]: The company shall not waive the recovery of any sum refundable by managerial person to unless approved by the company by special resolution within 2 years from the date the sum becomes refundable.

However, where any term loan of any bank or public financial institution is subsisting or the company has defaulted in payment of dues to non-convertible debenture holders or any other secured creditor, the prior approval of the bank or public financial institution concerned or the non-convertible debenture holders or other secured creditor, as the case may be, shall be obtained by the company before obtaining approval of such waiver

Increase in remuneration to be in accordance with Schedule V: If company pays remuneration to managerial personnel as per Schedule V due to no profits or inadequate profits, then subsequent increase in remuneration should also comply provisions of Schedule V and such remuneration should be within the limits laid down by the Schedule V.

Disclosure in board's report [Section 197(12)]: Every listed company shall disclose in the Board's report, the ratio of the remuneration of each director to the median employee's remuneration and such other details as may be prescribed.

Insurance premium not to be part of managerial remuneration [Section 197(13)]: A company may take insurance on behalf of its MD, WTD, Manager, CEO, CFO or CS for indemnifying any of them against any liability in respect of any negligence, default, misfeasance, breach of duty or breach of trust for which they may be guilty. The premium paid on such insurance shall not be treated as part of the managerial remuneration.

However, if such person is proved to be guilty, the premium paid on insurance shall be treated as part of the remuneration.

Receipt of remuneration from holding or subsidiary company [Section 197(14)]: A Managing Director or Whole-time director of the company can receive any remuneration or commission from any holding company or subsidiary company. However, company should make disclosure of such remuneration or commission in Board's Report.

Penalty [Section 197(15)]: If any person contravenes the provisions of Section 197, he shall be punishable with fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 5,00,000.

Reporting by Auditor [Section 197(16)]: The auditor of the company shall make a statement in his report as to whether the remuneration paid by the company to its directors is in accordance with the provisions of this section, whether remuneration paid to any director is in excess of the limit laid down under this section and give such other details as may be prescribed.

"Net Profit" for the purpose of managerial remuneration has to be calculated as per Section 198 of the Companies Act, 2013. Section 198 is discussed in details in subject "Company Accounts & Auditing Practices", Chapter No. 8 - Company Final Accounts.

Que. No. 8A] In the context of managerial remuneration, explain what does the expression 'inadequate profits' mean.
CS (Inter) - Dec 2006 (4 Marks)

Ans.: As per Companies Act, 2013 remuneration payable to any one managing director or whole-time director or manager shall not exceed 5% of the net profits and if there is more than one such director remuneration shall not exceed 10% of the net profits to all such directors and manager taken together. In case remuneration to be given to director is greater than 5% of the net profits then it is said that profit is inadequate.

Example:

Remuneration as per agreement with MD = ₹ 2,00,000 p.m. i.e. ₹ 24,00,000 annually.

Profit as per Section 198 of the Companies Act, 2013 = ₹ 4,50,00,000.

Maximum remuneration payable to MD as per Section 197(1) = $4,50,00,000 \times 5\% = ₹ 22,50,000$.

As maximum remuneration payable to MD as per Section 197(1) is less than remuneration payable to him as per agreement, profit is said to be inadequate.

Remuneration in case the company has no profits or its profits are inadequate [Section 197(3)]: If in any financial year, a company has no profits or its profits are inadequate, the company can pay remuneration to managing or whole-time director or manager in accordance with the provisions of Schedule V..

Que. No. 9] Prudent Ltd. is paying remuneration to its non-executive directors in the form of commission at the rate of 1% of the net profits of the company distributed equally among all the non-executive directors. The company is providing depreciation as per Schedule II to the Companies Act, 2013. The company seeks your advice in respect of following:

- Whether is it necessary to make adjustment in respect of depreciation for the purpose of arriving at the net profit of the company to determine the quantum of remuneration payable to its non-executive directors?
- Is it possible to pay remuneration to non-executive director besides sitting fees in the event of loss in a financial year?

CS (Inter) - Dec 2004 (5 Marks)

Ans.: Keeping in view the provisions of the Companies Act, 2013 answers to given problem is as follows:

- "Net Profit" for the purpose of managerial remuneration has to be calculated as per Section 198 of the Companies Act, 2013. As per said Section 198, depreciation is required to be deducted for calculation of net profit for the purpose of managerial remuneration.

Thus, it is necessary for the Prudent Ltd. to make adjustment in respect of depreciation for the purpose of arriving at the net profit of the company to determine the quantum of remuneration payable to its non-executive directors

- As per Section 197(1), except with the approval of the company in general meeting the remuneration payable to part-time director (non-executive director) shall not exceed -
 - 1% of the net profits, if there is a managing or whole-time director or manager
 - 3% of the net profits in any other case.

Thus, in the event of loss, remuneration to non-executive directors can be paid only after obtaining approval of shareholder in general meeting.

Que. No. 10] A Managing Director of a company stood as surety for the repayment of loan taken by it for which he was paid guarantee commission. Does this commission amount to managerial remuneration? Support your answer with decided case law, if any.

CS (Inter) - June 2009 (5 Marks)

Ans.: Guarantee commission received by the director is for personal liability which the director undertakes. Therefore, guarantee commission is not remuneration within the meaning of Section 197 of the Companies Act, 2013. [*Suessen Textile Bearings Ltd. v. Union of India* [1984] 55 Comp. Cas. 492 (Delhi)]

Que. No. 11] What are the provisions relating to payment of sitting fee to the director for attending board meetings?
CS (Inter) - Dec 2000 (4 Marks)

Ans.: **Sitting Fees [Section 197(5)]:** A director may receive remuneration by way of fee for attending meetings of the Board or Committee or for any other purpose whatsoever as may be decided by the Board. However, the amount of such fees shall not exceed the amount as may be prescribed.

Rule 4 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014 makes following provisions in relation to payment of sitting fees:

- A company may pay a sitting fee to a director for attending meetings of the Board or committees thereof.
- Amount of sitting fee shall be such sum as may be decided by the Board of directors.
- Amount of sitting fee shall not exceed ₹ 1,00,000 per meeting.
- Amount of sitting fee payable to Independent Directors and Women Directors shall not be less than the sitting fee payable to other directors.

Important Points:

- The Companies Act, 1956 did not make any provision for any sitting fees for attending general meeting. Now Companies Act, 2013 makes specific provision for payment of sitting fees for attending meeting for any other purpose.
- Sitting fees can be paid to directors even if company is making losses.
- A managing director or manager is not entitled to sitting fees. If sitting fee is paid to them it is subject limit of managerial remuneration as per Section 197 read with Schedule V.
- Where the articles contain a provision identical with Article 61(ii) of Table F, the directors may be paid travelling, hotel or other expenses incurred by them in attending meetings of the board or any committee thereof or general meetings of the company or in connection with the business of the company.
- Whether a director attending the Board meetings of two or three companies on the same day and in the same building was entitled to draw travelling allowance from one of them only or from all the companies provided amount does not exceed the expenses actually incurred.

Que. No. 12] Abhay is director in two companies - Goodluck India Ltd. and Lucky Winners India Ltd. Abhay attended Board meetings of these two companies on 22nd August, 2015 in the same building 'Welcome House' at 2 p.m. and 4 p.m. respectively.

- Can Abhay draw travelling allowance from both the companies?
- Is he entitled to receive sitting fees fully from both the companies?

CS (Executive) - June 2010 (6 Marks)

Ans.: As per Section 197(5), a director may receive remuneration by way of fee for attending meetings of the Board or Committee or for any other purpose whatsoever as may be decided by the Board.

Where the article contain a provision identical with Article 61(ii) of Table F, the directors may be paid travelling, hotel or other expenses incurred by them in attending meetings of the board or any committee thereof or general meetings of the company or in connection with the business of the company.

In view of above:

- Abhay can draw travelling allowance from one of the company only or from both the companies provided amount does not exceed the expenses actually incurred.
- Abhay is entitled to sitting fee fully from both the companies.

Que. No. 13] An article of association of a company has put a cap of ₹ 30,000 on sitting fee. There is a proposal to increase the sitting fee from present amount of ₹ 30,000 to ₹ 75,000. Advise the company.

CS (Inter) - June 2005 (5 Marks)

Ans.: As per Section 197(5), a director may receive remuneration by way of fee for attending meetings of the Board or Committee or for any other purpose whatsoever as may be decided by the Board.

Companies will have discretion to pay such amount by way of sitting fee as may be considered appropriate within ceiling of Rule 4 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014.

As per Rule 4, amount of sitting fee shall not exceed ₹ 1,00,000 per meeting.

In given case since the article of the company has put a cap of ₹ 30,000, so article will be required to be altered by passing special resolution.

Que. No. 14] Richie, the Managing Director of Prosperous Ltd. wants to get sitting fees for attending board meeting over and above his salary. Is this legally permissible?

CS (Inter) - Dec 2001 (3 Marks)

Ans.: A managing director is expected to devote his whole time to the affairs of the company. Attending the board meeting is part of his duties. As such question of payment of sitting fees to a managing director would not arise. But, if company chooses to pay him sitting fees it can do so provided the remuneration and sitting fees together do not exceed 5% of net profit.

Que. No. 15] Suresh, a solicitor, is appointed as director on the Board of Sam Organic Ltd. The company has obtained legal opinion from Suresh and paid a fee of ₹ 5 lakh during the financial year 2014 - 2015. Auditor has raised an objection that fee payable to Suresh exceeds the limit prescribed and hence payment made to him is illegal. Therefore, the company should take steps to recover the same from Suresh. Keeping in view the provisions of the Companies Act, 2013, give your opinion on the objection raised by the auditor.

CS (Inter) - June 2006 (5 Marks)

Ans.: As per Section 197(4), the remuneration payable to the directors of a company any other capacity shall also be included in 'remuneration payable to directors' under the provisions of Section 197(1).

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

- (a) The services rendered are of a professional nature

- (b) If company is required to form the Nomination & Remuneration Committee, then such committee is of the opinion that the director possesses the requisite qualification for the practice of the profession for which additional remuneration is payable.

In view of above, objection raised by auditor that fee payable to Suresh exceeds the prescribed limit and hence payment made to him is illegal is incorrect. Therefore, the company should not take steps to recover the same from Suresh.

Que. No. 16] Heal Ltd. owns a chain of hospitals in Mumbai. Dr. Aman, a practicing surgeon, has been appointed by the company as its non-executive ordinary director and wants to pay him fees on case-to-case basis for surgeries performed by him on patients at hospital. Advise the company, whether payment of such fees to him would amount to payment of managerial remuneration to a director under the Companies Act, 2013.

CS (Executive) - Dec 2014 (4 Marks)

Ans.: As per Section 197(4), the remuneration payable to the directors of a company any other capacity shall also be included in 'remuneration payable to directors' under the provisions of Section 197(1).

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

- (a) The services rendered are of a professional nature
- (b) If company is required to form the Nomination & Remuneration Committee, then such committee is of the opinion that the director possesses the requisite qualification for the practice of the profession for which additional remuneration is payable.

In view of above if, Heal Ltd. can pay fees to Dr. Aman for his professional service for surgeries performed by him on patients at hospital if Nomination & Remuneration Committee is of the opinion that the director possesses the requisite qualification for the practice of the profession for which additional remuneration is payable.

Que. No. 16A] It has been found that Mrs. Shweta, director of a company, has drawn remuneration in excess of the prescribed limits. The Chief Financial Officer of the company has sought your advice in the matter.

CS (Executive) - Dec 2016 (4 Marks)

Ans.: Refund of excess remuneration [Section 197(9)]: If any director draws or receives, directly or indirectly, by way of remuneration in excess of the limit prescribed or without the prior sanction of the Central Government, he shall refund such sums to the company and until such sum is refunded, hold it in trust for the company.

Company cannot waive the excess remuneration paid to managerial person [Section 197(10)]: The company shall not waive the recovery of any sum refundable by managerial person to unless permitted by the Central Government.

Penalty [Section 197(15)]: If any person contravenes the provisions of section 197, he shall be punishable with fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 5,00,000.

Thus, Mrs. Shweta cannot keep the excess remuneration. She shall refund such excess remuneration to company. Until such refund is made, she shall hold it in trust for the company. Further, company cannot waive the recovery of excess remuneration unless the Central Government permits the waiver of recovery of excess remuneration.

Que. No. 17] State the provisions of the Part I of the Schedule V of the Companies Act, 2013 relating to appointment of the Managing Director, Whole-time Director or Manager.

CS (Executive) - June 2011 (4 Marks), June 2012 (5 Marks)

Ans.: Appointment of the Managing Director, Whole-time Director or Manager [Section 196 (4)]: Subject to the provisions of Section 197 and Schedule V, Managing Director, Whole-time Director or Manager shall be appointed and the terms and conditions of such appointment and remuneration payable be approved at board meeting. Such appointment shall be subject to approval by a resolution at the next general meeting of the company.

Such appointment also requires prior approval of the Central Government in case appointment is at variance to the conditions specified in that Schedule V.

Notice of meeting to contain certain disclosure: A notice convening Board or general meeting for considering appointment of the Managing Director, Whole-time Director or Manager shall include the terms and conditions of such appointment, remuneration payable and such other matters including interest, of a director or directors in such appointments, if any.

Filling of Return with ROC: A return in Form No. MR - 1 shall be filed within 60 days of such appointment with the Registrar. [Rule 3 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014]

Validity of acts where appointment is not approved at general meeting: Where an appointment of a managing director, whole-time director or manager is not approved by the company at a general meeting, any act done by him before such approval shall not be deemed to be invalid.

Que. No. 18] State the various eligibility criteria prescribed under the Schedule V of the Companies Act, 2013 for the appointment of Managing Director, Whole-time Director or Manager?

Ans.: Conditions to be fulfilled for the appointment of a managing or whole-time director or a manager without the approval of the Central Government appointments [Part I of the Schedule V]: A person shall be eligible for appointment as a managing or whole-time director or a manager (hereinafter referred to as 'managerial person') of a company only if satisfies the following conditions, namely:

(a) He had not been sentenced to imprisonment for any period, or to a fine exceeding ₹ 1,000, for the conviction of an offence under any of the following Acts, namely -

- The Indian Stamp Act, 1899
- The Central Excise Act, 1944
- The Industries (Development & Regulation) Act, 1951
- The Prevention of Food Adulteration Act, 1954
- The Essential Commodities Act, 1955
- The Companies Act, 2013
- The Securities Contracts (Regulation) Act, 1956
- The Wealth-tax Act, 1957
- The Income-tax Act, 1961
- The Customs Act, 1962
- The Competition Act, 2002
- The Foreign Exchange Management Act, 1999
- The Sick Industrial Companies (Special Provisions) Act, 1985
- The Securities and Exchange Board of India Act, 1992
- The Foreign Trade (Development and Regulation) Act, 1922
- The Prevention of Money-Laundering Act, 2002 (15 of 2003);

(b) He had not been detained for *any period* under the Conservation of Foreign Exchange & Prevention of Smuggling Activities Act, 1974.

However, where the Central Government has given its approval to the appointment of a person convicted or detained under clauses (a) & (b) no further approval of the Central Government shall be necessary for the subsequent appointment of that person if he had not been so convicted or detained subsequent to such approval.

(c) He has completed the age of 21 years and has not attained the age of 70 years.

However, where he has attained the age of 70 years and where his appointment is approved by a special resolution passed by the company in general meeting, no further approval of the Central Government shall be necessary for such appointment.

(d) Where he is a managerial person in more than one company, he draws remuneration from one or more companies subject to the ceiling provided in Section V of Part II of Schedule V.

(e) He is resident of India.

Explanation I: Resident in India includes a person who has been staying in India for a continuous period of not less than 12 months immediately preceding the date of his appointment as a managerial person and who has come to stay in India, -

- (i) for taking up employment in India or
- (ii) for carrying on a business or vacation in India.

Explanation II: This condition shall not apply to the companies in SEZ as notified by Department of Commerce from time to time. Provided that a person, being a non-resident in India shall enter India only after obtaining a proper Employment Visa from the concerned Indian mission abroad. For this purpose, such person shall be required to furnish, along with the visa application form, profile of the company, the principal employer and terms and conditions of such person's appointment.

Que. No. 19] State the provisions of the Part II of the Schedule V of the Companies Act, 2013 relating to remuneration payable to the Managing Director, Whole-time Director or Manager.

Ans.: Remuneration of managerial personnel [Part II of the Schedule V]:

Section I - Remuneration payable by companies having profits: A company having profits in a financial year may pay remuneration to a managerial person or persons not exceeding the limits specified in Section 197.

Section II - Remuneration payable by companies having no profit or inadequate profit without Central Government approval: Where in any financial year during the currency of tenure of a managerial person, a company has no profits or its profits are inadequate, it may, without Central Government approval, pay remuneration to the managerial person not exceeding the higher of the limits under (A) and (B) given below:

(A) Remuneration based on effective capital:

| Where the effective capital is | Limit of yearly remuneration payable shall not exceed (₹) |
|---|---|
| Negative or less than 5 Crores | 60 Lakhs |
| 5 crores and above but less than 100 Crores | 84 Lakhs |
| 100 crores and above but less than 250 Crores | 120 Lakhs |
| 250 crores and above | 120 lakhs plus 0.01% of the effective capital in excess of ₹ 250 crores |

The above limits shall be doubled if the resolution passed by the shareholders is a special resolution.

If a period less than one year, the limits shall be pro-rated.

Explanation I: "Effective Capital" means the aggregate of the paid-up share capital (excluding share application money or advances against shares); amount, if any, for the time being standing to the credit of share premium account; reserves and surplus (excluding revaluation reserve); long-term loans and deposits repayable after one year (excluding working capital loans, overdrafts, interest due on loans unless funded, bank guarantee, etc., and other short-term arrangements) as reduced by the aggregate of any investments (except in case of investment by an investment company whose principal business is acquisition of shares, stock, debentures or other securities), accumulated losses and preliminary expenses not written off.

Explanation II:

- (a) Where the appointment of the managerial person is made in the year in which company has been incorporated, the effective capital shall be calculated as on the date of such appointment;
- (b) In any other case the effective capital shall be calculated as on the last date of the financial year preceding the financial year in which the appointment of the managerial person is made.

Explanation III: "Negative Effective Capital" means the effective capital which is calculated in accordance with the provisions contained in Explanation I of this Part is less than zero.

- (B) In case of a managerial person who is functioning in a professional capacity, no approval of Central Government is required, if such managerial person is not having any interest in the capital of the company or its holding company or any of its subsidiaries directly or indirectly or through any other statutory structures and not having any, direct or indirect interest or related to the directors or promoters of the company or its holding company or any of its subsidiaries at any time during the last two years before or on or after the date of appointment and possesses graduate level qualification with expertise and specialized knowledge in the field in which the company operates.

However, any employee of a company holding shares of the company not exceeding 0.5% of its paid up share capital under any scheme formulated for allotment of shares to such employees including Employees Stock Option Plan or by way of qualification shall be deemed to be a person not having any interest in the capital of the company.

Other conditions to be complied by company to pay remuneration as per Section II of the Part II of the Schedule V:

- (i) Payment of remuneration is approved by a resolution passed by the Board and Nomination & Remuneration Committee where the company is required to constitute such committee.
- (ii) The company has not made any default in repayment of any of its debts (including public deposits) or debentures or interest payable thereon for a continuous period of 30 days in the preceding financial year before the date of appointment of such managerial person.
- (iii) A special resolution has been passed at the general meeting of the company for payment of remuneration for a period not exceeding 3 years.
- (iv) A statement along with a notice calling the general meeting is given to the shareholders containing the following information, namely:

I. *General Information:*

- Nature of industry
- Date or expected date of commencement of commercial production
- In case of new companies, expected date of commencement of activities as per project approved by financial institutions appearing in the prospectus

- Financial performance based on given indicators
- Foreign investments or collaborations, if any.

II. *Information about the appointee:*

- Background details
- Past remuneration
- Recognition or awards
- Job profile and his suitability
- Remuneration proposed
- Comparative remuneration profile with respect to industry, size of the company, profile of the position and person (in case of expatriates the relevant details would be with respect to the country of his origin)
- Pecuniary relationship directly or indirectly with the company, or relationship with the managerial personnel, if any.

III. *Other information:*

- Reasons of loss or inadequate profits
- Steps taken or proposed to be taken for improvement
- Expected increase in productivity and profits in measurable terms.

IV. *Disclosures:* The following disclosures shall be mentioned in the Board of Director's report under the heading "Corporate Governance", if any, attached to the financial statement:—

- (i) all elements of remuneration package such as salary, benefits, bonuses, stock options, pension, etc., of all the directors;
- (ii) details of fixed component and performance linked incentives along with the performance criteria;
- (iii) service contracts, notice period, severance fees;
- (iv) stock option details, if any, and whether the same has been issued at a discount as well as the period over which accrued and over which exercisable.

Explanation: The Nomination and Remuneration Committee while approving the remuneration under Section II or Section III, shall —

- (a) take into account, financial position of the company, trend in the industry, appointee's qualification, experience, past performance, past remuneration, etc.;
- (b) be in a position to bring about objectivity in determining the remuneration package while striking a balance between the interest of the company and the shareholders.

Section III: Remuneration payable by companies having no profit or inadequate profit without Central Government approval in certain special circumstances:

In the following circumstances a company may, without the Central Government approval, pay remuneration to a managerial person in excess of the amounts provided in Section II above:

- (a) Where the remuneration in excess of the limits specified in Section I or II is paid by any other company [usually holding or parent company]

That other company is either a foreign company or has got the approval of its shareholders in general meeting to make such payment

Such other company treats this amount as managerial remuneration for the purpose of Section 197 of that company

The total managerial remuneration payable by such other company to its managerial persons including such amount or amounts is within permissible limits under Section 197.

(b) Where the company –

- (i) is a newly incorporated company, for a period of 7 years from the date of its incorporation, or
- (ii) is a sick company, for whom a scheme of revival or rehabilitation has been ordered by the BIFR or NCLT, for a period of 5 years from the date of sanction of scheme of revival, it may pay remuneration up to two times the amount permissible under Section II.
- (iii) is a company in relation to which a resolution plan has been approved by the National Company Law Tribunal under the Insolvency and Bankruptcy Code, 2016 for a period of five years from the date of such approval, it may pay remuneration up to two times the amount permissible under Section II.

(c) Where remuneration of a managerial person exceeds the limits in Section II but the remuneration has been fixed by the BIFR or the NCLT.

The limits under Section III shall be applicable subject to meeting all the conditions specified under Section II and the following additional conditions:

- (i) Except as provided in para (a) of Section III, the managerial person is not receiving remuneration from any other company;
- (ii) The auditor or CS of the company or where the company has not appointed CA, PCS certifies that all secured creditors and term lenders have stated in writing that they have no objection for the appointment of the managerial person as well as the quantum of remuneration and such certificate is filed along with the return as prescribed under Section 196(4).
- (iii) The auditor or CS or where the company has not appointed a secretary, a PCS certifies that there is no default on payments to any creditors, and all dues to deposit holders are being settled on time.

(d) A company in a SEZ as notified by Department of Commerce from time to time which has not raised any money by public issue of shares or debentures in India, and has not made any default in India in repayment of any of its debts (including public deposits) or debentures or interest payable thereon for a continuous period of thirty days in any financial year, may pay remuneration up to ₹ 2,40,00,000 p.a.

Section IV: Perquisites not included in managerial remuneration:

1. A managerial person shall be eligible for the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in Section II and Section III:
 - (a) Contribution to provident fund, superannuation fund or annuity fund to the extent these either singly or put together are not taxable under the Income Tax Act, 1961
 - (b) Gratuity payable at a rate not exceeding half a month's salary for each completed year of service; and
 - (c) Encashment of leave at the end of the tenure.
2. In addition to the perquisites specified in paragraph 1 of this section, an expatriate managerial person (including a non-resident Indian) shall be eligible to the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in Section II or Section III
3. (a) **Children's Education Allowance:** In case of children studying in or outside India, an allowance limited to a maximum of ₹ 12,000 p.m. per child or actual expenses incurred, whichever is less. Such allowance is admissible up to a maximum of 2 children.

- (b) Holiday package for children studying outside India or family staying abroad: Return holiday package once in a year by economy class or once in 2 years by first class to children and to the members of the family from the place of their study or stay abroad to India if they are not residing in India, with the managerial person.
- (c) **Leave travel concession:** Return package for self and family in accordance with the rules specified by the company where it is proposed that the leave be spent in home country instead of anywhere in India.

Explanation: "Family" means the spouse, dependent children and dependent parents of the managerial person.

Section V: Remuneration payable to a managerial person in two companies: A managerial person shall draw remuneration from one or both companies, provided that the total remuneration drawn from the companies does not exceed the higher maximum limit admissible from any one of the companies of which he is a managerial person.

Que. No. 19A] Ms. Jyoti is the Managing Director of Wise (India) Ltd., incorporated under the Companies Act, 2013. Board of directors of the company presents the following financial data extracted from the company's financial statements as at 31st March, 2015:

| Particulars | (₹ in Crores) |
|---------------------------------|---------------|
| Authorized equity share capital | 60 |
| Paid-up equity share capital | 10 |
| Debenture redemption reserve | 10 |
| Securities premium account | 20 |
| Profit and loss (loss) | (10) |
| Revaluation reserve | 20 |

Due to losses in the financial year 2014-2015, the company is not in a position to pay any remuneration to Ms. Jyoti, Managing Director of the company. As per the agreement of service between Ms. Jyoti and the company, in case of losses or inadequacy of profits in any financial year, she is to be paid remuneration on the basis of 'effective capital' of the company.

Based on the provisions of the Companies Act, 2013, decide the maximum remuneration payable to Ms. Jyoti for the financial year 2014-2015 without the approval of the Central Government.
CS (Executive) – Dec 2015 (4 Marks)

Ans.: "Effective Capital" means the aggregate of the paid-up share capital (excluding share application money or advances against shares); amount, if any, for the time being standing to the credit of share premium account; reserves and surplus (excluding revaluation reserve); long-term loans and deposits repayable after one year (excluding working capital loans, overdrafts, interest due on loans unless funded, bank guarantee, etc., and other short-term arrangements) as reduced by the aggregate of any investments (except in case of investment by an investment company whose principal business is acquisition of shares, stock, debentures or other securities), accumulated losses and preliminary expenses not written off.

Computation of effective capital for managerial remuneration:

| Particulars | ₹ in Crores |
|---|-------------|
| Paid-up capital | 10 |
| Debenture redemption reserve (not specifically excluded by definition of 'effective capital') | 10 |
| Securities premium account | 20 |
| Profit & loss account | (10) |
| Revaluation reserve (specifically excluded by definition of 'effective capital') | - |
| Effective Capital | 30 |

Remuneration payable by companies having no profit or inadequate profit without Central Government approval [Section II of the Part II of the Schedule V]: Where in any financial year during the currency of tenure of a managerial person, a company has no profits or its profits are inadequate, it may, without Central Government approval, pay remuneration to the managerial person not exceeding the limits given below:

Remuneration based on effective capital:

| Where the effective capital is | Limit of yearly remuneration payable shall not exceed (₹) |
|---|---|
| Negative or less than 5 Crores | 60 Lakhs |
| 5 Crores and above but less than 100 Crores | 84 Lakhs |
| 100 Crores and above but less than 250 Crores | 120 Lakhs |
| 250 Crores and above | 120 lakhs plus 0.01% of the effective capital in excess of ₹ 250 crores |

The above limits shall be doubled if the resolution passed by the shareholders is a special resolution. If a period less than one year, the limits shall be pro-rated.

Considering the above provisions, Ms. Jyoti, Managing Director of Wise (India) Ltd. can be remunerated in following ways without approval of Central Government:

- As company's 'effective capital' is between "₹ 5 Crores to 100 Crores"; Ms. Jyoti can be paid annual remuneration of ₹ 84 Lakhs i.e. monthly ₹ 7 Lakhs.
- If company pass special resolution, remuneration can be doubled i.e. ₹ 168 Lakhs per annum i.e. ₹ 14.00 Lakhs per month can be paid.

Que. No. 20] State the provisions of the Companies Act, 2013 relating to recovery of remuneration from managerial personnel?

Ans.: Recovery of remuneration in certain cases [Section 199]: If a company is required to re-state its financial statements due to fraud or non-compliance with any requirement under the Act and the rules made thereunder, the company shall recover remuneration (including stock option) in excess of what would have been payable as per restatement of financial statements from following past or present managerial personnel.

- Managing Director
- Whole-time director
- Manager
- CEO

Que. No. 21] State the powers of a company to fix remuneration under the Companies Act, 2013?

Ans.: Company to fix limit with regard to remuneration [Section 200]: A company may, while according its approval u/s 196, to any appointment or to any remuneration under Section 197 in respect of cases where the company has inadequate or no profits, fix the remuneration within the limits specified, at such amount or percentage of profits of the company, as it may deem fit and while fixing the remuneration. While fixing or limiting the remuneration the company shall take into consideration following factors:

- (a) The financial position of the company.
- (b) The remuneration or commission drawn by the individual concerned in any other capacity.

- (c) The remuneration or commission drawn by him from any other company.
- (d) Professional qualifications and experience of the individual concerned.
- (e) Such other matters as may be prescribed.

Que. No. 22] State the procedure for making application to the Central Government under Chapter XIII of the Companies Act, 2013.

Ans.: Forms of, and procedure in relation to, certain applications [Section 201]: Every application made to the Central Government under Section 196 shall be in prescribed form.

Before any application is made by a company to the Central Government, there shall be issued by or on behalf of the company a general notice to the members, indicating the nature of the application proposed to be made.

Such notice shall be published at least once in a newspaper in the principal language of the district in which the registered office of the company is situate and circulating in that district, and at least once in English in an English newspaper circulating in that district.

The copies of the notices, together with a certificate by the company as to the due publication thereof, shall be attached to the application.

Que. No. 23] Advise Super Specialties Ltd. in respect of the following proposals under consideration of its Board of Directors:

- (i) Appointment of Managing Director who is more than 70 years of age.
- (ii) Payment of commission of 4% of the net profits p.a. to the ordinary directors
- (iii) Payment of remuneration to an ordinary director of rendering professional services.
- (iv) Payment of remuneration of 40,000 p.m. to the whole time director of the company
 - If company is in profit
 - If company is running in loss and having an effective capital of ₹ 95.00 lakhs.

CA (Final) – May 2005 (8 Marks)

Ans.: Keeping in view the provisions of the Sections 196 and 197 of the Companies Act, 2013, answers to given problem is as follows:

- (i) As per Section 196(3), a company shall not appoint or continue the employment of person as Managing Director, Whole-time Director or Manager if such a person is below the age of 21 years or has attained the age of 75 years. However, the appointment of a person who has attained the age of 70 years may be made by passing a *special resolution* in which case the explanatory statement annexed to the notice for such motion shall indicate the justification for appointing such person.

Thus, Super Specialties Ltd. can appointment a person who is more than 70 years of age as its Managing Director by passing a *special resolution* in general meeting. However, age of such person should be below 75 years. The company should also comply with the other conditions prescribed in Schedule V of the Companies Act, 2013.

- (ii) As per Section 197(1), except with the approval of the company in general meeting the remuneration payable to part-time director (non-executive director) shall not exceed –
 - 1% of the net profits, if there is a managing or whole-time director or manager
 - 3% of the net profits in any other case.

Thus, Super Specialties Ltd. can pay commission of 4% to the ordinary directors only with the approval of the members in general meeting.

(iii) As per Section 197(4), the remuneration payable to the directors of a company any other capacity shall also be included in 'remuneration payable to directors' under the provisions of Section 197(1). However, any remuneration for services rendered by any director in other capacity shall not be so included in managerial remuneration if -

- The services rendered are of a professional nature
- If company is required to form the Nomination & Remuneration Committee, then such committee is of the opinion that the director possesses the requisite qualification for the practice of the profession for which additional remuneration is payable.

Thus, Super Specialties Ltd. can pay remuneration to an ordinary director for rendering professional services and such remuneration will not be treated as part of managerial remuneration.

(iv) As per Section 197(1), the company can be pay remuneration up to 5% of its net profit. Thus, if profit of the Super Specialties Ltd. is ₹ 96,00,000 or more ($40,000 \times 12 \times 100/5$) it can pay monthly remuneration of ₹ 40,000 to its whole time director.

As per Section 197(3), if in any financial year, a company has no profits or its profits are inadequate, the company can pay remuneration to managing or whole-time director or manager in accordance with the provisions of Schedule V.

As per Schedule V, company having effective capital less than ₹ 5 Crore can pay yearly remuneration of ₹ 30,00,000 (monthly ₹ 2,50,000). Thus, Super Specialties Ltd. can pay remuneration of ₹ 40,000 p.m. to its whole time director. However, the company has to comply with other provisions of Schedule V of the Companies Act, 2013.

Que. No. 24] A company wants to include the following clause in its Articles of Association:

"Each director shall be entitled to be paid out of the funds of the company for attending meetings of the Board or a Committee thereof including adjourned meeting such sum as sitting fees as shall be determined from time to time by the Directors but not exceeding a sum of ₹ 1,25,000 for each such meeting to be attended by the Director."

You are required to advise the company as to the validity of such a clause and the correct legal position under the provisions of the Companies Act, 2013.

CA (Final) - May 2009 (5 Marks)

Ans.: Validity of inclusion of proposed clause in Articles of Association is discussed below:

- As per Rule 4 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014, amount of sitting fee shall not exceed ₹ 1,00,000 per meeting. Since, proposed purports to payment of sitting fee of ₹ 1,25,000 which is more than prescribed sum of ₹ 1,00,000, hence it is not valid.
- Company can pay the sitting fee for adjourned board meeting for want of quorum, but where a adjourned board meeting is held at later date then sitting fee cannot be paid again, as adjourned meeting is mere continuance of original meeting and adjourned meeting along with original meeting constitute only one meeting and not two meetings.

Que. No. 25] Mr. Weldon was appointed as a director of Esquire Engineering Ltd. w.e.f. from 1st October, 2014. Since the Company wanted to take full advantage of the wisdom and experience of Mr. Weldon, it offered him attractive remuneration payable on monthly basis and made an application to the Central Government for approval to pay such remuneration. Anticipating the approval of the Central Government, Esquire Engineering Ltd. started paying such remuneration from the date of appointment and continued to do so till 31st March, 2015. The Central Government did not fully approve the remuneration proposed by the Company and restricted the same to a lower amount. On scrutiny of accounts, the Company noticed that till 31st March, 2015 it has paid to Mr. Weldon a total sum of ₹ 5.50 lakhs in excess of the remuneration sanctioned by the Central Government. Explain the relevant provisions of the Companies Act, 2013, in respect of recovery and waiver of recovery of the excess remuneration so paid.

CA (Final) - Nov 2009 (5 Marks)

Ans.: As per Section 197(9), if any director draws or receives, directly or indirectly, by way of remuneration any such sums in excess of the limit prescribed by this section or without the prior sanction of the Central Government, where it is required, he shall refund such sums to the company and until such sum is refunded, hold it in trust for the company.

Thus, Mr. Weldon cannot keep the excess remuneration of ₹ 5,50,000. He shall refund such excess remuneration to company. Until such refund is made, he shall hold it in trust for the company. Further, company cannot waive the recovery of excess remuneration unless the Central Government permits the waiver of recovery of excess remuneration.

Que. No. 26] Can a company pay compensation for loss of office to a managing or whole-time director or manager? Also state the cases in such managerial personnel are not allowed to receive compensation? What is the limitation on amount of compensation?

Ans.: Compensation for loss of office of managing or whole-time director or manager [Section 202(1)]: A company may pay compensation for loss of office to a managing or whole-time director or manager only. Compensation for loss of office cannot be paid to part-time director.

Compensation when not allowed [Section 202(2)]: Even compensation for loss of office to a managing or whole-time director or manager shall not be made in the following cases, namely:

- Where the director resigns from his office as a result of the reconstruction of the company, or of its amalgamation with any other body corporate and is appointed as the managing or whole-time director, manager or other officer of the reconstructed company or of the body corporate resulting from the amalgamation.
- Where the director resigns from his office otherwise than on the reconstruction of the company or its amalgamation.
- Where the office of the director is vacated u/s 167(1).
- Where the company is being wound up, whether by an order of the Tribunal or voluntarily, provided the winding up was due to the negligence or default of the director.
- Where the director has been guilty of fraud or breach of trust in relation to, or of gross negligence in or gross mismanagement of, the conduct of the affairs of the company or any subsidiary company or holding company.
- Where the director has instigated, or has taken part directly or indirectly in bringing about, the termination of his office.

Limit on amount of compensation [Section 202(3)]: Any compensation to a managing or whole-time director or manager shall be lower of the following:

- Remuneration for unexpired residue of his term or
- Remuneration for 3 years.

Que. No. 27] Mr. Doubtful was appointed as Managing Director of Carefree Industries Ltd. for a period of 5 years w.e.f. 1.4.2014 on a salary of ₹ 12 lakhs p.a. with other perquisites. The Board of Directors of the company on coming to know of certain questionable transactions, terminated the services of the Managing Director from 1.3.2017. Mr. Doubtful termed his removal as illegal and claimed compensation from the company. Meanwhile the company paid a sum of ₹ 5 lakhs on ad hoc basis to Mr. Doubtful pending settlement of his dues.

Discuss whether:

- The company is bound to pay compensation to Mr. Doubtful and, if so, how much.
- The company can recover the amount of ₹ 5 lakhs paid on the ground that Mr. Doubtful is not entitled to any compensation, because he is guilty of corrupt practices.

CA (Final) - Nov 2004 (4 + 4 = 8 Marks)

Ans.: Keeping in view of the provisions of the Companies Act, 2013 answer to given problem is as follows:

- As per Section 202(3), any compensation to a managing or whole-time director or manager shall be lower of the following:
 - Remuneration for unexpired residue of his term [25 months × 1,00,000 = ₹ 25,00,000]
 - Remuneration for 3 years [36 months × 1,00,000 = ₹ 36,00,000]

Thus, compensation payable to Mr. Doubtful cannot exceed ₹ 25,00,000. If company has already paid ₹ 5,00,000 then remaining ₹ 20,00,000 is payable from the company.

- As per Section 202(2)(e), where the director has been guilty of fraud or breach of trust in relation to, or of gross negligence in or gross mismanagement of, the conduct of the affairs of the company or any subsidiary company or holding company, he shall not be paid any compensation.

However, it was held by the House of Lords that after paying compensation if the company comes to know that managerial personnel to whom the compensation has been paid was guilty of serious breaches of duty and corrupt practices, the company cannot recover the same. [Bell vs. Lever Bros 1932 AC 161]

Thus, if compensation has already been paid to Mr. Doubtful, the compensation cannot be recovered back as per decision in Bell vs. Lever Bros.

However, if breach of duty and corrupt practices of Mr. Doubtful comes to light at the time when his service is terminated, the company is not liable to pay any compensation to him.

Que. No. 28] State the provisions of the Companies Act, 2013 relating to appointment of key managerial personnel (KMP)?

CS (Inter) - Dec 2001 (5 Marks)

CS (Executive) - June 2015 (2 Marks)

CS (Executive) - Dec 2015 (3 Marks)

Ans.: Appointment of key managerial personnel [Section 203(1)]: Every prescribed classes of companies shall have the following whole-time key managerial personnel -

- Managing Director, or Chief Executive Officer (CEO) or Manager and in their absence, a whole-time director
- Company Secretary (CS)
- Chief Financial Officer (CFO)

Rule 8 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014 prescribes the following types of companies:

- Every listed company
- Every other company having paid up share capital of ₹ 10 Crore or more.

As Rule 8A, a company other than company covered under Rule 8 which has paid up capital of 5 Crore or more shall have a whole-time Company Secretary.

Chairperson not to be CEO or MD [Proviso Section 203 (1)]: An individual shall not be appointed or reappointed as the Chairperson as well as the MD or CEO of the company at the same time unless -

- The articles of such a company provide otherwise or
- The company does not carry multiple businesses.

However, this provision shall not apply to:

- Class of companies engaged in multiple businesses and
- Which has appointed one or more Chief Executive Officers for each such business

KMP to appointed at board meetings [Section 203(2)]: Every whole-time key managerial personnel of a company shall be appointed by means of a resolution of the Board containing the terms and conditions of the appointment including the remuneration.

Number of companies in which a person can be appointed as KMP [Section 203(3)]: A whole-time KMP shall not hold office in more than one company except in its subsidiary company at the same time. However, key managerial personnel can be director of any company with the permission of the Board.

Managing Director in two companies [Proviso to Section 203(3)]: A company may appoint or employ a person who is already Managing Director or manager of other company if following conditions are fulfilled:

- If he is Managing Director or Manager of one, and of not more than one, other company.
- Appointment is made by a resolution passed at Board meeting with unanimous consent.
- Specific notice of board meeting is given to all the directors then in India.

Vacancy in the office of whole-time KMP [Section 203(4)]: If the office of any whole-time KMP is vacated, the resulting vacancy shall be filled-up by the Board at a meeting of the Board within a period of 6 months from the date of such vacancy.

Que. No. 29] Kapil is branch head of a limited company. The Company proposes to elevate Kapil to the board. Enumerate the steps involved in such proposal.

CS (Executive) - June 2013 (4 Marks)

Ans.: To elevate Kapil to the board following steps/provisions are required to be observed:

- To see that Kapil is not disqualified for appointment of director. [Section 164]
- Kapil shall inform to the company about his disqualification under Section 164(2) in Form DIR-8 before he is appointed.
- Kapil shall furnish his Director Identification Number to the company before appointment.

- After taking into board to the Kapil number of directors should not exceed 15. [Section 149]
- Kapil will be appointed as additional director. [Section 161(1)] In next AGM he can be appointed as regular director.
- Kapil can be appointed for a term not exceeding 5 years at a time, if he is appointed as whole-time director. [Section 196(2)]
- Kapil shall furnish to the company a consent in writing to act as such in Form DIR-2.
- The company shall, within 30 days of the appointment of Kapil as a director, file such consent with the Registrar in Form DIR-12 along with prescribed fee.
- After appointment of Kapil as a director, an entry has to be made in "Register of directors and key managerial personnel and their shareholding". [Section 170]

Que. No. 29A] Can director or KMP enter into forward dealing contract of securities of the company?

Ans.: Prohibition on forward dealings in securities of company by director or KMP [Section 194]: Section 194 has been deleted by the Companies (Amendment) Act, 2017. Hence, question is not relevant for Dec 2018 and onward exams.

COMPANY SECRETARY

Que. No. 30] Define the term: Company Secretary

Ans.: Company Secretary [Section 2(24)]: "Company Secretary" or "Secretary" means a company secretary as defined in Section 2(1)(c) of the Company Secretaries Act, 1980 who is appointed by a company to perform the functions of a Company Secretary under the Act.

As per Section 2(1)(c) of the Company Secretaries Act, 1980, Company Secretary means a person who is a member of the ICSI.

Company Secretary in Practice [Section 2(25)]: "company secretary in practice" means a company secretary who is deemed to be in practice as per Section 2(2) of the Company Secretaries Act, 1980.

As per Section 2(2) of the Company Secretaries Act, 1980, a member of the ICSI shall be deemed "to be in practice" when, individually, or in partnership with one or more members of the Institute in practice or in partnership with members of such other recognized professions as may be prescribed, he, in consideration of remuneration received or to be received, -

- (a) engages himself in the practice of the profession of Company Secretaries to, or in relation to, any company; or
- (b) offers to perform or performs services in relation to the promotion, forming, incorporation, amalgamation, reconstruction, reorganization or winding up of companies; or
- (c) offers to perform or performs such services as may be performed by -
 - (i) an authorized representative of a company with respect to filing, registering, presenting, attesting or verifying any documents (including forms, applications and returns) by or on behalf of the company,
 - (ii) a share transfer agent,
 - (iii) an issue house,
 - (iv) a share and stock broker,
 - (v) a secretarial auditor or consultant,

- (vi) an adviser to a company on management, including any legal or procedural matter falling under the Industries (Development and Regulation) Act, 1951, the Companies Act, 2013, the Securities Contracts (Regulation) Act, 1956, any of the rules or bye-laws made by a recognized stock exchange, the Competition Act, 2002, the Foreign Exchange Management Act, 1999, or under any other law for the time being in force,
- (vii) issuing certificates on behalf of, or for the purposes of a company; or
- (d) holds himself out to the public as a Company Secretary in practice; or
- (e) renders professional services or assistance with respect to matters of principle or detail relating to the practice of the profession of Company Secretaries; or
- (f) renders such other services as, in the opinion of the Council, are or may be rendered by a Company Secretary in practice.

Que. No. 31] What functions has be performed by the Company Secretary under the Companies Act, 2013?

Ans.: Functions of the Company Secretary [Section 205]: The functions of the Company Secretary includes the following -

- (a) To report to the Board about compliance with the provisions of the Companies Act, 2013 and the rules made thereunder and other laws applicable to the company.
- (b) To ensure that company complies with Secretarial Standards.
- (c) To discharge other prescribed duties.

Explanation: The expression "Secretarial Standards" means secretarial standards issued by the ICSI and approved by the Central Government.

Duties of Company Secretary [Rule 10 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014]: The Company Secretary shall discharge the following duties:

- (1) To provide guidance to the directors with regard to their duties, responsibilities and powers.
- (2) To facilitate the convening of meetings and attend Board, committee and general meetings and maintain the minutes of these meetings.
- (3) To obtain approvals from the Board, general meeting, the government and other authorities as required under the provisions of the Act.
- (4) To represent before various Regulators, and other authorities in connection with discharge of various duties.
- (5) To assist the Board in the conduct of the affairs of the company.
- (6) To assist and advise the Board in ensuring and in complying good corporate governance and best practices.
- (7) To discharge other specified duties under the Act or Rules.
- (8) To discharge other duties as may be assigned by the Board from time to time.

Que. No. 32] State the provisions and procedure relating to appointment of Company Secretary.

Ans.: As per Section 2(51), Company Secretary is Key Managerial Personnel (KMP). Section 203 deals with the mandatory appointment of KMP in certain classes of companies.

Thus, as per Section 203 read with Rules 8 & 8A of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014, appointment of Company Secretary in mandatory in following types of companies:

- Every listed company
- Every other public company paid-up capital of which is ₹ 5 Crore or more

Section 8 company's i.e. non-profit making companies need to appoint Company Secretary. [MCA Notification dated 5.6.2015]

Appointment of Company Secretary: A Company Secretary shall be appointed by resolution of board of directors, containing the terms and conditions of appointment including remuneration.

Filing of Return: Return of appointment of Company Secretary as well as cessation has to be filed with ROC in Form No. DIR. 12. In addition to this, Form No. MR. 1 is also required to be filed as Company Secretary is KMP.

Details to be entered in Register of KMP: The Company Secretary is KMP and his details has to be included in "Register of Directors & KMP" maintained u/s 170.

A whole-time Company Secretary can be Company Secretary of subsidiary company: A whole-time KMP (which includes Company Secretary) shall not hold office in more than one company except in its subsidiary company at the same time. [Section 203(3)]

Company Secretary can be director of any company: A Company Secretary can be appointed as director of the company or of any other company with the permission of Board. [Section 203(3)]

Vacancy to be filed in 6 months: Any vacancy in the post of Company Secretary should be filled within 6 months. [Section 203(4)]

Company Secretary as Compliance Officer: As per Regulation 6 of the SEBI (Listing Obligation & Disclosure Requirements) Regulation, 2015, a listed company shall appoint qualified Company Secretary as the Compliance Officer.

Officer in default: The Company Secretary is included in definition of 'Officer in default'. Thus, he may be penalized for non-compliance of the provisions of the Companies Act, 2013 and Rules and Regulations made thereunder.

Que. No. 33] What are the statutory duties of the Company Secretary under the Companies Act, 2013?
CS (Executive) - June 2014 (4 Marks)

Ans.: Duties of Company Secretary [Rule 10 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014: The Company Secretary shall discharge the following duties, namely:

- (1) To provide to the directors of the company, collectively and individually, such guidance as they may require, with regard to their duties, responsibilities and powers.
- (2) To facilitate the convening of meetings and attend Board, committee and general meetings and maintain the minutes of these meetings.
- (3) To obtain approvals from the Board, general meeting, the government and such other authorities as required under the provisions of the Act.
- (4) To represent before various regulators, and other authorities under the Act in connection with discharge of various duties under the Act.
- (5) To assist the Board in the conduct of the affairs of the company.
- (6) To assist and advise the Board in ensuring good corporate governance and in complying with the corporate governance requirements and best practices.
- (7) To discharge such other duties as may be assigned by the Board from time to time.
- (8) To discharge such other duties as have been specified under the Act or Rules.



INTER-CORPORATE LOANS & INVESTMENTS

This Chapter Covers:

- Applicability of Section 186
- Higher loan, guarantee or investment by passing special resolution
- Register of loans made, guarantees given, securities provided and investments made
- Inspection of register
- Penalties and exemptions
- Investments to be held in company's own name and exemptions

Que. No. 1] Write a short note on: Restriction on investment through investment subsidiaries

Ans.: Restriction on investment through investment subsidiaries [Section 186(1)]: Section 186(1) has been deleted by the Companies (Amendment) Act, 2016. Hence, question is not relevant for Dec. 2016 and onward exam.

Que. No. 2] Outline the provisions of the Companies Act, 2013 regarding

(i) Inter-corporate investments

(ii) Inter-corporate loans

CS (Inter) - Dec 1998 (8 + 8 = 16 Marks)
CS (Inter) - June 2000 (12 Marks), Dec 2003 (12 Marks)

The power to invest funds of the company is the prerogative of the Board of directors under Section 179. Discuss the limitations on such powers of the Board, if any, relating to inter-corporate loans and investments under Section 186.

CS (Executive) - Dec 2004 (8 Marks), Dec 2009 (6 Marks)

What are the circumstances under which approval of members is not required in respect of inter-corporate loans and investments?

CS (Inter) - June 2001 (6 Marks), June 2003 (6 Marks)

Ans.: Loan and investment by company [Section 186(2)]: A company can directly or indirectly give loan, guarantee or provide security or make investment other body corporate or person up to higher of the following two limits:

- [Paid-up Capital + Free Reserves + Securities Premium Account] × 60% or
- [Free Reserves + Securities Premium Account] × 100%

Explanation: The word "person" does not include any individual who is in the employment of the company.

Due to explanation, loan made by the company to any individual who is in employment of the company will be excluded for the purpose of monetary limit. At the same time, any guarantee provided or security provided in connection with loan will also be excluded.

Higher loan, guarantee or investment by passing special resolution [Section 186(3)]: Where the aggregate of the loans and investment so far made, the amount for which guarantee or security so far provided to or in all other bodies corporate along with the investment, loan, guarantee or security proposed to be made or given by the Board, exceed the specified limits, no investment or loan shall be made or guarantee shall be given or security shall be provided unless previously authorized by a special resolution passed in a general meeting.

As per Rule 22(j) of the Companies (Management & Administration) Rules, 2014, in case of companies having more than 200 members, the special resolution for giving loan or extending guarantee or providing security in excess of limit laid down is required to be passed by postal ballot.

Exemption in case of Wholly Owned Subsidiary (WOS): The requirement of passing special resolution is not necessary:

- (a) Where a loan or guarantee is given or where a security has been provided by a company to its Wholly Owned Subsidiary (WOS) or a joint venture company, or
- (b) Where acquisition is made by a holding company, by way of subscription, purchase of the securities of its WOS.

However, the company shall disclose the details of such loans or guarantee or security or acquisition in the financial statement.

Disclosure [Section 186(4)]: The company shall disclose to the members in the financial statement the full particulars of the loans given, investment made or guarantee given or security provided and the purpose for which the loan or guarantee or security is proposed to be utilized by the recipient of the loan or guarantee or security.

Consent of board and prior approval of public financial institution [Section 186(5)]: No investment shall be made or loan or guarantee or security given by the company unless the resolution sanctioning it is passed at a meeting of the Board with the *consent of all the directors present at the meeting* and the prior approval of the public financial institution concerned where any term loan is subsisting, is obtained.

However, prior approval of a public financial institution shall not be required where the aggregate of the loans and investments so far made, the amount for which guarantee or security so far provided to or in all other bodies corporate, along with the investments, loans, guarantee or security proposed to be made or given does not exceed the specified limit and there is no default in repayment of loan instalments or payment of interest thereon as per the terms and conditions of such loan to the public financial institution.

Special provision for companies registered u/s 12 of the SEBI Act, 1992 [Section 186(6)]: No company, which is registered u/s 12 of the SEBI Act, 1992 and covered under such class or classes of companies as may be prescribed, shall take inter-corporate loan or deposits exceeding the prescribed limit and such company shall furnish in its financial statement the details of the loan or deposits.

Minimum rate of interest [Section 186(7)]: No loan shall be given under this section at a rate of interest lower than the prevailing yield of 1 year, 3 years, 5 years or 10 years Government Security closest to the tenor of the loan.

No subsisting defaults in deposits or interest on it [Section 186(8)]: No company which is in default in the repayment of any deposits accepted or in payment of interest thereon, shall give any loan or give any guarantee or provide any security or make an acquisition till such default is subsisting.

Register [Section 186(9)]: Every company giving loan or giving a guarantee or providing security or making an acquisition shall keep a register which shall contain such particulars and shall be maintained in Form No. MBP - 3.

Place where Register has to be kept and its inspection [Section 186(10)]: The Register of loan, guarantee & investment shall be kept at the registered office of the company.

Such Register shall be open to inspection at registered office and extracts may be taken by any member. If any member of the company demands its copy, it should be furnished on payment of prescribe fees.

Power to make Rules [Section 186(12)]: The Central Government may make rules for the purposes of this section.

Penalty [Section 186(13)]: If a company contravenes the provisions of this section, the company shall be punishable -

- With fine which shall not be less than ₹ 25,000 but which may extend to ₹ 5,00,000 and
- Every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 2 years and with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 1,00,000.

Que. No. 3] State the circumstances under which Section 186 does not apply.

Ans.: Cases where provisions of Section 186 are not applicable [Section 186(11)]:

Nothing contained in this section shall apply -

- (a) To any loan made, any guarantee given or any security provided or any investment made by banking or insurance or housing finance company in the ordinary course of its business, or a company established with the object of and engaged in the business of financing industrial enterprises, or of providing infrastructural facilities.
- (b) To any investment -
 - (i) made by an investment company
 - (ii) made in shares allotted in Section 62(1)(a) or in shares allotted in pursuance of rights issues made by a body corporate;
 - (iii) made, in respect of investment or lending activities, by a non-banking financial company registered under the RBI Act, 1934 and whose principal business is acquisition of securities.

A company will be deemed to be principally engaged in the business of acquisition of shares, debentures or other securities, if its assets in the form of investment in shares, debentures or other securities constitute not less than 50% of its total assets, or if its income derived from investment business constitutes not less than 50% as a proportion of its gross income.

Que. No. 4] Following information is available from the Balance Sheet as at 31.3.2015 of ASK Ltd:

| Capital & Liabilities | | ₹ |
|--|-------------|-----------|
| Shareholders Funds: | | |
| Equity Share Capital (5,00,000 shares of ₹ 10 each) | 50,00,000 | |
| Less: Calls in arrear | (50,000) | 49,50,000 |
| Preference Share Capital | | 15,00,000 |
| Share Application Money | | 10,00,000 |
| Reserves & Surplus | | |
| Securities Premium | | 15,00,000 |
| Capital Redemption Reserve | | 12,00,000 |
| Fixed Assets Revaluation Reserve | | 10,50,000 |
| Sinking Fund Reserve | | 11,00,000 |
| General Reserve | | 40,00,000 |
| Profit and Loss Account | | 22,00,000 |
| Dividend Equalization Reserve | | 6,00,000 |
| Non-Current Liabilities: | | |
| Current Liabilities: | | |
| Cash Credit facility from Bank | 1,00,00,000 | |
| Fixed Deposits (From general public maturing after 31.12.2015) | 20,00,000 | |
| Other Current Liabilities | 12,50,000 | |
| Short Term Provisions: | | |
| Provision for Taxation | 10,00,000 | |
| | 3,33,50,000 | |
| ASSETS | | ₹ |
| Non-Current Assets: | | |
| Goodwill | 10,00,000 | |
| Land & Buildings | 75,00,000 | |
| Plant & Machinery | 1,50,00,000 | |
| Furniture & Other Assets | 2,50,000 | |
| Investments: | | |
| - Equity shares in wholly owned subsidiary – KMC Ltd. | 12,50,000 | |
| - Equity Shares representing 90% of Share capital of MTC Ltd. | 4,50,000 | |
| - Debentures in SKT Ltd. | 12,00,000 | |
| - Preference Shares in HUT Ltd. | 5,00,000 | |
| - Capital account balance in Partnership Firm – BKP & Co. | 8,00,000 | |
| Current Assets: | | |
| Stock & Books Debts | 14,00,000 | |
| Cash & Bank Balances | 1,00,000 | |
| Inter-Corporate Deposits | 25,00,000 | |
| Business Advances | 14,00,000 | |
| | 3,33,50,000 | |

The directors of the company want to make further investments stated below by taking a decision in the meeting of Board of directors without seeking approval of shareholders:

| | ₹ |
|---|-----------|
| (a) Loan to KMC Ltd. | 25,00,000 |
| (b) Loan to MTC Ltd. | 15,00,000 |
| (c) Purchase of further debentures in SKT Ltd. | 8,00,000 |
| (d) Purchase of shares from the open market in Glaxo Ltd. | 15,00,000 |

You are required to state, with reference to the relevant provisions of the Companies Act, 2013, whether the directors can do so and mention the relevant calculations.

Ans.:

| | | |
|--------------------|--------------------------------------|-------------|
| Paid-up capital | : (49,50,000 + 15,00,000) | ₹ 64,50,000 |
| Free Reserves | : (40,00,000 + 22,00,000 + 6,00,000) | ₹ 68,00,000 |
| Securities Premium | : | ₹ 15,00,000 |

Calculation of overall limit: Higher of the following two.

| | |
|---|-------------|
| - [64,50,000 + 68,00,000 + 15,00,000] × 60% | ₹ 88,50,000 |
| - [68,00,000 + 15,00,000] × 100% | ₹ 83,00,000 |

Investment already made:

| | |
|---|-----------|
| Equity Shares representing 90% of Share capital of MTC Ltd. | 4,50,000 |
| Debentures in SKT Ltd. | 12,00,000 |
| Preference Shares in HUT Ltd. | 5,00,000 |
| Inter-Corporate Deposits | 25,00,000 |
| | 46,50,000 |

Proposed loan & investments:

| | |
|---|-----------|
| Loan to MTC Ltd. | 15,00,000 |
| Purchase of further debentures in SKT Ltd. | 8,00,000 |
| Purchase of shares from the open market in Glaxo Ltd. | 15,00,000 |
| | 38,00,000 |

Since, investment already made along with proposed investment (₹ 46,50,000 + ₹ 38,00,000 = ₹ 84,50,000) do exceed prescribed limit (₹ 88,50,000), proposed investment/loan can be made by passing a unanimous resolution in a Board Meeting and prior approval by means of a special resolution passed at a general meeting shall not be necessary.

For the purpose of computation of limit investment/loan to wholly owned subsidiary will not be taken into consideration. [Rule 11 of the Companies (Meetings of Board & its Powers) Rules, 2014]

Que. No. 5] The Board of directors of an Indian company passed a resolution for incorporation of a company in Singapore with the initial paid-up capital of \$10,000. Comment whether investment to be made in the Singapore company is exempt from the provisions of Section 186. CS (Inter) – June 2006 (4 Marks)

Ans.: Provisions contained in Section 186(2) & (3) will be applicable for incorporation of a company in Singapore with the initial paid-up capital of \$10,000 because company incorporated in foreign country will be body corporate. Hence, all the limits and condition prescribed in Section 186(2) & (3) has to be complied with.

However, after incorporation if it becomes Wholly Owned Subsidiary then for making further investment they can take the benefit of Rule 11 of the Companies (Meetings of Board & its Powers) Rules, 2014.

As per Rule 11 of the Companies (Meetings of Board & its Powers) Rules, 2014, the requirement of passing special resolution is not necessary:

- (a) Where a loan or guarantee is given or where a security has been provided by a company to its Wholly Owned Subsidiary (WOS) or a joint venture company, or
- (b) Where acquisition is made by a holding company, by way of subscription, purchase of the securities of its WOS

Que. No. 6] State the procedure for granting loan by one company to another company.

CS (Executive) – June 2011 (6 Marks)

Ans.: A company which directly or indirectly give loan, guarantee or provide security or make investment other body corporate or person must follow the procedure detailed below:

- (1) Issue notice for board meeting as per the provisions of Section 173(3).
- (2) Hold board meeting to consider the proposal to give loan, guarantee or provide security or make investment other body corporate or person.
 - a. If the aggregate amount of proposed loan/guarantee/security/investment is within the limits then pass the resolution with all the directors present at the meeting consenting specifying the limit for such loan/guarantee/security/investment.
 - b. If the aggregate amount of proposed loan/guarantee/security/investment exceeds the specified limits then fix time, date and venue for holding general meeting to pass the special resolution.
- (3) Draft the notice of the special resolution which must contain the prescribed details.
- (4) Issue notice in writing at least 21 clear days before the date of the general meeting.
- (5) In case of listed companies, send 3 copies of the notice to each Stock exchange, where shares of the company are listed.
- (6) Hold the general meeting and pass the special resolution. (In case of companies having more than 200 members, the special resolution for giving loan or extending guarantee or providing security in excess of limit laid down is required to be passed by postal ballot.)
- (7) File the special resolution in Form No. MGT – 14 and file it with ROC within 30 days.
- (8) Ensure that approval of the Public Financial Institution(s) has been obtained before implementing the proposal if the company has taken any term loan from any one of the financial institutions.
- (9) Ensure that company has not defaulted in complying with the provisions of Section 73 of the Companies Act, 2013 relating to "acceptance or repayment of deposits".
- (10) Also ensure that loan to any body corporate is not made at a rate of interest lower than the prevailing yield of 1 year, 3 year, 5 year or 10 year Government Security closest to the tenor of the loan.
- (11) Enter the prescribed particulars in Register of inter corporate loans & investments within 7 days.

Que. No. 7] High Dream Ltd. proposes to invest ₹ 37 lakhs by acquiring equity shares capital of XYZ Ltd. The financial position of High Dream Ltd. at the end of the financial year is as under:

| | |
|--------------------------|-------------|
| Issued & Paid-up Capital | ₹ 50,00,000 |
| Free Reserves | ₹ 10,00,000 |

Advise the high Dream Ltd. about the requirement to be complied with for the proposed investment in XYZ Ltd. CS (Inter) – June 2002 (10 Marks)

Ans.:

| | |
|--------------------|--------------|
| Paid-up capital | : ₹ 50 Lakhs |
| Free Reserves | : ₹ 10 Lakhs |
| Securities Premium | : Nil |

Calculation of overall limit: Higher of the following two.

| | |
|-------------------|--------------|
| - [50 + 10] × 60% | = ₹ 36 Lakhs |
| - 10 × 100% | = ₹ 10 Lakhs |

Proposed investment in XYZ Ltd. : ₹ 37 Lakhs

Since, proposed investment exceed prescribed limit, proposed investment can be made by taking prior approval by means of a special resolution passed at a general meeting. [Section 186(3)]

Such special resolution is not required to be passed by postal ballot as per Rule 22 of the Companies (Management & Administration) Rules, 2014 as it requires passing of resolution by postal ballot only in case of giving loan or extending guarantee or providing security in excess of limit laid down and not for making investments.

Que. No. 8] Balance sheet of ABC Ltd. as at 31st March, 2015 shows the following liabilities:

| | |
|---------------------------------------|------------|
| Paid-up Capital | ₹ 10 Crore |
| Reserves & Surplus | ₹ 20 Crore |
| Reserves for redemption of debentures | ₹ 5 Crore |

The company has already advanced to the following companies:

| | |
|----------|-------------|
| XYZ Ltd. | - ₹ 6 Crore |
| MNO Ltd. | - ₹ 2 Crore |

ABC Ltd. has given corporate guarantee of ₹ 5 Crore to STU Ltd.

PQR Ltd. has approached ABC Ltd. for inter-corporate loan of ₹ 8 Crore.

As the Company Secretary of ABC Ltd., advise the management on the limits of making loans and inter-corporate investments. CS (Inter) – Dec 2005 (6 Marks)

Ans.:

| | |
|--------------------|---------------|
| Paid-up capital | : ₹ 10 Crores |
| Free Reserves | : ₹ 20 Crores |
| Securities Premium | : Nil |

Calculation of overall limit: Higher of the following two.

| | |
|-------------------|---------------|
| - [10 + 20] × 60% | = ₹ 18 Crores |
| - 20 × 100% | = ₹ 20 Crores |

Loan & Investments already made:

| | |
|---------------------------------|----------|
| Advance to XYZ Ltd. | 6 Crore |
| Advance MNO Ltd. | 2 Crore |
| Corporate guarantee to STU Ltd. | 5 Crore |
| | 13 Crore |

Proposed loan to PQR Ltd. : ₹ 8 Crores

Since, investment/loan/guarantee already made or given (₹ 13 Crore) along with proposed investment/loan/guarantee (₹ 8 Crore) exceed prescribed limit, proposed investment/loan can be made by taking prior approval by means of a special resolution passed at a general meeting. [Section 186(3)]

However, if ABC Ltd. has more than 200 members, the special resolution for giving loan or extending guarantee or providing security in excess of limit laid down is required to be passed by postal ballot. [Rule 22 of the Companies (Management & Administration) Rules, 2014]

Que. No. 9] Balance sheet of DEF Ltd. as at 31st March, 2015 shows among others the following information:

| | |
|--------------------------------------|----------|
| | ₹ |
| Paid-up Share Capital | 20 Crore |
| Reserves & Surplus | 35 Crore |
| Reserve for redemption of debentures | 15 Crore |
| Capital Reserves | 5 Crore |

The company has already given following loans/stood guarantees for loans to other companies :

- Loan to GHI Ltd. : ₹ 12 Crore
- Guarantee given on behalf of JKL Ltd. : ₹ 11 Crore

MNO Ltd. has approached DEF Ltd. for loan of ₹ 15 Crore. Advise the management whether DEF Ltd. can give the loan of ₹ 15 Crore to MNO Ltd. and if yes, set out the procedure therefor. CS (Inter) - Dec 2006 (10 Marks)

Ans.:

| | |
|--------------------|---------------|
| Paid-up capital | : ₹ 20 Crores |
| Free Reserves | : ₹ 35 Crores |
| Securities Premium | : Nil |

Calculation of overall limit: Higher of the following two.

- $[20 + 35] \times 60\%$ = ₹ 33 Crores
- $35 \times 100\%$ = ₹ 35 Crores

Loan & Investments already made:

| | |
|---------------------------------------|----------|
| Loan to GHI Ltd. | 12 Crore |
| Guarantee given on behalf of JKL Ltd. | 11 Crore |
| | 23 Crore |

Proposed loan to MNO Ltd. : ₹ 15 Crores

Since, investment/loan/guarantee already made or given (₹ 23 Crore) along with proposed investment/loan/guarantee (₹ 15 Crore) exceed prescribed limit, proposed investment/loan

can be made by taking prior approval by means of a special resolution passed at a general meeting. [Section 186(3)]

However, if DEF Ltd. has more than 200 members, the special resolution for giving loan or extending guarantee or providing security in excess of limit laid down is required to be passed by postal ballot. [Rule 22 of the Companies (Management & Administration) Rules, 2014]

Que. No. 10] Following information has been extracted from the balance sheet of Richy Rich Ltd.:

| | |
|-------------------------------|------------|
| (i) Paid-up Share Capital | ₹ 20 Crore |
| (ii) Reserves & Surplus | ₹ 80 Crore |
| (iii) Capital Reserve | ₹ 5 Crore |
| (iv) Investment in securities | ₹ 10 Crore |
| (v) Loan to companies | ₹ 30 Crore |

DEF Ltd. has requested Richy Rich Ltd. for a loan of ₹ 50 Crore which the Board of directors will consider at its ensuing meeting. Explain the legal position and advise the Board. CS (Inter) - June 2006 (10 Marks)

Ans.:

| | |
|--------------------|---------------|
| Paid-up capital | : ₹ 20 Crores |
| Free Reserves | : ₹ 80 Crores |
| Securities Premium | : Nil |

Calculation of overall limit: Higher of the following two.

- $[20 + 80] \times 60\%$ = ₹ 60 Crores
- $80 \times 100\%$ = ₹ 80 Crores

Loan & Investments already made:

| | |
|--------------------------|-----------|
| Investment in securities | 10 Crores |
| Loan to companies | 30 Crores |
| | 40 Crores |

Proposed loan to DEF Ltd. : ₹ 50 Crores

Since, investment/loan/guarantee already made or given (₹ 40 Crore) along with proposed loan (₹ 50 Crore) exceed prescribed limit, proposed loan can be given by taking prior approval by means of a special resolution passed at a general meeting. [Section 186(3)]

However, if Richy Rich Ltd. has more than 200 members, the special resolution for giving loan or extending guarantee or providing security in excess of limit laid down is required to be passed by postal ballot. [Rule 22 of the Companies (Management & Administration) Rules, 2014]

Que. No. 11] As on 31st March, 2015, the balance sheet of ABC Ltd. shows the following:

| | ₹ in Crores |
|-------------------------------------|-------------|
| Paid-up share capital | 30 |
| Reserves & Surplus | 40 |
| Reserve for redemption of debenture | 20 |
| Capital Reserve | 10 |

The company made loan/stood guarantee for loans to other companies as below:

| | |
|---------------------------------------|------------|
| Loan to DEF Ltd. | ₹ 15 Crore |
| Guarantee given on behalf of GHK Ltd. | ₹ 15 Crore |

LKP Ltd. approached ABC Ltd. for loan of an amount of ₹ 20 Crore. Advise the management of ABC Ltd. as to whether the company can give loan of ₹ 20 Crore to LKP Ltd.
CS (Executive) - June 2011 (4 Marks)

Ans.:

Paid-up capital : ₹ 30 Crores

Free Reserves : ₹ 40 Crores

Securities Premium : Nil

Calculation of overall limit: Higher of the following two.

- $[30 + 40] \times 60\%$ = ₹ 42 Crores
- $40 \times 100\%$ = ₹ 40 Crores

Loan & Investments already made:

| | |
|---------------------------------------|----------|
| Loan to DEF Ltd. | 15 Crore |
| Guarantee given on behalf of GHK Ltd. | 15 Crore |
| | 30 Crore |

Proposed loan to LKP Ltd. : ₹ 20 Crores

Since, investment/loan/guarantee already made or given (₹ 30 Crore) along with proposed loan (₹ 20 Crore) exceeds prescribed limit, proposed loan can be given by taking prior approval by means of a special resolution passed at a general meeting.

However, if ABC Ltd. has more than 200 members, the special resolution for giving loan or extending guarantee or providing security in excess of limit laid down is required to be passed by postal ballot.

Que. No. 12] Board of directors of Joy Ltd., by a resolution passed at its meeting, decide to provide a loan of ₹ 50 Crore to Happy Ltd. The paid-up share capital of Joy Ltd. on the date of resolution was ₹ 100 Crore and the aggregate balance in the Free Reserves and Securities Premium Account stood at ₹ 40 Crore. Examining the provisions of the Companies Act, 2013, decide whether the Board's resolution to provide a loan of ₹ 50 Crore to Happy Ltd. is valid?
CS (Executive) - June 2015 (4 Marks)

Ans.:

Paid-up capital : ₹ 100 Crores

Free Reserves & Securities Premium : ₹ 40 Crores

Calculation of overall limit: Higher of the following two.

- $[100 + 40] \times 60\%$ = ₹ 84 Crores
- $40 \times 100\%$ = ₹ 40 Crores

Proposed loan to Happy Ltd. : ₹ 50 Crores

Since, the proposed loan (₹ 50 Crore) does not exceeds prescribed limit, proposed loan can be given by passing a unanimous resolution in a Board Meeting and prior approval by means of a special resolution passed at a general meeting shall not be necessary.

INVESTMENT IN THE NAME OF OTHERS

Que. No. 13] All investments made by a company must be held by its own name. Comment.
CS (Inter) - Dec 2007 (5 Marks)

Ans.: Investments of company to be held in its own name [Section 187(1)]: All investments made or held by a company in any property, security or other asset shall be made and held by it in its own name.

Investment in other name is permitted only in following circumstances. [Section 187(2)]

- (1) **Shares in the name of nominee in subsidiary company:** The company may hold shares in its subsidiary company in the name of any nominee, if it is necessary to ensure that the number of members of the subsidiary company is not reduced below the statutory limit i.e. 2 in case of private company and 7 in case of public company.
- (2) **Depositing shares or securities with banks for collection of dividend and interest:** Shares or securities can be deposited with bankers of the company for collection of any dividend or interest payable thereon.
- (3) **Transfer in the name of banker for further transfer:** A company can transfer securities in the name of its bankers (State Bank of India or any scheduled bank) to facilitate further transfer. However, if the securities are not further transferred within 6 months, the securities should be retransferred in the name of the company within 6 months.
- (4) **Transfer as security for loans:** If a company has obtained loan by giving security its investment in securities, such securities can be deposited with or transferred in the name of lender.
- (5) **Holding securities in depository mode:** A company can hold investment in the name of depository. However, name of the company should be recorded as beneficial owner in the records of the depository.

Register of investment not in own name [Section 187(3)]: Where any securities in which investments have been made by a company are not held by it in its own name, the company shall maintain a register in prescribed form.

Inspection of register: Such register shall be open to inspection by members or debenture-holders without any charge during business hours subject to such reasonable restrictions as the company may impose.

As per Rule 14 of the Companies (Meetings of Board and its Powers) Rules, 2014, every company shall maintain a register in Form MBP-3 and enter chronologically, the particulars of investments not held in its own name. The company shall also record the reasons for not holding the investments in its own name and the relationship or contract under which the investment is held in the name of any other person.

The register shall be maintained at the registered office of the company. The register shall be preserved **permanently** and shall be kept in the custody of the Company Secretary or any director or any other officer authorized by the Board.

The entries in the register shall be authenticated by the Company Secretary or by any other person authorized by the Board.

CHAPTER 19

DEPOSITS

This Chapter Covers:

- Invitation and acceptance of deposits
- Application of provisions of Section 73 to guarantee companies and Section 8 Companies.
- Non-banking non financial companies
- Exemption of applicability of Section 73
- Nomination by depositors
- Companies right to reject application
- Ceiling limit for acceptance of deposits
- The Companies (Acceptance of Deposits) Rules, 2014
- Form and particulars of advertisement
- Renewal of deposits
- Repayment of deposits
- Penalties
- Remedy if the company fails to repay on due date.

Note: In this chapter, unless otherwise stated 'Rule' means the Companies (Acceptance of Deposits) Rules, 2014.



PUBLIC DEPOSIT

Que. No. 1] How the acceptance of deposit by companies is regulated under the Companies Act, 2013?

Ans.: Sections 73 to 76 read with the Companies (Acceptance of Deposits) Rules, 2014 regulate the invitation and acceptance of deposits. It prohibits acceptance of deposits except from the members through **ordinary resolution** or acceptance deposits by "eligible company" being a public company, subject to conditions specified in the rules. (Eligible company is defined under the rules based on net worth and turnover).

The act provides for stringent penalty for any violations in complying with the provisions in this regard.

Que. No. 2] Certain companies are exempted from the provisions of Section 73 of the Companies Act, 2013. Comment. CS (Inter) – Dec 2007 (5 Marks)

Discuss the law relating to acceptance of deposits by non-banking non-financial Companies. CS (Inter) – Dec 2005 (5 Marks), June 2006 (5 Marks)

Provisions of Section 73 are not applicable to guarantee companies and Section 8 Companies (i.e., associations not for profit). CS (Executive) – June 2009 (5 Marks)

Ans.: Proviso to Section 73(1) read with Rule 1(3) of the Companies (Acceptance of Deposits) Rules, 2014 excludes banking Companies, non-banking financial companies as defined in the Reserve Bank of India Act, 1934 and registered with RBI, a housing finance company registered with NHB established under the National Housing Bank Act, 1987 and any other company as may be specified by the government in this regard.

Que. No. 3] Define the term 'deposits' and list out the receipts of money which are not considered as deposits. CS (Executive) – Dec 2016 (8 Marks)

Ans.: Deposit [Section 2(31)]: Deposit includes any receipt of money by way of deposit or loan or in any other form by a company, but does not include such categories of amount as may be prescribed in consultation with the RBI.

Inclusive definition of the word "Deposit" under Rule 2(1)(c) is as under:

Deposit [Rule 2(1)(c)]: Deposit includes any receipt of money by way of deposit or loan or in any other form, by a company, but does not include:

- (i) Any amount received from the Central or State Government, or any amount received from any other source whose repayment is guaranteed by the Central or State Government or any amount received from a local authority, or any amount received from a statutory authority constituted under an Act of parliament or a state legislature.
- (ii) Any amount received from foreign Governments, foreign/international banks, multilateral financial institutions (including, but not limited to, International Finance Corporation, Asian Development Bank, Commonwealth Development Corporation and International Bank for Industrial and Financial Reconstruction), foreign government owned development financial institutions, foreign export credit agencies, foreign collaborators, foreign bodies corporate and foreign citizens, foreign authorities or persons resident outside India subject to the provisions of FEMA Act, 1999 and rules and regulations made thereunder.
- (iii) Any amount received as a loan or facility from any banking company or from the SBI or any of its subsidiary banks or from a banking institution notified by the Central Government.
- (iv) Any amount received as a loan or financial assistance from Public Financial Institutions notified by the Central Government in this behalf in consultation with the RBI, regional financial institutions, Insurance Companies, Scheduled Banks as defined in the RBI Act, 1934.
- (v) Any amount received against issue of commercial paper or any other instrument issued in accordance with the guidelines or notification issued by the RBI.
- (vi) Any amount received by a company from any other company.
- (vii) Any amount received and held pursuant to an offer made in accordance with the provisions of the Act towards subscription to any securities, including share application money

or advance towards allotment of securities pending allotment, so long as such amount is appropriated only against the amount due on allotment of the securities applied for. If the securities for which application money or advance for such securities was received cannot be allotted within 60 days from the date of receipt of the application money or advance for such securities and such application money or advance is not refunded to the subscribers within 15 days from the date of completion of 60 days, such amount shall be treated as a deposit under these rules. For the purpose of this rule any adjustment of the amount for any other purpose will not be treated as refund.

- (viii) Any amount received from a person who, at the time of the receipt of the amount, was a director of the company or relative of director of company or relative of director of private company. The director from whom money is received, furnishes to the company at the time of giving the money, a declaration in writing to the effect that the amount is not being given out of funds acquired by him by borrowing or accepting loans or deposits from others.
- (ix) Any amount raised by the issue of bonds or debentures secured by a first charge or a charge ranking *pari passu* with the first charge on any assets referred to in Schedule III of the Act excluding intangible assets of the company or bonds/debentures compulsorily convertible into shares of the company within 10 years. If such bonds or debentures are secured by the charge of any assets referred to in Schedule III of the Act excluding intangible assets, the amount of such bonds or debentures shall not exceed the market value of such assets as assessed by a registered valuer.
- (x) Any amount received from an employee not exceeding his annual salary, under a contract of employment with the company in the nature of non-interest bearing security deposit.
- (xi) Any non-interest bearing amount received or held in trust.
- (xii) Any amount received in the course of or for the purposes of the business of the company:
 - (a) As an advance for the supply of goods or provision of services provided that such advance is appropriated against supply of goods or provision of services within a period of 365 days from acceptance of such advance. In case of any advance which is subject matter of any legal proceedings before any court of law, the said time limit of 365 days shall not apply.
 - (b) As advance, accounted for in any manner whatsoever, received in connection with consideration for property under an agreement or arrangement, provided that such advance is adjusted against the property in accordance with the terms of agreement or arrangement.
 - (c) As security deposit for the performance of the contract for supply of goods or provision of services.
 - (d) As advance received under long term projects or for supply of capital goods except those covered under item (b) above. If the amount received under (a), (b) & (c) above becomes refundable (with or without interest) because the company accepting the money does not have necessary permission or approval to deal in the goods or properties or services for which the money is taken, the amount received shall be deemed to be a Deposit under these rules.
 - (e) As an advance towards consideration for providing future services in the form of a warranty or maintenance contract as per written agreement or arrangement, if the period for providing such services does not exceed the period prevalent as per common business practice or 5 years, from the date of acceptance of such service whichever is less.
 - (f) As an advance received and as allowed by any sectoral regulator or in accordance with directions of Central or State Government.

- (g) As an advance for subscription towards publication, whether in print or in electronic to be adjusted against receipt of such publications

Explanation: For the purpose of this sub-clause the amount shall be deemed to be deposits on the expiry of 15 days from the date they become due for refund.

- (xiii) Any amount brought in by the promoters of the company by way of unsecured loan in pursuance of the stipulation of any lending financial institution or a bank subject to fulfilment of the following conditions:

- The loan is brought in pursuance of the stipulation imposed by the lending institutions on the promoters to contribute such finance and
- The loan is provided by the promoters themselves or by their relatives or by both and
- The exemption under this sub-clause shall be available only till the loans of financial institution or bank are repaid and not thereafter.

- (xiv) Any amount accepted by a Nidhi Company in accordance with the rules made under section 406 of the Act.

Explanation: For the purposes of this clause, any amount –

- Received by the company, whether in the form of instalments or otherwise, from a person with promise or offer to give returns, in cash or in kind, on completion of the period specified in the promise or offer, or earlier, accounted for in any manner whatsoever, or
- Any additional contributions, over and above the amount under item (a) above, made by the company as part of such promise or offer,

shall be considered as deposits unless specifically excluded under this clause.

- Any amount raised by issue of non-convertible debenture not constituting a charge on the assets of the company and listed on a recognized stock exchange as per applicable regulations made by Securities and Exchange Board of India.
- Any amount received by way of subscription in respect of a chit under the Chit Fund Act.
- Any amount received by the company under any *collective investment scheme* in compliance with regulations framed by the SEBI.
- An amount of Rs. 25 lakh or more received by a start-up company, by way of a convertible note (convertible into equity shares or repayable within a period not exceeding 5 years from the date of issue) in a single tranche, from a person.

Explanation:

“Start-up company” means a private company incorporated under the Companies Act, 2013 or Companies Act, 1956 and recognized as such by the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry.

“Convertible note” means an instrument evidencing receipt of money initially as a debt, which is repayable at the option of the holder, or which is convertible into such number of equity shares of the start-up company upon occurrence of specified events and as per the other terms and conditions agreed to and indicated in the instrument.

- Any amount received by a company from Alternate Investment Funds, Domestic Venture Capital Funds and Mutual Funds registered with the SEBI in accordance with regulations made by it.

Que. No. 3A] Whether following receipts by company amount to ‘deposit’ as per Rule 2(1)(C) under the Companies (Acceptance of Deposits) Rules, 2014.

- Amount received from Central Government.
- Amount received as loan from banking company.
- Amount received on issue of commercial paper.
- Deposits received from another company.
- Amount received from HUF.
- Amount received as share application money for 90 days or more and still no shares are allotted to the applicant.
- Amount received from Mr. Neel, a director of company who in turn has borrowed amount from his relative.
- Amount received on issue of secured debentures.
- Amount received on issue of convertible debentures which are to be converted in to shares after 12 years.
- Amount received as advance against supply of goods where goods is to be supplied after 15 months.
- Security deposit received from the employee ₹ 1,50,000. Salary of the employee is ₹ 10,000 p.m.

Ans.:

| Particulars | Deposit or not | Reason |
|---|----------------|--|
| Amount received from Central Government | No | Specifically excluded under the definition of ‘Deposit’ as per Rule 2(1)(c)(i). |
| Amount received as loan from banking company. | No | Specifically excluded under the definition of ‘Deposit’ as per Rule 2(1)(c)(iii). |
| Amount received on issue of commercial paper | No | Specifically excluded under the definition of ‘Deposit’ as per Rule 2(1)(c)(v). |
| Deposits received from another company. | No | Specifically excluded under the definition of ‘Deposit’ as per Rule 2(1)(c)(vi). |
| Amount received from HUF | Yes | Not excluded under the definition of ‘Deposit’. |
| Amount received as share application money for 90 days or more and still no shares are allotted to the applicant. | Yes | If the securities for which application money or advance for such securities was received cannot be allotted within 60 days from the date of receipt of the application money or advance for such securities and such application money or advance is not refunded to the subscribers within 15 days from the date of completion of 60 days, such amount shall be treated as a deposit under these rules |
| Amount received from Mr. Neel, a director of company who in turn has borrowed amount from his relative. | Yes | Any amount received from director of the company does not to ‘deposit’. However, the director from whom money is received, furnishes to the company at the time of giving the money, a declaration in writing to the effect that the amount is not being given out of funds acquired by him by borrowing or accepting loans or deposits from others. As director as deposited money with company by borrowing from relative, it amounts to ‘deposit’ as per Rule 2(1)(c)(viii). |
| Amount received on issue of secured debentures | No | Specifically excluded under the definition of ‘Deposit’ as per Rule 2(1)(c)(ix). |

| Particulars | Deposit or not | Reason |
|--|----------------|---|
| Amount received on issue of convertible debentures which are to be converted into shares after 12 years. | Yes | Amount received on issue of convertible debentures which are to be converted within a period of 10 years does not amount to 'deposit'. In given case conversion period is more than 10 years and hence it amounts to 'deposit'. |
| Amount received as advance against supply of goods where goods are to be supplied after 15 months | Yes | Amount received as advance against supply of goods up to 1 year does not amount to deposit. In given case advance is received for period exceeding 1 year and hence it will amount to 'deposit'. |
| Security deposit received from the employee ₹ 1,50,000. Salary of the employee is ₹ 10,000 p.m. | Yes | Security deposit received from an employee not exceeding his annual salary does not amount to deposit. In given case since security deposit exceeds his annual salary it amounts to 'deposit'. |

Que. No. 3B] Prism Ltd. has accepted ₹ 10 lakhs as advance towards the supply of goods to certain parties. As per the agreement, the company will supply the goods after two years from the date of deposit. Later on, internal auditors qualified their report on the ground that the company has violated the provisions of the Companies Act, 2013. Directors explained that this is required to complete the order. Examining the relevant provisions of the Companies Act, 2013 state whether the explanation given by the directors is justified.

CS (Executive) – June 2016 (4 Marks)

Ans.: As per Section 2(31), deposit includes any receipt of money by way of deposit or loan in any other form by a company, but does not include such categories of amount as may be prescribed in consultation with the RBI.

As per Rule 2(1)(c)(xii)(d) of the Companies (Acceptance of Deposits) Rules, 2014, deposit does not include any amount received in the course of or for the purposes of the business of the company as an advance for the supply of goods or provision of services provided that such advance is appropriated against supply of goods or provision of services within a period of 365 days from acceptance of such advance.

As per facts given in case Prism Ltd. has accepted ₹ 10 lakh as advance towards the supply of goods to certain parties. As per the agreement, the company will supply the goods after two years from the date of deposit.

Thus, company has accepted advance for more than 365 days for the supply of goods and hence it is 'Deposit' as per Section 2(31) read with Rule 2(1)(c)(xii)(d) of the Companies (Acceptance of Deposits) Rules, 2014. The Company has defaulted in accepting deposit without complying the provision and hence remark passed by internal auditor is correct and explanation given by the director is not sufficient.

Que. No. 4] Unsecured loans from promoters are always treated as exempt deposits. Comment.

CS (Inter) – June 2002 (5 Marks)

Ans.: As per Rule 2(b)(xi), deposit does not include any amount brought in by the promoters by way of unsecured loans in pursuance of stipulations of financial institutions subject to the fulfilment of the following conditions, namely:

- The loans are brought in pursuance of the stipulation imposed by the financial institutions in fulfilment of the obligation of the promoters to contribute such finance;
- The loans are provided by the promoters themselves and/or by their relatives, and not from their friends and business associates; and
- The exemption under this sub-clause shall be available only till the loans of financial institutions are repaid and not thereafter.

Que. No. 5] Specify the conditions subject to which the following are treated as exempt deposits:

- Unsecured loans from promoters.
- Debenture secured by secured by a first charge
- Deposit from directors of public company

CS (Inter) – June 2001 (6 + 2 + 2 = 8 Marks)

CS (Inter) – June 2003 (2 + 2 = 4 Marks)

Ans.:

- Unsecured loans from promoters: See the answer of Question No. 4
- Debenture secured by mortgaged property: As per Rule 2(b)(ix), deposit does not include any amount raised by the issue of bonds or debentures secured by a first charge or a charge ranking *pari passu* with the first charge on any assets referred to in Schedule III of the Act excluding intangible assets of the company or bonds/debentures compulsorily convertible into shares of the company within 5 years. If such bonds or debentures are secured by the charge of any assets referred to in Schedule III of the Act excluding intangible assets, the amount of such bonds or debentures shall not exceed the market value of such assets as assessed by a registered valuer.
- Deposit from directors of public company: Deposit from the directors of public company is not exempt under clause of Rule 2(b). Hence, it is covered by the definition of 'Deposit'.

Que. No. 5A] Issue of unsecured debentures by a company to another company, where the debentures have an option for compulsory conversion into equity shares within seven years, cannot be termed as deposits.

CS (Executive) – Dec 2016 (5 Marks)

Ans.: Rule 2(c)(ix) of the Companies (Acceptance of Deposits) Rules, 2014 excludes from the definition of Deposits the amounts raised by the issue of bonds or debentures secured by a first charge or a charge ranking *pari passu* with the first charge on any assets referred to in Schedule III excluding intangible assets of the company or bonds or debentures compulsorily convertible into shares of the company within 10 years. This exclusion essentially signifies that a secured debenture, regardless of its tenure or convertibility, shall be exempt from the purview of deposits.

However, an unsecured debenture shall only be exempt from the purview of deposits as long as it is compulsorily convertible within 10 years. This would mean that non-convertible unsecured debentures would be considered as deposits.

Further, it may be noted that Rule 2(c)(vi) exempts from the definition of deposits any amount received by a company from another company.

Thus, issue of unsecured debentures by company to another company for a given case does not amount to deposit under the Companies (Acceptance of Deposits) Rules, 2014.

Que. No. 6] Distinguish between: Deposits & Loan CS (Inter) – June 2002 (5 Marks)

Ans.: There have been a number of judicial decisions bringing out distinction between a loan and a deposit. In *Annamalai vs. Veerappa* AIR 1956 SC 12, it was held that the term 'deposit' and 'loan' are not synonymous and whether a transaction is a deposit or loan does not merely depend on the terms of document, but has to be judged from the intention of the parties.

In a sense, deposit is also a loan with this difference that a loan is repayable the minute it is incurred. In the case of deposit the repayment will depend on the maturity date fixed therefore or the terms of agreement relating to the demand on the making of which the deposit becomes

payable. In other words, unlike a loan, there is no immediate obligation to repay in the case of deposits.

Under the Limitation Act, 1963, the periods when limitation would begin in case of loan and in case of deposits are provided for differently. In the former case the limitation commences from the date when the loan is made, whereas in the latter from the date when the demand is made. Therefore, the distinction between a loan and a deposit is fine but appreciable.

Que. No. 7] Distinguish between: Deposit & Debenture

Ans.: According to Section 2(30), debenture includes debenture stock, bonds and any other securities of a company whether constituting a charge on the assets of the company or not. A debenture is a document which either creates or acknowledges a debt. A debenture may be secured or unsecured. Where the debenture is unsecured, it will surely fall within the definition of deposit. It is only the debentures which satisfy the conditions stipulated in Rule 2(b)(ix) of the Companies (Acceptance of Deposits) Rules, 2014, which are excluded from the definition of deposits.

Que. No. 8] Who is depositor?

Ans.: Depositor [Rule 2(1)(d)]: Depositor means-

- (i) Any member of the company who has made a deposit with the company in accordance with Section 73(2) or
- (ii) Any person who has made a deposit with a public company in accordance with Section 76 of the Act.

Que. No. 9] State the provisions relating to acceptance of deposit by 'eligible companies'.

Ans.: Acceptance of deposits from public by eligible companies [Section 76]: A public company, having such net worth or turnover as may be prescribed, may accept deposits from persons other than its members subject to compliance with the requirements of Section 73(2) and subject to such rules as the Central Government may, in consultation with the RBI, prescribe.

Credit rating to be obtained: Such a company shall be required to obtain the rating (including its net worth, liquidity and ability to pay its deposits on due date) from a recognized credit rating agency for informing the public the rating given to the company at the time of invitation of deposits from the public which ensures adequate safety and the rating shall be obtained for every year during the tenure of deposits.

Creation of charge: Every company accepting secured deposits from the public shall within 30 days of such acceptance, create a charge on its assets of an amount not less than the amount of deposits accepted in favour of the deposit holders in accordance with such rules as may be prescribed.

Eligible Company [Rule 2(1)(e)]: Eligible Company means a public company having a net worth of not less than Rs. 100 Crore or a turnover of not less than Rs. 500 Crore and which has obtained the prior consent of the company in general meeting by means of a special resolution and also filed the said resolution with the ROC and with the RBI before making any invitation to the public for acceptance of deposits.

However, an eligible company, which is accepting deposits within the limits specified in Section 180(1)(c), may accept deposits by means of an ordinary resolution.

As per Section 180(1)(c) the board of directors of the company can borrow money, where the money to be borrowed, together with the money already borrowed by the company will exceed aggregate of its paid-up share capital and free reserves, apart from temporary loans obtained from the company's bankers in the ordinary course of business.

Que. No. 10] Can a company accept or renew any deposit which is repayable on demand?

Ans.: Terms and conditions of acceptance of deposits by companies [Rule 3(1)]: No company and no eligible company shall accept or renew any deposit, whether secured or unsecured, which is repayable on demand or upon receiving a notice, within a period of less than 6 months or more than 36 months from the date of acceptance or renewal of such deposit.

Exceptions: A company may, for the purpose of meeting any of its short-term requirements of funds, accept or renew such deposits for repayment earlier than 6 months from the date of deposit or renewal, subject to the condition that-

- (a) Such deposits shall not exceed 10% of the aggregate of the paid up share capital and free reserves of the company, and
- (b) Such deposits are repayable not earlier than 3 months from the date of such deposit or renewal thereof.

Que. No. 11] A single fixed deposit holder, after marriage, applied for adding the name of his wife as joint holder. The company refused to do so. Comment.

CS (Executive) - June 2011 (4 Marks)

Ans.: As per Rule 3(2), where depositors so desire, deposits may be accepted in joint names not exceeding three, with or without any of the clauses, namely, "Jointly", "Either or Survivor", "First named or Survivor", "Anyone or Survivor". Thus, company cannot refuse to add the name of wife of deposit holder.

Que. No. 12] Write a short note on: Ceiling limits for acceptance of deposits

A company cannot raise deposits for an unlimited amount. Comment.

CS (Inter) - Dec 2006 (5 Marks)

Ans.: Ceiling for acceptance of deposits [Rule 3(3)]: No company shall accept or renew any deposits if the amount of deposits together with the amount of other deposits outstanding as on the date of acceptance or renewal of such deposits exceeds 35% of the aggregate of the paid-up share capital, free reserves and securities premium account of the company.

However, a private company may accept from its members monies not exceeding 100% of aggregate of the paid up share capital, free reserves and securities premium account and such company shall file the details of monies so accepted to the Registrar in such manner as may be specified.

Ceiling for acceptance of deposits for eligible company [Rule 3(4)]: No eligible company shall accept or renew:

- (a) Any deposit from its members, if the amount of such deposit together with the amount of deposits outstanding as on the date of acceptance or renewal of such deposits from members exceeds 10% of the paid up share capital, free reserves and securities premium account of the company.
- (b) Any other deposit, if the amount of such deposit together with the amount of such other deposits, outstanding on the date of acceptance or renewal exceeds 25% aggregate of the paid up share capital, free reserves and securities premium account of the company.

Deposits by Government Companies [Rule 3(5)]: No Government company eligible to accept deposits shall accept or renew any deposit, if the amount of deposits together with the amount of other deposits outstanding as on the date of acceptance or renewal exceeds 35% of the aggregate of the paid up share capital, free reserves and securities premium account of the company.

Que. No. 13] As per the audited balance sheet of Dowell Ltd. as at 31st March, 2015, the details of share capital and reserves and surplus are as under.

| | ₹ in crores |
|--|-------------|
| Equity Share Capital | 300.00 |
| Reserves & Surplus: | |
| Profit & Loss A/c | 62.75 |
| General Reserves | 12.00 |
| Securities Premium | 25.00 |
| Break up of unsecured loans as at 31st March, 2015 in given below: | |
| Deposits from public | 13.00 |
| Deposits from shareholders | 3.62 |

Compute the limits up to which Dowell Ltd. can accept further deposits from public & shareholders. Assume that Dowell Ltd. is 'Eligible Company'.

CS (Inter) - Dec 1999 (8 Marks)

Ans.: Calculation of paid-up capital and free reserve as per balance sheet as at 31.3.2015.

| Particulars | ₹ in crores |
|--------------------------------|-------------|
| Equity Share Capital | 300.00 |
| Profit & Loss Account | 62.75 |
| General Reserves | 12.00 |
| Securities premium | 25.00 |
| Paid-up capital & free reserve | 399.75 |

Calculation of acceptance of deposit from shareholder and from public: ₹ in crores

| Particulars | From Shareholders | From public |
|--|-------------------|-------------|
| Limit up to which Dowell Ltd. can accept deposits | | |
| - 10% from shareholder & 25% from public of ₹ 399.75 lakhs | 39.975 | 99.9375 |
| - Existing deposits as at 31 st March, 2015 | (3.62) | (13.00) |
| Further deposits that can be accepted. | 36.355 | 86.9375 |

Que. No. 14] As per the audited balance sheet of Seelu Ltd. as at 31st March, 2015, the details of share capital and reserves and surplus are as under.

| | ₹ in crores |
|----------------------------|-------------|
| Equity Share Capital | 200 |
| Preference Share Capital | 50 |
| Reserves & Surplus: | |
| Profit & Loss A/c | 40 |
| General Reserves | 20 |
| Securities Premium | 15 |
| Revaluation Reserve | 25 |
| Capital Redemption Reserve | 10 |

Deferred revenue expenditure to the extent not written off as on 31st March 2015 is ₹ 0.50 crores.

Break up of unsecured loans as at 31st March, 2015 in given below:

| | |
|----------------------------|---|
| Deposits from public | 5 |
| Deposits from shareholders | 1 |
| Inter-corporate deposit | 6 |

This apart unsecured debenture as on 31st March, 2015 are as follows:

| | |
|---|---|
| Convertible debenture | 3 |
| (Convertible into equity shares within 31st December, 2015) | 2 |
| Non-convertible debenture | |

Compute the limits up to which Seelu Ltd. can accept further deposits from public & shareholders. CS (Inter) - Dec 2001 (12 Marks)

Ans.: Calculation of paid-up capital and free reserve as per balance sheet as at 31.3.2015.

| Particulars | ₹ in crores |
|----------------------------------|-------------|
| Equity Share Capital | 200 |
| Preference Share Capital | 50 |
| Profit & Loss Account | 40 |
| General Reserves | 20 |
| Securities premium | 15 |
| Capital redemption reserve | 10 |
| (-) Deferred revenue expenditure | (0.50) |
| Paid-up capital & free reserve | 334.50 |

Calculation of acceptance of deposit from shareholder and from public: ₹ in crores

| Particulars | From Shareholders | From public |
|---|-------------------|-------------|
| Limit up to which Dowell Ltd. can accept deposits | | |
| -10% from shareholder & 25% from public of ₹ 334.50 lakhs | 33.45 | 83.625 |
| -Existing deposits as at 31 st March, 2015 | (1.00) | (7.00) |
| Further deposits that can be accepted. | 32.45 | 76.625 |

Important Notes:

- Revaluation reserve is not free reserve hence will not be added while calculating paid-up capital and free reserve.
- Inter-corporate deposit will not be treated as deposit as per Rule 2(b).
- Unsecured non-convertible debenture are deposit as per Rule 2(b), hence will be treated as existing deposit.

Que. No. 15] As per the audited balance sheet of Hi-Fi Ltd. (an eligible company) as at 31st March, 2015, the details of share capital, reserves and surplus are as under:

| | ₹ in crores |
|---------------------------------|-------------|
| Equity share capital | 300.00 |
| Reserves and surplus: | |
| Profit & Loss A/c | 62.75 |
| General Reserves | 12.00 |
| Securities Premium | 25.00 |
| Capital Subsidy (Central Grant) | 10.00 |
| Revaluation Reserve | 30.00 |
| | 139.75 |

Break up of unsecured loans as at 31st March, 2015 in given below:

| | |
|------------------------------|--------------|
| Deposits from public | 13.00 |
| Deposits from shareholders | 3.62 |
| Inter-corporate deposits | 15.00 |
| Deferred sales tax liability | 28.63 |
| | <u>60.25</u> |

Compute the limits up to which Hi-Fi Ltd. can accept further deposits from public & shareholders. (Answer to the nearest rupees in crores) CS (Inter) - June 2005 (8 Marks)

Hint: Further deposits that can be accepted: From Shareholders - ₹ 37.355 crores, From Public - ₹ 89.4375 crores. "Capital Subsidy (Central Grant)" will be treated as part of paid-up capital & free reserve.

Que. No. 15A] Write a short note on: Ceiling on rate of interest & brokerage on deposits

Ans.: Ceiling on rate of interest on deposits [Rule 3(6)]: No company or any eligible company shall invite or accept or renew any deposits carrying a rate of interest or pay brokerage at a rate exceeding the maximum rate of interest or brokerage prescribed by the RBI for acceptance of deposits by non-banking financial companies.

Who is eligible to receive brokerage [Explanation to Rule 3(6)]: Only the person who is authorized, in writing, by a company to solicit deposits on its behalf and through whom deposits are actually procured will be entitled to the brokerage. Payment of brokerage to any other person for procuring deposits shall be deemed to be in violation of these Rules.

Prohibition on alteration of the terms & conditions of the deposit [Rule 3(7)]: The company shall not reserve to itself either directly or indirectly a right to alter, to the prejudice or disadvantage of the depositor, any of the terms and conditions of the deposit, deposit trust deed and deposit insurance contract after circular or circular in the form of advertisement is issued and deposits are accepted.

Que. No. 15B] Board of directors of Green Field Ltd. decides to accept deposits from the public at a compound interest rate of 12% per annum. Examining the provisions of the Companies Act, 2013, advise whether the Board can go ahead with its proposal.

CS (Executive) - June 2016 (4 Marks)

Ans.: As per Rule 3(6) of the Companies (Acceptance of Deposit) Rules, 2014, no company or any eligible company shall invite or accept or renew any deposits carrying a rate of interest or pay brokerage at a rate exceeding the maximum rate of interest or brokerage prescribed by the RBI for acceptance of deposits by non-banking financial companies.

Thus, Green Field Ltd. can accept deposit at a compound interest rate provided that rate of interest should not exceed the rate prescribed by the RBI for acceptance of deposits by non-banking financial companies.

Que. No. 15C] Every company accepting deposit from the public is required to obtain credit rating from the credit rating agency. Comment.

Ans.: Credit rating for acceptance of deposits [Rule 3(8)]: Every eligible company shall obtain, at least once in a year, credit rating for deposits accepted by it and a copy of the rating shall be sent to the Registrar of Companies along with the return of deposits in Form DPT-3.

The credit rating shall not be below the minimum investment grade rating or other specified credit rating for fixed deposits, from any one of the approved credit rating agencies as specified for NBFC's in the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998, issued by the RBI, as amended from time to time.

Que. No. 16] Every advertisement inviting deposit public must contain certain particulars. What are those particulars?

CS (Inter) - June 2000 (9 Marks), Dec 2002 (10 Marks)

What is the period of validity of such advertisement? CS (Inter) - June 2000 (2 Marks)

Can Company accept deposit without issuing such advertisement? Explain position with reference to relevant rules.

CS (Inter) - June 2000 (5 Marks), June 2003 (6 Marks)

A company can accept deposits without issuing advertisement. Comment.

CS (Inter) - June 2007 (5 Marks), June 2008 (5 Marks)

Every company intending to invite deposits from public u/s 58A must issue an advertisement which shall be signed by all the directors of the company.

CS (Executive) - Dec 2011 (5 Marks)

Ans.: Form and particulars of advertisements/circulars [Rule 4]:

- (1) Every company intending to invite deposit from its members shall issue a circular Form No. DPT. 1 to all its members by registered post with acknowledgement due or speed post or by electronic mode. In addition to issue of circular, the circular may be published in an English newspaper and in vernacular language newspaper.
- (2) Every eligible company intending to invite deposits shall issue a circular in the form of an advertisement in Form No. DPT. 1 for the purpose in English newspaper and in vernacular language newspaper.
- (3) Every company inviting deposits from the public shall upload a copy of the circular on its website.
- (4) Any circular or a circular in the form of advertisement inviting deposits has to be issued in the authority and in the name of the board of directors of the company.
- (5) A copy of circular or a circular in the form of advertisement has to be delivered to the ROC 30 days before the date of issue. It has to be signed by a majority of the directors or their agents, duly authorized by them in writing.
- (6) A circular or circular in the form of advertisement issued shall be valid until the expiry of 6 months from the date of closure of the financial year in which it is issued or until the date on which the financial statement is laid before the company in AGM or, where the AGM for any year has not been held, the latest day on which AGM should have been held, whichever is earlier. A fresh circular or circular in the form of advertisement shall be issued, in each succeeding financial year, for inviting deposits during that financial year.
- (7) The date of the issue of the newspaper in which the advertisement appears shall be taken as the date of issue of the advertisement and the effective date of issue of circular shall be the date of dispatch of the circular.

Que. No. 17] What are provisions made under the Companies (Acceptance of Deposit) Rules, 2014 relating to "Deposit Insurance"?

Ans.: Deposit Insurance [Rule 5]:

- (1) Every company and every other eligible company inviting deposits shall enter into a contract for providing deposit insurance at least 30 days before the issue of circular or advertisement or at least 30 days before the date of renewal. For this purposes the amount as specified in the deposit insurance contract shall be deemed to be the amount in respect of both principal amount and interest due thereon.
- (2) The deposit insurance contract shall specifically provide that in case the company defaults in repayment of principal and interest, the depositor shall be entitled to the repayment of principal and the interest by the insurer up to the aggregate monetary ceiling as specified in the contract.

In the case of deposit and interest not exceeding ₹ 20,000, the deposit insurance contract shall provide for payment of the full amount of the deposit and interest.

In the case of deposit and the interest in excess of ₹ 20,000, the deposit insurance contract shall provide for payment of an amount not less than ₹ 20,000 for each depositor.

- (3) The amount of insurance premium on deposits shall be borne by the company and shall not be recovered from the depositors.
- (4) If any default is made by the company in complying with the terms and conditions of the deposit insurance contract which makes the insurance cover ineffective, the company shall either rectify the default immediately or enter into a fresh contract within 30 days.

The amount of deposits covered under the deposit insurance contract and interest payable shall be repaid within the next 15 days.

If a company does not repay the amount of deposits within said 15 days it shall pay 15% interest p.a. for the period of delay and shall be treated as having defaulted and shall be liable to be punished in accordance with the provisions of the Act.

Que. No. 18] What are the provisions made under the Companies (Acceptance of Deposit) Rules, 2014 for "Creation of Security" for deposit accepted by the companies?

Ans.: Creation of Security [Rule 6]:

- (1) Every company and every eligible company inviting secured deposits shall provide for security by way of a charge on its assets as referred to in Schedule III excluding intangible assets of the company for the due repayment of deposit and interest which shall not be less than the amount remaining unsecured by the deposit insurance. In the case of deposits which are secured by the charge on the assets referred to in Schedule III excluding intangible assets, the amount of such deposits and the interest payable shall not exceed the market value of such assets as assessed by a registered valuer.

It is clarified that the company shall ensure that the total value of the security either by way of deposit insurance or by way of charge or by both on company's assets shall not be less than the amount of deposits accepted and the interest payable thereon.

It is also clarified that pending notification, valuation of stocks, shares, debentures, securities etc. shall be conducted by an independent merchant banker who is registered with the SEBI or an independent practicing CA having a minimum experience of 10 years.

- (2) The security (not being in the nature of a pledge) for deposits shall be created in favour of a trustee for the depositors on:
 - (a) Specific movable property of the company, or
 - (b) Specific immovable property of the company wherever situated, or any interest therein.

Que. No. 19] Write a short note on: Appointment of deposit trustees

Ans.: Appointment of deposit trustees [Rule 7]: No company or any eligible company shall issue a circular or advertisement inviting secured deposits unless the company has appointed one or more deposit trustees for depositors for creating security for the deposits. A written consent shall be obtained from the deposit trustee before their appointment and a statement shall appear in the circular or circular in the form of advertisement with reasonable prominence to the effect that the deposit trustee have given their consent to the company to be so appointed.

Execution of deposit trust deed before issuing advertisement: The company shall execute a deposit trust deed in Form No. DPT. 2 at least 7 days before issuing the circular or circular in the form of advertisement.

Certain persons not to be appointed as deposit trustees: Following person shall not be appointed as a trustee for the deposit holders:

- (a) Who is a director, KMP or any officer or employee of the company or of its holding, subsidiary or associate company or a depositor in the company.
- (b) Who is indebted to the company, or its subsidiary or its holding or associate company or a subsidiary of such holding company.
- (c) Who has any material pecuniary relationship with the company.

(d) Who has given guarantee in respect of principal debts secured by the deposits or interest.

(e) Who is related to any person specified in clause (a) above.

Removal of deposit trustees: No deposit trustee may be removed from office after the issue of circular or advertisement and before the expiry of his term except with the consent of all the directors present at a meeting of the board. In case the company is required to appoint independent directors, at least one independent director shall be present in such meeting of the Board.

Que. No. 20] Write a short note on: Duties of Deposit Trustees

Ans.: Duties of Deposit Trustees [Rule 8]: It shall be the duty of every deposit trustee -

- ◆ To ensure that the assets and deposit insurance are sufficient to cover the repayment of the principal and interest on deposits.
- ◆ To satisfy himself that the circular or advertisement inviting deposits does not contain any information which is inconsistent with the deposit scheme or trust deed and is in compliance with the Rules and provisions of the Act.
- ◆ To ensure that the company does not commit any breach of covenants and provisions of the trust deed.
- ◆ To take reasonable steps to procure a remedy for any breach of covenants of the trust deed or the terms of invitation of deposits.
- ◆ To take steps to call a meeting of deposit holders as and when such meeting is required to be held.
- ◆ To supervise the implementation of the conditions regarding creation of security for deposits and the terms of deposit insurance.
- ◆ To do such acts as are necessary in the event the security becomes enforceable.
- ◆ To carry out acts necessary for the protection of the interest of depositors and to resolve their grievances.

Que. No. 21] Write a short note on: Meeting of depositors through deposit trustee

Ans.: Meeting of depositors through deposit trustee [Rule 9]: The meeting of all the depositors shall be called by the deposit trustee on:

- (1) Requisition in writing signed by at least 1/10th of the depositors in value for the time being outstanding.
- (2) The happening of any event, which constitutes a default or which in the opinion of the deposit trustee, affects the interest of the depositors.

Que. No. 22] Write a short note on: Form of application for deposits

Ans.: Form of application for deposits [Rule 10]:

- (i) No company shall accept, or receive any deposit, whether secured or unsecured, unless an application in prescribed form is submitted by the intending depositor.
- (ii) The application shall contain a declaration by the intending depositor to the effect that the deposit is not being made out of any money borrowed by him from any other person.

Que. No. 23] Write a short note on: Nomination

Ans.: Nomination [Rule 11]: A depositor may, at any time, make a nomination and the provisions of Section 72 shall apply to the nomination made under this Rule.

Que. No. 24] Write a short note on: Furnishing of deposit receipts to depositors.

A depositor had deposited some money in a cumulative scheme of an eligible non-banking non-financial company registered under the provisions of the Companies Act, 2013, but he did not receive the fixed deposit receipts until 42 days of the date of deposit. However he got it on 47th day. State with reasons whether an infringement of law is involved in this case.

CS (Inter) - June 2004 (6 Marks)

Ans.: Furnishing of deposit receipts to depositors [Rule 12]: Every company shall furnish to the depositor or his agent a deposit receipt within a period of 2 weeks from the date of receipt of money or realization of cheques on acceptance of a deposit.

Deposit receipt shall be signed by an officer of the company duly authorized by the Board in this behalf and shall state

- Date of deposit,
- Name and address of the depositor,
- Amount received by the company as deposit,
- Rate and periodicity of interest payable
- Date on which the deposit is repayable.

Que. No. 25] Write a short note on: Maintenance of liquid assets and creation of Deposit Repayment Reserve Account

Ans.: Maintenance of liquid assets and creation of Deposit Repayment Reserve A/c [Rule 13]: Every company and every eligible company shall on or before the 30th day of April of each year, deposit the sum which shall not be less than 20% of the amount of its deposits maturing during the following financial year. Such sum can be deposited in any scheduled bank.

The amount so deposited shall not be utilized for any purpose other than for the repayment of deposits.

The amount remaining deposited shall not at any time fall below 15% of the amount of deposits maturing, until the end of the current financial year and the next financial year.

Que. No. 26] State the requirements relating to keeping of "register of deposits" under the Companies (Acceptance of Deposit) Rules, 2014.

Ans.: Registers of deposits [Rule 14]:

- (1) Every company accepting deposits shall keep at its registered office registers for deposits accepted or renewed. Following particulars are required to be entered in such deposit register:
 - Name, address and PAN of the depositors
 - Particulars of guardian, in case of a minor
 - Particulars of the nominee
 - Deposit receipt number
 - Date and amount of each deposit
 - Duration of the deposit and the date on which each deposit is repayable
 - Rate of interest
 - Due dates for payment of interest
 - Mandate and instructions for payment of interest and for non-deduction of tax at source, if any
 - Date or dates on which payment of interest will be made
 - Details of deposit insurance including extent of deposit insurance
 - Particulars of other security/charge created
 - Any other particulars relating to the deposit;
- (2) Entries in the register shall be made within 7 days from the date of issuance of the deposit receipt. Such entries shall be authenticated by a director or Company Secretary of the company or by any other authorized officer.
- (3) The register shall be preserved in good order for a period of not less than 8 years from the financial year in which the latest entry is made in the register.

Que. No. 27] What are the provisions of the Companies (Acceptance of Deposit) Rules, 2014 for premature repayment of deposits?

CS (Inter) – Dec 2000 (5 Marks), Dec 2003 (6 Marks)

Shine Well Ltd. has accepted deposits from the public under the Companies (Acceptance of Deposits) Rules, 2014. The company now decided to repay some of its deposits before maturity. Can the company do so? If yes, what are the conditions attached there to?

CS (Executive) – June 2011 (4 Marks)

Ans.: General provisions regarding premature repayment of deposits [Rule 15]: When a company makes a repayment of deposits, on the request of the depositor, after the expiry of a period of 6 months from the date of such deposit, the rate of interest payable on such deposit shall be reduced by 1%.

When a depositor is permitted to renew his deposit, before the expiry of the period for which deposit was accepted by the company, for availing of a higher rate of interest, the company shall pay interest to depositor at the higher rate if such deposit is renewed in accordance with the other provisions of these rules and for a period longer than the unexpired period of the deposit. Where the period for which the deposit had run contains any part of a year, then, if such part is less than 6 months, it shall be excluded and if such part is 6 months or more, it shall be reckoned as one year.

Que. No. 28] Your company has accepted the deposits of ₹ 50,45,000. Advise the Managing Director of your company regarding filing of return of deposits?

Ans.: Return of deposits to be filed with the Registrar [Rule 16]: Every company shall on or before the 30th day of June, of every year, file with the Registrar, a return in Form No. DPT. 3 along with the prescribed fee and furnish the information contained therein as on the 31st day of March of that year duly audited by the auditor of the company.

Que. No. 28A] What types of disclosures are required to be made in financial statement regarding acceptance of deposit by the companies?

Ans.: Disclosures in the financial statement [Rule 16A]: Every company, other than a private company, shall disclose in its financial statement, by way of notes, about the money received from the director.

Every private company shall disclose in its financial statement, by way of notes, about the money received from the directors, or relatives of directors.

Que. No. 29] Write a short note on: Penal rate of interest on deposits

Ans.: Penal rate of interest [Rule 17]: Every company shall pay a penal rate of interest of 18% p.a. for the overdue period in case of deposits, whether secured or unsecured, matured and claimed but remaining unpaid.

Que. No. 30] Sun-beam Ltd. failed to pay interest on repayment of deposits. One depositor approached the consumer forum with the request to issue order against the company for payment of interest on deposits. The company contended that the consumer forum was not a proper authority to issue such directions. Advise the company suitably.
CS (Executive) – Dec 2014 (8 Marks)

Ans.: In Neela Raje vs. Amogh Industries RP No. 409 of the 1992 dated 26.8.1993, 840 12 CLA 90 (NCDRC), the National Commission was faced with a query as to whether a complaint lodged in regard to the failure to pay interest on repayment of the principal amount on the maturity of a deposit by a company could be entertained by a consumer forum.

The commission pointed out that after the Amendment Act, 1993, a consumer forum can direct payment of amounts due to a depositor under the provisions of Section 14 of the Consumer Protection Act, 1986.

Thus, the contention of Sun-beam Ltd. is not valid.

CHAPTER 20

ACCOUNTS & AUDIT

This Chapter Covers:

- Requirement of keeping books of account.
- Maintenance of costing records.
- Inspection of books of account.
- Statutory books and statistical books.
- Financial statements.
- Directors responsibility statement.
- Accounts of holding and subsidiary company.
- Appointment of auditor.
- Qualifications and disqualifications of Auditor.
- Remuneration of auditor and their term of office.
- Resignation and removal of auditors.
- Auditors of government companies.
- Rights, powers, duties and liabilities of auditors.
- Audit of branch accounts.
- Notes on accounts and its contents.

BOOKS OF ACCOUNT

Que. No. 1] Define the term 'books of account'

Ans.: Books of Account [Section 2(13)]: Books of account includes records maintained in respect of -

- (i) All sums of money received and expended
- (ii) All sales and purchases of goods and services rendered

- (iii) Assets and liabilities
- (iv) Costing records (in case of specified companies)

Que. No. 2] Define the term 'Financial Statement'

Ans.: Financial Statement [Section 2(40)]: Financial statement in relation to a company, includes -

- (i) Balance Sheet
- (ii) Profit & Loss A/c or Income & Expenditure A/c
- (iii) Cash Flow Statement
- (iv) Statement of changes in equity
- (v) Explanatory notes annexed to financial statement

With respect to OPC, Small Company and Dormant Company financial statement do not include the Cash Flow Statement.

Que. No. 3] What are the provisions under the Companies Act, 2013 regarding keeping of books of account of a company? CS (Inter) - June 2000 (5 Marks)

A company having its registered office in New Delhi wants to maintain its books of account at its factory in Kolkata. Comment. CS (Inter) - June 2001 (4 Marks)

Ans.: Keeping of books of account & financial statement [Section 128(1)]: Every company shall prepare and keep books of account and other relevant books and papers and financial statement for every financial year.

Such books of account should give a *true and fair view* of the state of the affairs of the company. Books of account shall be kept on accrual basis and according to the double entry system of accounting.

Every company shall also keep books of account of its branch office which should explain the transactions effected both at the registered office and its branches.

The company may keep books of account or other relevant papers in electronic mode in prescribed manner.

Que. No. 3A] Board of directors of KM Ltd. proposes to transfer 11.33% of the net profits of the company for the financial year 2016-2017 to general reserves. Examining the provisions of the Companies Act, 2013 advise the Board whether it can go ahead with its proposal.

CS (Executive) - Dec 2016 (4 Marks)

Ans.: Transfer to reserve [First proviso to Section 128(1)]: A company may, before the declaration of any dividend in any financial year, transfer such percentage of its profits for that financial year as it may consider appropriate to the reserves of the company.

Thus, board of directors of KM Ltd. may transfer 11.33% of the net profit to general reserve.

Que. No. 4] Write a short note on: True and fair view

CS (Executive) - Dec 2011 (4 Marks)

Ans.: According to Section 128(1), every company shall prepare and keep at its registered office books of account and other relevant books and papers and financial statement for every financial year which give a *true and fair view* of the state of the affairs of the company.

The books and papers and financial statement are said to be give a *true and fair view*:

- If proper books of account as required by law, have been kept by the company

- If books of account are kept on accrual basis and according to double entry system of accounting
- If the accounts of the company give the information required by the Act in the manner so required
- If the balance sheet and profit and loss accounts are drawn up in a format and in accordance with the provisions of the Act and in the form provided in Schedule III
- If the financial position and working results of the company are stated clearly
- If any material change in the method of accounting and the effect thereof on the financial position of the company is clearly indicated
- If there is a proper and full disclosure of the financial position of the company
- If the financial statements comply with the accounting standards notified under Section 133
- If books of account are not suppressing any transaction nor contain any fictitious transaction

Que. No. 5] At which place the books of account of a company are required to be kept as per the provisions of the Companies Act, 2013?

A company having its registered office in New Delhi wants to maintain its books of account at its factory in Kolkata. Comment. CS (Inter) - June 2001 (4 Marks)

Ans.: Place at which books of account should be kept [Proviso to Section 128(1)]: Every company shall prepare and keep books of account and other relevant books and papers and financial statement at its registered office

However, all or any of the books of account and other relevant papers may be kept at such other place in India as the Board of Directors may decide. As per Rule 2A of the Companies (Accounts) Rules, 2014, the company shall, within 7 days file with the Registrar a notice giving the full address of that other place in Form No. AOC 5.

In case of branch, books of account can be kept at branch. However, proper summarized returns are required to be sent periodically by the branch office to the company at its registered office or the other place where books of account are kept.

Que. No. 6] Where a company has a branch office, whether in India or abroad, the original books of account, records, etc. of the branch office will have to be maintained in the registered office of the company. CS (Inter) - June 2013 (5 Marks)

Ans.: As per Section 128(1), in case of branch, books of account can be kept at branch. However, proper summarized returns are required to be sent periodically by the branch office to the company at its registered office or the other place where books of account are kept.

Thus, it is incorrect to say that the original books of account, records, etc. of the branch office will have to be maintained in the registered office of the company.

Que. No. 7] State the provisions of the Companies Act, 2013 relating to inspection of books of account?

Write a short note on: Right to inspection of books of account by a director or his duly appointed attorney. CS (Inter) - Dec 2006 (4 Marks)

A director has absolute right of inspection of books of account. Comment.

CS (Executive) - Dec 2013 (4 Marks)

Ans.: **Inspection of books of account [Section 128(3)]:** The books of account and other books and papers shall be open for inspection at the registered office of the company or at such other place in India by any director during business hours.

In the case of financial information maintained outside the country, copies of such financial information shall be maintained and produced for inspection by any director subject to prescribed conditions.

The inspection in respect of any subsidiary of the company shall be done only by the person authorized in this behalf by a resolution of the Board of Directors of holding company.

The officers and other employees of the company shall give to the person making inspection all assistance in connection with the inspection which the company may reasonably be expected to give.

Inspection of financial information maintained outside India [Rule 4 of the Companies (Accounts) Rules, 2014]:

- (1) The summarized returns of the books of account of the company kept and maintained outside India shall be sent to the registered office at quarterly intervals, which shall be kept and maintained at the registered office of the company and kept open to directors for inspection.
- (2) Where any other financial information maintained outside the country is required by a director, the director shall furnish a request to the company setting out the full details of the financial information sought, the period for which such information is sought.
- (3) The company shall produce such financial information to the director within 15 days of the date of receipt of the written request.
- (4) The financial information shall be sought for by the director himself and not by or through his power of attorney holder or agent or representative.

Inspection by other persons: Apart from directors of the company, following person can also inspect the books of account of the company:

- (1) Registrar of Company [Section 206]
- (2) Authorized officer of the Central Government [Section 206]
- (3) Officers of Serious Fraud Investigation Office (SFIO) [Section 212]

Regulation 89 of the Table F:

- (i) The Board shall from time to time determine whether and to what extent and at what times and places and under what conditions or regulations, the accounts and books of the company, or any of them, shall be open to the inspection of members not being directors.
- (ii) No member shall have any right of inspecting any account or book or document of the company except as conferred by law or authorised by the Board or by the company in general meeting.

Judicial Views:

- ♦ A director is entitled to take inspection of accounts personally or through an agent provided that there is no reasonable objection to the person chosen and the agent undertakes not to utilize the information obtained by him for any purpose other than the purpose of his principal. [*Vakharia vs. Supreme General Film Exchange Co. Ltd.*, (1948) 18 Com Cases 34 : AIR 1948 Bom 301]
- ♦ The petitioners (directors) wanted to exercise their right of inspection of books of account accompanied by a CA. The CLB allowed it subject to the undertaking being given by the CA that he would disclose the information obtained through inspection only to the petitioners and not to others. [*M.L. Thukral vs. Krone Communications Ltd.*, (1996) 86 Com Cases 643 (CLB-New Delhi)]

Que. No. 8] XYZ Ltd. was registered in the year 2014 under Companies Act, 2013. There are allegations that the 3 directors who manage the affairs of the company are siphoning the funds of the company. The company has not declared any dividends on the ground that company is incurring losses. Mr. A, who controls 51% of the share capital of the company sends a notice to the management that he will inspect the books of account to verify the allegations. Examine the right of Mr. A to carry out the inspection. State the persons who have the right to carry out the inspection under the Companies Act, 2013.

CA (Final) – May 2011 & Nov 2014 (5 Marks)

Ans.: As per provisions of the Companies Act, 2013 only following persons are entitled to inspect the books of account:

- Director of the company [Section 128(3)]
- Registrar of Company [Section 206]
- Authorized officer of the Central Government [Section 206]
- Officers of Serious Fraud Investigation Office (SFIO) [Section 212]

Thus, member of the company is not entitled to inspect the books of account.

Regulation 89 of the Table F makes the following provisions for inspection of books of account by the members:

- (i) The Board shall from time to time determine whether and to what extent and at what times and places and under what conditions or regulations, the accounts and books of the company, or any of them, shall be open to the inspection of members not being directors.
- (ii) No member shall have any right of inspecting any account or book or document of the company except as conferred by law or authorised by the Board or by the company in general meeting.

In the given case, Mr. A has not been authorized to inspect the books of account by the Board or by the members in the general meeting. Thus, Mr. A shall not have any right to inspect the books of account even if he holds 51% capital of the company.

Que. No. 9] Chatur is a director of Hopes Ltd., a public limited company, registered under the Companies Act, 2013. He wants to inspect the books of account and other books and papers of the company. Can he do so? Will your answer be different, if the director wants to inspect the books of account through an agent?

CA (Final) – May 2013 (5 Marks)

CS (Executive) – June 2011 (4 Marks)

Ans.: As per Section 128(3), the books of account and other books and papers shall be open for inspection at the registered office of the company or at such other place in India by any director during business hours.

In *Vakharia vs. Supreme General Film Exchange Co. Ltd.*, it was held that a director is entitled to take inspection of accounts personally or through an agent provided that there is no reasonable objection to the person chosen and the agent undertakes not to utilize the information obtained by him for any purpose other than the purpose of his principal.

Thus, Chatur will be allowed to inspect the books of account. He can also inspect the books of account through an agent provided that there is no reasonable objection to the person chosen and the agent undertakes not to utilize the information obtained by him for any purpose other than the purpose of his principal i.e. Chatur.

Que. No. 10] Vir is a director in DJA Ltd. (the company). The company holds 75% shares of MRN Ltd. Vir wants to inspect the books of MRN Ltd. Examining the provisions of the Companies Act, 2013 advise whether Vir, the director of DJA Ltd. can be allowed to inspect the books of MRN Ltd.

CS (Executive) – June 2015 (4 Marks)

Ans.: As per Section 128(3), the inspection in respect of any subsidiary of the company shall be done only by the person authorized in this behalf by a resolution of the Board of Directors of holding company.

Thus, Vir can inspect the books of account of MRN Ltd. (subsidiary of DJA Ltd.) if he is authorized by the resolution of the Board of Directors of DJA Ltd.

Que. No. 10A] Suresh, a member of Ruchi Ltd., wants to inspect the register of deposits maintained by the company as required under the provisions of the Companies Act, 2013. The company refused to provide the register for inspection without assigning any reason. Referring to the provisions of the Act, examine the validity of the company's refusal. What shall be your answer if the same Register is demanded by the statutory auditors of the company for inspection and for their audit?

CS (Executive) – Dec 2016 (4 Marks)

Ans.: A member of the company is not entitled to inspect the books of account of the company.

Register of deposit is part of the books of account and hence are not normally open for inspection by members of the company. Hence, Suresh a member of company cannot inspect the Register of deposit and company can refuse to inspection of the register without giving any reason.

The auditor enjoys the right of accessibility to books and records because he has to mention in his report whether proper books and records are maintained. Thus, company cannot refuse inspection of Register of deposit to statutory auditor.

Que. No. 11] It is not obligatory for every company to preserve its books of account.

CS (Executive) – June 2012 (5 Marks)

Ans.: **Preservation of books of account** [Section 128(5)]: Every company is required to preserve books of account along with vouchers of last 8 financial years.

However, if an investigation has been ordered in respect of the company, the Central Government may direct to keep the books of account for longer period.

Que. No. 12] Who are responsible for keeping the books of account a company? What are the liabilities imposed on them for their failure in this regard?

CS (Inter) – Dec 2004 (6 Marks)

Ans.: **Person responsible for keeping books of account** [Section 128(6)]: Following persons are responsible for maintaining the books of account:

- Managing director,
- Whole-time director in charge of finance
- Chief Financial Officer or
- Any other person charged by the Board with the duty of complying with the provisions of Section 128

Penalty: If person responsible for keeping and maintains of books of account fails to comply with the provisions of Section 128 he shall be punishable

- with imprisonment for a term which may extend to 1 year or

Ans.: The financial statements are required to be placed only at an AGM and *not at any other meeting*. The board of directors cannot delegate power to approve the financial statements to a committee of directors. In case the financial statements are not ready for laying at the AGM, the company may adjourn the said AGM to a subsequent date when the financial statements are expected to be ready for laying. This may be done by adopting a suitable resolution adjourning the said AGM to a specified date. However, the adjourned AGM should, be held within statutory time limit.

Que. No. 16] What are the provisions of the Companies Act, 2013 regarding re-opening of accounts on Court's or Tribunal's orders?

Ans.: Re-opening of accounts on Court's or Tribunal's orders [Section 130]: A company shall not re-open its books of account and not recast its financial statements, unless an application in this regard is made by the Central Government, the Income-tax authorities, SEBI, any other statutory regulatory body or authority or any person concerned and an order is made by a Court of competent jurisdiction or the Tribunal to the effect that -

- (i) The relevant earlier accounts were prepared in a fraudulent manner or
- (ii) The affairs of the company were mismanaged during the relevant period, casting a doubt on the reliability of financial statements

However, the Court or the Tribunal shall give notice to the Central Government, the Income-tax authorities, SEBI or any other statutory regulatory body or authority concerned or any other person concerned and shall take into consideration the representations, if any, made by such authorities.

The accounts so revised or re-cast shall be final.

Period of which accounts can be re-opened: No order shall be made in respect of re-opening of books of account relating to a period earlier than 8 financial years immediately preceding the current financial year. However, where a direction has been issued by the Central Government for keeping of books of account for a period longer than 8 years, the books of account may be ordered to be re-opened within such longer period.

Que. No. 17] What are the provisions of the Companies Act, 2013 regarding voluntary revision of financial statements or Board's report?

Ans.: Voluntary revision of financial statements or Board's report [Section 131]: If it appears to the directors of a company that the financial statement of the company or the report of the Board, do not comply with the provisions of Section 129 or 134, they may prepare revised financial statement or a revised report in respect of any of the 3 preceding financial years after obtaining approval of the Tribunal. Such application has to be made by the company in prescribed form and in prescribed manner and a copy of the order passed by the Tribunal shall be filed with the Registrar.

The Tribunal shall give notice to the Central Government and the Income tax authorities and shall take into consideration the representations before passing any order amending the financial statements.

Such revised financial statement or report shall not be prepared or filed more than once in a financial year.

The detailed reasons for revision of financial statement or report shall also be disclosed in the Board's report in the relevant financial year in which such revision is being made.

Limitation of revision of financial statements [Section 131(2)]: Where copies of the previous financial statement or report have been sent out to members or delivered to the Registrar or laid before the company in general meeting, the revisions must be confined to -

- (a) The correction in respect of which the previous financial statement or report do not comply with the provisions of section 129 or 134 and
- (b) The making of any necessary consequential alternation.

Rules by Central Government for revision of financial statement [Section 131(3)]: The Central Government may make rules in relation to revised financial statement or a revised director's report. Such rules may, in particular -

- (a) make different provisions according to which the previous financial statement or report are replaced or are supplemented by a document indicating the corrections to be made
- (b) make provisions with respect to the functions of the company's auditor in relation to the revised financial statement or report
- (c) require the directors to take such steps as may be prescribed.

Que. No. 17A] The paid-up equity share capital of Strong Foundry Ltd. is ₹ 45 lakh. President (Finance) of the company seeks your advice whether it is possible to re-open its books of account and recast the company's financial statements of the previous year. You being the Secretary of the company, advise the President (Finance) by preparing a note in this regard.
CS (Executive) - June 2016 (4 Marks)

Ans.: Please refer to Answer of Que. Nos. 16 & 17.

Que. No. 18] Write a short note on: National Financial Reporting Authority

Ans.: Constitution of National Financial Reporting Authority [Section 132(1)]: The Central Government may, by notification, constitute a National Financial Reporting Authority (NFRA) to provide for matters relating to accounting and auditing standards under Companies Act, 2013.

Functions of NFRA [Section 132(2)]: Functions of the National Financial Reporting Authority are as follows-

- (a) To make recommendations to the Central Government on the formulation and laying down of accounting and auditing policies and standards for adoption by companies or class of companies or their auditors
- (b) To monitor and enforce the compliance with accounting standards and auditing standards
- (c) To oversee the quality of service of the professions associated with ensuring compliance with such standards, and suggest measures required for improvement in quality of service and other related prescribed matters
- (d) To perform such other functions relating to clauses (a), (b) and (c) as may be prescribed.

Que. No. 19] Mention the importance of 'notes on accounts'. Will it convey meaning to stakeholders?
CS (Executive) - Dec 2014 (4 Marks)

Ans.: One of the main objectives of the Annual Accounts of a company is to communicate effectively its strengths and weaknesses. The bare figures encompassing the amounts are not sufficient by themselves to depict and explain the true and fair view of the state of affairs of a company. It has, therefore, become necessary to explain and communicate some of the vital information through 'Notes on Accounts'. By and large the notes on accounts are explanatory. They elucidate the figures in the accounts and explain their significance.

Sometimes, these notes are clarificatory to meet the requirements of law. Whether a particular note is explanatory or clarificatory will depend on the facts in each case and the manner in

which it is stated. Notes on accounts form an integral part of the accounts of a company and contain very interesting and vital information.

Contents of notes on accounts: The notes on accounts are intended to clarify and elucidate the financial position of a company as disclosed in its balance sheet and profit and loss account. Generally, the notes on accounts covers the following matters:

1. Basis of accounting
2. Significant accounting policies
3. Material changes, if any, in the method of accounting
4. The effect of material changes in the method of accounting on any item in the financial statement in physical terms to the extent ascertainable. Where such amount is not ascertainable, either wholly or in part, the fact should be stated.
5. Method of valuation of fixed assets
6. Method of valuation of trade and other investments
7. Method of providing depreciation
8. Valuation of inventories
9. Treatment of any income and expenditure on cash basis as against accrual basis
10. Expenditure in foreign currency account
11. Foreign exchange conversion
12. Any disputed liabilities and claims against the company
13. Any major litigation pending by or against the company
14. Method of providing for retirement and terminal benefits
15. Remuneration paid to managerial personnel and their calculation thereof.

The above list is only illustrative and not exhaustive. There could be many other items in the Books of Account which may be required to be explained, clarified or amplified so as to project a true and fair view of the state of affairs of the company.

Que. No. 20] Who is authorized to prescribe accounting standards for the companies under the Companies Act, 2013?

Ans.: Central Government to prescribe accounting standards [Section 133]: The Central Government may prescribe the standards of accounting or any *addendum* thereto, as recommended by the Institute of Chartered Accountants of India, constituted under Section 3 of the **Chartered Accountants Act, 1949**, in consultation with and after examination of the recommendations made by the NFRA.

Que. No. 21] Explain the legal provisions relating to approval and signing of financial statement under the Companies Act, 2013? CS (Executive) – Dec 2013 (4 Marks)

Financial statements shall be signed by only by the Chairperson of the company. Explain. CS (Executive) – June 2015 (4 Marks)

Ans.: Approval and signing of financial statement [Section 134(1)]: The financial statement, including consolidated financial statement, if any, shall be approved by the Board of Directors before signing.

The financial statements are signed on behalf of the Board by the following persons:

- The Chairperson (*where he is authorized by the Board*) or
- Two directors out of which one shall be Managing Director and the CEO
- The CFO and the Company Secretary (*if they are appointed*)

In the case of OPC, the financial statements are signed by only one director, for submission to the auditor for his report.

Attachment of Auditor's Report [Section 134(2)]: The auditor's report shall be attached to every financial statement.

Que. No. 22] The Board of Directors of Vishwakarma Electronics Ltd. consists of Mr. Ghanshyam, Mr. Hyder (Directors) and Mr. Indersen (Managing Director). The company has also employed a full time Secretary. The Profit & Loss Account and Balance Sheet of the company were signed by Mr. Ghanshyam and Mr. Hyder. Examine whether the authentication of financial statements of the company was in accordance with the provisions of the Companies Act, 2013? CA (Final) – Nov 2011 (5 Marks)

Ans.: As per Section 134(1), the financial statements are signed on behalf of the Board by the following persons:

- The Chairperson (*where he is authorized by the Board*) or
- Two directors out of which one shall be Managing Director and the CEO
- The CFO and the Company Secretary (*if they are appointed*)

As per the facts given in the financial statements are signed by only two directors and it amounts to contravention of Section 134(1).

The financial statement should have been signed by –

- (1) Mr. Indersen (Managing Director)
- (2) Mr. Ghanshyam or Mr. Hyder (Directors)
- (3) Whole time Company Secretary

Que. No. 22A] Adorable Ltd., incorporated under the Companies Act, 2013 has on its Board, 5 directors and a Managing Director. The company has also appointed a Company Secretary. The financial statements of the company, viz., balance sheet and statement of profit and loss for the year ended 31st March, 2015, were authenticated under signatures of one director and the Company Secretary.

Referring to the provisions of the Companies Act, 2013, examine the validity of authentication. What shall be your answer in case the company in question is a 'one person company'? CS (Executive) – Dec 2015 (4 Marks)

Ans.: As per Section 134(1), the financial statements are signed on behalf of the Board by the following persons:

- The Chairperson (*where he is authorized by the Board*) or
- Two directors out of which one shall be Managing Director and the CEO
- The CFO and the Company Secretary (*if they are appointed*)

As per the facts given in the financial statements are signed by only one director and Company Secretary and it amounts to contravention of Section 134(1).

The financial statement should have been signed by –

- (1) Managing Director
- (2) One director other than Managing Director
- (3) Whole time Company Secretary

In the case of OPC, the financial statements are signed by only one director, for submission to the auditor for his report.

Que. No. 23] The power of directors to approve the financial statement can be delegated to a committee of directors or some of the directors. Comment.

CS (Executive) – June 2010 (5 Marks), June 2012 (5 Marks)

Ans.: As per Section 134 (1), the financial statement, including consolidated financial statement, if any, shall be approved by the Board of Directors before signing.

Thus, to approval of the financial statement cannot be delegated to a committee of directors or some of the directors.

Que. No. 23A] The time gap between date of approval of financial statement by the board of directors of the company and the date of notice of annual general meeting should be 45 days. Comment.

CS (Executive) – June 2016 (5 Marks)

Ans.: As per Section 101, notice of every meeting including AGM has to be given 21 clear days before the date of meeting.

As per Section 134(1), the financial statement shall be approved by the Board of Directors before signing.

As per Section 136(1), a copy of the financial statements, auditor's report and every other document required by law to be *annexed or attached* to the financial statements, which are to be laid before a company in its general meeting, shall be sent to –

- (1) Every member of the company
- (2) Every trustee for the debenture-holder
- (3) All persons who are entitled notice of the meeting (*i.e. auditor, directors, legal representative of any deceased member and the assignee of an insolvent member*)

The notice of the meeting is required to be sent at least 21 clear days. Hence, financial statements have also to be sent at least 21 clear days before the meeting.

Thus, the board of director should approve the financial statement at least before sending the notice of AGM. There is no specific provision in the Companies Act, 2013 regarding gap between approval of financial statement and sending the notice of meeting.

Que. No. 24] Write a short note on: Directors Responsibility Statement

Ans.: Directors Responsibility Statement [Section 134 (5)]: The Directors Responsibility Statement referred shall state following in Board's Report –

- (a) in the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures;
- (b) the directors had selected such accounting policies and applied them consistently and made judgments and estimates that are *reasonable and prudent* so as to give a *true and fair view* of the state of affairs of the company at the end of the financial year and of the profit and loss of the company for that period;
- (c) the directors had taken *proper and sufficient care* for the maintenance of adequate accounting records in accordance with the provisions of this Act for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities;
- (d) the directors had prepared the annual accounts on a going concern basis; and
- (e) the directors, in the case of a listed company, had laid down internal financial controls to be followed by the company and that such internal financial controls are adequate and were operating effectively.
- (f) the directors had devised proper systems to ensure compliance with the provisions of all applicable laws and that such systems were adequate and operating effectively.

Que. No. 25] Write a short note on: Issue, circulation and publication of various documents

Ans.: Issue, circulation and publication of various documents [Section 134 (7)]: A signed copy of every financial statement, including consolidated financial statement, if any, shall be issued, circulated or published along with a copy each of –

- (a) Notes annexed to or forming part of financial statement
- (b) Auditor's Report
- (c) Board's Report

Que. No. 26] Who are entitled to receive the copy of financial statement? Can company sent abridged financial statement instead of sending full financial statement?

Ans.: Right of member to copies of audited financial statement [Section 136(1)]: A copy of the financial statements, auditor's report and every other document required by law to be *annexed or attached* to the financial statements, which are to be laid before a company in its general meeting, shall be sent to –

- (1) Every member of the company
- (2) Every trustee for the debenture-holder
- (3) All persons who are entitled notice of the meeting (*i.e. auditor, directors, legal representative of any deceased member and the assignee of an insolvent member*)

The notice of the meeting is required to be sent at least 21 clear days. Hence, financial statements have also to be sent at least 21 clear days before the meeting.

Exception: If the copies of the documents are sent less than 21 days before the date of the meeting, they shall, notwithstanding that fact, be deemed to have been duly sent if it is so agreed by members –

- (a) holding, if the company has a share capital, majority in number entitled to vote and who represent not less than 95% of such part of the paid-up share capital of the company as gives a right to vote at the meeting; or
- (b) having, if the company has no share capital, not less than 95% of the total voting power exercisable at the meeting.

Abridged financial statement in case of listed company [Proviso to Section 136(1)]: A listed company can send abridged financial statement in Form No. AOC-3 as per Rule 10 of the Companies (Accounts) Rules, 2014. However, copies of the financial statement and other documents should be made available for inspection at its registered office during working hours for a period of 21 days before the date of the meeting.

If a shareholder asks for full financial statement, it shall be sent to him.

Financial statement on website in case of listed company: A listed company shall also place its financial statements including consolidated financial statements, if any, and all other documents required to be attached thereto, on its website, which is maintained by or on behalf of the company.

Every listed company having a subsidiary or subsidiaries shall place separate audited accounts in respect of each of subsidiary on its website, if any.

However, a listed company which has foreign subsidiary –

- (a) Where such foreign subsidiary is statutorily required to prepare consolidated financial statement under any law of the country of its incorporation, the requirement shall be deemed to be met if consolidated financial statement of such foreign subsidiary is placed on the website of the listed company.

- (b) Where such foreign subsidiary is not required to get its financial statement audited under any law of the country of its incorporation and which does not get such financial statement audited, the holding Indian listed company may place such unaudited financial statement on its website and where such financial statement is in a language other than English, a translated copy of the financial statement in English shall also be placed on the website.

Que. No. 27] Write a short note on: Mode of sending financial statements

Ans.: Mode of sending financial statements [Section 20 & Rule 11 of the Companies (Accounts) Rules, 2014: Financial statements can be sent to members and others through post or courier or hand delivery.

However, in case of listed company or a public company whose net worth is more than one crore and turnover of more than ₹ 10 Crores, financial statement can be sent by –

- E-mail if shares in demat form and e-mail id is registered with depository
- E-mail if shares are in physical form and members has consented in writing for receiving by e-mail.
- Post, courier or hand delivery.

Que. No. 28] What are the provisions of the Companies Act, 2013 relating to inspection of financial statements?

Ans.: Inspection of financial statements [Section 136 (2)]: A company shall allow every member or trustee of the holder of any debentures issued by the company to inspect the financial statements, auditor's report and every other document required by law to be annexed or attached to the financial statements at its registered office during business hours.

Every company having a subsidiary or subsidiaries shall provide a copy of separate audited or unaudited financial statements, as the case may be, as prepared in respect of each of its subsidiary to any member of the company who asks for it.

Que. No. 29] An auditor of a company signed the balance sheet, profit & loss account and schedules/notes and furnished the auditor's report on the same date on which the reports were signed by the directors on behalf of the board. On the director raised objection stating that the audit cannot be completed and certified in a day. Do you agree with directors and if not, why?

CS (Executive) – Dec 2012 (5 Marks)

Ans.: Time gap between authentication of accounts and signing by auditor: Section 143 gives the auditors access at all times to the books of account and vouchers of the company, which amply suggests that they do not have to remain idle at any time after their appointment as auditors. Subject to the convenience of the company, he may actually commence the checking up of vouchers, etc., and the company may prepare Trial balances, balance sheets etc., which will save time for the auditors in the preparation of their report in due course. Thus, if the auditor signs the balance sheet on the same date on which the directors have approved it, it may not be inferred from the circumstances that the auditor has not performed the audit efficiently. There is no violation of Section 134 where the audit is completed before approval of the balance sheet by the Board of directors.

Que. No. 30] What are the provisions regarding filing of financial statement and other documents with ROC?

Give your opinion whether the Registrar of Companies can take financial statement on record even if it is not laid before annual general meeting or placed before the extraordinary general meeting.

CS (Inter) – Dec 2006 (4 Marks)

Ans.: Copy of financial statement to be filed with Registrar [Section 137(1)]: A copy of the financial statements, including consolidated financial statement, along with all the documents attached to financial statements, duly adopted at the AGM, shall be filed with the Registrar within 30 days of the date of AGM in prescribed manner along with prescribed fees.

As per Rule 12 of the Companies (Accounts) Rules, 2014 –

- A financial statement shall be filed in Form No. AOC-4 which should be pre-certified by Practicing CA.
- The class of companies as may be notified by the Central Government, shall mandatorily file financial statement in Extensible Business Reporting Language (XBRL) format.

Financial accounts to be filed even if not adopted in AGM: Even if financial statements are not adopted at AGM or adjourned AGM, such un-adopted financial statements along with other required documents shall be filed with the Registrar within 30 days of the date of AGM and the Registrar shall take them in his records as provisional till the financial statements are filed with him after their adoption in the adjourned AGM for that purpose.

Financial statements adopted in the adjourned AGM shall be filed with the Registrar within 30 days of the date of such adjourned AGM.

Filing of financial statement in case of OPC: OPC shall file a copy of the financial statements duly adopted by its member, along with all the documents which are required to be attached to such financial statements, within 180 days from the closure of the financial year.

Filing of financial statement in case of companies having subsidiary outside India: In case of companies having subsidiary outside India and which has no place of business in India, the accounts of subsidiary should also be filed along with financial statement of the holding company.

However, in the case of foreign subsidiary which is not required to get its financial statement audited under any law of the country of its incorporation and which does not get such financial statement audited, the requirements shall be deemed to be met if the holding Indian company files such unaudited financial statement along with a declaration to this effect and where such financial statement is in a language other than English, along with a translated copy of the financial statement in English.

Financial statement to be filed even if AGM is not held [Section 137(2)]: Where the AGM of a company for any year has not been held, the financial statements along with the documents required to be attached, duly signed along with the statement of facts and reasons for not holding the AGM shall be filed with the Registrar within 30 days of the last date before which the AGM should have been held.

Que. No. 31] Director of the company along with another director were prosecuted under for their failure to file return, annual accounts and audited balance sheet required to be laid before the annual general meeting. The director moved the Court to quash the prosecution initiated by the ROC. As a Company Secretary in Practice advise in the matter.

CS (Executive) – Dec 2013 (4 Marks)

Ans.: The facts of the given case are similar to *Kishan Prasad Palaypu vs. Registrar of Companies [(2008) 83 SCL 376 (AP)]*. A director of the company along with another director were prosecuted for their failure to file return, annual accounts and audited balance sheet required to be laid before the annual general meeting. The director moved the Court under Section 482 of the Code of criminal procedure for quashing the proceedings contending that the complaints filed were barred by limitation. Dismissing the petition, the Court held that Section provides for penalty at the rate of ₹ 1,000 for every day till the default continues, it was held that default in complying with the provisions is a continuing default covered by Section 472 of the Code of Criminal Procedure. The contravention is a continuing offence and the period of limitation prescribed under Section 468 of the Code does not apply to the prosecution launched against the company. Thus, the Court will reject to quash the prosecution initiated by the ROC.

Que. No. 31A] Grow More Ltd. is a government company in which the Central Government and many State Governments in India are members. The company has recently convened its annual general meeting at its registered office. Does the legislature have any access to the annual reports of such a company? Give your advice.

CS (Executive) - June 2011 (4 Marks)

Ans.: As per Sections 394 & 395, in case of Government Companies, the Central Government must place before both the Houses of Parliament an annual report on the working and affairs of each Government company within three months of its annual general meeting together with a copy of the audit report and any comments upon or supplement to such report made by the Comptroller and Auditor General of India. Where a State Government is a member of a Government company, the annual report is likewise to be placed before the State Legislature.

Que. No. 31B] Prudent General Insurance Company Ltd. is engaged in the general insurance business. The company is not listed in any stock exchange in India but is a subsidiary of Reliable General Insurance Company Ltd., listed at Bombay Stock Exchange. The turnover of Prudent General Insurance Company Ltd. is ₹ 330 Crore. Examining the provisions of the Companies Act, 2013, state whether the company is required to file XBRL enabled balance sheet.

CS (Executive) - June 2016 (4 Marks)

Ans.: The following class of companies has to file their Balance Sheet, Profit & Loss A/c and other documents with the Registrar using the Extensible Business Reporting Language (XBRL) namely:

- (1) All Companies listed with any Stock Exchange in India and their Indian subsidiaries.
- (2) All Companies having paid up capital of ₹ 5 Crore or above.
- (3) All companies having turnover of ₹ 100 Crore or above.

Companies in Banking, Insurance, Power Sectors, Non-Banking Financial companies and Housing Finance Companies are exempted for Extensible Business Reporting Language (XBRL) filing. Thus, Prudent General Insurance Company Ltd. being an insurance company is not required to file their Balance Sheet and Profit & Loss A/c in XBRL.

ANNUAL RETURN

Que. No. 32] Write a short note on: Annual Return

Right of member to obtain copy of annual return. Discuss.

CS (Inter) - Dec 2001 (2 Marks)

Ans.: Annual Return [Section 92(1)]: Every company shall prepare an annual return in the prescribed form containing the particulars as they stood on the close of the financial year regarding -

- (a) its registered office, principal business activities, particulars of its holding, subsidiary and associate companies
- (b) its shares, debentures and other securities and shareholding pattern
- (c) [Deleted by Companies (Amendment) Act, 2017]
- (d) its members and debenture-holders along with changes therein since the close of the previous financial year
- (e) its promoters, directors, key managerial personnel along with changes therein since the close of the previous financial year

- (f) meetings of members or a class thereof, Board and its various committees along with attendance details
- (g) remuneration of directors and key managerial personnel
- (h) penalty or punishment imposed on the company, its directors or officers and details of compounding of offences and appeals made against such penalty or punishment
- (i) matters relating to certification of compliances, disclosures as may be prescribed
- (j) details, as may be prescribed, in respect of shares held by or on behalf of the Foreign Institutional Investors
- (k) other prescribed matters.

Signing of Annual Return: Annual Return has to be and signed by a director and the Company Secretary, or where there is no Company Secretary, by Practicing Company Secretary.

In case of OPC and small company, the annual return shall be signed by the Company Secretary, or where there is no Company Secretary, by the director of the company.

Annual return in case of bigger companies [Section 92(2)]: The annual return, filed by a listed company or, by a company having prescribed paid-up capital or turnover, shall be certified by a Practicing Company Secretary in the prescribed form, stating that the annual return discloses the facts correctly and adequately and that the company has complied with all the provisions of the Companies Act, 2013

As per Rule 7(2) of the Companies (Management & Administration) Rules, 2014, the annual return, filed by a listed company or a company having paid-up share capital of ₹ 10 Crore or more or turnover of ₹ 50 Crore or more, shall be certified by Practicing Company Secretary and the certificate shall be in Form No. MGT-8.

Form of Annual Return [Section 92(3)]: An extract of the annual return shall be such form as may be prescribed and every company shall place a copy of the annual return on the website of the company, if any and the web-link of such annual return shall be disclosed in the Board's report.

As per Rule 7(1) of the Companies (Management & Administration) Rules, 2014, every company shall prepare its annual return in Form No. MGT-7.

Filing of Annual Return [Section 92(4)]: Every company shall file with the Registrar a copy of the annual return, within 60 days from the date on which the AGM is held or where no AGM is held in any year within 60 days from the date on which the AGM should have been held together with the statement specifying the reasons for not holding the AGM.

Punishment for default in filing annual return [Section 92(5)]: If a company fails to file its annual return or within extended time with late fee, the company shall be punishable with fine which shall not be less than ₹ 50,000 but which may extend to ₹ 5,00,000 and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 6 months or with fine which shall not be less than ₹ 50,000 but which may extend to ₹ 5,00,000, or with both.

If Practicing Company Secretary certifies the annual return otherwise than in conformity with the requirements of section 92 or the rules made thereunder, he shall be punishable with fine which shall not be less than ₹ 50,000 but which may extend to ₹ 5,00,000.

Que. No. 32A] Pioneer Fisheries Ltd. has borrowed an amount of ₹ 50 Crore from a financial institution. The annual general meeting of the company was held on 1st September, 2015. Examining the provisions of the Companies Act, 2013, state as to who will sign and certify the annual return while filing the same with the Registrar of Companies after the annual general meeting.

CS (Executive) - June 2016 (4 Marks)

Ans.: Please refer to Answer of Que. No. 32.

Que. No. 32B] Virat, a person of 21 years of age is pursuing MBA (Finance) course at a reputed recognized business school. He is not a shareholder of Grow (Pvt.) Ltd. He wishes to inspect the register of investments in securities not held in company's name and annual return of Grow (Pvt.) Ltd. He also wants to take copies thereof. Examining the relevant provisions of the Companies Act, 2013, advise Virat whether he would be successful in this regard.

CS (Executive) - June 2016 (4 Marks)

Ans.: Inspection and copies of "Register of Investment not held in Company's name": As per Section 187, any shares or securities in which investments have been made by a company are not held by it in its own name, the company shall maintain a register which shall contain such particulars as may be prescribed and such register shall be open to inspection by *any member or debenture-holder* of the company *without any charge during business hours* subject to such reasonable restrictions as the company may by its articles or in general meeting impose.

As per facts given in case Virat is not shareholder of Grow (P) Ltd. and hence he cannot inspect or take copies of "Register of Investment not held in Company's name".

Inspection and copies of Annual Return: The register of security holders and their indices, except when they are closed and the copies of all the returns shall be open for inspection by any member, debenture-holder, other security holder or beneficial owner, during business hours without payment of any fees. Any other person can also inspect the same but on payment of prescribed fees.

Any such member, debenture-holder, other security holder or beneficial owner or any other person may –

- (a) Take extracts from any register, or index or return without payment of any fee; or
- (b) Require a copy of any such register or entries therein or return on payment of such fees as may be prescribed.

If any inspection or the making of any extract or copy required is refused, the company and every officer of the company who is in default shall be liable, for each such default, to a penalty of ₹ 1,000 for every day subject to a maximum of ₹ 1 lakh during which the refusal or default continues.

Thus, Virat can inspect and can also take copies of Annual Return but on payment of prescribed fees even though he is not shareholder of Grow (P) Ltd.

Que. No. 33] Is any return is to be filed for change in promoters shareholding under the Companies Act, 2013?

Ans.: Return to be filed with Registrar in case promoters stake changes [Section 93]: Section 93 is deleted by Companies (Amendment) Act, 2017; hence question is not relevant for Dec. 2018 and onward exam.

AUDIT

Que. No. 34] Who can be appointed as auditor of a company?

CS (Inter) - June 2001 (4 Marks)

The Board of Directors of X Ltd. desirous of appointing CD & Co. as their auditors. What qualifications are necessary for the auditor to be so appointed?

Ans.: Who can be appointed as auditor of a company [Section 141(1)]: A person shall be eligible for appointment as an auditor of a company only if he is a Chartered Accountant. A firm whereof majority of partners practicing in India are qualified for appointment as aforesaid may be appointed by its firm name to be auditor of a company.

Where a firm including a Limited Liability Partnership (LLP) is appointed as an auditor of a company, only the partners who are Chartered Accountants shall be authorized to act and sign on behalf of the firm.

Que. No. 35] Discuss the provisions of the Companies Act, 2013 relating to appointment of auditor of a company.

Ans.: Appointment of auditor [Section 139(1)]: Every company whether it is public or private limited shall have an auditor to audit its accounts. The appointment of auditor is mandatory in the Annual General Meeting (AGM).

Every company shall, at its first AGM, appoint an individual or a firm as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its 6th AGM and thereafter till the conclusion of every 6th meeting.

Before appointment of auditor, the written consent to such appointment, and a certificate in should be obtained from the auditor. Such certificate shall also indicate whether the auditor satisfies the criteria provided in Section 141.

After appointing the auditor the company shall inform the auditor concerned of his or its appointment, and also file a notice of such appointment with the Registrar within 15 days of the meeting in which the auditor is appointed. As per Rule 4(2) of the Companies (Audit & Auditors) Rules, 2014, such notice is required to be filed in Form ADT-1.

Recommendations of audit committee [Section 139(11)]: If a company is required to constitute an Audit Committee u/s 177, all appointments, including the filling of a casual vacancy of an auditor shall be made after taking into account the recommendations of such committee.

Que. No. 36] Explain the concept of rotation of auditors as per Companies Act, 2013. Also state the class of companies to which it is applicable.

Ans.: Rotation of auditors [Section 139(2)]: Listed company or a company belonging to such class or classes of companies as may be prescribed, shall not appoint or re-appoint –

- (a) An individual as auditor for more than one term of 5 consecutive years and
- (b) An audit firm as auditor for more than two terms of 5 consecutive years.

However, an individual auditor who has completed his term of 5 years shall not be eligible for re-appointment as auditor in the same company for 5 years from the completion of his term.

In case of an audit firm which has completed its 2 term of 5 years shall not be eligible for re-appointment as auditor in the same company for 5 years from the completion of such term.

It is further provided that as on the date of appointment no audit firm having a common partner or partners to the other audit firm, whose tenure has expired in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of 5 years.

As per Rule 5 of the Companies (Audit & Auditors) Rules, 2014 for the purposes of Section 139(2), the class of companies shall mean the following classes of companies excluding one person companies and small companies:-

- (a) All unlisted public companies having paid up share capital of ₹ 10 Crore or more;
- (b) All private limited companies having paid up share capital of ₹ 20 Crore or more;
- (c) All companies having public borrowings from financial institutions, banks or public deposits of ₹ 50 Crore or more.

Strict provisions relating to rotation can be imposed by members [Section 139(3)]: Members of a company may resolve to provide that:

- (a) In the audit firm appointed by it, the auditing partner and his team shall be rotated at such intervals as may be resolved by members or
- (b) The audit shall be conducted by more than one auditor.

Power of Central Government to prescribe rules relating to rotation [Section 139(4)]: The Central Government may, by rules, prescribe the manner in which the companies shall rotate their auditors in pursuance of Section 139(2).

Que. No. 37] On recommendation of the Board of Directors of DJA Ltd. (listed company), Mr. R is appointed at the AGM held on 1st October, 2014 as the company's auditor for a period of 10 years. A resolution to this effect was passed unanimously with no vote against the resolution. Explaining the provisions of the Companies Act, 2013 relating to the appointment and re-appointment of auditors:

- (i) Examine the validity of the above resolution.
- (ii) What shall be your answer in case an audit firm Messrs R & Associate is appointed as the company's auditor?

CA (Final) - Nov 2014 (5 Marks)

Ans.: As per Section 139(2), an individual shall not appointed or re-appointed as auditor for more than one term of 5 consecutive years. Thus, the appointment of Mr. R as auditor of the company for 10 years is not valid.

As per Section 139(2), an audit firm shall not appointed or re-appointed as auditor for more than two term of 5 consecutive years. This means that a firm can be appointed for 5 years and thereafter may be reappointed for further 5 years. The total period for which a firm can be appointed is 10 years. A firm cannot be appointed as auditor for 10 years by a single resolution. Thus, the appointment of Messrs R & Associate as the company's auditor for ten years by a single resolution is not valid.

Que. No. 38] State the provisions relating to appointment of first auditor.

CS (Inter) - Dec 1998 (3 Marks), Dec 2001 (4 Marks)

Ans.: Appointment of first auditor [Section 139(6)]: The first auditor of a company shall be appointed by the Board of Directors within 30 days from the date of registration of the company. If the Board of Directors fails to appoint such auditor, it shall inform the members of the company, who shall within 90 days at an extraordinary general meeting appoint auditor and such auditor shall hold office till the conclusion of the first AGM.

Appointment of first auditor by Government company [Section 139(7)]: In the case of a Government Company or any other company owned or controlled, directly or indirectly, by the Central or any State Government(s) the first auditor shall be appointed by the Comptroller & Auditor-General (CAG) within 60 days from the date of registration of the company. If CAG does not appoint auditor within 60 days, the Board of Directors of the company shall appoint auditor within the next 30 days and in the case of failure of the Board to appoint such auditor within the next 30 days, it shall inform the members of the company who shall appoint such auditor within the 60 days at an EGM, who shall hold office till the conclusion of the first AGM.

Tenure of first auditor: The first auditor shall hold office till the conclusion of first AGM.

Que. No. 39] State the provisions relating to appointment of subsequent auditor in case of Government Companies.

Ans.: Appointment of subsequent auditor in case of Government Companies [Section 139(5)]: In the case of a Government company or any other company owned or controlled, directly or

indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, the Comptroller and Auditor-General of India shall, in respect of a financial year, appoint an auditor duly qualified to be appointed as an auditor of companies, within a period of 180 days from the commencement of the financial year.

Tenure: The auditor shall hold office till the conclusion of the AGM.

Que. No. 40] Write a short note on: Filling of casual vacancy of auditors

Ans.: Filling of casual vacancy of auditors [Section 139(8)(i)]: Any casual vacancy in the office of an auditor shall be filled by the Board of Directors within 30 days. If such casual vacancy is as a result of the resignation of an auditor, such appointment shall also be approved by the company at a general meeting convened within 3 months of the recommendation of the Board and he shall hold the office till the conclusion of the next AGM.

Filling of casual vacancy of auditors by government company [Section 139(8)(ii)]: In the case of a government company, any casual vacancy in the office of an auditor shall be filled by the CAG within 30 days. If the CAG does not fill the vacancy within the said period, the Board of Directors shall fill the vacancy within next 30 days.

Que. No. 41] Mr. A was appointed auditor of AAS Ltd. by Board to fill the casual vacancy that arose due to death of the auditor originally appointed in AGM. Subsequently, Mr. A also resigned on health grounds during the tenure of appointment. Comment how the vacancy arising in the place of audit will be filled up?

Ans.: As per Section 139(8), any casual vacancy in the office of an auditor shall be filled by the Board of Directors within 30 days. If casual vacancy is as a result of the resignation of an auditor, such appointment shall also be approved by the company at a general meeting convened within 3 months of the recommendation of the Board.

In the present case the auditor Mr. A resigned and the vacancy had been filled in by Board. But, the vacancy caused by resignation cannot be filled by Board, since it does not amount to casual vacancy; it can be filled only shareholders in general meeting.

The fact that Mr. A was appointed by the Board of Directors, originally is a matter irrelevant in this situation. If the cause of vacancy is resignation, then the power of appointment shall vest with the general meeting only.

Que. No. 42] Due to the resignation of the existing auditor, the board of directors of Hanuman Ltd. appoints Ram as the auditor. Comment.

Ans.: As per Section 139(8) of the Companies Act, 2013, a casual vacancy, caused by the resignation of an auditor, can be filled only by the company in a general meeting convened within 3 months of the recommendation of the Board. Thus, the appointment of Ram by the Board of Directors of Hanuman Ltd. is not valid.

Que. No. 43] Write a short note on: Re-appointment of Auditors

Ans.: Re-appointment of Auditors [Section 139(9)]: A retiring auditor may be re-appointed at an AGM if:

- (a) He is not disqualified for re-appointment
- (b) He has not given the company a notice in writing of his unwillingness to be re-appointed; and
- (c) A special resolution has not been passed at that meeting appointing some other auditor or providing expressly that he shall not be re-appointed.

It is, however, to be noted that the re-appointment of the existing auditor is not automatic as there must be an act of the company re-appointing him by passing a resolution.

No auditor is appointed or re-appointed [Section 139(10)]: Where at any annual general meeting, no auditor is appointed or re-appointed, the existing auditor shall continue to be the auditor of the company.

Que. No. 44] Write a short note on: Removal of auditors

Rao & Rao, a firm of chartered accountants, have to be appointed in place of Shah & Shah as the auditor of Freebee Ltd. explain the steps to be taken with regard to appointment of auditor.
CS (Inter) – June 2003 (4 Marks)

Ans.: Removal of auditors [Section 140(1)]: The auditor may be removed from his office before the expiry of his term only by a **special resolution** of the company, after obtaining the previous approval of the Central Government. The outgoing auditor shall be given a reasonable opportunity of being heard.

As per Rule 7(1) of the Companies (Audit & Auditors) Rules, 2014, the application to the Central Government for removal of auditor shall be made in Form ADT-2 along with prescribed fees.

The application shall be made to the Central Government within 30 days of the resolution passed by the Board.

The company shall hold the general meeting within 60 days of receipt of approval of the Central Government for passing the special resolution.

Requirement of special notice [Section 140(4)]: Special notice shall be required for a resolution at an AGM appointing as auditor a person other than a retiring auditor, or providing expressly that a retiring auditor shall not be re-appointed. However, special notice is not required if the retiring auditor is not appointed due to completion of consecutive tenure of 5 years or 10 years, as provided under Section 139(2).

On receipt of notice of such a resolution, the company shall forthwith send a copy to the retiring auditor.

Where notice is given and the retiring auditor makes representation in writing to the company of a reasonable length and requests its notification to members of the company, the company shall, unless the representation is received by it too late for it to do so,

- in any notice of the resolution given to members of the company, state the fact of the representation having been made and
- send a copy of the representation to every member of the company to whom notice of the meeting is sent, whether before or after the receipt of the representation by the company

If a copy of the representation is not sent because it was received too late or because of the company's default, the auditor may require that the representation shall be read out at the meeting.

If copy of representation is not sent a copy thereof shall be filed with the Registrar.

If the Tribunal is satisfied on an application either of the company or of any other aggrieved person that the rights conferred by Section are being abused by the auditor, then, the copy of the representation may not be sent and the representation need not be read out at the meeting.

The Tribunal either *suo motu* or on an application made to it by the Central Government or by any person concerned, if it is satisfied that the auditor of a company has, whether directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its directors or officers, it may, by order, direct the company to change its auditors.

If the application is made by the Central Government and the Tribunal is satisfied that any change of the auditor is required, it shall within 15 days of receipt of such application, make an order that he shall not function as an auditor and the Central Government may appoint another auditor in his place.

An auditor, whether individual or firm, against whom final order has been passed by the Tribunal shall not be eligible to be appointed as an auditor of any company for a period of 5 years from the date of passing of the order and the auditor shall also be liable for action u/s 447.

Explanation I: It is clarified that the case of a firm, the liability shall be of the firm and that of every partner or partners who acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its director or officers.

Explanation II: "Auditor" includes a firm of auditors.

Que. No. 45] Write a short note on: Resignation by Auditor

Ans.: Resignation by Auditor [Section 140(2)]: The auditor who has resigned from the company shall file within a period of 30 days from the date of resignation, a statement in the prescribed form with the company and the Registrar, and in case of government companies referred to in Section 139(5), the auditor shall also file such statement with the CAG indicating the reasons and other facts as may be relevant with regard to his resignation.

As per Rule 8 of the Companies (Audit & Auditors) Rules, 2014, when an auditor has resigned from the company, he shall file a statement in Form ADT-3.

Que. No. 45A] Manohar, the auditor of Belle Ltd. appointed by the company in its last general meeting has resigned from the office of auditor of the company for some personal reasons.

Referring to the provisions of the Companies Act, 2013, answer the following:

- Who is the competent authority to accept and approve the resignation?
 - State the manner in which the vacancy caused by Manohar's resignation shall be filled in.
- CS (Executive) – Dec 2015 (4 Marks)

Ans.: Resignation by Auditor [Section 140(2)]: The auditor who has resigned from the company shall file within a period of 30 days from the date of resignation, a statement in the prescribed form with the company and the Registrar, and in case of government companies referred to in Section 139(5), the auditor shall also file such statement with the CAG indicating the reasons and other facts as may be relevant with regard to his resignation.

As per Rule 8 of the Companies (Audit & Auditors) Rules, 2014, when an auditor has resigned from the company, he shall file a statement in Form ADT-3.

There is no specific provision in the Companies Act, 2013 regarding approval of resignation of auditor, but as general power of company vest in directors they are competent to accept and approve the resignation of auditor.

Filling of casual vacancy of auditors [Section 139(8)(i)]: Any casual vacancy in the office of an auditor shall be filled by the Board of Directors within 30 days. *If such casual vacancy is as a result of the resignation of an auditor, such appointment shall also be approved by the company at a general meeting convened within 3 months of the recommendation of the Board and he shall hold the office till the conclusion of the next AGM.*

Filling of casual vacancy of auditors by government company [Section 139(8)(ii)]: In the case of a government company, any casual vacancy in the office of an auditor shall be filled by the CAG within 30 days. If the CAG does not fill the vacancy within the said period, the Board of Directors shall fill the vacancy within next 30 days.

Que. No. 46] Write a short note on: Disqualification of Statutory Auditor

CS (Inter) – Dec 1998 (4 Marks)

CS (Executive) – June 2014 (4 Marks)

Ans.: Disqualification of Statutory Auditor [Section 141(3)]: The following persons shall not be eligible for appointment as an auditor of a company, namely:

- (a) A body corporate other than a limited liability partnership
- (b) An officer or employee of the company
- (c) A person who is a partner or employee of an officer or employee of the company
- (d) A person who, or his relative or partner -
 - (i) Is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company. However the relative may hold security or interest in the company of face value not exceeding ₹ 1,000 or such sum as may be prescribed.

As per Rule 10(1) of the Companies (Audit & Auditors) Rules, 2014, for the purpose of Section 141(3)(d)(i), a relative of an auditor may hold securities in the company of face value not exceeding ₹ 1,00,000.

Meaning of relative: the term "relative" means the spouse of a person and includes a parent, sibling or child of such person or of the spouse, financially dependent on such person, or who consults such person in taking decisions in relation to his investments.

- (ii) Is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of such amount as may be prescribed

As per Rule 10(2) of the Companies (Audit & Auditors) Rules, 2014, for the purpose of Section 141(3)(d)(ii), person who or whose relative or partner is indebted to the company or its subsidiary or its holding or associate company or a subsidiary of such holding company, in excess of ₹ 5,00,000 shall not be eligible for appointment.

- (iii) Has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, for such amount as may be prescribed

As per Rule 10(3) of the Companies (Audit & Auditors) Rules, 2014, for the purpose of Section 141(3)(d)(iii), a person who or whose relative or partner has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of ₹ 1,00,000 shall not be eligible for appointment.

- (e) A person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as may be prescribed

As per Rule 10(4) of the Companies (Audit & Auditors) Rules, 2014, for the purpose Section 141(3)(e), the term "business relationship" shall be construed as any transaction entered into for a commercial purpose, except -

- (i) commercial transactions which are in the nature of professional services permitted to be rendered by an auditor or audit firm under the Act and the Chartered Accountants Act, 1949 and the rules or the regulations made under those Acts;
 - (ii) commercial transactions which are in the ordinary course of business of the company at arm's length price - like sale of products or services to the auditor, as customer, in the ordinary course of business, by companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses.
- (f) A person whose relative is a director or is in the employment of the company as a director or key managerial personnel
 - (g) A person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of more than 20 companies

In case of private companies Section 141(3)(g) shall apply with the modification that the words "other than one person companies, dormant companies, small companies and private companies having paid-up share capital less than ₹ 100 Crores" shall be inserted after the words "twenty companies" - Notification [F no. 1/1/2014 - CL.V], dated 5.6.2015.

- (h) A person who has been convicted by a court of an offence involving fraud and a period of 10 years has not elapsed from the date of such conviction
- (i) A person who, directly or indirectly renders any services referred to in section 144 to the company or its holding company or its subsidiary company.

Vacation of office if auditor is disqualified after appointment [Section 141(4)]: Where a person appointed as an auditor of a company incurs any of the disqualifications mentioned in Section 141(3) after his appointment, he shall vacate his office as such auditor and such vacation shall be deemed to be a casual vacancy in the office of the auditor.

Que. No. 47] Mr. A is a part-time Practicing Chartered Accountant and is the financial controller of X Ltd. The company wants to appoint him as its auditor in the ensuing annual general meeting. Offer your comments in the matter.

Ans.: As per Section 141(3), an officer or employees of the company are not qualified for appointment as auditor of a company. In the present case Mr. A is the financial controller and thus an officer of the company. Therefore, he is disqualified for appointment as an auditor of the company.

Que. No. 48] Ram and Hanuman Associates, Chartered Accountants in practice have been appointed as Statutory Auditor of Krishna Ltd. for the accounting year 2014-2015. Mr. Hanuman holds 100 equity shares of Shiva Ltd., a subsidiary company of Krishna Ltd.

Ans.: As per Section 141(3)(d), a person who is holding any security of the company or its subsidiary is disqualified for appointment as auditor.

In the present case, Mr. Hanuman, a partner of M/s. Ram and Hanuman Associates, holds 100 equity shares of Shiva Ltd., which is a subsidiary of Krishna Ltd. As such, the firm, M/s. Ram and Hanuman Associates would be disqualified to be appointed as statutory auditor of Shiva Ltd. Thus, firm is also disqualified for appointment of auditor in Krishna Ltd. (i.e. Holding Company)

Que. No. 49] Amol & Co., a proprietary firm of Amol, a Chartered Accountant in practice, has been appointed as the statutory auditor by a private limited company. Subsequently, it came to light that Mr. Amol has been holding less than 1% of the shares of that company. Will this vitiate the appointment of the statutory auditor? Answer with reasons.

CS (Inter) - June 2005 (4 Marks)

Ans.: As per Section 141(3)(d), a person who is holding any security of the company or its subsidiary is disqualified for appointment as auditor. Since Mr. Amol has been holding some shares of the company, he is disqualified for appointment as auditor and his appointment is *not valid*.

Que. No. 49A] Sanjay, a Chartered Accountant, is the financial controller of Sonik Industries (Pvt.) Ltd. for the last five years. The company now wants to appoint him as the statutory auditor of the company. Examining the provisions of the Companies Act, 2013, advise whether the company can appoint Sanjay as its statutory auditor.

CS (Executive) - June 2016 (4 Marks)

Ans.: As per Section 141(1), a person shall be eligible for appointment as an auditor of a company only if he is a Chartered Accountant.

As per Section 141(3), an officer or employee of the company is disqualified for appointment as an auditor.

As per facts given in case, Sanjay is employee of Sonik Industries Ltd. working as financial controller and he is disqualified for appointment as an auditor.

Que. No. 50] Write a short note on: Remuneration of auditors

Ans.: Remuneration of auditors [Section 142]: The remuneration of the auditor shall be fixed in its general meeting or in such manner as may be determined therein. However the Board may fix remuneration of the first auditor appointed by it.

The remuneration shall, in addition to the fee payable to an auditor, include the expenses, if any, incurred by the auditor in connection with the audit of the company and any facility extended to him but does not include any remuneration paid to him for any other service rendered by him at the request of the company.

Que. No. 51] Discuss in brief the various rights of statutory auditors.

Ans.: Statutory Auditor of a company has been given enough vested power by the act so as to enable him to carry out the auditing of the books of account independently. The rights of a auditors are discussed herein given below:

- (1) **Right to receive information and explanations:** The company auditor has to state in his report, whether he has received necessary information and explanations for the purpose of audit. When the auditor is not provided the information required by him his only remedy would be to report the same to the shareholder's through qualification in the auditor's report. [Section 143(1)]
- (2) **Right of accessibility to the books and records:** The auditor enjoys the right of accessibility to books and records because he has to mention in his report whether proper books and records are maintained. It is for the auditor to determine what record or document is necessary for the purpose of the audit. [Section 143(1)]

The auditor of a company which is a holding company shall also have the right of access to the records of all its subsidiaries and associate companies in so far as it relates to the consolidation of its financial statements with that of its subsidiaries and associate companies. [Proviso to Section 143(1)]

- (3) **Right to visit branches:** Since the auditor has to report on the consolidated financial statements which also include the results of the branch operations, he has the right to visit the branches to obtain information. Even if the branch accounts are audited by another auditor, this right is still available because it is possible that the auditor may not be getting full information from the branch auditor regarding the branch accounts.
- (4) **Right of lien:** The term lien refers to the right of possession. The auditor enjoys this right over the books of the clients if there is a fee due. The guidelines to be followed while exercising this right is:
 - (a) Documents retained must belong to the client who owes the money.
 - (b) Documents must have come into possession of the auditor on the authority of the client. They must not have been received through irregular or illegal means. In case of a company client, they must be received on the authority of the board of directors.
 - (c) Such of the documents can be retained which are connected with the work on which fees have not been paid.

Que. No. 52] Discuss in brief the various duties of statutory auditors.

CS (Inter) - June 2002 (10 Marks)

Ans.: The duties of an auditor are many and varied. He must examine the original books of account, kept by the company to discover any inaccuracies or omissions therein, to examine the company's balance sheet and profit and loss account, and report on the original books of account and the annual accounts to the members.

Duties of Auditor [Section 143(1)]: An auditor has to inquire:

- (a) Whether loans and advances are properly secured and the terms on which they have been made are not prejudicial to the interests of the company or its members;
- (b) Whether transactions which are represented merely by book entries are not prejudicial to the interests of the company;
- (c) Where the assets of the company as consists of shares, debentures and other securities have not been sold at a price less than that at which they were purchased by the company (except for investment or a banking company);
- (d) Whether loans and advances made by the company have not been shown as deposits;
- (e) Whether personal expenses have not been charged to revenue accounts;
- (f) Whether cash has actually been received in respect of any shares shown in the books to have been allotted for cash; and if no cash has actually been so received, the position as stated in the books is correct, regular and is not misleading.

Duty of the auditor to make a report to the members [Section 143(2)]: It is the duty of the auditor to make a report to the members of the company on the accounts examined by him, and on every balance sheet, every profit and loss account and on every other document to be part of or annexed to the balance sheet or profit and loss account and laid before the company in general meeting.

Auditors Report [Section 143(3)]: The report, besides other things necessary in any particular case, must expressly state:

- (a) Whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;
- (b) Whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him
- (c) Whether the report on the accounts of any branch office of the company by a person other than the company's auditor has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;
- (d) Whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;
- (e) Whether in his opinion, the financial statements comply with the accounting standards;
- (f) The observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;
- (g) Whether any director is disqualified from being appointed as a director u/s 164(2);
- (h) Any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;

- (i) Whether the company has adequate internal financial controls with reference to financial statements in place and the operating effectiveness of such controls;
- (j) Such other matters as may be prescribed.

Duty to give reason for qualification in audit report [Sections 143(4)]: Where any of the above matters is answered in the negative or with a qualification, the auditor's report must state the reason for the same.

Duty to comply with Auditing Standards [Sections 143(9)]: Every auditor *shall comply* with the Auditing Standards.

As per Sections 143(10), the Central Government may prescribe the standards of auditing or any addendum thereto, as recommended by the ICAI in consultation with the National Financial Reporting Authority (NFRA). However until any auditing standards are notified, any standard or standards of auditing specified by the ICAI shall be deemed to be the auditing standards.

Duty to sign audit reports [Section 145]: The person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document and the qualifications, observations or comments on financial transactions or matters, which have any adverse effect on the functioning of the company mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

Duty to attend general meeting [Section 146]: All notices of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company, and the auditor shall, unless otherwise exempted by the company, attend either by himself or through his authorized representative, who shall also be qualified to be an auditor, any general meeting and shall have right to be heard at such meeting on any part of the business which concerns him as the auditor.

Under Section 143(11) the Central Government may, in consultation with the NFRA, by general or special order, direct, in respect of certain class or description of companies, that the auditor's report shall also include a statement on such matters as may be specified therein the Central Government is empowered to issue order requiring the auditor to include in his report a statement on such matters as may be specified.

Que. No. 52A] Peculiar Ltd., an unlisted company, did not prepare its financial statements for the year ended 31st March, 2017 in conformity with some of the mandatory accounting standards. With reference to the provisions of the Companies Act, 2013, state the responsibilities of the directors and statutory auditors of the company in this regard.

CS (Executive) - Dec 2016 (4 Marks)

Ans.: As per Section 129(1), the financial statements shall comply with the accounting standards notified under Section 133. The items contained in financial statements shall be in accordance with the applicable accounting standards.

As per Section 129(5), where the financial statements of a company do not comply with the accounting standards referred, the company shall disclose in its financial statements, the deviation from the accounting standards, the reasons for such deviation and the financial effects, if any, arising out of such deviation.

As per Section 134(5), the Directors Responsibility Statement referred shall state in Board's Report that in the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures.

As per Section 143(9), every auditor *shall comply* with the Auditing Standards. Duty to comply with accounting standards in on company and its directors and not on auditor of the company. Auditor has to comply only with Auditing Standards only.

Que. No. 53] The auditors of PQR Ltd. accepted the Certificate of the Manager, a person of knowledge, competence and high reputation, as to the value of the stock in trade. The stock was grossly overstated for several years in the balance sheets of the company. As a result of this over valuation dividends were paid out of capital.

The Auditors did not examine the books of account very minutely. If they had done so and compared the amount of stock at the beginning of the year, with the purchases and sales during the year, they would have noticed the over valuation. The company subsequently went into liquidation and the auditors were sued to make good the loss caused by the wrongful payment of dividends relying on the balance sheets figures. Based on the above facts, you are required to decide, with reference to the provisions of the Companies Act, 2013 and the decided case laws, the following issues:

- (i) Whether auditors of the company will be liable for the loss caused to the company by the wrongful payment of dividends based on the Balance Sheets duly audited by the Auditors.
- (ii) What are statutory duties of the Auditors in this regard?

CA (Final) - Nov 2015 (8 Marks)

Ans.: Section 143 provides that the main duty of the auditor is to make a report to the members of the company on the accounts examined by him and the balance sheet and the profit and loss account and on every document which is annexed to the balance sheet or profit and loss account laid before the company in general meeting. The auditor owes a duty to the members to state whether the accounts give a true and fair view of the affairs of the company at the end of the financial year and of the profit and loss account of the year.

The duty of an auditor is to give information in direct and express terms and not merely to arouse inquiry. [*Crichton's Oil Co. Re* (1902) 2 ch 86]

If he discovers that any illegal or improper payments or any other papers have been made, his duty will be to make it public by reporting.

The auditor occupies a fiduciary position in relation to the shareholders and in auditing the accounts maintained by the directors, he must act in the best interest of the shareholders who are in the position of beneficiaries. But, there is a limitation relating the duties to be performed by the auditors. An auditor is not bound to be a detective, as loss laid to approach his work with suspicion or with a foregone conclusion that there is something wrong. He is a watchdog but not a bloodhound. He is justified in believing tried servants of the company in whom confidence is placed by the company. He is entitled to assume that they are honest and to rely upon their representations, provided he takes reasonable care. If there is anything calculated to excite suspicion, he should probe it to the bottom, but in the absence of anything of that kind he is only bound to be reasonably cautious and careful.

The above problem is related to case of *Kingston Mill Co. Re* (No 2) (1896) 2 ch 279. In this case it was held that, the auditors were not liable. It is not auditor's duty to take stock. There are many matters in which he may rely on the honesty and accuracy of others. Further they (auditors) do not guarantee the discovery of all frauds.

Que. No. 54] What are the special provisions are made under the Companies Act, 2013 in relation to audit of Government Companies?

Ans.: Direction by CAG in relation to government audit [Section 143(5)]: In the case of a Government company or any other company owned or controlled by the Central or State Governments, the Comptroller & Auditor-General (CAG) of India shall appoint the auditor Section 139(5) or 139(7).

The Comptroller & Auditor-General direct appointed auditor the manner in which the accounts of the Government companies are required to be audited.

The auditor so appointed shall submit a copy of the audit report to the Comptroller & Auditor-General of India.

Such audit report includes the directions issued by the Comptroller & Auditor-General of India, the action taken thereon and its impact on the accounts and financial statement of the company.

Right of CAG to conduct supplementary audit [Section 143(6)]: The Comptroller & Auditor-General of India shall within 60 days from the date of receipt of the audit report have a right to conduct a supplementary audit of the financial statement of the government company by person authorized him. For the purposes of such audit, he may require information or additional information to be furnished to person authorized by him, on such matters and in such form, as the Comptroller and Auditor-General of India may direct.

The Comptroller & Auditor-General of India may comment upon or supplement such audit report.

Any comments given by the Comptroller & Auditor-General of India upon, or supplement to, the audit report shall be sent by the company to every person entitled to copies of audited financial statements and also be placed before the AGM of the company at the same time and in the same manner as the audit report.

Test Audit [Section 143(7)]: The Comptroller & Auditor-General of India may by an order, cause test audit of the accounts and the provisions of section 19A of the **Comptroller and Auditor-General's (Duties, Powers & Conditions of Service) Act, 1971**, shall apply to the report of such test audit.

Que. No. 55] Write a brief note on branch audit.

Ans.: Branch Audit [Section 143(8)]: Where a company has a branch office, the accounts of that office shall be audited either by the company's auditor appointed for the company or by any other person qualified for appointment as an auditor of the company.

Where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country.

The duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be such as may be prescribed.

As per Rule 12 of the **Companies (Audit & Auditors) Rules, 2014**, duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor are as follows.

- (1) For the purposes of sub-section (8) of section 143, the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be as contained in section 143(1) to 143 (4).
- (2) The branch auditor shall submit his report to the company's auditor.
- (3) The provisions of Section 143(12) with Rule 12 hereunder regarding reporting of fraud by the auditor shall also extend to such branch auditor to the extent it relates to the concerned branch.

The branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary.

Que. No. 56] State the provisions relating to reporting of fraud by an auditor as contained in the Companies Act, 2013.

Ans.: Duty to report fraud [Section 143(13) to (15)]: If an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud involving prescribed amount, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within prescribed time and in prescribed manner.

In case of a fraud involving lesser than the specified amount, the auditor shall report the matter to the audit committee constituted under Section 177 or to the Board in other cases within prescribed time and in prescribed manner.

The companies, whose auditors have reported frauds to the audit committee or the Board but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in prescribed manner.

Reporting of frauds by auditor [Rule 12 of the Companies (Audit & Auditors) Rules, 2014]:

- (1) For the purpose of Section 143(12), in case the auditor has sufficient reason to believe that an offence involving fraud, is being or has been committed against the company by officers or employees of the company, he shall report the matter to the Central Government immediately but not later than 60 days of his knowledge and after following the procedure indicated below:
 - (i) Auditor shall forward his report to the Board or the Audit Committee, as the case may be, immediately after he comes to knowledge of the fraud, seeking their reply or observations within 45 days.
 - (ii) On receipt of 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 (on reply or observations of the Board or the Audit Committee) to the Central Government within 15 days of receipt of such reply or observations.
 - (iii) In case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of 45 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 failed to receive any reply or observations within the stipulated time.
- (2) 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.
- (3) The report shall be on the letter-head of the auditor containing postal address, e-mail address and contact number and be signed by the auditor with his seal and shall indicate his Membership Number.
- (4) The report shall be in the form of a statement as specified in **Form ADT-4**.
- (5) The provision of this rule shall also apply, *mutatis mutandis*, to a Cost Auditor and a Secretarial Auditor during the performance of his duties under Sections 148 & 204 respectively.

Que. No. 57] Which type of services cannot be provided by the auditor as provided in Section 144 of the Companies Act, 2013?

Ans.: Auditor not to render certain services [Sections 144]: An auditor shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, but which shall not include any of the following services whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company, namely:

- (i) Accounting and book keeping services
- (ii) Internal audit
- (iii) Design and implementation of any financial information system
- (iv) Actuarial services
- (v) Investment advisory services
- (vi) Investment banking services
- (vii) Rendering of outsourced financial services

- (viii) Management services and
(ix) Any other kind of prescribed services

Explanation: The term "directly or indirectly" shall include rendering of services by the auditor:

- (i) In case of auditor being an individual, either himself or through his relative or any other person connected or associated with such individual or through any other entity, whatsoever, in which such individual has significant influence or control, or whose name or trade mark or brand is used by such individual
- (ii) In case of auditor being a firm, either itself or through any of its partners or through its parent, subsidiary or associate entity or through any other entity, whatsoever, in which the firm or any partner of the firm has significant influence or control, or whose name or trade mark or brand is used by the firm or any of its partners.

Que. No. 58] State the provisions of the Companies Act, 2013 relating to signing of audit report.

Ans.: Auditor to sign audit reports [Section 145]: The person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document of the company in accordance with the provisions of Section 141(2).

Qualification to be read in general meeting and inspection thereof: The qualifications, observations or comments on financial transactions or matters, which have any adverse effect on the functioning of the company mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

Que. No. 59] Whether it obligatory for the auditor to attend the annual general meeting under the Companies Act, 2013? What are the right available to him, when he attends such meeting?

Ans.: Auditors to attend general meeting [Section 146]: All notices, of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company.

The auditor shall, unless otherwise exempted by the company, attend either by himself or through his authorized representative, who shall also be qualified to be an auditor, any general meeting and shall have right to be heard at such meeting on any part of the business which concerns him as the auditor.

Que. No. 60] What are the punishments provided under the Companies Act, 2013 relating to contravention of provisions relating to "audit & auditors (i.e. Sections 139 to 146)"?

Ans.: Punishment for contravention to company and its officers [Section 147(1)]: If any of the provisions of sections 139 to 146 (both inclusive) is contravened:

- The company shall be punishable with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 5,00,000 or 4 times of his remuneration whichever is less.
- Every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 1 year or with fine which shall not be less than ₹ 10,000 but which may extend to ₹ 1,00,000 or with both.

Punishment for Auditors [Section 147(2)]: If an auditor of a company contravenes any of the provisions of Section 139, 143, 144 or 145, the auditor shall be punishable with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 5,00,000.

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 1 year and with fine which shall not be less

than ₹ 50,000 but which may extend to ₹ 25,00,000 or 8 times of his remuneration whichever is less.

Conviction of auditor [Section 147(3)]: Where an auditor has been convicted Section 147(2), he shall be liable to—

- (i) refund the remuneration received by him to the company; and
- (ii) pay for damages to the company, statutory bodies or authorities or to members or creditors of the company for loss arising out of incorrect or misleading statements of particulars made in his audit report.

Measures for prompt payment of damages [Section 147(4)]: The Central Government shall, by notification, specify any statutory body or authority or an officer for ensuring prompt payment of damages to the company or the persons under Section 147(3)(ii).

Such body, authority or officer shall after payment of damages to such company or persons file a report with the Central Government in respect of making such damages in such manner as may be specified in the said notification.

Joint and several liability of partners [Section 147(5)]: Where, in case of audit of a company being conducted by an audit firm, it is proved that the partner or partners of the audit firm has or have acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to or by, the company or its directors or officers, the liability, whether civil or criminal as provided in Companies Act, 2013 or in any other law for the time being in force, for such act shall be of the partner or partners concerned of the audit firm and of the firm jointly and severally.

Que. No. 61] Write a short note on: Liabilities of an auditor

Ans.: Apart from liability under the common law, the statutory liabilities of an auditor could be either Civil or Criminal.

Civil Liability: An auditor may be held liable to the company for negligence where loss is caused to the company due to the failure of the auditors to perform his duties with reasonable care and skill.

He is also liable for:

- (i) breach of trust regarding any money or property of the company or
- (ii) breach of duty.

Criminal Liability: An auditor is responsible for the destruction, mutilation, alteration, falsification or fraudulent concealment of any books, papers or documents belonging to the company with an intent to defraud or deceive; and also where he makes intentionally any false statement in any report or document prepared by him.

Criminal liability of an auditor may extend to imprisonment and/or fine at the discretion of the court.

COST AUDIT

Que. No. 62] What do you understand by Cost Audit? Explain the provisions of Companies Act, 1956 relating to cost audit?

Write a short note on: Appointment of cost auditor CS (Executive) – June 2012 (4 Marks)

Ans.: Cost Audit is a critical review undertaken for the purpose of:

- (a) Verification of the correctness of cost accounts and
- (b) Checking that cost accounting plan is adhered to.

The Institute of Cost Accountants of India defines statutory cost audit as, "A system of audit introduced by the Government of India for the review, examination and appraisal of the cost accounting records and added information required to be maintained by the specified industries".

Maintenance of costing records [Section 148(1)]: The Central Government may, by order, in respect of such class of companies engaged in the production of such goods or providing such services as may be prescribed, direct that particulars relating to the utilization of material or labour or to other items of cost as may be prescribed shall also be included in the books of account kept by that class of companies.

The Central Government shall, before issuing such order in respect of any class of companies regulated under a special Act, consult the regulatory body constituted or established under such special Act.

Rule 5 of the Companies (Cost Records & Audit) Rules, 2014 makes following provisions relating to maintenance of costing records:

- (1) Every company under Rule 3 including all units and branches, shall, maintain cost records in Form CRA-1.
- (2) The cost records shall be maintained on regular basis in such manner as to facilitate calculation of per unit cost of production or cost of operations, cost of sales and margin for each of its products and activities for every financial year on monthly or quarterly or half-yearly or annual basis.
- (3) The cost records shall be maintained in such manner so as to enable the company to exercise, as far as possible, control over the various operations and costs to achieve optimum economies in utilization of resources and these records shall also provide necessary data which is required to be furnished under these rules.

Cost Audit [Section 148(2)]: If the Central Government is of the opinion, that it is necessary to do so, it may, by order, direct that the audit of cost records of class of companies, which are covered under Section 148(1) and which have a net worth of prescribed amount or a turnover of prescribed amount, shall be conducted in the manner specified in the order.

Rule 4 of the Companies (Cost Records & Audit) Rules, 2014 specifies the following class of companies:

- (1) Every company specified in item (A) of Rule 3 shall get its cost records audited in accordance with these rules if the overall annual turnover of the company from all its products and services during the immediately preceding financial year is ₹ 50 Crore or more and the aggregate turnover of the individual product or products or service or services for which cost records are required to be maintained under rule 3 is ₹ 25 Crore or more.
- (2) Every company specified in item (B) of Rule 3 shall get its cost records audited in accordance with these rules if the overall annual turnover of the company from all its products and services during the immediately preceding financial year is rupees ₹ 100 Crore or more and the aggregate turnover of the individual product or products or service or services for which cost records are required to be maintained under Rule 3 is ₹ 35 Crore or more.
- (3) The requirement for cost audit under these rules shall not apply to a company which is covered in Rule 3 and
 - (i) whose revenue from exports, in foreign exchange, exceeds 75% of its total revenue or
 - (ii) which is operating from a special economic zone.

Appointment of cost auditor [Section 148(3)]: The cost audit shall be conducted by Cost Accountant who shall be appointed by the Board on such remuneration as may be determined by the members.

No person appointed under Section 139 (i.e. statutory auditor) as an auditor of the company shall be appointed for conducting the audit of cost records.

The cost auditor shall comply with the cost auditing standards.

Cost audit shall be in addition to the audit conducted under section 143.

Qualifications, disqualifications, rights, duties and obligations applicable to cost auditor [Section 148(5)]: The qualifications, disqualifications, rights, duties and obligations applicable to statutory auditors, so far as may be applicable, also apply to a cost auditor.

It shall be the duty of the company to give all assistance and facilities to the cost auditor for auditing the cost records of the company.

The cost audit report shall be submitted by the cost accountant to the Board of Directors of the company.

Submission of cost audit report to the Central Government [Section 148(6)]: Within 30 days from receipt of cost audit report from cost auditor, the company shall furnish the cost audit report to the Central Government, along with full information and explanation on every reservation or qualification contained therein.

Further information and explanation [Section 148(7)]: If, after considering the cost audit report and the information and explanation furnished by the company, the Central Government is of the opinion that any further information or explanation is necessary, it may call for such further information and explanation.

The company shall furnish the same within time specified by the Central Government.

Rule 6 of the Companies (Cost Records & Audit) Rules, 2014 makes following provisions relating to appointment of cost audit and procedure for cost audit:

- (1) The category of companies specified in Rule 3 and the thresholds limits laid down in rule 4, shall within 180 days of the commencement of every financial year, appoint a cost auditor.
- (2) The company shall inform the cost auditor of his or its appointment and file a notice of such appointment with the Central Government within a period of 30 days of the Board meeting in which such appointment is made or within a period of 180 of the commencement of the financial year, whichever is earlier, through electronic mode, in Form CRA-2, along with prescribed fees.
- (3) Every cost auditor appointed as such shall continue in such capacity till the expiry of 180 from the closure of the financial year or till he submits the cost audit report, for the financial year for which he has been appointed.
- (4) Every cost auditor, who conducts an audit of the cost records of a company, shall submit the cost audit report along with his or its reservations or qualifications or observations or suggestions, if any, in Form CRA-3.
- (5) Every cost auditor shall forward his report to the Board of Directors of the company within a period of 180 from the closure of the financial year to which the report relates and the Board of Directors shall consider and examine such report particularly any reservation or qualification contained therein.
- (6) The company within a period of 30 days from the date of receipt of a copy of the cost audit report, furnish the Central Government with such report along with full information and explanation on every reservation or qualification contained therein, in Form CRA-4 along with prescribed fee.

Que. No. 63] Distinguish between: Cost Audit & Statutory Audit

Ans.: The following are the main points of distinction between cost audit and statutory audit:

| Points | Cost Audit | Statutory Audit |
|--------------------|---|---|
| To whom it applies | Covers only select specified industries. Productwise coverage and not the whole company. | Compulsory for all companies incorporated under the Companies Act, 2013. |
| How applies | The Central Government may, by order, in respect of certain class of companies engaged in the production of prescribed goods or services direct that particulars relating to the utilization of material or labour or to other items of cost as may be prescribed shall also be included in the books of account kept by that class of companies. | Automatic application of provisions for all registered companies as per Section 139 of Companies Act, 2013. |

| Points | Cost Audit | Statutory Audit |
|-----------------------------------|--|---|
| By whom | Cost Audit is done by Cost Accountant. | Statutory Audit is done by Chartered Accountant. |
| Appointment of auditor | The Cost Auditor is appointed by the Board of directors. | Statutory Auditor is appointed by the members in AGM. |
| To Whom Audit report is submitted | The cost audit report shall be submitted by the Cost Accountant to the Board of Directors of the company. A company shall within 30 days from the date of receipt of a copy of the cost audit report furnish the Central Government such report along with full information and explanation on every reservation or qualification contained therein. | Audit report is submitted to the members in the AGM. |
| Base of report | The report is on <i>efficiency and propriety</i> . | The report is on <i>true & fair view</i> of the state of affairs and the profit and loss. |
| Emphasis is on | The emphasis is on adequacy or otherwise of the cost accounting system. | The emphasis is on verification & authenticity of transactions. |
| Form of audit report | Every cost auditor, who conducts an audit of the cost records of a company, shall submit the cost audit report along with his or its reservations or qualifications or observations or suggestions, if any, in Form CRA-3 | There is no specific format provided for statutory audit under the Companies Act, 2013. |

Que. No. 64] List out eight industry covered by the Companies (Cost Records & Audit) Rules, 2014. CS (Inter) - Dec 2001 (4 Marks)

Ans.: Some of the industries covered by Rule 3 of the Companies (Cost Records & Audit) Rules, 2014 are:

- Cement
- Tyres & tubes
- Electricals or electronic machinery
- Coffee and tea
- Drugs and pharmaceuticals
- Sugar and industrial alcohol
- Paper
- Plastics and polymers
- Milk powder
- Jute and jute products

INTERNAL AUDIT & AUDIT COMMITTEE

Que. No. 65] Write a short note on: Internal Audit

Whether a private company is mandatorily required to appoint an internal auditor? Who may be appointed as internal auditor? CS (Executive) - June 2015 (4 Marks)

Ans.: **Internal Audit [Section 138]:** Such class or classes of companies as may be prescribed shall be required to appoint an internal auditor, who shall either be a Chartered Accountant or a Cost Accountant, or such other professional as may be decided by the Board to conduct internal audit of the functions and activities of the company.

The Central Government may, by rules, prescribe the manner and the intervals in which the internal audit shall be conducted and reported to the Board.

Rule 13 of the Companies (Accounts) Rules, 2014 makes following provisions relating to internal audit: The following class of companies shall be required to appoint an internal auditor or a firm of internal auditors, namely:

- Every listed company
- Every unlisted public company having -

- paid up share capital of ₹ 50 Crore or more during the preceding financial year or
 - turnover of ₹ 200 Crore or more during the preceding financial year or
 - outstanding loans or borrowings from banks or public financial institutions exceeding ₹ 100 Crore or more at any point of time during the preceding financial year or
 - outstanding deposits of ₹ 25 Crore or more at any point of time during the preceding financial year
- (c) Every private company having -
- turnover of ₹ 200 Crore or more during the preceding financial year or
 - outstanding loans or borrowings from banks or public financial institutions exceeding ₹ 100 Crore or more at any point of time during the preceding financial year:

Explanation: For the purposes of this rule -

- The internal auditor may or may not be an employee of the company.
- The term "Chartered Accountant" shall mean a Chartered Accountant whether engaged in practice or not.

The Audit Committee of the company or the Board shall, in consultation with the Internal Auditor, formulate the scope, functioning, periodicity and methodology for conducting the internal audit.

Que. No. 66] PQR Ltd. is an unlisted public company having paid-up share capital of ₹ 80 Crores during the preceding financial year 2014-2015. The turnover of the company was ₹ 110 Crores for the same period. Referring to the provisions of the Companies Act, 2013, answer the following:

- Is it mandatory for the above company to appoint internal auditor for the financial year 2015-2016?
- What are the qualifications of the Internal Auditor?

CA (Final) - May 2015 (6 Marks)

Ans.: As per Section 138 read with Rule 13 of the Companies (Accounts) Rules, 2014, in case of unlisted public company, appointment of internal auditor is mandatory in following cases:

- If paid-up share capital is ₹ 50 Crore or more during the preceding financial year or
- If turnover is ₹ 200 Crore or more during the preceding financial year or
- If outstanding loans or borrowings from banks or public financial institutions exceeds ₹ 100 Crore or more at any point of time during the preceding financial year or
- If outstanding deposits is ₹ 25 Crore or more at any point of time during the preceding financial year.

As per the facts given in the question, PQR Ltd is an unlisted public company with the paid-up share capital of ₹ 80 Crores during the preceding financial year with the turnover of ₹ 110 crores. Since PQR Ltd. fulfils one of the criteria with paid up share capital of more than ₹ 50 Crore during the preceding financial year, it is mandatory for the PQR Ltd. to appoint an internal auditor for the financial year 2015-2016.

Qualifications of Internal Auditor: Internal Auditor shall either be a Chartered Accountant or a Cost Accountant or such other professional as may be decided by the Board to conduct internal audit of the functions and activities of the company. The internal auditor may or may not be an employee of the company.

Que. No. 67] Which types of Companies are required to constitute audit committee? Also state the scope and powers of audit committee.

Ans.: Constitution of Audit Committee [Section 177(1)]: The Board of Directors of every listed company and such other class or classes of companies, as may be prescribed, shall constitute an Audit Committee.

As per Rule 6 of the Companies (Meetings of Board & its Powers) Rules, 2014, the Board of directors of every listed companies and the following classes of companies shall constitute an Audit Committee and a Nomination and Remuneration Committee of the Board-

- (i) All public companies with a paid up capital of ₹ 10 Crore or more
- (ii) All public companies having turnover of ₹ 100 Crore or more;
- (iii) All public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding ₹ 50 Crore or more.

The paid up share capital or turnover or outstanding loans, or borrowings or debentures or deposits, as the case may be, as existing on the date of last audited Financial Statements shall be taken into account.

Composition of Audit Committee [Section 177(2)]: The Audit Committee shall consist of a minimum of 3 directors with independent directors forming a majority.

The majority of members of Audit Committee including its Chairperson shall be persons with ability to read and understand, the financial statement.

Scope of Audit Committee [Section 177(4)]: Every Audit Committee shall act in accordance with the terms of reference specified in writing by the Board which shall, inter alia, include –

- (i) The recommendation for appointment, remuneration and terms of appointment of auditors of the company.
- (ii) Review and monitor the auditor's independence and performance, and effectiveness of audit process.
- (iii) Examination of the financial statement and the auditors' report.
- (iv) Approval or any subsequent modification of transactions of the company with related parties. However, the audit committee may make omnibus approval for related party transactions proposed to be entered by the company subject to such conditions as may be prescribed.
- (v) Scrutiny of inter-corporate loans and investments
- (vi) Valuation of undertakings or assets of the company, wherever it is necessary.
- (vii) Evaluation of internal financial controls and risk management systems
- (viii) Monitoring the end use of funds raised through public offers and related matters.

"Omnibus Approval" shall mean a blanket pre activity approval by the Audit Committee subject to compliance of the conditions as laid in this Policy. [Revised Clause 49 mandated by the SEBI effective from October 1, 2014]

In case of transaction, other than related party transactions if Audit Committee does not approve the transaction, it shall make its recommendations to the Board of directors.

In case any transaction involving any amount not exceeding ₹ 1 Crore is entered into by a director or officer of the company without obtaining the approval of the Audit Committee and it is not ratified by the Audit Committee within 3 months from the date of the transaction, such transaction shall be voidable at the option of the Audit Committee and if the transaction is with the related party to any director or is authorized by any other director, the director concerned shall indemnify the company against any loss incurred by it.

However, the provisions of Section 174(4)(iv) shall not apply to a transaction, other than a transaction referred to in section 188, between a holding company and its wholly owned subsidiary company.

Interaction with internal and statutory auditors [Section 177(5)]: The Audit Committee may call for the comments of the auditors about internal control systems, the scope of audit, includ-

ing the observations of the auditors and review of financial statement before their submission to the Board and may also discuss any related issues with the internal and statutory auditors and the management of the company.

Power to investigate and obtains professional advice [Section 177(6)]: The Audit Committee shall have authority to investigate into any matter in relation to the items specified Section 177(4) or referred to it by the Board and shall have power to obtain professional advice from external sources and have full access to information contained in the records of the company.

Auditor and KMP right to be heard in the meetings of the Audit Committee [Section 177(7)]: The auditors of a company and the key managerial personnel shall have a right to be heard in the meetings of the Audit Committee when it considers the auditor's report but shall not have the right to vote.

Disclosure in Board's report [Section 177(8)]: The Board's report Section 134(3) shall disclose the composition of an Audit Committee and where the Board had not accepted any recommendation of the Audit Committee, the same shall be disclosed in such report along with the reasons.

Que. No. 68] What are the provisions of the Companies Act, 2013 regarding establishment of Vigil Mechanism?

Ans.: Establishment of Vigil Mechanism [Section 177(9)]: Every listed company or prescribed classes of companies shall establish a vigil mechanism for directors and employees to report genuine concerns in prescribed manner.

Requirements of Vigil Mechanism [Section 177(10)]: The vigil mechanism shall provide for adequate safeguards against victimization of persons who use such mechanism and make provision for direct access to the chairperson of the Audit Committee in appropriate or exceptional cases.

Disclosure: The details of establishment of vigil mechanism shall be disclosed by the company on its website and in the Board's report.

As per Rule 7 of the Companies (Meetings of Board & its Powers) Rule, 2014, every listed company and the companies belonging to the following class or classes shall establish a vigil mechanism for their directors and employees to report their genuine concerns or grievances-

- (a) The Companies which accept deposits from the public
- (b) The Companies which have borrowed money from banks and public financial institutions in excess of ₹ 50 Crore.

Audit committee to see the vigil mechanism: The companies which are required to constitute an audit committee shall oversee the vigil mechanism through the committee and if any of the members of the committee have a conflict of interest in a given case, they should rescue themselves and the others on the committee would deal with the matter on hand.

In case of other companies, the Board of directors shall nominate a director to play the role of audit committee for the purpose of vigil mechanism to whom other directors and employees may report their concerns.

Safeguards against victimization and access to audit committee: The vigil mechanism shall provide for adequate safeguards against victimization of employees and directors who avail of the vigil mechanism and also provide for direct access to the Chairperson of the Audit Committee or the director nominated to play the role of Audit Committee in exceptional cases.

Safeguards against frivolous complaints: In case of repeated frivolous complaints being filed by a director or an employee, the audit committee or the director nominated to play the role of audit committee may take suitable action against the concerned director or employee including reprimand.

SECRETARIAL AUDIT

Que. No. 69] Which type of companies are required to conduct secretarial audit? By whom such audit will be conducted? What is the penalty for or not conducting secretarial audit?

CS (Executive) - June 2015, Dec 2015 (4 Marks)

Ans.: Secretarial audit for bigger companies [Section 204]: Every listed company and a company belonging to prescribed class shall annex with its Board's report, a secretarial audit report, given by Practicing Company Secretary (PCS) in prescribed form.

It shall be the duty of the company to give all assistance and facilities to the PCS, for auditing the secretarial and related records of the company.

The Board of Directors, in their report shall explain in full any qualification or observation or other remarks made by the PCS.

If a company or any officer or PCS, contravenes the provisions of this section, they shall be punishable with fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 5,00,000.

Secretarial Audit Report [Rule 9 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014]: For the purposes Section 204(1), the other class of companies shall be as under-

- (a) Every public company having a paid-up share capital of ₹ 50 Crore or more or
- (b) Every public company having a turnover of ₹ 200 Crore or more.

The format of the Secretarial Audit Report shall be in Form No. MR. 3.

Secretarial audit is a compliance audit and it is a part of total compliance management in an organization. The Secretarial audit is an effective tool for corporate compliance management. It helps to detect non-compliance and to take corrective actions.

CHAPTER

21

DIVISIBLE PROFITS & DIVIDENDS

This Chapter Covers:

- > Definition and meaning of dividend
- > Difference between dividend and interest
- > Types of dividend
- > Dividend on preference shares
- > Dividend on equity shares
- > Restrictions on declaration of dividend
- > Ascertainment of divisible profits and dividends
- > Payment of Dividend without providing depreciation
- > Declaration of dividend
- > Revocation of declared dividend
- > Who is eligible to receive dividend
- > When Dividend is payable
- > Establishment of Investor Education and Protection Fund
- > Dividend warrants
- > Dividend mandate
- > Payment of interest out of capital
- > Payment of Dividend out of Capital Profits
- > Remittance of dividend or interest or sale proceeds to NRIs, foreigners and foreign companies.

DIVIDEND

Que. No. 1] Define the term 'dividend'.

CS (Inter) - June 1999 (2 Marks)

Ans.: Dividend [Section 2(35)]: Dividend includes any interim dividend.

Thus, all the provisions that are applicable to final dividend are also applicable to interim dividend.

Dividend is the return on the share capital subscribed for and paid to a company by its shareholders.

Payment of dividend in proportion to amount paid-up [Section 51]: A company may, if so authorized by its articles, pay dividends in proportion to the amount paid-up on each share.

As per Regulation 83 of Table F, dividend can be paid on the paid-up value of shares. Dividend cannot be paid on calls-in-advance.

Que. No. 2] Write a short note on: Types of Dividend

CS (Inter) – Dec 2003 (4 Marks), June 2007 (4 Marks)

Write a short note on: Interim Dividend

CS (Inter) – Dec 2003 (4 Marks)

CS (Executive) – June 2009 (4 Marks)

Ans.: Following are the various types on dividend:

- (1) **Final Dividend:** Final dividend is recommended by the board of directors in its report to the shareholders, which is attached to the balance sheet. It is declared by the shareholders at the AGM. Usually AOA of companies provide that the shareholders *cannot increase* the rate or amount of dividend than the one recommended by the Board. The shareholders may, however, declare the payment of dividend on equity shares at a rate *lower than* the one recommended by the directors in their report.

It is the discretion of the board of directors to recommend or not to recommend the declaration of final dividend, which has to be exercised in good faith in the interest of the company. The shareholders have no power to declare final dividend in the absence of a recommendation of the board of directors in this regard.

- (2) **Interim Dividend:** The interim dividend is paid in the middle of the year. A company can normally estimate its profits for the current financial year on a fairly reasonable basis and in that event it can allocate to the reserves the prescribed percentage of profits on the basis of its estimated profits. As a measure of precaution, the company may allocate to the reserves a higher amount than the actual amount based on the prescribed percentage of its estimated profits.

Interim dividend stands on the same footing as that of the final dividend. Both interim and final dividend when declared become debt and are payable within 30 days of declaration.

Que. No. 3] Distinguish between: Dividend & Interest CS (Inter) – June 2006 (5 Marks)

Ans.: The following are the main points of distinction between dividend & interest:

| Points | Dividend | Interest |
|---------|---|---|
| Meaning | Dividend is the return on the share capital subscribed for and paid to a company by its shareholders. As per Section 2(35), "dividend includes any interim dividend." | Interest is the return on the debenture issued and deposit accepted by the company. The term interest is not defined under the Companies Act, 2013. |
| Paid on | Dividend is paid on preference and equity shares. | Interest is paid on debenture, deposit, bonds, long term borrowings and short term borrowings. |
| Rate | Rate of dividend is variable in case of equity shares and on preference shares dividend is on fixed rate. | Interest rate is fixed normally at the time of issue and in case of loan at the time of agreement. |

| Points | Dividend | Interest |
|-----------------------|--|--|
| Debt | A dividend becomes a debt only after it has been declared by the company. | Interest becomes debts on the expiry of fixed period which may monthly, quarterly or yearly. |
| divisible profit | Dividend can be paid only when there is divisible profit. | Interest has to be paid whether there is divisible profit or not. |
| Treatment in accounts | Dividend is an appropriation of profits. In accounts it is debited to profit & loss Appropriation Account. | Interest is a charge on profits. In accounts it is debited to profit & loss Account |

Que. No. 4] Write a short note on: Dividend on Preference Shares

Ans.: A preference share carries a preferential right as to dividend in accordance with the term of issue and the articles of association, subject to the availability of distributable profits. The preferential right to a dividend could either be a fixed amount or an amount calculated at a fixed rate. It may be cumulative or non-cumulative. Preference shares can carry dividend of a fixed amount, before any dividend is paid on the equity shares.

Preference shares are part of the company's share capital, consequently, preference dividends can be paid only if the company has earned sufficient profits. A dividend becomes payable to the shareholders only when it is declared in the manner laid down in the Act and by the company's articles. There should have been a formal declaration. Preference shareholders are not entitled to treat the preference dividend as a debt and sue for its payment. However, if the articles specify that the company's profit shall be applied, by way of payment of the preference dividend, the preference shareholder can sue for it even though it has not been declared.

Que. No. 5] Write a short note on: Divisible Profits

CS (Executive) – Dec 2011 (4 Marks)

Ans.: Divisible profit means the profits which the law allows the company to distribute to the shareholders by way of dividend. "Profits available for dividend" has been held to mean the profits which the directors consider should be distributed after making provision for depreciation or past losses, for reserves or for other purposes.

Que. No. 6] Write a short note on: Sources of dividend

What provisions and rules are to be observed by company before declaring dividend?

CS (Inter) – June 1999 (2 Marks)

Dividend can be paid out of capital, if the articles of association authorize such payment.

Comment. CS (Executive) – Dec 2011 (5 Marks), Dec 2012 (5 Marks)

Ans.: Dividend cannot be paid out of capital, even if the AOA authorize such payment.

Sources of dividend [Section 123(1)]: A company can pay dividend from the following sources:

- (1) **Dividend out of current profits:** A company can pay dividend out of the profits of the company for that year arrived at after providing for depreciation as per Section 123(2). In computing profits any amount representing unrealized gains, notional gains or re-valuation of assets and any change in carrying amount of an asset or of a liability on measurement of the asset or the liability at fair value shall be excluded.
- (2) **Dividend out of profits of previous financial years:** A company can pay dividend out of profits for any previous financial years after providing for depreciation and remaining undistributed.
- (3) **Dividend out of money provided by the Central or State Government:** A company can pay dividend out of money provided by the Central or State Government for the payment of dividend by the company in pursuance of a guarantee given by that Government.

Dividend can be declared out of free reserve only: No dividend shall be declared or paid by a company from its reserves other than free reserves.

Prohibition on declaration of dividend [Section 123(6)]: If a company fails to comply with the provisions of Section 73 (*Prohibition of acceptance of deposits from public*) & Section 74 (*Repayment of deposits, etc., accepted before the commencement of the Companies Act, 2013*) shall not declare any dividend on its equity shares so long as such failure continues.

Que. No. 7] The Board of Directors of ABC Ltd. proposes to declare dividend at the rate of 20% to the equity shareholders, despite the fact that the company has defaulted in repayment of public deposits accepted before the commencement of Companies Act, 2013.
Comment. CA (Final) – May 2015 (3 Marks)

Ans.: Section 123(6) specifically provides that a company which fails to comply with the provisions of Section 73 (Prohibition of acceptance of deposits from public) and Section 74 (Repayment of deposits, etc., accepted before the Commencement of the Companies Act, 2013) shall not, so long as such failure continues, declare any dividend on its equity shares.

In the given instance, the Board of Directors of ABC Ltd. proposes to declare dividend at the rate of 20% to the equity share holders, in spite of the fact that the Company has defaulted in repayment of public deposits accepted before the commencement of the Companies Act, 2013. So, according to the above provision, declaration of dividend by the ABC Ltd. is not valid.

Que. No. 8] Outline the provisions with regard to transfer of profits to reserves which should be borne in mind at the time of declaration of dividend by a company.

CS (Inter) – Dec 2006 (4 Marks)

Ans.: Transfer to reserve [First proviso to Section 128(1)]: A company may, before the declaration of any dividend in any financial year, transfer such percentage of its profits for that financial year as it may consider appropriate to the reserves of the company.

Que. No. 9] Can dividend be declared without providing depreciation? Whether it is necessary to set off previous losses and depreciation before declaration of dividend?

CS (Inter) – June 2006 (8 Marks)

Ans.: Depreciation [Section 128(2)]: For the purposes of Section 123(1)(a), depreciation shall be provided in accordance with the provisions of Schedule II.

Dividend cannot be declared unless previous losses and depreciation are set off [Fourth proviso to Section 128(1)]: No company shall declare dividend unless carried over previous losses and depreciation not provided in previous years are set off against profit of the company for the current year.

Que. No. 10] Under Section 123(1), depreciation will have to be provided for working out distributable profit. Though, the present value of land of a company, dealing with land, is much less than the book value, the difference between the book value and market value was not amortized before declaring dividend. Discuss.

CS (Executive) – Dec 2008 (8 Marks)

Ans.: As per Section 123(1), dividend can be paid by a company out of the profits of the company for that year after providing for depreciation as per Section 123(2). However the 'land' is not subject to depreciation hence question adjusting difference between the book value and market value by way of amortization does not arise.

Que. No. 11] Can the dividend be declared out of previous year's profits transferred to reserve? Discuss.
 CS (Executive) – Dec 2008 (6 Marks)

Ans.: Declaration of dividend out of reserve [Second proviso to Section 128(1)]: If due to inadequacy or absence of profits in any financial year, any company proposes to declare dividend out of the accumulated profits earned by it in previous years and transferred by the company to the free reserves, such declaration of dividend shall be made except in accordance with such rules as may be prescribed in this behalf.

However, no company shall declare dividend unless carried over previous losses and depreciation not provided in previous year(s) are set off against profit of the company for the current year.

As per Rule 7 of the Companies (Declaration & Payment of Dividend) Rules, 2014, in the event of inadequacy or absence of profits in any year, a company may declare dividend out of surplus subject to the fulfilment of the following conditions:

- (1) The rate of dividend declared shall not exceed the average of the rates at which dividend was declared by it in the 3 years immediately preceding that year.
- (2) The total amount to be drawn from such accumulated profits shall not exceed 1/10th of the sum of its paid-up share capital and free reserves as appearing in the latest audited financial statement.
- (3) The amount so drawn shall first be utilized to set off the losses incurred in the financial year in which dividend is declared before any dividend in respect of equity shares is declared.
- (4) The balance of reserves after such withdrawal shall not fall below 15% of its paid up share capital as appearing in the latest audited financial statement.
- (5) No company shall declare dividend unless carried over previous losses and depreciation not provided in previous year are set off against profit of the company of the current year the loss or depreciation, whichever is less, in previous years is set off against the profit of the company for the year for which dividend is declared or paid.

Free Reserves [Section 12(43)]: Free reserves means such reserves which, as per the latest audited balance sheet of a company, are available for distribution as dividend

There is restriction on declaration of dividend out of reserves. There is no restriction in distributing dividend out of balance on profit & loss account i.e. undistributed profit of previous year.

Que. No. 12] Yash Ltd. has only one type of capital, viz. 40,000 equity shares of ₹ 100 each. It also has got reserves totalling ₹ 20,00,000. The company closes its books on 31st March each year. It has paid dividends @ 15% up to 2012-2013 and 20% thereafter. In 2015-2016, the company suffered a loss of ₹ 2,50,000; therefore, it wishes to draw required amount out of the reserves to pay dividend at 12%. Advise the company.

CS (Inter) – Dec 2005 (4 Marks)

Ans.: Dividends can be declared out of past years profits transferred to reserves. In this case, the company has to comply with the Companies (Declaration of Dividend Out of Reserves) Rules, 2014. It lay down the following conditions subject to which a dividend may be declared by a company in the event of inadequacy or absence of profits in any year out of the profits earned by it in previous years and transferred to reserves.

- (1) The rate of dividend declared shall not exceed the average of the rates at which dividend was declared by it in the 3 years immediately preceding that year.

| Year | Dividend Rate |
|-----------|---------------|
| 2012-2013 | 15% |
| 2013-2014 | 20% |
| 2014-2015 | 20% |
| | 55% |

Average rate of dividend = $55/3 = 18.33\%$

So, 18.33% dividend can be paid at first instance.

Amount required for dividend at 18.33% = $40,00,000 \times 18.33\% = 7,33,200$.

- (2) The total amount to be drawn from such accumulated profits shall not exceed 1/10th of the sum of its paid-up share capital and free reserves as appearing in the latest audited financial statement.

$1/10^{\text{th}}$ of (Paid up capital + Free Reserve) = $(40,00,000 + 20,00,000) \times 1/10 = 6,00,000$.

Thus, above amount in condition (1) will be restricted to ₹ 6,00,000.

- (3) The amount so drawn shall first be utilized to set off the losses incurred in the financial year in which dividend is declared before any dividend in respect of equity shares is declared.

| | |
|--|------------|
| Total amount to be drawn from such accumulated profits | 6,00,000 |
| (-) Losses incurred | (2,50,000) |
| (-) Preference dividend | - |
| Amount that can be drawn from accumulated profits | 3,50,000 |

So, rate of dividend = $3,50,000/40,00,000 \times 100 = 8.75\%$

- (4) The balance of reserves after such withdrawal shall not fall below 15% of its paid up share capital as appearing in the latest audited financial statement.

| | |
|---|------------|
| Reserves | 20,00,000 |
| Amount that can be drawn from accumulated profits | (3,50,000) |
| Balance of reserve | 16,50,000 |

Paid up capital $\times 15\% = 40,00,000 \times 15\% = 6,00,000$

As balance of reserve i.e. 16,50,000 is more than 6,00,000. This condition is fulfilled.

So, rate of dividend can be 8.75%.

Que. No. 13] State the provisions of the Companies Act, 2013 relating to 'interim dividend'.
CS (Executive) – June 2009 (4 Marks)

Ans.: Declaration of interim dividend [Section 123(3)]: The Board of Directors of a company may declare interim dividend during any financial year or at any time during the period from closure of financial year till holding of AGM

- Out of the surplus in the profit and loss account or
- Out of profits of the financial year for which such interim dividend is sought to be declared or
- Out of profits generated in the financial year till the quarter preceding the date of declaration of the interim dividend

Restriction on interim dividend in case of loss: In case the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding 3 financial years.

Que. No. 14] WL Ltd. is facing loss in business during the current financial year 2015-2016. In the immediate preceding 3 financial years, the company had declared dividend at the rate of 8%, 10% & 12% respectively. To maintain the goodwill of the company, the Board of Directors has decided to declare 12% interim dividend for the current financial year. Examine the applicable provisions of the Companies Act, 2013 and state whether the Board of Directors can do so?
CA (Final) – May 2015 (3 Marks)

Ans.: According to Section 123(3) in case the company has incurred loss during the current financial year up to the end of quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years.

In the given case the company is facing loss during the current financial year 2015-2016.

In the immediate preceding three financial years, the company declared dividend at the rate of 8%, 10% & 12%. As per the above mentioned provision, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years [i.e. $8+10+12=30/3=10\%$]. Therefore, decision of Board of Directors to declare 12% of the interim dividend for the current financial year is not tenable.

Que. No. 15] Distinguish between: Interim Dividend & Final Dividend

CS (Executive) – Dec 2014 (5 Marks)

Ans.: The following are the main points of distinction between interim & final dividend:

| Points | Interim Dividend | Final Dividend |
|-----------------------------|---|---|
| Meaning | Dividend which is paid in the middle of the year is known as interim dividend. | Dividend which is recommended by the board of directors and approved by the shareholders in AGM is known as final dividend. |
| Shareholder's approval | Interim dividend can be declared by the board of directors and it does not require approval of the shareholder. | Final dividend is recommended by the board of directors and must be approved by the shareholders. |
| Decrease in rate | Since interim dividend does not require approval of shareholders, rate of interim dividend cannot be decreased. | The shareholders cannot increase the rate of dividend than the one recommended by the Board. The shareholders may, however, declare the payment of dividend on equity shares at a rate lower than the one recommended by the directors in their report. |
| Sources | A company may declare interim dividend during any financial year out of the surplus in the profit and loss account and out of profits of the financial year in which such interim dividend is sought to be declared. | A company can pay final dividend from the following sources: <ul style="list-style-type: none"> - out of current profits - out of profits of previous financial years - out of money provided by the Central or State Government |
| Restriction in case of loss | In case the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding 3 financial years. | If due to inadequacy or absence of profits in any financial year, any company proposes to declare final dividend out of the accumulated profits earned by it in previous years and transferred by the company to the reserves, such declaration of dividend shall be made as per the Companies (Declaration & Payment of Dividend) Rules, 2014. |

Que. No. 16] Is company required to deposit the amount of dividend declared to separate account? Also state to whom the dividend is payable?

Ans.: Deposit in a separate account of dividend after declaration [Section 123(4)]: The amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate account within 5 days from the date of declaration of such dividend.

Any dividend payable in cash may be paid by cheque or warrant or in any electronic mode to the shareholder entitled to the payment of the dividend.

Payment of dividend to registered shareholder [Section 123(5)]: Dividend shall be paid by a company in respect of any share to the registered shareholder only or to his order or to his banker and shall be payable in cash. (Thus, dividend cannot be paid in 'kind' e.g. in form of gifts, goods)

However, the capitalization of profits or reserves of a company for the purpose of issuing fully paid-up bonus shares or paying up any amount for the time being unpaid on any shares held by the members of the company is permitted.

Que. No. 17] When dividend is payable?

CS (Inter) – June 2008 (2 Marks)

State the legal provisions relating to disposal of unpaid and unclaimed dividends.

CS (Inter) – June 1999 (2 Marks), Dec 2005 (4 Marks)

CS (Inter) – Dec 2006 (6 Marks)

Ans.: Unpaid Dividend Account [Section 124(1)]: After declaration of dividend, a company has to pay dividend within 30 days of declaration of dividend. If amount of dividend remains unpaid or unclaimed for 30 days of declaration of dividend, then in next 7 days the company has to transfer the amount unclaimed to a special account in any scheduled bank to be called the "Unpaid Dividend Account".

Posting the details of unpaid dividend on website [Section 124(2)]: The company shall, within a period of 90 days of making any transfer of an amount to the Unpaid Dividend Account, prepare a statement containing the names, their last known addresses and the unpaid dividend to be paid to each person and place it on the website of the company and also on any other website approved by the Central Government, in prescribe form and in prescribed manner.

Payment of interest [Section 124(3)]: If any default is made in transferring the total amount to the Unpaid Dividend Account, the company shall pay interest at the rate of 12% p.a. on so much of the amount as has not been transferred to the Unpaid Dividend Account.

Claiming dividend from Unpaid Dividend Account [Section 124(4)]: Any person claiming to be entitled to any money transferred under Section 124(1) to the Unpaid Dividend Account of the company may apply to the company for payment of the money claimed.

Transfer from Unpaid Dividend Account to Investor Education & Protection Fund [Section 124(5)]: Any money transferred to the Unpaid Dividend Account and which remains unpaid or unclaimed for a period of 7 years from the date of such transfer shall be transferred by the company along with interest accrued thereon to the Investor Education & Protection Fund established Section 125 (1).

The company shall send a statement in the prescribed form of the details of such transfer to the authority which administers the said Fund and that authority shall issue a receipt to the company as evidence of such transfer.

Transfer of shares to Investor Education & Protection Fund [Section 124(6)]: All shares in respect of which dividend has been claimed for seven consecutive years or more shall be transferred by the company in the name of Investor Education and Protection Fund along with a statement containing prescribed details.

However, any claimant of shares transferred above shall be entitled to claim the transfer of shares from Investor Education and Protection Fund in accordance with prescribed procedure and on submission of prescribed documents.

Que. No. 18] Write a short note on: Investor Education & Protection Fund

CS (Inter) – June 2008 (4 Marks)

CS (Executive) – Dec 2010 (4 Marks), June 2013 (4 Marks)

Rise Ltd., a company with diversified interests, has constituted Investor Education and Protection Fund as required under the provisions of the Companies Act, 2013. The company has so far not deposited any amount to the fund. The President (Finance) has asked you, the Company Secretary, to submit a note on amounts payable to the credit of the fund and the period within which amount shall be paid. Prepare the said note.

CS (Executive) – Dec 2016 (4 Marks)

Ans.: Establishment of Investor Education & Protection Fund [Section 125 (1)]: The Central Government shall establish a Fund to be called the Investor Education and Protection Fund (herein referred to as the Fund).

Amount credited to Fund [Section 125(2)]: There shall be credited to the Fund –

- (a) Amount given by the Central Government by way of grants
- (b) Donations given by the Central Government, State Governments, companies or any other institution
- (c) Amount in the Unpaid Dividend Account
- (d) Amount in the general revenue account of the Central Government which had been transferred as per Section 205A(5) of the Companies Act, 1956
- (e) Amount lying in the Investor Education and Protection Fund under Section 205C of the Companies Act, 1956
- (f) Interest or other income received out of investments made from the Fund
- (g) Amount received Section 38(4)
- (h) Application money received by companies for allotment of any securities and due for refund
- (i) Matured deposits with companies other than banking companies
- (j) Matured debentures with companies
- (k) Interest accrued on the amounts referred to in clauses (h) to (j)
- (l) Sale proceeds of fractional shares arising out of issuance of bonus shares, merger and amalgamation for 7 or more years
- (m) Redemption amount of preference shares remaining unpaid or unclaimed for 7 or more years and
- (n) Other prescribed amounts

Amount referred to in clauses (h) to (j) shall form part of the Fund unless such amount has remained unclaimed and unpaid for a period of 7 years from the date it became due for payment.

Utilization of Fund [Section 125(3)]: The Fund shall be utilized for –

- (a) Refund in respect of unclaimed dividends, matured deposits, matured debentures, the application money due for refund and interest thereon.
- (b) Promotion of investor's education, awareness and protection.

- (c) Distribution of any disgorged amount among eligible and identifiable applicants for shares or debentures, shareholders, debenture-holders or depositors who have suffered losses due to wrong actions by any person, in accordance with the orders made by the Court which had ordered disgorgement.
- (d) Reimbursement of legal expenses incurred in pursuing class action suits under Sections 37 & 245 by members, debenture-holders or depositors as may be sanctioned by the Tribunal
- (e) Any other incidental purpose, in accordance with prescribed rules.

Explanation: The disgorged amount refers to the amount received through disgorgement or disposal of securities.

Any person claiming to be entitled to the amount referred in Section 125(2) may apply to the authority constituted Section 125(5) for the payment of the money claimed.

Que. No. 19] When dividend can be held in abeyance?

Ans.: Right to dividend, rights shares and bonus shares to be held in abeyance pending registration of transfer of shares [Section 126]: Where any instrument of transfer of shares has been delivered to any company for registration and the transfer of such shares has not been registered by the company, it shall -

- (a) transfer the dividend in relation to such shares to the Unpaid Dividend Account unless the company is authorized by the registered holder of such shares in writing to pay such dividend to the transferee specified in such instrument of transfer and
- (b) keep in abeyance in relation to such shares, any offer of rights shares and any issue of fully paid-up bonus shares.

Que. No. 20] What is the penalty if a dividend has not been paid by the company within 30 days from the date of declaration? Also state the circumstances when a company will not be deemed to have committed any offence if it does not pay dividend in prescribed period?

Write a short note on: Punishment for failure dividend and its exceptions
CS (Executive) - June 2016 (4 Marks)

Ans.: Punishment for failure to distribute dividends [Section 127]: Where a dividend has been declared by a company but has not been paid or the dividend warrant has not been posted within 30 days from the date of declaration to any shareholder entitled to the payment of the dividend, every director of the company shall, if he is knowingly a party to the default, be punishable:

- With imprisonment which may extend to 2 years and
- With fine which shall not be less than ₹ 1,000 for every day during which such default continues

The company shall also be liable to pay simple interest at the rate of 18% p.a. during the period for which such default continues.

When payment of dividend may be withheld: In following cases, non-payment of dividend will be permitted i.e. it will not be treated as offence:

- (a) Where the dividend could not be paid by reason of the operation of any law.
- (b) Where a shareholder has given directions to the company regarding the payment of the dividend and those directions cannot be complied with and the same has been communicated to him.
- (c) Where there is a dispute regarding the right to receive the dividend.

- (d) Where the dividend has been lawfully adjusted by the company against any sum due to it from the shareholder.
- (e) Where the failure to pay the dividend or to post the warrant was not due to any default on the part of the company.

Que. No. 21] The Annual General Meeting of ABC Ltd. declared a dividend at the rate of 30% payable on paid up equity share capital of the company as recommended by Board of Directors on 30th April, 2014. But the company was unable to post the dividend warrant to Ranjan, an equity shareholder, up to 30th June, 2014. Ranjan filed a suit against the company for the payment of dividend along with interest at the rate of 20% p. a. for default period. Decide in the light of provisions of the Companies Act, 2013, whether Ranjan would succeed? Also state the director's liability in this regard.

CA (Final) - Nov 2013 (5 Marks)

Ans.: As per Section 124(1), a company has to pay dividend within 30 days of declaration of dividend. The posting of dividend warrant by the company within 30 days will be deemed to be payment irrespective of the fact whether the shareholder has encashed it or not.

Failure to pay or post dividend warrant within 30 days constitutes an offence and as per Section 127, the company shall be liable to pay simple interest at the rate of 18% p.a. during the period for which such default continues.

In the given case, the AGM of ABC Ltd. declared a dividend at the rate of 30% payable on paid up equity share capital as recommended by the board of directors on 30th April, 2014. But, the company was unable to post the dividend warrant to Mr. Ranjan, up to 30th June, 2014 and thus there is contravention of Section 127.

- (i) In view of the above provisions, Mr. Ranjan can file a suit against the company for the payment of dividend because failure to pay or post dividend warrant within 30 days. Thus, he would succeed but he is entitled for simple interest at the rate of 18% p.a. (and not 20% as claimed) during the period for which such default continues.
- (ii) Every director of the company, if he is knowingly a party to the default, is punishable
 - With imprisonment which may extend to 2 years and
 - With fine which shall not be less than ₹ 1,000 for every day during which such default continues

Que. No. 22] A company for the financial year 2014-2015 declared dividend on 19th September 2015 but failed to pay the same within the prescribed time. A case was filed against director in this regard. The director has contended that he had resigned before the declaration of dividend. Decide the fate of directors in the light of relevant provisions of the Companies Act, 2013.
CS (Executive) - Dec 2013 (4 Marks)

Ans.: As per Section 124(1), a company has to pay dividend within 30 days of declaration of dividend. Failure to pay or post dividend warrant within 30 days constitutes an offence and directors of the company are liable to punishment as provided under Section 127.

However, in *N. Kumar vs. M.O. Roy, Assistant Director, S.F.I.O (2007) 80 SCL 55 (MAD)*, it was held that if the director has resigned before declaration of dividend then he cannot be held liable for the default of non-payment of dividend within 30 days of declaration of dividend as he may not be aware about the entire affairs of the company after his resignation.

Que. No. 23] How and who declares the dividend? Can shareholder increase the rate of dividend recommended by board of director?

Ans.: Board of director of company recommends dividend and it is approved by the shareholder in the AGM. Shareholder can reduce the rate of dividend proposed by shareholder but cannot increase it.

Company can declare dividend in extra ordinary general meeting (EOGM), if it could not declare dividend in annual general meeting (AGM). [Department Circular No. 22 dated 25.9.1975]

However, if dividend is declared in AGM, it cannot be increased in further in subsequent EGM.

Que. No. 23A] A resolution was passed by the shareholders in an annual general meeting approving final dividend @ 20% for the financial year 2016-2017 and one month later the Board of directors decided to pay further dividend @ 5% for the financial year 2016-2017.
CS (Executive) - Dec 2008 (5 Marks)

Ans.: Board of director of company recommends dividend and it is approved by the shareholder in the AGM. Shareholder can reduce the rate of dividend proposed by shareholder but cannot increase it.

Company can declare dividend in extraordinary general meeting (EOGM), if it could not declare dividend in annual general meeting (AGM). [Department Circular No. 22 dated 25.9.1975]

However, if dividend is declared in AGM, it cannot be increased in further in subsequent EGM or board meeting.

Thus, decisions of directors to pay further dividend @ 5% for the financial year 2016-2017 for which already dividend is declared @ 20% is invalid.

Que. No. 24] Dividend once declared becomes debt. Comment.

CS (Inter) - Dec 2004 (4 Marks)

Can decision to pay interim dividend be revoked? CS (Inter) - June 2002 (2 Marks)

The board of directors of a company in a meeting held on 30th April, 2015 declared interim dividend. In another meeting held on 18th May 2015, the board of directors revoked the interim dividend declared without assigning any reason. Advise the company in the matter.
CS (Executive) - Dec 2013 (8 Marks), Dec 2014 (4 Marks)

Ans.: A dividend when declared becomes a debt and a shareholder is entitled to sue for recovery of the same after expiry of the period of 30 days prescribed u/s 207. A dividend when proposed does not become a debt but only becomes debt when declared.

Revocation of declared dividend: A dividend including interim dividend once declared becomes a debt and cannot be revoked, *except with the consent of the shareholders*. But where a dividend has been illegally declared, the directors will be justified in revoking the declared dividend. If an illegally declared dividend is paid then the directors shall be responsible, liable and accountable to the company personally.

As per Section 2(35), "dividend includes any interim dividend." Hence, interim dividend also cannot be revoked.

Que. No. 24A] In Evergreen Ltd., the Board of directors declared an interim dividend but could not distribute the dividend due to objections of audit committee that the accounts considered by the Board were false; and true financial results were inflated by not incorporating outstanding liabilities and over-valuation of inventories. A shareholder filed a suit for non-payment of dividend. One of the directors contended that he never attended the Board meeting where the issue relating to payment of interim dividend was declared on the basis of false accounts. Discuss about the validity of contention of the director.

CS (Executive) - Dec 2014 (4 Marks)

Ans.: As per Section 124(1), a company has to pay dividend within 30 days of declaration of dividend. Failure to pay or post dividend warrant within 30 days constitutes an offence and directors of the company are liable to punishment as provided under Section 127.

A dividend including interim dividend once declared becomes a debt and cannot be revoked, *except with the consent of the shareholders*. But where a dividend has been illegally declared, the directors will be justified in revoking the declared dividend.

Que. No. 25] Write a short note on: Dividend Warrant CS (Inter) - Dec 1999 (4 Marks)

Ans.: "Dividend warrant" is an order by the company to its banker to pay the amount specified therein to the shareholder whose name is written therein. The shareholder may, at his discretion thereafter draw the amount of the warrant from his account with the bank and with whom he deposits the warrant for collection.

Dividend Mandate: The shareholders may desire that their dividends be credited directly to their bank account. The request will be made in a form duly filled and sent to the company. This is known as "Dividend Mandate". This authorizes the company to pay dividends directly to bank account of the shareholder. This form is also used for purposes like payment of interest on debentures and other securities.

Que. No. 26] What is 'capital profit'? Can dividend be declared out of capital profit? If so, under what circumstances?
CS (Inter) - June 2008 (4 Marks)

CS (Executive) - Dec 2008 (6 Marks)

Ans.: The term capital profits may be defined to mean those profits which arise otherwise than in the normal course of the business and earned out of capital transactions. The usual sources of capital profits are:

- Profits on sale of fixed assets
- Profits on revaluation of fixed assets
- Premium on issue of shares/debentures/bonds
- Profits on reissue of forfeited shares
- Capital redemption reserve account
- Profit prior to incorporation

The Act does not mention specifically whether capital profits i.e. profits which arise where a company sells part of its fixed assets at a price higher than the original cost of such asset, can be distributed as dividend. However, in the two important cases *Lubbock vs. British Bank of South America* (1892) 2 Ch. 198 and *Foster vs. The New Trinidad Lake Asphalt Co. Ltd.* (1901) 1 Ch.208, the Courts have held that capital profits cannot be considered as available for distribution as dividend *unless*:

- (a) The AOA authorize such a distribution and
- (b) The surplus is realized and remains after a valuation of the whole of the assets and liabilities.

CHAPTER

22

BOARD'S REPORT
& DISCLOSURES

This Chapter Covers:

- Disclosures in director's report under Companies Act, 2013
- Disclosures director's report due listing agreement
- Disclosures pursuant to directions of RBI
- Approval of the Board's Report
- Signing and dating of the Board's Report
- Filing of the Board's Report
- Right of members to copies of Balance sheet, Board's Report etc.
- Liability of mis-statement

Que. No. 1] What do you understand by the 'Board Report'?

Ans.: The Board's Report is an important means of communication by the Board of Directors, serving to inform the stakeholders about the performance and prospects of the company, relevant changes in management, capital structure, major policies, and recommendations as to the distribution of profits, future programmes of expansion, modernization and diversification, capitalization of reserves, further issue of capital, etc.

- ◆ The matters to be included in the Board's Report have been specified in Section 134(3). Apart from this, Sections 92, 102(2), 131, 135(2), 135(5), 136, 137, 177(8), 178(4), 179(3)(g), 188(2), 197(12), 197(14), 204(1), 204(3) also contain provisions in relation to the Board's Report.
- ◆ The Board's Report of companies whose shares are listed on a stock exchange must include additional information as specified in the Listing Agreement.
- ◆ Further, the RBI Act, 1934, the SEBI Act, 1992 and the regulations, rules, directions, guidelines, circulars, etc. issued there under, necessitate certain additional disclosures to be made in the Board's Report.
- ◆ ICSI issued **Secretarial Standard 10**, which seeks to lay down practices pertaining to the preparation and presentation of the Board's Report.

Que. No. 2] What matters to be included in the Board's Report under Section 134 and other provisions under the Companies Act, 2013?

CS (Inter) - Dec 2002 (2 + 2 + 1 = 5 Marks), June 2003 (4 Marks)

Ans.: Board's Report [Section 134(3)]: There shall be attached to statements laid before a company in general meeting, a report by its Board of Directors, which shall include -

- (a) The web address, where the annual return has been placed.
- (b) Number of meetings of the Board.
- (c) Directors' Responsibility Statement.
- (d) Details in respect of frauds reported by the auditor under Section 143(12) other than those which are reportable to the Central Government.
- (e) A statement on declaration given by independent directors Section 149(6).
- (f) In case of a company required to constitute Nomination & Remuneration Committee, company's policy on directors appointment and remuneration including criteria for determining qualifications, positive attributes, independence of a director and other matters provided under Section 178(3).
- (g) Explanations or comments by the Board on every qualification, reservation or adverse remark or disclaimer made:
 - (i) by the auditor in his report and
 - (ii) by the Company Secretary in practice in his secretarial audit report.
- (h) Particulars of loans, guarantees or investments under Section 186.
 - (i) Particulars of contracts or arrangements with related parties referred to Section 188(1) in the prescribed form.
 - (j) The state of the company's affairs.
 - (k) The amounts, if any, which it proposes to carry to any reserves.
 - (l) The amount, if any, which it recommends should be paid by way of dividend.
- (m) Material changes and commitments, if any, affecting the financial position of the company which have occurred between the end of the financial year of the company to which the financial statements relate and the date of the report.
- (n) The conservation of energy, technology absorption, foreign exchange earnings and outgo, in prescribed manner.
- (o) A statement indicating development and implementation of a risk management policy for the company including identification therein of elements of risk, if any, which in the opinion of the Board may threaten the existence of the company.
- (p) The details about the policy developed and implemented by the company on corporate social responsibility initiatives taken during the year.
- (q) In case of a listed company and every other public company having prescribed paid-up share capital, a statement indicating the manner in which formal annual evaluation has been made by the Board of its own performance and that of its committees and individual directors.
- (r) Details in respect of frauds reported by auditors u/s 143(12) other than those which are reportable to the Central Government.
- (s) Such other matters as may be prescribed.

Report of the Board of Directors in case of OPC [Section 134(4)]: In case of OPC, the report of the Board of Directors to be attached to the financial statement should contain explanations

or comments by the Board on every qualification, reservation or adverse remark or disclaimer made by the auditor in his report.

Thus, in case of OPC, details as required by under Section 134 (3) are not required.

Directors' Responsibility Statement [Section 134 (5)]: *Separately discussed in next question.*

Other provisions of the Companies Act, 2013 relating to Board's Report:

- ◆ An extract of the annual return shall form part of the Board's report. [Section 92 (3)]
- ◆ The consideration of the Board's report is ordinary business. [Section 102 (2)]
- ◆ If it appears to the directors of a company that the financial statement of the company or the report of the Board, do not comply with the provisions of Section 129 or 134, they may prepare revised financial statement or a revised report in respect of any of the 3 preceding financial years after obtaining approval of the Tribunal. Such application has to be made by the company in prescribed form and in prescribed manner and a copy of the order passed by the Tribunal shall be filed with the Registrar. [Section 131]
- ◆ The Board's report shall disclose the composition of the CSR Committee. [Section 135 (2)]
- ◆ The Board of every company referred to Section 135(1), shall ensure that the company spends, in every financial year, at least 2% of the average net profits of the company made during the 3 immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy. [Section 135(5)]
- ◆ Financial statement and Board's Report shall be sent to every member of the company, to every trustee for the debenture-holder of any debentures issued by the company, and to all persons other than such member or trustee, being the person so entitled, not less than 21 days before the date of the meeting. [Section 136(1)]
- ◆ A copy of the financial statements and Board's report duly adopted at the AGM shall be filed with the Registrar within 30 days of the date of AGM. [Section 137(1)]
- ◆ The Board's report shall disclose the composition of an Audit Committee and where the Board had not accepted any recommendation of the Audit Committee, the same shall be disclosed in such report along with the reasons. [Section 177(8)]
- ◆ The policy adopted by the Nomination and Remuneration Committee is also required to be disclosed in Board's report. [Section 178(4)]
- ◆ The Board of Directors of a company shall approve financial statement and the Board's report by means of resolutions passed at meetings of the Board. [Section 179(3)(g)]
- ◆ Every related party transactions entered by the company under Section 188 (1) shall be referred to in the Board's report to the shareholders along with the justification for entering into such related party transactions. [Section 188(2)]
- ◆ Every listed company shall disclose in the Board's report, the ratio of the remuneration of each director to the median employee's remuneration and such other details as may be prescribed. [Section 197(12)]
- ◆ A whole time director or managing director who is getting commission from the company can get commission or remuneration from its holding or subsidiary company, subject to disclosure by the company in its Board's report. [Section 197(14)]
- ◆ Every listed company and a company belonging to prescribed class of companies shall annex with its Board's report, a secretarial audit report, given by a Company Secretary in practice, in prescribed form. [Section 204(1)]
- ◆ The Board of Directors, in their report, shall explain in full any qualification or observation or other remarks made by the Company Secretary in practice in his report under Section 204(1). [Section 204(3)]

Matters to be included in Board's report [Rule 8 of the Companies (Accounts) Rules, 2014]:

- (1) The Board's Report shall be prepared based on the stand alone financial statements of the company and shall report on the highlights of performance of subsidiaries, associates and joint venture companies and their contribution to the overall performance of the company during the period under report.
- (2) The Report of the Board shall contain the particulars of contracts or arrangements with related parties Section 188(1) in the Form AOC-2.
- (3) The report of the Board shall contain the following information and details, namely:
 - (A) Conservation of energy:
 - (i) The steps taken or impact on conservation of energy;
 - (ii) The steps taken by the company for utilizing alternate sources of energy;
 - (iii) The capital investment on energy conservation equipments;
 - (B) Technology absorption-
 - (i) The efforts made towards technology absorption;
 - (ii) The benefits derived like product improvement, cost reduction, product development or import substitution;
 - (iii) In case of imported technology (imported during the last three years reckoned from the beginning of the financial year)-
 - (a) the details of technology imported;
 - (b) the year of import;
 - (c) whether the technology been fully absorbed;
 - (d) if not fully absorbed, areas where absorption has not taken place, and the reasons thereof; and
 - (iv) The expenditure incurred on Research and Development.
 - (C) Foreign exchange earnings and Outgo-
 The Foreign Exchange earned in terms of actual inflows during the year and the Foreign Exchange outgo during the year in terms of actual outflows.
- (4) Every listed company and every other public company having a paid up share capital of ₹ 25 Crores or more calculated at the end of the preceding financial year shall include, in the report by its Board of directors, a statement indicating the manner in which formal annual evaluation has been made by the Board of its own performance and that of its committees and individual directors.
- (5) In addition to the information and details specified in Rule 8 (4), the report of the Board shall also contain -
 - (i) The financial summary or highlights;
 - (ii) The change in the nature of business, if any;
 - (iii) The details of directors or key managerial personnel who were appointed or have resigned during the year;
 - (iv) The names of companies which have become or ceased to be its Subsidiaries, joint ventures or associate companies during the year;
 - (v) The details relating to deposits, covered under Chapter V of the Act,-
 - (a) accepted during the year;
 - (b) remained unpaid or unclaimed as at the end of the year;

- (c) whether there has been any default in repayment of deposits or payment of interest thereon during the year and if so, number of such cases and the total amount involved-

- at the beginning of the year;
- maximum during the year;
- at the end of the year;

- (vi) The details of deposits which are not in compliance with the requirements of Chapter V of the Companies Act, 2013;
- (vii) The details of significant and material orders passed by the regulators or courts or tribunals impacting the going concern status and company's operations in future;
- (viii) The details in respect of adequacy of internal financial controls with reference to the Financial Statements.

Disclosure and requirements of SEBI Guideline and Listing Agreement: In addition to compliance of the various provisions of the Companies Act, 2013, the company should also comply with SEBI Guideline and Listing Agreement as applicable to preparation and presentation of Board's Report.

Details as required in Board's Report as per listing agreement:

- ◆ Report on Corporate Governance
- ◆ Compliance certificate regarding Corporate Governance
- ◆ Disclosure of remuneration to non-executive directors
- ◆ Management Discussion and Analysis Report
- ◆ Code of Conduct as per Clause 49 (I)(D) of the listing agreement
- ◆ Deviation in projected utilization and actual utilization of funds, if company had raised funds by issue of prospectus
- ◆ Cash flow statement
- ◆ Deviation from accounting standards
- ◆ Disclosure about relationship between directors
- ◆ Business responsibility statement

Details as required in Board's Report as per various SEBI Regulations:

- ◆ Details of ESOS/ESOP
- ◆ Details if name changed
- ◆ Details of issue of securities

Que. No. 3] Write a short note on: Directors Responsibility Statement

CS (Executive) - Dec 2013 (4 Marks)

The Board of directors of Charming Ltd. seek your advice on the matters to be included in the directors' responsibility statement forming part of the company's annual report to shareholders. As the Company Secretary of Charming Ltd., advise the Board.

CS (Executive) - June 2015 (4 Marks)

Ans.: As per Section 134(3)(c), Directors Responsibility Statement is required to be attached to the Board's Report.

Directors Responsibility Statement [Section 134(5)]: The Directors' Responsibility Statement referred to in Section 134(3)(c) shall state that -

- (a) In the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures;
- (b) The directors had selected such accounting policies and applied them consistently and made judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company at the end of the financial year and of the profit and loss of the company for that period;
- (c) The directors had taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of this Act for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities;
- (d) The directors had prepared the annual accounts on a going concern basis;
- (e) The directors, in the case of a listed company, had laid down internal financial controls to be followed by the company and that such internal financial controls are adequate and were operating effectively; and
- (f) The directors had devised proper systems to ensure compliance with the provisions of all applicable laws and that such systems were adequate and operating effectively.

Que. No. 4] State the provisions relating to signing of Board's Report?

CS (Inter) - Dec 2005 (5 Marks)

Ans.: **Signing of Board's report [Section 134(6)]:** The Board's report and any annexures thereto shall be signed by its Chairperson of the company if he is authorized by the Board and where he is not so authorized, shall be signed by atleast 2 directors, one of whom shall be a Managing Director, or by the director where there is one director.

Que. No. 5] State the provisions of the Companies Act, 2013 relating to filing of the board's report?

Ans.: As per Section 137(1), a copy of the financial statements and Board's report duly adopted at the AGM shall be filed with the Registrar within 30 days of the date of AGM.

Que. No. 6] The Directors Report of Ayush Ltd. for the financial year ended 31st March, 2015 has been dated 15th May, 2015, whereas the Auditors' Report for the same period is dated 16th May, 2015. Is this in order? Explain. CS (Executive) - June 2013 (4 Marks)

Ans.: As Section 134(3)(f), there shall be attached to statements laid before a company in general meeting, a report by its Board of Directors, which shall include explanations or comments by the Board on every qualification, reservation or adverse remark or disclaimer made by the auditor in his report.

Thus, ideally the date of Directors Report should be on same date or later than the date of Auditors Report. If the Auditors Report is subsequent to the date of Directors Report it would not be possible for the board to comply with the requirements of Section 134(3)(f). Hence, dating of Directors Report earlier than Auditors Report is not in order.

Que. No. 7] Write a short note on: 'Management Discussion and Analysis Report'

Priya, a nominee director on the Board of Aroma Ltd., a listed company, informed the Board of directors during a Board meeting that the next annual report of the company shall contain a 'Management Discussion and Analysis Report'. You being the Company Secretary have been asked by the Board to prepare the said report. State the matters you would include in the report.

CS (Executive) - Dec 2016 (4 Marks)

Ans.: Regulation 34 of the SEBI (Listing Obligations & Disclosure Requirements) Regulation, 2015 provides that as a part of the director's report or as an addition thereto, a Management Discussion and Analysis report should form part of the Annual Report to the shareholders.

This Management Discussion & Analysis should include discussion on the following matters within the limits set by the company's competitive position:

1. Industry structure and developments.
2. Opportunities and Threats.
3. Segment-wise or product-wise performance.
4. Outlook.
5. Risks and concerns.
6. Internal control systems and their adequacy.
7. Discussion on financial performance with respect to operational performance.
8. Material developments in Human Resources/Industrial Relations.

Que. No. 8] Narrate briefly the importance of Corporate Governance Report and state who can certify such report.
CS (Executive) - Dec 2014 (4 Marks)

Ans.: Corporate governance aims to improve the company's image, efficiency, effectiveness and social responsibility. It encompasses in itself a range of corporate controls and accountability mechanisms designed to meet the aims of corporate stockholders. It deals with issues regarding transparency accounting integrity, composition of the board of directors, the role of non-executive directors and their accountability to shareholders, etc.

Clause 49 of the listing agreement relates to reporting on corporate governance. It provides that there shall be a separate section on Corporate Governance in the Annual Reports of company.

The suggested list of items to be included in this report is as follows:

Mandatory Requirements

1. A brief statement on company's philosophy on code of governance.
2. Details relating to Board of Directors
3. Details relating to Audit Committee, Shareholders Committee and other committees
4. Details with respect to General Body meetings: Location and time, where last three AGMs held, special resolutions passed in the previous 3 AGMs etc.
5. Detailed disclosures with respect to materially significant related party transactions, non-compliance by the company etc.
6. Details of Means of communication adopted by the company
7. General Shareholder information relating to Date of Book closure, Stock Code, Dividend Payment Date, Market Price Data, Plant Locations etc.

Non-Mandatory Requirements

1. Tenure of Independent Directors
2. Constitution of remuneration committee
3. Training of Board Members

The company shall obtain a certificate from either the auditors or Practicing Company Secretaries regarding compliance of conditions of corporate governance as in Clause 49 of the listing agreement and annex the certificate with the director's report, which is sent annually to all the shareholders of the company. The same certificate shall also be sent to the Stock Exchanges along with the annual report filed by the company.

The reference of inclusion of report on corporate governance in the annual report should be made in the Board's Report and, as a good corporate practice, information relating to any non-compliance of the requirements of Clause 49 of the listing agreement should be incorporated in the Board's Report.

Que. No. 8A] What disclosures are required to be made in 'Directors Report' for ESOS & ESPS?
CS (Executive) - June 2009 (5 Marks)

Ans.: The Board of Directors is required to disclose the following details in relation to ESOS & ESPS in the Directors Report:

- (a) Options granted
- (b) Pricing formula
- (c) Options vested
- (d) Options exercised
- (e) Total number of shares arising as a result of exercise of option
- (f) Options lapsed
- (g) Variation of terms of options
- (h) Money realised by exercise of options
- (i) Total number of options in force
- (j) Employee-wise details of options
- (k) Diluted Earnings Per Share (DEPS)
- (l) Weighted-average exercise prices and weighted-average fair values of options
- (m) A description of the method and significant assumptions used during the year to estimate the fair values of options, including the following weighted average information:
 - Risk-free interest rate
 - Expected life
 - Expected volatility
 - Expected dividends and
 - Price of the underlying share in market at the time of option grant.

CORPORATE SOCIAL RESPONSIBILITY

Que. No. 9] Explain the concept of 'CSR' (Corporate Social Responsibility) as introduced by the Companies Act, 2013. Examining the provisions of the Act, answer the following:

- (i) Which companies are required to constitute a CSR Committee?
- (ii) Which companies are excluded from the requirements of the provisions of the Act in relation to CSR Committee?
- (iii) What is the minimum contribution the companies are required to make towards CSR?

CS (Executive) - June 2016 (4 Marks)

Ans.: Corporate Social Responsibility [Section 135]:

- (1) Every company fulfilling following criteria shall constitute a Corporate Social Responsibility (CSR) Committee of the Board consisting of 3 or more directors, out of which at least one director shall be an independent director -
 - Company having net worth of ₹ 500 Crore or more, or
 - Company having turnover of ₹ 1,000 Crore or more or
 - Company having net profit of ₹ 5 Crore or more

Net worth/Turnover/Net profit of the immediately preceding financial year should be taken for the purpose of this section.

However, if company is not required to appoint independent director the CSR committee should have two or more directors.

- (2) The Board's report shall disclose the composition of the CSR Committee.
- (3) The CSR Committee shall:
 - (a) Formulate and recommend to the Board, a CSR Policy to be undertaken by the company as specified in **Schedule VII**
 - (b) Recommend the amount of expenditure to be incurred on the activities covered under CSR Policy of the company from time to time.
- (4) The Board shall disclose contents of policy in its report and also place it on the company's website in prescribed manner.
- (5) The Board shall ensure that the company spends, in every financial year, atleast 2% of the average net profits of the company made during the 3 immediately preceding financial years, in pursuance of its CSR Policy.
- (6) The company shall give preference to the local area for spending the amount earmarked for CCSR activities.
- (7) If the company fails to spend such amount, the Board shall in its report specify the reasons for not spending the amount.

Explanation: "Average net profit" shall be calculated as per Section 198.

Disclosures about CSR Policy [Rule 9 of the Companies (Accounts) Rules, 2014]: The disclosure of contents of Corporate Social Responsibility Policy in the Board's report and on the company's website, if any, shall be as per annexure attached to the Companies (Corporate Social Responsibility Policy) Rules, 2014.

Companies excluded from the requirements of CSR Committee:

Every company which ceases to be a company as per Section 135 (1) of the Act for three consecutive financial years -

- (1) shall not be required to constitute a CSR Committee, and
- (2) is not required to comply with the provisions as per Section 135.

Que. No. 10] Brave Ltd. is listed at Bombay Stock Exchange and has a net worth of over ₹ 600 Crore. The company has constituted a corporate social responsibility (CSR) committee with Jay and Vijay as its members. Both Jay and Vijay are directors of the company, Jay being an independent director.

Explaining the provisions of the Companies Act, 2013 relating to 'corporate social responsibility', examine whether the company has complied with the provisions of the Act in this regard.

CS (Executive) - June 2015 (4 Marks)

Ans.: As per Section 135, every company fulfilling following criteria shall constitute a Corporate Social Responsibility (CSR) Committee of the Board consisting of 3 or more directors, out of which at least one director shall be an independent director -

- Company having net worth of ₹ 500 Crore or more, or
- Company having turnover of ₹ 1,000 Crore or more or
- Company having net profit of ₹ 5 Crore or more

Brave Ltd. has net worth above ₹ 500 Crore; hence constitution of CSR Committee is mandatory for it. As per Section 135 at least 3 directors are required in CSR Committee out of which at least one director shall be an independent director. However, Brave Ltd. has only two directors in CSR Committee, hence it should appoint one more director to comply with the provisions of the Section 135.

Que. No. 11] Whether CSR expenditure of a company can be claimed as a business expenditure?

Ans.: The amount spent by a company towards CSR cannot be claimed as a business expenditure. The Finance Act, 2014 provides that any expenditure incurred by an assessee on the activities relating to Corporate Social Responsibility referred to in Section 135 of the Companies Act, 2013 shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession.

Que. No. 12] Can CSR expenditure be spent on the activities beyond Schedule VII?

Ans.: MCA has clarified that the statutory provision and provisions of CSR Rules, 2014, is to ensure that activities undertaken in pursuance of the CSR policy must be relatable to Schedule VII of the Companies Act, 2013.

The entries in the said Schedule VII must be interpreted liberally so as to capture the essence of the subjects enumerated in the said Schedule. The items enlisted in Schedule VII of the Act, are broad-based and are intended to cover a wide range of activities. The General Circular also provides an illustrative list of activities that can be covered under CSR. In a similar way many more can be covered. It is for the Board of the company to take a call on this.

Que. No. 13] Referring to the provisions of the Companies Act, 2013 relating to 'Corporate Social Responsibility' (CSR), answer the following:

- (i) Which activities would not qualify as CSR?
- (ii) Whether the average net profit criteria for CSR is before tax or after tax?

CS (Executive) - Dec 2016 (4 Marks)

Ans.:

- (i) **Activities that would not qualify as CSR:** Following are some of the activities that cannot constitute CSR activity:

- ◆ The CSR projects or programs or activities that benefit only the employees of the company and their families.
- ◆ One-off events such as marathons/awards/charitable contribution/advertisement/ sponsorships of TV programmes etc.
- ◆ Expenses incurred by companies for the fulfilment of any other Act/Statute of regulations (such as Labour Laws, Land Acquisition Act, 2013, Apprentice Act, 1961 etc.)
- ◆ Contribution of any amount directly or indirectly to any political party.
- ◆ Activities undertaken by the company in pursuance of its normal course of business.
- ◆ The project or programmes or activities undertaken outside India.

- (ii) **Average net profit criteria for CSR:** Computation of net profit for section 135 is as per section 198 of the Companies Act, 2013 which is primarily Profit Before Tax (PBT).

Que. No. 14] Whether display of CSR policy of a company on website of the company is mandatory?

Ans.: As per Section 135(4) the Board of Directors of the company shall, after taking into account the recommendations of CSR Committee, approves the CSR policy for the company and disclose contents of such policy in its report and the same shall be displayed on the company's website, if any.

CHAPTER 23

REGISTERS, FORMS & RETURNS

This chapter covers:

- Procedure for keeping registers and returns at a place other than the registered office
- Non-statutory Registers
- Electronic forms
- Filing of various forms/Returns with Registrar of Companies
- Preparation and filing of returns with the Registrar of Companies
- Guidelines for preparing/filing forms, documents, returns etc.
- Penalty for filing false documents/statements with the Registrar

Que. No. 1] Write a short note on: Statutory Books

What are the statutory books prescribed under Companies Act, 2013?

CS (Inter) - June 2004 (4 Marks)

CS (Executive) - June 2009 (8 Marks)

Ans.: The Companies Act, 2013 lays down that every company incorporated under this Act must maintain and keep at its registered office certain books, registers and copies of certain returns, documents etc. and to give certain notices, file certain returns, forms, reports, documents etc. with the Registrar of Companies within certain specified time limits and with the prescribed filing fees. These books are known as Statutory Books. Some of the statutory registers are required to be kept open by the company for inspection by directors, members, creditors of the company and by other persons. The company is also required to allow extracts to be taken from certain documents, registers, returns etc. and furnish copies of certain documents on demand by a member or by any other person on payment of specified fees.

Every company incorporated under the Act is required to keep at its registered office, *inter alia*, the following statutory books and registers:

| Name of Register/Return/documents | Form No. | Relevant Section and Rule |
|---|----------|--|
| Register of renewed and duplicate share certificate | SH-2 | Section 46(3) & Rule 6(3)(a) of the Companies (Share Capital & Debentures) Rules, 2014 |
| Register of sweat equity shares | SH-3 | Section 54 & Rule 8(14) of the Companies (Share Capital & Debentures) Rules, 2014 |
| Register of employee stock option | SH-6 | Section 62(1)(b) & Rule 12(10) of the Companies (Share Capital & Debentures) Rules, 2014 |
| Register of shares/other securities bought back | SH-10 | Section 68(9) & Rule 17(12) of the Companies (Share Capital & Debentures) Rules, 2014 |
| Register of deposits | | Sections 73 & 74 & Rule 14 of the Companies (Acceptance of Deposits) Rules, 2014 |
| Register of charges | CHG-7 | Section 85 & Rule 10(1) of the Companies (Registration of Charges) Rules, 2014 |
| Register of Members | MGT-1 | Section 88(1)(a) & Rule 3(1) of the Companies (Management & Administration) Rules, 2014 |
| Register of debenture holders and other securities holders | MGT-2 | Section 88(1)(b) & (c) & Rule 4 of the Companies (Management & Administration) Rules, 2014 |
| Foreign register of members, debenture holders, other security holders or beneficial owners residing outside India | - | Section 88(4) & Rule 7 of the Companies (Management & Administration) Rules, 2014 |
| Annual Return | | Section 92 |
| Register of postal ballot | - | Section 110 & Rule 22 of the Companies (Management & Administration) Rules, 2014 |
| Minutes of proceedings of general meeting, meeting of board of directors and other meeting & resolutions passed by postal ballot. | - | Section 118 |
| Books of account | - | Section 128 |
| Register of directors and key managerial personnel and their shareholding | - | Section 170 & Rule 17 of the Companies (Appointment & Qualification of Director) Rules, 2014 |
| Register of loans, guarantee, security & acquisition made by company | MBP-2 | Section 186(9) & Rule 12(1) of the Companies (Meetings of Boards & its Powers) Rules, 2014 |
| Register of investment not held in its own name by the company | MBP-3 | Section 187(3) & Rule 14(1) of the Companies (Meetings of Boards & its Powers) Rules, 2014 |
| Register of contracts with related party and contracts and bodies etc. in which directors are interested | MBP-4 | Section 189 & Rule 16(1) of the Companies (Meetings of Boards & its Powers) Rules, 2014 |

Que. No. 2] Write a short note on: Statistical Books

Ans.: In addition to books of account and statutory books, companies usually maintain the certain books which give details information regarding holding and transfer of shares and debentures, calls made on shareholders and debenture holders, interest paid to debenture holders, interest paid to debenture holders share warrants issued and surrendered and such other matters not covered by the books of account and such other matter not covered by the books of account and statutory books:

| Name of the register/book |
|---|
| (1) Share application and allotment book |
| (2) Share call book |
| (3) Debenture call book |
| (4) Register of share transfers |
| (5) Shareholders dividend book |
| (6) Debenture interest book |
| (7) Register of certification & balance tickets |
| (8) Debenture transfer register |
| (9) Register of share certificates |
| (10) Register of probates |
| (11) Register of share warrants |
| (12) Register of dividend mandates |
| (13) Agenda book |
| (14) Register of sealed documents |
| (15) Register of powers of attorney |

Que. No. 3] Distinguish between: Statutory Books & Statistical Books

CS (Executive) - Dec 2008 (4 Marks)

CS (Executive) - June 2011 (3 Marks), June 2012 (4 Marks)

Ans.: Following are the main points of distinction between statutory books & statistical books:

| Point | Statutory Books | Statistical Books |
|------------|--|---|
| Meaning | As per the provisions of different sections of the Companies Act, 2013 the certain books must be maintained by the company which are known as statutory books. | In addition to books of account and statutory books, companies usually maintain the certain books which are known as Statistical books. |
| Place | Statutory books must be kept at the register office of the company. | Statistical books may be kept at any place other than register office of the company. |
| Compulsion | Keeping of statutory books is compulsory. | Keeping of Statistical books is optional. |
| Examples | <ul style="list-style-type: none"> - Register of charges - Register & index of members, debenture holders - Minutes of proceedings of general meeting, meeting of Board of Directors - Register of investments not held in the company name - Register of contracts or arrangements in which directors are interested - Register of directors and key managerial personnel and their shareholding. - Register of loans and investment made other body corporate | <ul style="list-style-type: none"> - Share application & allotment book - Share call book - Debenture call book - Register of share transfers - Shareholders dividend book - Debenture interest book - Debenture transfer register - Register of share certificates - Register of probates - Register of share warrants - Register of dividend mandates - Agenda book - Register of sealed documents - Register of powers of attorney |

STATUTORY REGISTERS

Que. No. 4] Write a short note on: Register of renewed and duplicate share certificate

Ans.: Refer to Question No. 5 of Chapter No. 11 - "Allotment & Issue of Certificates".

Que. No. 5] Write a short note on: Register of sweat equity shares

Ans.: Refer to Question No. 11 of Chapter No. 6 - "Concept of Capital & Financing of Companies".

Que. No. 6] Write a short note on: Register of employee stock option

Ans.: Refer to Question No. 17 of Chapter No. 6 - "Concept of Capital & Financing of Companies".

Que. No. 7] Write a short note on: Register of shares/other securities bought back

Ans.: Refer to Question No. 10 of Chapter No. 7 - "Alteration of Share Capital".

Que. No. 8] Write a short note on: Register of deposits

Ans.: Refer to Question No. 26 of Chapter No. 19 - "Deposits".

Que. No. 9] Write a short note on: Register of charges

Ans.: Refer to Question No. 19 of Chapter No. 10 - "Creation & Registration of Charges".

Que. No. 10] Write a short note on: Register of Members

Ans.: Refer to Question No. 14 of Chapter No. 12 - "Membership".

Que. No. 11] Write a short note on: Register of debenture holders and other securities holders

Ans.: Refer to Question No. 14 of Chapter No. 12 - "Membership".

Que. No. 12] Write a short note on: Foreign register of members, debenture holders, other security holders or beneficial owners residing outside India

Ans.: Refer to Question No. 22 of Chapter No. 12 - "Membership".

Que. No. 13] Write a short note on: Annual Return

Ans.: Refer to Question No. 32 of Chapter No. 20 - "Accounts & Audit".

Que. No. 14] Write a short note on: Register of postal ballot

Ans.: Refer to Question No. 52 of Chapter No. 14 - "Meetings".

Que. No. 15] Write a short note on: Minutes of proceedings of general meeting, meeting of board of directors and other meeting & resolutions passed by postal ballot.

Ans.: Refer to Question No. 66 of Chapter No. 14 - "Meetings".

Que. No. 16] Write a short note on: Register of directors and key managerial personnel and their shareholding

Ans.: Refer to Question No. 57 of Chapter No. 3 - "Institution of Directors".

Que. No. 17] Write a short note on: Register of contracts with related party and contracts and bodies etc. in which directors are interested

Ans.: Refer to Question No. 27 of Chapter No. 16 - "Powers & Duties of Directors".

OTHER REGISTERS

Que. No. 18] Write a short note on: Directors Attendance Book

Ans.: A company must possess proof or evidence of the fact that at a particular Board meeting, the directors who were present, absent and who had sought leave of absence from the Board because of their inability to attend a meeting.

According to Section 167, the office of a director becomes vacant if he absents himself from all the meetings of the Board of Directors held during a period of 12 months with or without seeking leave of absence of the Board.

If at any stage, the Board declares vacant the office of any one of its directors, the company must have a proper record of attendance of its directors at each Board meeting to establish that the particular director had in fact absented, without leave of the Board, from the specified number of meetings or from all the meetings for the specified period of time.

In compliance with the provisions of Section 118 (4), the minutes of each Board meeting contain the names of all the directors present at the meeting. In fact minutes of each Board meeting commence with the caption - "Directors present at the meeting".

Articles of most of the companies contain a provision to the effect that the directors attending a Board meeting must sign in the book kept by the company for the purpose. This is based on Regulation 65 in Table F, which reads as:

"Every director present at any meeting of the Board or a committee thereof shall sign against his name in a book to be kept for that purpose".

In view of the above provisions, a practice has been established with companies to keep a directors attendance book, in which attendance of each director is marked by writing his name below details of the meeting. Signatures of all the directors attending Board meetings are obtained by the company secretary before the commencement of the meeting. Attendance of special invitees, like the solicitors, advocates, advisers, senior managers of the company etc. is also marked in the said register by writing names and designations.

The Director's attendance book is not open for inspection.

Some companies, instead of keeping a supplementary record in the form of a separate book for directors attendance, get the signatures of the attending directors on the pages of the minutes themselves instead of keeping a separate book of directors attendance. This is done by preparing the first page of minutes of each Board meeting in advance and at the time of the meeting, directors are requested to put their signatures against their names.

Entries in the register should be authenticated by the Company Secretary or by any other person authorized by the Board for the purpose, by appending his signature to each entry. The book should be preserved for a period of 8 years and should be kept in the custody of the Company Secretary or by any other person authorized by the Board for the purpose.

Que. No. 19] Write a short note on: Shareholders/Proxies Attendance Register

Ans.: For keeping proper record of the members attending every general meeting of a company, shareholders attendance register is maintained. The secretarial staff present at the venue of

each general meeting of the company, take the signatures of the members/proxies coming for attending the meeting, before they enter the meeting hall.

The register has the following columns:

1. Name of the shareholder
2. Folio No. of the shareholder
3. No. of shares registered in his/her name
4. Name of the proxy holder and No. of shares for which proxy is given
5. Signature of the shareholder or proxy holder

The register should be maintained at the registered office of the company.

The register of Shareholders/proxies attendance in relation to a particular meeting should be open for inspection to every member entitled to vote at that meeting, during the period beginning 24 hours before the time fixed for the commencement of the meeting and ending with the conclusion of the meeting.

No person is entitled to copies of the register or any portion thereof.

Entries in the register should be authenticated by the Company Secretary or by any other person authorized by the Board for the purpose, by appending his signature to each entry. The register should be preserved for a period of 8 years from the date of the meeting and should be kept in the custody of the Company Secretary or by any other person authorized by the Board for the purpose.

Que. No. 20] Write a short note on: Dividend Register

Ans.: Whenever a company pays dividend, interim or final, this register is used. Details of every dividend are entered in the register. This register is to be maintained as a permanent record.

The register contains the following columns:

1. Name of the company
2. Registered office address of the company
3. Name of the shareholder
4. Register of members Folio No.
5. Number of shares held
6. Amount of dividend/interim dividend payable Remarks column for initials of the authenticating officer of the company.

Entries in the register should be made within 7 working days of the date of payment of dividend. The register should be maintained at the registered office of the company.

The register is not open for inspection.

Entries in the register should be authenticated by the Company Secretary or by any other person authorized by the Board for the purpose.

The register should be preserved for a period of 8 years from the date of payment and should be kept in the custody of the Company Secretary or by any other person authorized by the Board for the purpose.

Dividend reconciliation statement should be preserved as long as any dividend remains unclaimed.

Que. No. 21] Write a short note on: Register of Fixed Assets

Ans.: Under the Companies (Auditors Report) Order, 2015 (CARO), the Auditors have to include a statement in their report which *inter alia* specify whether the company is maintaining proper records to show full particulars including quantitative details and situation of fixed assets. Hence, this register is a statutory register.

Each company should keep and maintain this register.

Maintenance of such register shall help the management to fix accountability and detect misuse, misappropriation and fraud about the assets of the company.

The following may be the columns of this register:

1. Serial No.
2. Date of entry
3. Particulars of assets
4. Quantity
5. Cost price
6. Date of purchase
7. Situation
8. Details of disposal
9. Remarks.

Que. No. 22] Write a short note on: Register of Form No. MBP. 1 from directors

Ans.: Under Section 184, every director of a company has to give a general notice in Form No. MBP. 1 prescribed under the Companies (Meeting of Board and its powers) Rule, 2014, to the board of directors of the company to the effect that he is a director or a member of a specified body corporate or is a member of a specified firm and is to be regarded as concerned or interested in contracts or arrangements with them.

Failure to comply with the provisions of this section the office of such defaulting director shall become vacant under Section 167(1)(d).

In view of the above, a Company Secretary has to keep and maintain this register as to ascertain the director whose office shall fall vacant.

Its columns may be the following:

1. Serial No.
2. Name of director
3. Date of appointment
4. Details of Form No. MBP. 1 received
 - Date of receipt
 - Date of Board meeting where it was read and recorded
 - Date of validity.

Que. No. 23] Write a short note on: Register of Nomination

Ans.: As per Section 72, every holder of securities at any time, nominate in the prescribed manner, a person to whom his securities shall vest in the event of his death.

Under Rule 19 of the Companies (Share Capital & Debentures) Rules, 2014, Form No. SH.13 has been prescribed. In view of the above, every company should keep and maintain a Register of Nominees for each class of shares, and debentures separately. Simultaneously, the details of the nominee should be recorded in the respective folio of the Register of Members and Register of Debenture holders.

The following may be the columns of this register:

1. Serial No.
2. Date of entry
3. Date of receipt of Nomination Form
4. Name & address of nominee
5. Date of birth (minor)
6. Name & address of guardian of nominee (minor)
7. No. of shares/debentures
8. Remarks.

This register is required to be maintained permanently.

Que. No. 24] Write a short note on: Register of Share Warrants

Ans.: When a company issues share warrants, this register is required to be maintained. The name of the warrant holder is struck off from the register of members after making an appropriate reference there. His name and other relevant particulars are entered in the register of share warrants. The register must have, *inter alia*, the following columns:

1. Name of share warrant holder
2. Address of share warrant holder
3. No. and date of issue of share warrant
4. His register of members folio No.
5. No. of shares, with distinctive numbers, in lieu whereof share warrants have been issued
6. Remarks (for any other information and for signature of the Company Secretary, who must authenticate each entry in the register).

FORMS, FILING FEES AND PUNISHMENT FOR FRAUD AND FALSE STATEMENTS**Que. No. 25] Write a short note on: Filing of Forms & Returns under the Companies Act, 2013**

Ans.: As per Section 398, various applications, forms, returns and documents can be filed electronically.

Fee for filing [Section 403(1)]: Fees are payable for registration of company as well as for filing any document.

Mode of Payment [Rule 13 of the Companies (Registration Offices & Fees) Rules, 2014]: The fees, charges or other sums payable for filing any application, form, return or any other document shall be paid by means of credit card; or internet banking; or remittance at the counter of the authorized banks or any other mode as approved by the Central Government.

Payment of additional fees for late filing of documents [Proviso to Section 403(1)]: The documents have to be filed within the time prescribed in various sections. If filing is delayed,

additional fee is payable. If late fee is not paid, the documents will not be deemed to have been filed. Filing of additional fees has been prescribed in Annexure to the Rule.

Que. No. 26] Write a short note on: Defective Forms/Documents

Ans.: A form or document is defective for any one of the following reasons:

- (i) the form or document does not contain the necessary enclosures
- (ii) certain particulars in the document or form have been left unfilled
- (iii) certain particulars apparent on the face of it seem false
- (iv) the document is not filed in proper time or is not accompanied by the requisite filing fee
- (v) the document is not properly signed or certified.

If a document is found to be not in order for any of the reasons stated above the Registrar will not register the document until the particulars left unfilled are filled or the error is rectified by the company. For this purpose, facility of resubmission is available under MCA-21 portal. However, resubmission can be made, only when the ROC requires that the company resubmit the form with corrections. If within the date document is required to be filed, the blank is not filled in or the apparent error is not corrected then the Registrar is at liberty to launch prosecution against the company and its officers for default in filing the document.

If the defect is one which requires filing of a revised document, then, in certain cases, the ROC may accept the revised form on payment of additional fee which he may determine in terms of Section 403 of the Act.

Que. No. 27] Chairman of your company wants to know the procedure of condonation of delay by the Central Government in filing the documents with the ROC. As a Company Secretary, prepare a note for consideration of the Chairman.

CS (Executive) - Dec 2013 (8 Marks)

Ans.: Condonation of delay in certain cases [Section 460]: The Central Government may for reasons to be recorded in writing, condone the delay in following cases:

- (a) Where any application required to be made to the Central Government in respect of any matter is not made within the time specified therein and
- (b) Where any document required to be filed with the Registrar is not filed within the time specified therein.

Procedure for condonation of delay by Central Government in relation to filing of documents with ROC:

- (1) Convene a board meeting and pass a resolution for seeking condonation of delay in filing the document.
- (2) Submit an application to the Central Government along with the reasons for such delay. The application should be accompanied by a copy of the board resolution seeking condonation of delay, latest audited balance sheet and profit and loss account, certified copy of the memorandum and articles of association and filing fees.
- (3) The Central Government may for reasons to be recorded in writing, condone the delay.



INSPECTION & INVESTIGATION

This Chapter Covers:

- Power to call for information, inspect books and conduct inquiries
- Conduct of inspection and inquiry
- Report on inspection made
- Search and seizure
- Investigation into affairs of company
- Establishment of Serious Fraud Investigation Office
- Investigation into affairs of company by Serious Fraud Investigation Office
- Investigation into company's affairs in other cases
- Security for payment of costs and expenses of investigation
- Firm, body corporate or association not to be appointed as inspector
- Investigation of ownership of company
- Procedure, powers of inspectors
- Protection of employees during investigation
- Power of inspector to conduct investigation into affairs of related companies
- Seizure of documents by inspector
- Freezing of assets of company on inquiry and investigation
- Imposition of restrictions upon securities
- Inspector's report
- Actions to be taken in pursuance of inspector's report
- Expenses of investigation
- Legal advisers and bankers not to disclose certain information
- Investigation of foreign companies

INSPECTION

Que. No. 1] Explain the power of the Registrar to call for information, inspect the books of account and conduct inquiries.

Ans.: Power to call for information, inspect books and conduct inquiries [Section 206 (1)]: Where on a scrutiny of any document filed by a company or on any information received, the ROC is of the opinion that any further information or explanation or documents relating to the company is necessary, he may by a written notice require the company -

- To furnish in writing such information or explanation or
- To produce such documents as may be specified in the notice within reasonable time.

Duty of the company to furnish information and documents [Section 206 (2)]: On the receipt of a notice, it shall be the duty of the company and of its officers to furnish such information or explanation to the best of their knowledge and power and to produce the documents to the ROC within the time specified or extended by the ROC. Information and explanation can also be called from past officers of the company.

Power of Registrar to order production of books for inspections [Section 206 (3)]: If no information or explanation is furnished or it is inadequate, ROC may by written notice call on the company to produce for his inspection books of account, books, papers and explanations as he may require at such place and at such time as he may specify in the notice.

However, the ROC shall record his reasons in writing for issuing such notice.

Power of ROC to call for information or carry out inquiry [Section 206 (4)]: If the ROC is satisfied on the basis of information available with or furnished to him or on a representation made to him by any person that the business of a company is being carried on for a fraudulent or unlawful purpose or not in compliance with the provisions of the Act or if the grievances of investors are not being addressed, the ROC may, after informing the company of the allegations made against it by a written order, call on the company to furnish in writing any information or explanation on matters specified in the order within specified time and carry out such inquiry as he deems fit after providing the company a reasonable opportunity of being heard.

The Central Government may, if it is satisfied that the circumstances so warrant, direct the ROC or an inspector appointed by it for the purpose to carry out the inquiry.

Where business of a company has been or is being carried on for a fraudulent or unlawful purpose, every officer of the company who is in default shall be punishable for fraud as per Section 447.

Power of Central Government to direct inspection of books by an inspector [Section 206 (5)]: If the Central Government is satisfied that the circumstances so warrant, it may direct inspection of books and papers of a company by an inspector appointed by it.

Power of Central Government to authorize statutory authority to carry out the inspection [Section 206 (5)]: The Central Government may by general or special order, authorize any statutory authority to carry out the inspection of books of account of a company or class of companies.

Investigation of foreign companies [Section 228]: The provisions of this Chapter (Section 206 to Section 229) shall apply *mutatis mutandis* to inspection, inquiry or investigation in relation to foreign companies.

Que. No. 2] Explain the provisions of the Section 207 of the Companies Act, 2013 relating to "conduct of inspection and inquiry".

Ans.: Duty to produce books for inspection [Section 207 (1)]: Where a ROC or inspector calls for the books of account and other books and papers u/s 206, it shall be the duty of every director, officer or employee of the company to produce it and shall render all assistance to the ROC or inspector in connection with such inspection.

Power of ROC or Inspector to make copies and place identification mark [Section 207 (2)]: The ROC or inspector, making an inspection or inquiry u/s 206 may make copies of books of account and other books and papers or place any marks of identification in books in token of the inspection having been made.

Power of Civil Court vested in ROC & Inspector [Section 207 (3)]: The ROC or inspector shall have all the powers as are vested in a Civil Court under the Code of Civil Procedure, 1908, while trying a suit in respect of the following matters, namely:

- Discovery and production of books of account and other documents, at such place and time as may be specified by such Registrar or inspector making the inspection or inquiry
- Summoning and enforcing the attendance of persons and examining them on oath and
- Inspection of any books, registers and other documents of the company at any place.

Que. No. 3] Explain the duty of Registrar to make a report on the inspection made by him.

Ans.: Report on inspection made [Section 208]: After the inspection of the books of account or an inquiry u/s 206 and other books and papers of the company u/s 207, the Registrar or inspector shall submit a report in writing to the Central Government along with necessary documents. The report may include a recommendation that further investigation into the affairs of the company is necessary giving his reasons in support.

Que. No. 4] Explain the power of Registrar to make search and seizure.

Can Registrar of Companies seize the books and documents of the company? Explain.

CS (Executive) - Dec. 2012 (4 Marks)

Ans.: Power of Registrar to make search and seizure [Section 209 (1)]: Where the Registrar or inspector has reasonable ground to believe that the books and papers of a company, or relating to the KMP or any director or auditor or Practicing Company Secretary if the company has not appointed a Company Secretary, are likely to be destroyed, mutilated, altered, falsified or secreted, he may, after obtain an order from the Special Court for the seizure of such books and papers. For this purpose, he may -

- Enter, with assistance and search, the place where such books or papers are kept and
- Seize 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.

Return of books and paper seized [Section 209 (2)]: The Registrar or inspector shall return the books and papers seized u/s 209 (1) to the company, as soon as may be but not later than 180 day after seizure.

However, the books and papers may be called for by the Registrar or inspector for a further period of 180 days by an order in writing if they are needed again.

The Registrar or inspector may, before returning books and papers, take copies of, or extracts from them or place identification marks on them or deal with the same in such other manner as he considers necessary.

Applicability of the Cr PC to searches or seizures [Section 209 (3)]: The provisions of the Code of Criminal Procedure, 1973 relating to searches or seizures shall apply, *mutatis mutandis*, to every search and seizure made under this section.

INVESTIGATION

Que. No. 5] Explain the provisions relating to investigation into the affairs of the company under the Companies Act, 2013.

Ans.: Power of the Central Government to order investigation into affairs of company [Section 210 (1)]: In following cases the Central Government *may* order an investigation into the affairs of the company if it 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 u/s 208
- (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.

Duty of the Central Government to order investigation into affairs of company [Section 210 (2)]: 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.

Appointment of inspectors [Section 210 (3)]: The Central Government may appoint one or more persons as inspectors to investigate into the affairs of the company and to report thereon in such manner as the Central Government may direct.

Que. No. 6] A majority of the Board of directors of High Value Infotech Ltd. have realized that some of the business activities carried out in the name of the company are not in the interest of either the company or its members. They want that the company should make an application to the Central Government to appoint an Inspector to carry out investigation and find out the whole truth. Explain the steps that should be taken to achieve the purpose under the Companies Act, 2013.

Ans.: According to Section 210 (1) : In following cases the Central Government *may* order an investigation into the affairs of the company if it 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 u/s 208
- (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.

According to Section 210(3) the Central Government may appoint one or more persons as inspectors to investigate into the affairs of the company and to report thereon in such manner as the Central Government may direct.

In the given case, the majority of directors are already of the view that the affairs of the company are not conducted in a manner beneficial either to the company or to the members and want to make an application to the Central Government to appoint an inspector.

Therefore, the steps to be carried out for the purpose will be as under:

- (i) Convene an EOGM of members for passing the required special resolution. The provisions for convening the meeting should be complied with and the explanatory statement with the notice of the meeting must provide full details of the proposed special resolution.

- (ii) Once the special resolution is passed, a copy of it along with the copy of the notice should be filed with the Registrar.
- (iii) An application should be made to the Central Government requesting it to appoint an inspector to investigate the affairs of the company.
- (iv) The Central Government on receipt of such notice will ask for information, documents and other supporting evidence and may order an investigation only if it is of the opinion that an investigation is warranted. It may appoint one or more inspectors to investigate into the affairs of the company and to report thereon in such manner as it may direct.

Que. No. 7] Explain the provisions relating to "establishment of serious fraud investigation office" under the Companies Act, 2013.

Ans.: Establishment of Serious Fraud Investigation Office [Section 211(1)]: The Central Government shall establish the Serious Fraud Investigation Office (SFIO) to investigate frauds relating to a company by notification.

Composition of SFIO [Section 211(2)]: The SFIO shall be headed by a Director and consist of number of experts from various fields. Experts appointed in SFIO shall be the person of ability, integrity and have experience in banking, corporate affairs, taxation, forensic audit, capital market, information technology, law, or other prescribed fields.

Director in the SFIO [Section 211(3)]: The Central Government shall appoint a Director in the SFIO, who shall be an officer not below the rank of a Joint Secretary to the Government of India having knowledge and experience in dealing with matters relating to corporate affairs.

Officers and employees in the SFIO [Section 211(4)]: The Central Government may appoint such experts and other officers and employees in the SFIO as it considers necessary for the efficient discharge of its functions under the Act.

The terms and conditions of officers of SFIO [Section 211(4)]: The terms and conditions of service of Director, experts, and other officers and employees of the SFIO shall be such as may be prescribed.

Que. No. 8] Explain the provisions relating to investigation into affairs of company by Serious Fraud Investigation Office under the Companies Act, 2013.

Ans.: Investigation into affairs of company by SFIO [Section 212(1)]: The Central Government *may* by order assign the investigation into the affairs of the company to the SFIO and may designate inspectors for the purpose of investigation in following cases :

- (a) On receipt of a report of the Registrar or inspector u/s 208
- (b) On intimation of a special resolution passed by a company that its affairs are required to be investigated
- (c) In the public interest or
- (d) On request from any Department of the Central or State Government

On assignment of case to SFIO, no other agency can investigate [Section 212(2)]: If a case is assigned by the Central Government to the SFIO for investigation, no other investigating agency of Central or State Government shall proceed with investigation in case in respect of any offence under the Act.

If any investigation has already been initiated, it shall not be proceeded further with.

The concerned agency shall transfer the relevant documents and records in respect of such offences to SFIO.

Investigation by SFIO and report to Central Government [Section 212(3)]: Where the investigation into the affairs of a company has been assigned by the Central Government to SFIO, it shall conduct the investigation and submit its report to the Central Government within period specified in the order.

Powers of investigation officer [Section 212(4)]: The Director, SFIO shall cause the affairs of the company to be investigated by an Investigating Officer who shall have the power of the inspector u/s 217.

Duty of officers of the company to provide information etc. to [Section 212(5)]: The company and its officers and employees, who are or have been in employment of the company shall be responsible to provide all information, explanation, documents and assistance to the Investigating Officer as he may require for conduct of the investigation.

Conditions for release on bail [Section 212(6)]: The offences which attract the punishment for fraud provided in Section 447 shall be cognizable and no person accused of any offence 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 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.

However, a person, who, is under the age of 16 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 except upon a complaint in writing made by –

- (i) The Director, SFIO or
- (ii) Any officer of the Central Government authorized, by a general or special order in writing in this behalf by that Government.

Limitation on granting of bail [Section 212(7)]: The limitation on granting of bail specified in Section 212(6) is in addition to the limitations under the Code of Criminal Procedure, 1973 or any other law for the time being in force on granting of bail.

Arrest of person [Section 212(8)]: If Additional or Assistant Director of SFIO authorized by the Central Government by general or special order, has on the basis of material in his possession reason to believe that any person has been guilty of any offence punishable under Section 212(6), he may arrest such person and shall, as soon as may be, inform him of the grounds for arrest.

Forwarding copy of order to SFIO after arrest [Section 212(9)]: The Additional or Assistant Director shall, immediately after arrest of person, forward a copy of the order, along with the material in his possession to the SFIO in a sealed envelope, in prescribed manner and SFIO shall keep order and material for prescribed period.

Arrested person to be presented before Magistrate within 24 hours [Section 212(10)]: Every person arrested shall within 24 hours, be taken to a Judicial or Metropolitan Magistrate having jurisdiction to try the case. However, the period of 24 hours shall exclude the time necessary for the journey from the place of arrest to the Magistrate's Court.

Interim Report [Section 212(11)]: The Central Government if so directs, the SFIO shall submit an interim report to the Central Government.

Final Report [Section 212(12)]: On completion of the investigation, the SFIO shall submit the investigation report to the Central Government.

Right to obtain copies of investigation report [Section 212(13)]: A copy of the investigation report may be obtained by any person concerned by making an application to the Court.

Direction by Central Government to initiate prosecution [Section 212(14)]: On receipt of the investigation report, the Central Government may, after examination of the report direct the SFIO to initiate prosecution against the company and its officers or employees, who are or have been in employment of the company or any other person directly or indirectly connected with the affairs of the company.

Investigation report – deemed to police report [Section 212(15)]: The investigation report filed with the Special Court for framing of charges shall be deemed to be a report filed by a police officer under section 173 of the Code of Criminal Procedure, 1973.

Other investigating agency to provide information or documents to SFIO [Section 212(17)(a)]: In case SFIO has been investigating any offence under this Act, any other investigating agency, State Government, police authority, income-tax authorities having any information or documents in respect of such offence shall provide all such information or documents available with it to the SFIO.

Sharing of information or documents with Other investigating agency [Section 212(17)(b)]: The SFIO shall share any information or documents available with it, with any investigating agency, State Government, police authority or income tax authorities, which may be relevant or useful for investigating agency, State Government, police authority or income-tax authorities in respect of any offence or matter being investigated or examined by it under any other law.

Que. No. 9] In which circumstances members of the company or any other person can apply Tribunal for investigation into affairs of the company.

Ans.: Investigation into company's affairs on application by members [Section 213(1)(a)]: The Tribunal on an application made by following specified person and supported by necessary evidence may pass an order for conducting an investigation into the affairs of the company:

In the case of a company having a share capital: 100 members or members holding 10% voting power.

In the case of a company not having a share capital: 20% members

Investigation into company's affairs on application by other persons [Section 213(1)(b)]: Tribunal can also pass order for investigation into company's affairs on an application made to it by any other person, if it is satisfied that there exist any of the following circumstances:

- (i) The business of the company is being conducted with intent to defraud its creditors, members or any other person or otherwise for a fraudulent or unlawful purpose, or in a manner oppressive to any of its members or that the company was formed for any fraudulent or unlawful purpose.
- (ii) Persons concerned in the formation of the company or the management of its affairs have in connection therewith been guilty of fraud, misfeasance or other misconduct towards the company or towards any of its members.
- (iii) The members of the company have not been given all the information with respect to its affairs which they might reasonably expect, including information relating to the calculation of the commission payable to a managing or other director, or the manager, of the company,

Tribunal may pass order to be investigate the affairs of the company by inspectors appointed by the Central Government. The Tribunal is required to give a reasonable opportunity of being heard to the parties concerned.

Appointment of inspectors: Where such an order is passed, the Central Government shall appoint one or more competent persons as inspectors to investigate into the affairs of the company and to report to it in such manner as the Central Government may direct.

Punishment: If after investigation it is proved that the business of the company is being conducted with intent to defraud its creditors, members or any other persons or otherwise for a fraudulent or unlawful purpose, or that the company was formed for any fraudulent or unlawful purpose or any person concerned in the formation of the company or the management of its affairs have in connection therewith been guilty of fraud, then, every officer of the company who is in default and the person or persons concerned in the formation of the company or the management of its affairs shall be punishable for fraud in the manner as provided in Section 447.

Que. No. 10] One of the major creditor of Joy Ltd. is of the opinion that an investigation in the affairs of the company needs to be undertaken in the interest of the company and creditors. Can he make application for investigation of Joy Ltd. to the Tribunal?

CS (Executive) - Dec 2013 (4 Marks)

Ans.: As per Section 213(1)(b), Tribunal can also pass order for investigation into company's affairs on an application made to it and supported by necessary evidence by any person other than members, if it is satisfied that circumstances mentioned in that section exists. Thus, creditor of Joy Ltd. can make application for investigation of Joy Ltd. to the Tribunal.

Que. No. 11] Can Central Government demand security before making order for investigation into affairs of the company?

Ans.: Security for payment of costs and expenses of investigation [Section 214]: Where an investigation is ordered by the Central Government in pursuance of Section 210(1)(b) or in pursuance of an order made by the Tribunal u/s 213, the Central Government may before appointing an inspector Section 210(3) or Section 213(1)(b), require the applicant to give such security not exceeding ₹ 25,000 as may be prescribed, as it may think fit, for payment of the costs and expenses of the investigation.

Such security shall be refunded to the applicant if the investigation results in prosecution.

Que. No. 12] Can Firm, body corporate or association be appointed as inspector for investigation?

Ans.: Firm, body corporate or association not to be appointed as inspector [Section 215]: No firm, body corporate or other association shall be appointed as an inspector.

Que. No. 13] Explain the provisions relating to investigation of ownership of the company.

Ans.: Investigation of ownership of company [Section 216(1)]: Where it appears to the Central Government that there is a reason so to do, it may appoint one or more inspectors to investigate and report on matters relating to the company, and its membership for the purpose of determining the true persons -

- Who are or have been financially interested in the success or failure, whether real or apparent, of the company or
- Who are or have been able to control or to materially influence the policy of the company or

- Who have or had beneficial interest in shares of a company or who are or have been beneficial owners or significant beneficial owner of the company.

Appointment of inspectors [Section 216(2)]: The Central Government shall appoint one or more inspectors, if the Tribunal, in the course of any proceeding before it, directs by an order that the affairs of the company ought to be investigated as regards the membership of the company and other matters relating to the company.

Central Government to define the scope of investigation [Section 216(3)]: While appointing an inspector, the Central Government may define the scope of the investigation, whether as respects the matters or the period to which it is to extend or otherwise, and in particular, may limit the investigation to matters connected with particular shares or debentures.

Powers of inspector [Section 216(4)]: Subject to the terms of appointment of an inspector, his powers shall extend to the investigation of any circumstances suggesting the existence of any arrangement or understanding which, though not legally binding, is or was observed or is likely to be observed in practice and which is relevant for the purposes of his investigation.

Que. No. 14] Explain the provisions relating to procedure to be followed for investigation and powers that can be exercised by the inspector for the purpose of investigation.

Ans.: Procedure, powers, etc., of inspectors [Section 217]

Duty of officers and employees to give information and assistance to the inspector [Section 217(1)]: It shall be the duty of all past and present officers, employees and agents of a company which is under investigation and where the affairs of any other body corporate or a person are investigated u/s 219 -

- To preserve and to produce to an inspector or any person authorized by him in this behalf all books and papers of the company or relating to the other body corporate or the person, which are in their custody or power and
- Otherwise to give to the inspector all assistance in connection with the investigation which they are reasonably able to give.

Power of inspector [Section 217(2)]: The inspector may require any body corporate to furnish information to, or produce such books and papers before him or any person authorized by him, if it is relevant or necessary for the purposes of his investigation.

Retention of books by inspector [Section 217(3)]: The inspector shall not keep in his custody any books and papers for more than 180 days and return the same to the company, body corporate, firm or individual as the case may be. However, the books and papers may be called for by the inspector if they are needed again for a further period of 180 days by an order in writing.

Examination on oath [Section 217(4)]: An inspector may examine on oath -

- any of the persons referred to in Section 217(1); and
- with the prior approval of the Central Government, any other person,

He may also require any of above persons to appear before him personally.

Inspector shall have powers of Civil Court [Section 217(5)]: The inspector making an investigation shall have all the powers as are vested in a Civil Court under the Code of Civil Procedure, 1908, while trying a suit in respect of the following matters, namely:

- Discovery and production of books of account and other documents, at such place and time as may be specified by such person;
- Summoning and enforcing the attendance of persons and examining them on oath and
- Inspection of any books, registers and other documents of the company at any place.

Consequences of disobeying the direction issued [Section 217(6)]: 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 1 year and with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 1,00,000.

If a director or an officer of the company has been convicted of an offence under this section, the director or the officer shall, on and from the date on which he is so convicted, be deemed to have vacated his office as such and on such vacation of office, shall be disqualified from holding an office in any company.

Notes of any examination [Section 217(7)]: The notes of any examination of any person shall be taken down in writing and shall be read over to, or by, and signed by, the person examined, and may thereafter be used in evidence against him.

Punishment [Section 217(8)]: A person shall be punishable with imprisonment for a term which may extend to 6 months and with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 1,00,000, and also with a further fine which may extend to ₹ 2,000 for every day after the first during which the failure or refusal continues, if he fails without reasonable cause or refuses to do the following:

- To produce to an inspector or any person authorized by him in this behalf any book or paper which is his duty to produce
- To furnish any information which is his duty to furnish
- To appear before the inspector personally when required to do so or to answer any question which is put to him by the inspector or
- To sign the notes of any examination

Duty of certain authorities to provide assistance to inspectors [Section 217(9)]: The officers of the Central Government, State Government, police or statutory authority shall provide assistance to the inspector for the purpose of inspection, inquiry or investigation, which the inspector may, with the prior approval of the Central Government, require.

Reciprocal arrangements with foreign State [Section 217(10)]: The Central Government may enter into an agreement with the Government of a foreign State for reciprocal arrangements to assist in any inspection, inquiry or investigation under the Act or under the corresponding law in force in that State.

Reference of matter by India Court to Foreign Court [Section 217(11)]: Inspector can make application to local court to request foreign court or authority to record statement of a person in that country and send that statement to court in India. Such statement will be admissible as evidence.

Foreign Court to refer the matter to India Court [Section 217(12)]: If court or authority in foreign country request, the court in India shall record the statement and send it to foreign court or authority through Central Government.

Que. No. 15] Can company dismiss the employee or change the terms of his employment, if such employee has disclosed information during the course of investigation?

Ans.: Protection of employees during investigation [Section 218]: An employee who has disclosed information during the course of investigation is protected against dismissal, discharge or removal or change in terms of employment to his disadvantage, during the investigation, without permission of Tribunal.

The company should give intimation to Tribunal of proposed action and if no reply is received within 30 days, proposed action can be taken.

If the company is not satisfied with the order of Tribunal, it can file appeal within 30 days. Such removal or change in terms of employment is subject to provisions of other laws also.

Que. No. 16] Write a short note on: Investigation into affairs of related companies

Ans.: Power of inspector to conduct investigation into affairs of related companies [Section 219]: An inspector appointed u/s 210 or 212 or 213 can carry out investigation of -

- Holding company or a subsidiary company
- Any other body corporate which was managed by managing director or manager of the company
- Any other body corporate whose board of directors comprises nominees of the company or is accustomed to act in accordance with the directions or instructions of the company or any of its directors or
- Any person who is or has at any relevant time been the company's managing director or manager or employee,

Power of investigation of into affairs of related companies is subject to prior approval of the Central Government.

Que. No. 17] Explain the powers of inspectors to seize the books and papers.

Ans.: Seizure of documents by inspector [Section 220]: If the inspector has reasonable grounds to believe that the books and papers relating to affairs of the company are likely to be destroyed, mutilated, altered, falsified or secreted, he can enter into places or premises where books and papers are placed, to search the place and to seize the books and papers as necessary.

Company can take copies of the documents at its cost.

Search and seizure provisions must be according to the Code of Criminal Procedure, 1973. The seized papers can be kept till the conclusion of investigation. The inspector can take copies of any documents or place identification marks on them before returning the books and papers.

Que. No. 18] Write a short note on: Freezing of assets of company on inquiry and investigation

Ans.: Freezing of assets of company on inquiry and investigation [Section 221]: If on inquiry or investigation of the company, the Tribunal is satisfied that the removal, transfer or disposal of funds, assets, properties of the company is prejudicial to the interests of the company or its shareholders or creditors or in public interest, it may by order direct that transfer, removal or disposal shall not take place during period not exceeding 3 years as may be specified in the order or may take place subject to such conditions and restrictions as the Tribunal may deem fit.

In case of any removal, transfer or disposal of funds, assets, or properties of the company in contravention of the order of the Tribunal,

- The company shall be punishable with fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 25,00,000 and
- Every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 3 years or with fine which shall not be less than ₹ 50,000 but which may extend to ₹ 5,00,000 or with both.

Que. No. 19] State the provisions relating to power of Tribunal to restrict issue or transfer of securities of a company under investigation?

Ans.: Imposition of restrictions upon securities [Section 222]: During the investigation, the Tribunal can order restrictions on issue or transfer of securities as it deems fit, for a period up to 3 years. Thus, Tribunal may order that any share transfer may not be effected.

Where securities in any company are issued or transferred in contravention of an order of the Tribunal, the company shall be punishable with fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 25,00,000 and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 6 months or with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 5,00,000, or with both.

Que. No. 20] Write a short note on: Inspector's Report

Ans.: Inspector's report [Section 223]: An inspector has to submit interim report or a final report to the Central Government.

Every report shall be in writing or printed as the Central Government may direct.

A copy of the report may be obtained by members, creditors or any person whose interest is likely to be affected by making an application in this regard to the Central Government.

The report of any inspector shall be authenticated either –

- by the seal of the company, if any or
- by a certificate of a public officer having the custody of the report, as provided under section 76 of the Indian Evidence Act, 1872,

Such report shall be admissible in any legal proceeding as evidence in relation to any matter contained in the report.

Provisions of this section shall apply to the report referred to in Section 212.

Que. No. 21] Who shall bear the expenses of investigation?

Ans.: Expenses of investigation [Section 225]: The expenses of investigation by an inspector appointed by the Central Government other than expenses of inspection u/s 214 shall be defrayed in the first instance by the Central Government, but shall be reimbursed by the following persons:

- Any person who is convicted after prosecution, to the extent as may be specified by the Court;
- Any company or body corporate in whose name proceedings are brought, to the extent of the amount or value of property recovered by it as a result of such proceedings;
- If prosecution is not launched expenses of investigation will be borne by the following to such extent as the Central Government may direct
 - Any company, body corporate, managing director or manager dealt with by the report of the inspector; and
 - The applicants for the investigation, where the inspector was appointed u/s 213

Any amount recoverable is first charge on property of the company.

Que. No. 22] State the provisions relating to professional immunity to legal advisor and bankers under the Companies Act, 2013.

Ans.: Legal advisers and bankers not to disclose certain information [Section 227]: A legal advisor cannot be compelled to supply any privileged communication made to him except the name and address of his client.

A banker has to disclose information about the company under investigation but not of other customer.

Que. No. 23] Mr. Sharma is a legal adviser of ABC Ltd. and in that capacity he has rendered legal advice by way of written communication to the company. The Registrar of Companies, Mumbai, issues an order to Mr. Sharma to disclose and furnish a copy of the communication made by him. Examine the power of Registrar to call for the said document from Mr. Sharma.
CA (Final) – Nov 2002 (5 Marks)

Ans.: As per Section 227, a legal adviser cannot be compelled to supply any privileged communication made to him except the name and address of his client. Thus, order of Registrar to Mr. Sharma to disclose and furnish a copy of the communication made by him with ABC Ltd. is not valid.

Que. No. 24] List out the kind of investigation carried out under the Companies Act, 2013.
CS (Executive) – June 2011 (4 Marks)

Ans.: The Companies Act, 2013 provides for carrying out following kinds of investigation:

- ◆ Investigation into affairs of company. [Section 210]
- ◆ Investigation into affairs of company by Serious Fraud Investigation Office. [Section 212]
- ◆ Investigation into company's affairs in other cases. [Section 213]
- ◆ Investigation of ownership of company. [Section 216]
- ◆ Investigation of foreign companies. [Section 228]

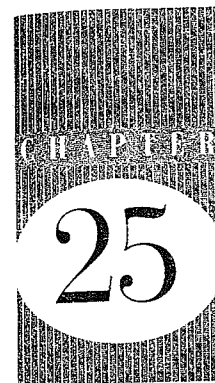
Que. No. 25] Distinguish between: Inspection and Investigation

CS (Executive) – June 2015 (4 Marks)

Ans.: Following are the main points of distinction between inspection and investigation:

| Points | Inspection | Investigation |
|-------------|--|---|
| When | <p>If no information or explanation is furnished or it is inadequate, ROC may by written notice call on the company to produce for his inspection books of account, books, papers and explanations as he may require at such place and at such time as he may specify in the notice. [Section 206(3)]</p> <p>If the Central Government is satisfied that the circumstances so warrant, it may direct inspection of books and papers of a company by an inspector appointed by it. [Section 206(5)]</p> | <p>In following cases the Central Government may order an investigation into the affairs of the company, if it is of the opinion that it is necessary to investigate into the affairs of a company –</p> <ol style="list-style-type: none"> On the receipt of a report of the Registrar or inspector u/s 208 On intimation of a special resolution passed by a company that the affairs of the company ought to be investigated or In public interest. [Section 210(1)] <p>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. [Section 210(2)]</p> |

| Points | Inspection | Investigation |
|---------|--|--|
| By whom | Inspection may be carried out by ROC or the inspector authorized by the Central Government and in case of listed company SEBI is also authorized to inspect. | Investigation is always carried out by the inspector or authorized officer of Central Government. |
| Nature | Inspection is routine exercise. | The investigation means in-depth analysis of books of account, transaction, and event and always carried out with specific objectives. |



MAJORITY RULE & MINORITY RIGHTS

This Chapter Covers:

- Rule in *Foss v. Harbottle*
- Minority rights and shareholder's remedies.
- Statutory remedy under the Companies Act, 2013.
- Meaning of oppression and its prevention.
- Persons entitled to apply.
- Powers of the Tribunal and Central Government to prevent oppression or mismanagement.

Que. No. 1] The Court of law will not interfere with the internal management of companies acting within their powers. CS (Executive) – June 2012 (5 Marks)

Discuss the provisions related to 'majority rule' and 'minority rights' with reference to the concept of rights of majority. CS (Inter) – Dec 2006 (8 Marks), June 2008 (10 Marks)

Discuss the rule of *Foss vs. Harbottle*. CS (Inter) – Dec 2007 (4 Marks)

Ans.: Powers of Majority: As a company is an artificial person with no physical existence, it functions through the instrumentality of the Board of directors who is guided by the wishes of the majority. Therefore, a cardinal rule of company law that *prima facie* a majority of members of a company are entitled to exercise the powers of the company and generally to control its affairs.

The principle of non-interference: In case of difference amongst the members the issue is decided by a vote of the majority. Since the majority of the members are in an advantageous position to run the company according to their command, the minorities of shareholders are often oppressed. The company law provides for adequate protection for the minority shareholders when their rights are trampled by the majority. But the protection of the minority is not generally available when the majority does anything in the exercise of the powers for internal administration of a company. The court will not usually intervene at the instance of shareholders in matters of internal administration, and will not interfere with the management of a company by its directors so long they are acting within the powers conferred on them under the articles of the company. In other words, the articles are the protective shield for the

majority of shareholders who compose the board of directors for carrying out their object at the cost of minority of shareholders.

The basic principle of non-interference with the internal management of company by the court is laid down in a celebrated case of *Foss vs. Harbottle* (1843) 2 Hare 461 = (1843) 67 ER 189 that no action can be brought by a member against the directors in respect of a wrong alleged to be committed to a company. The company itself is the proper party of such an action.

When minority can intervene: The principle that majority rule has certain well established exceptions as follows:

- (1) **Ultra Vires Acts:** Where the directors representing the majority of shareholders perform an illegal or ultra vires act for the company, an individual shareholder has right to bring an action. The majority of shareholders have no right to confirm an illegal or ultra vires transaction of the company. In such case a shareholder has the right to restrain the company by an order or injunction of the Court from carrying out an ultra vires act.
- (2) **Fraud on Minority:** Where an act done by the majority amounts to a fraud on the minority; an action can be brought by an individual shareholder.

It would be a shocking thing if the majority of shareholders are allowed to put something into their pockets at the expenses of the minority. In this case, the majority of members of 'Company A' were also members of 'Company B', and at a meeting of 'Company A' they passed a resolution to compromise an action against 'Company B', in a manner alleged to be favourable to 'Company B', but unfavourable to 'Company A'. Held, the minority shareholders of 'Company A' could bring an action to have the compromise set aside. [*Menier vs. Hooper's Telegraph Works*, (1874) L.R. 9 Ch. App. 350]

- (3) **Wrongdoers in Control:** If the wrongdoers are in control of the company, the minority shareholders representative action for fraud on the minority will be entertained by the court.
- (4) **Resolution requiring Special Majority but is passed by a simple majority:** A shareholder can sue if an act requires a special majority but is passed by a simple majority. Simple or rigid, formalities are to be observed if the majority wants to give validity to an act which purports to impede the interest of minority.
- (5) **Personal Actions:** Individual membership rights cannot be invaded by the majority of shareholders. He is entitled to all the rights and privileges appertaining to his status as a member. An individual shareholder can insist on the strict compliance with the legal rules, statutory provisions.
- (6) **Breach of Duty:** The minority shareholder may bring an action against the company, where although there is no fraud, there is a breach of duty by directors and majority shareholders to the detriment of the company.

The plaintiff, who was minority shareholders of a company, brought an action against the two directors of the company and the company itself. In their statement of the claim they alleged that the company, on the instruction of the two directors who were majority shareholders, sold the company's land to one of the directors (who was the wife of the other) for £4,250 and the directors knew or ought to have known that the sale was at an under value. Four years after the sale, she sold the same land for £1,20,000. The directors applied for the statement of claim to be disclosed on reasonable cause of action or otherwise as an abuse of the process of the Court. Held, the application of director should be dismissed. [*Daniels v. Daniels*, (1978) 2 W.L.R. 73]

Que. No. 2] Sky-High Ltd. is engaged in the business of construction of projects. A, B and C, directors of the Sky-High Ltd. are holding 75% of the capital of this company. The company passed a resolution at its general meeting that it would not be interested in a particular contract for construction of bridge. Subsequently, the same contract was obtained by A, B and C in their own names. Comment.

CS (Final) - Dec 1995 (5 Marks), Dec 2001 (5 Marks)

Ans.: The basic principle of non-interference with the internal management of company by the court is laid down in a celebrated case of *Foss vs. Harbottle* (1843) 2 Hare 461 = (1843) 67 ER 189 that no action can be brought by a member against the directors in respect of a wrong alleged to be committed to a company. The company itself is the proper party of such an action.

However, if the majority misuses its powers to defraud or oppress the majority, an action can be brought by minority shareholders.

As per facts given in case, three directors holding 75% of the capital used their position and obtained contract in their own names. This amounts to breach of duty and fraud on minority as directors utilized the contract for their person gain. Thus, minority shareholder can bring action against the directors.

Que. No. 3] Explain the protection accorded to the minority shareholder under the company law.

CS (Inter) - June 1999 (8 Marks)

CS (Executive) - Dec 2008 (7 Marks)

Briefly explain the rule of majority and its exceptions. CS (Inter) - Dec 2000 (6 Marks)

How does the Companies Act, 2013 provide the protection of the right of minority shareholder? CS (Inter) - June 2002 (6 Marks), Dec 2002 (5 Marks)

CS (Inter) - Dec 2005 (16 Marks), Dec 2006 (6 Marks)

Ans.: Though the shareholder's democracy is supreme under the Companies Act and the decided cases suggest that the majority shall not be allowed to act in an unfair, fraudulent, or oppressive way against the interests of the minority shareholders.

The Companies Act, 2013, extends protection to minority by granting various rights to minority shareholders which are discussed as below:

- (1) **The variation of class rights:** The rights attached to the shares of any class can be varied as per Section 48 (1) with the consent in writing of the holder of not less than 3/4th of the issued shares of that class or with the sanction of a special resolution passed at a separate meeting of the holders of the issued shares of that class. But the holders of not less than 10% of the shares of that class who had not assented to the variation may apply to the Tribunal for the cancellation of the variation as per Section 48(2).
- (2) **Schemes of reconstruction and amalgamation:** The minority is accorded protection in cases where they dissent to the scheme of reconstruction or amalgamation.
- (3) **Oppression and mismanagement:** The principle of majority rule does not apply to cases where Sections 241 to 246 are applicable for prevention of oppression and mismanagement. A member, who complains that the affairs of the company are being conducted, in a manner oppressive to some of the members including himself, or against public interest, he may apply to the Tribunal.
- (4) **Alternative remedy to winding up:** Any member or members, who complain that the affairs of the company are being conducted in a manner oppressive to some of the members including themselves, may apply for winding up of company.

- (5) **Investigation by the Government:** As per **Section 210** the Central Government may appoint one or more competent persons as inspectors to investigate the affairs of any company and to report thereon in such manner as the Central Government may direct.

OPPRESSION & MISMANAGEMENT

Que. No. 4] Give five example of 'oppression'.

Ans.: The term 'oppression' is not defined in the Companies Act, 2013. Oppression, according to the dictionary meaning of the word, is any act exercised in a manner burdensome, harsh and wrongful.

Some the acts held as oppressive are as follows:

- > Continuous refusal to register shares to retain control over affairs of the company.
- > Illegal removal of director one group and appointing other director without notice to one group of directors.
- > Calling board meeting with 2 days notice so that NRI directors cannot attend and allotting shares to one group so that it comes into majority.
- > Issuing shares to wife of directors for wholly illusive consideration.
- > Attempt to deprive members of his ordinary membership rights e.g. denial of voting right or denial to contest election as director
- > Wrong share transfer of shares to reduce the shares of other groups.
- > Diversion of business opportunity to another company where some directors are interested.

Que. No. 5] Give five example of 'mismanagement'

Ans.: Some the acts held as mismanagement are as follows:

- > Not allowing director to function as director
- > Reckless sanction and disbursement of loans.
- > Serious violation of legal provisions
- > Acting beyond authority of memorandum and articles.
- > Directors do not take serious actions in case of corruption, embezzlement etc.
- > Diversion of funds
- > Operation of bank accounts by unauthorized persons.

Que. No. 6] What are remedial measures available for 'Oppression' & 'Mismanagement' under the Companies Act, 2013? Who can make such application?

CS (Inter) - Dec 2000 (10 Marks)

Explain the power of Tribunal to prevent 'Oppression' & 'Mismanagement'.

CS (Inter) - June 2003 (8 Marks), June 2006 (8 Marks)

Ans.: Application to Tribunal for relief in cases of oppression by members of the company [Section 241(1)]: Members of a company as specified in Section 244 may apply to the Tribunal for relief in cases of oppression & mismanagement. Such application can be made in following cases:

- (a) Where the affairs of the company have been or are being conducted in a manner prejudicial to public interest or in a manner prejudicial or oppressive to him or any other member or members or in a manner prejudicial to the interests of the company; or
- (b) The material change has taken place in the management or control of the company and that by reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to its interests or its members or any class of members.

Such change may relate to alteration in the Board of Directors, or manager, or in the ownership of the company's shares, or if it has no share capital, in its membership, or in any other manner whatsoever.

Application to Tribunal for relief in cases of oppression by the Central Government [Section 241(2)]: The Central Government may itself apply to the Tribunal for relief in cases of oppression & mismanagement if it is of the opinion that the affairs of the company are being conducted in a manner prejudicial to public interest.

Power of Tribunal [Section 242]: On receiving application u/s 241, the Tribunal may, with a view to bringing to an end the matters complained of, make such order as it thinks fit.

Right to apply under section 241 [Section 244]: The following members of a company shall have the right to apply u/s 241, namely:

- (a) **In the case of a company having a share capital:** 100 members of the company or 10% of the total number of members, whichever is less. *(The applicants must have paid all calls and other sums due on their shares. Thus, holders of partly paid-up shares cannot apply)*
- (b) **In the case of a company not having a share capital:** 20% of the total number of members

However, the Tribunal may, on an application, waive all or any of the above requirements so as to enable the members to apply u/s 241.

Where any share or shares are held by two or more persons jointly, they shall be counted only as one member.

Where any members of a company are entitled to make an application section 244, any one or more of them having obtained the consent in writing of the rest, may make the application on behalf and for the benefit of all of them.

Que. No. 6A] Distinguish between: Oppression & Mismanagement

CS (Executive) - Dec 2014 (4 Marks)

Ans.: Following are the main points of distinction between oppression & mismanagement;

| Points | Oppression | Mismanagement |
|-----------------|--|---|
| Meaning | The term 'Oppression' is not defined in the Companies Act, 2013. Oppression, according to the dictionary meaning of the word, is any act exercised in a manner burdensome, harsh and wrongful. Oppression means violation of condition of fair play. The complaining member must be under a burden which is unjust, harsh or tyrannical. It involves lack of probity or fair dealing to a member in the matter of rights as a shareholder. | The term 'Mismanagement' is also not defined in the Companies Act, 2013. Normally mismanagement means gross misconduct of affairs of the company or misuse of powers given to directors or members under the Companies Act, 2013. |
| Examples | Some of the acts held as oppressive are as follows: <ul style="list-style-type: none"> ◆ Continuous refusal to register shares to retain control over affairs of the company. | Some of the acts held as mismanagement are as follows: <ul style="list-style-type: none"> ◆ Not allowing director to function as director ◆ Reckless sanction and disbursement of loans. |

| Points | Oppression | Mismanagement |
|--------|---|---|
| | <ul style="list-style-type: none"> Illegal removal of director one group and appointing other director without notice to one group of directors. Calling board meeting with 2 days notice so that NRI directors cannot attend and allotting shares to one group so that it comes into majority. Issuing shares to wife of directors for wholly illusive consideration. Attempt to deprive members of his ordinary membership rights e.g. denial of voting right or denial to contest election as director | <ul style="list-style-type: none"> Serious violation of legal provisions Acting beyond authority of memorandum and articles. Directors do not take serious actions in case of corruption, embezzlement etc. Diversion of funds Operation of bank accounts by unauthorized persons. |

Que. No. 7] A private company was required under the Foreign Exchange Management Act, 1999 and direction issued by RBI to reduce its foreign shareholding 60% to 40%. It made an offer of right shares to all existing shareholder but issued shares to Indian shareholders. The foreign company, which is a shareholder, contents that non-issue of right shares to it amounts to 'oppression'. Comment. CS (Final) – June 1997 (5 Marks)

Ans.: The term 'oppression' is not defined in the Companies Act, 2013. Oppression, according to the dictionary meaning of the word, is any act exercised in a manner burdensome, harsh and wrongful. Non-issuing right shares to foreign shareholder to comply with Foreign Exchange Management Act, 1999 and direction issued by RBI does not amount to 'oppression'.

Further in relief granted against Section 241 only against continuous acts of oppression. Mere isolated act do not amount to oppression. [Shanti Prasad vs. Kalinga Tubes, (1965) 35 Comp. Cas 351]

Therefore, contention of foreign shareholder that non-issue of right shares to it amounts to 'oppression' is not correct.

Que. No. 8] 60% shares of Indo-French Ltd. are held by French Group and balance by an Indian Group. As per Articles of Association of the company both groups had equal managerial powers. The relationship between the two groups soured and the operations of the company reached a deadlock. The Indian Group approached the Tribunal for action against the French Group for oppression. Based on these facts, you are required to decide, with reference to the provisions of the Companies Act, 2013 and/or the decided case laws, the following issues:

- Whether the contention of oppression against the French Group by the Indian Group is tenable?
- What are the powers of the Tribunal in this regard?

CA (Final) – May 2005 & May 2007 (5 Marks)

Ans.: An application seeking relief from Tribunal must make out a prima facie that the affairs of the company have been or are being conducted in a manner prejudicial to public interest or in a manner prejudicial or oppressive to applicant or any other members in a manner prejudicial to the interests of the company.

As per facts given in the case, both the India Group and French Group are equally strong and one is unable to oppress the other. As such there may be deadlock but not oppression. Thus, relief under Section 241 will not be available. Thus, contention of India Group that the French Group is acting in a manner oppressive to India Group is not tenable.

The powers of the Tribunal under the provisions of Section 242 are discretionary in character. Apart from the general powers, the Tribunal u/s 242(2)(b), may order the purchase of the shares of one group by the other group. In the case of *Yashovardhan Saboo vs. Groz Beckert Saboo Ltd.* 1993 1 Comp. L.J. 20, the foreign group ordered to buy the shares of the minority group at the fair price with necessary permission under the laws governing the foreign exchange. But in case where there is a deadlock and the matters are not sorted out by any other means, an order for winding up of the company may also be made under the just and equitable clause by the Court hearing petition u/s 241/242. [Kishan Kumar Ahuja vs. Suresh Kumar Ahuja].

Thus, if the Indian Group or the French Group fails to buy out the shares of the other group, the Tribunal may order the winding up of the company in accordance with the provisions of the Companies Act, 2013.

Que. No. 9] Zebra Private Ltd was incorporated in the year 2014 under the Companies Act, 2013 by 3 brothers, namely A, B & C. All the three were promoter-directors named in the AOA and subscribed for 100 shares each in the company through MOA. Thereafter, from time to time, further shares were allotted in proportion of one third to each of them and in due course the company started earning substantial profits. Due to greed of money, the two brothers, namely A and B joined hands together and assumed complete control of the company leaving their brother C in lurch. Both the brothers got further shares allotted to themselves, thereby their joint shareholding increased from 66% to 90%, while the shareholding of C got reduced from the erstwhile 33% to 10%. No notice of any Board Meeting was sent to C, who was sidelined and was also removed as a Director. Aggrieved by the decisions taken by his two brothers at his back, C seeks your advice for taking out appropriate proceedings before the Court or Judicial authority of competent jurisdiction. Also suggest the nature of reliefs he may claim while filing his case.

CA (Final) – Nov 2011 (8 Marks)

Ans.: As per Section 241, member(s) of a company as specified in Section 244 may apply to the Tribunal for relief in cases of oppression & mismanagement.

As per Section 242, on receiving application u/s 241, the Tribunal may, with a view to bringing to an end the matters complained of, make such order as it thinks fit.

The Tribunal may, with a view to bringing to an end the matters complained of, make such order as it thinks fit.

As per Section 244, a member holding 10% shares is entitled to file such a petition.

In the present case, C was holding 33% shares in the company which is nothing but a quasi partnership and was participating in the management. By further allotment of shares in a clandestine manner and without the consent of C, his shareholding was reduced to 10% while the shareholding of his brothers stood at 90%. This is a serious act of oppression of C, a minority shareholder. On similar facts, it was held by Supreme Court in *Dale & Carrington Invt. Private Ltd. vs. P.K. Prathpan*, (2004) 122 Comp Cas. 175 that assuming meetings of board of directors did take place, the manner in which the shares were issued without informing other shareholders about it and without offering them to any other shareholder, was totally *mala fide* and the sole object in this was to gain control of the company by becoming a majority shareholder. This was clearly an act of oppression. The only relief that has to be granted in the present case was to undo the advantage gained by majority shareholder through their manipulation and fraud. The allotment of all the additional shares had to be set aside.

Section 241 protects the rights of shareholders and not as a director. It has been held in a number of cases that in a family company like the present one, removal of the promoter-director is also an act of oppression.

In the facts and circumstances of this case, C is advised to file a petition under section 241. Being a 10% shareholder he is entitled to file the petition before the Tribunal. He may seek the following reliefs:

- (i) The alleged allotment of further shares be declared null and void and set aside;
- (ii) The alleged removal of the petitioner, C be declared as null and void and set aside;
- (iii) The Board of directors be re-constituted with the petitioner and his two brothers and an independent person, as the Chairman of the Board of directors to be appointed by the Tribunal with casting vote;
- (iv) The petitioner may be appointed as Managing director of the company having substantial powers of management.

Que. No. 10] The profits of MJR Ltd. for the financial year 2015-2016 fell considerably due to recession. The Board of directors of the company, therefore, *bona fide* did not recommend any dividend for the year. At the AGM, a group of shareholders objected to the Board's decision and wanted the Board to make recommendation for dividend. On refusal by the Board, the members, who feel oppressed by the Board's decision to skip the dividend, move to the Tribunal and complain against the Board on the ground of oppression and mismanagement. Examining the provisions of the Companies Act, 2013 and decide:

- (1) Whether the shareholders contention shall be tenable?
- (2) Whether the act of Board of Directors not to recommend any dividend shall amount to oppression and mismanagement?

Ans.: Under Section 241, members may apply to the Tribunal in cases of oppression and mismanagement. However, *bona fide* decisions consistent with the company's MOA and AOA are not to be equated with mismanagement even if they turn out to be wrong in the circumstances or these cause temporary losses. The machinery created by the section not to be used by the minority for compelling the majority to come to terms, where the company is honestly managed. Directors *bona fide* decision not to declare dividend and to accumulate available profits into reserves is not mismanagement. [*Thomas Vettom (V.J.) vs. Kuttanad Rubber Co. Ltd. (1984) 56 Comp. Cas. 284 (Ker.)*]

Furthermore, the shareholders cannot compel the Board to recommend a dividend. The Board's recommendations are placed in the general meeting. The general meeting can reduce the dividend, but cannot even increase the dividend as recommended by the Board.

Therefore, the shareholders cannot compel the company to declare dividend and cannot charge the directors with oppression or mismanagement.

In view of above:

- (1) The contention of shareholders shall not be tenable.
- (2) The act of the Board of directors who acted *bona fide*, not to recommend any dividend shall not amount to oppression or mismanagement.

Que. No. 10A] Due to inadequacy of profits, the Board of directors of Rise Ltd. decided not to recommend any dividend for the financial year ended 31st March, 2015. Certain shareholders of the company complained to the Tribunal regarding mismanagement of the affairs of the company, since the Board of the company did not recommend any dividend. Explaining the provisions of the Companies Act, 2013, examine whether the contention of the shareholders is tenable. CS (Executive) - June 2015 (4 Marks)

Ans.: Under Section 241, members may apply to the Tribunal in cases of oppression and mismanagement. However, *bona fide* decisions consistent with the company's MOA and AOA are not to be equated with mismanagement even if they turn out to be wrong in the circumstances or these cause temporary losses. The machinery created by the section not to be used by the minority for compelling the majority to come to terms, where the company is honestly managed. Directors *bona fide* decision not to declare dividend and to accumulate available profits into reserves is not mismanagement. [*Thomas Vettom (V.J.) v. Kuttanad Rubber Co. Ltd. (1984) 56 Comp. Cas. 284 (Ker.)*]

Furthermore, the shareholders cannot compel the Board to recommend a dividend. The Board's recommendations are placed in the general meeting. The general meeting can reduce the dividend, but cannot even increase the dividend as recommended by the Board.

Therefore, the shareholders cannot compel the company to declare dividend and cannot charge the directors with oppression or mismanagement.

In view of above:

- (1) The contention of shareholders shall not be tenable.
- (2) The act of the Board of directors who acted *bona fide*, not to recommend any dividend shall not amount to oppression or mismanagement.

Que. No. 11] What is meant by 'oppression'? State whether the aggrieved party would succeed in obtaining relief from Tribunal on the ground of oppression in the following cases:

- (i) The majority of the Board of directors overrides the minority directors and the minority directors apply to Tribunal complaining oppression by majority directors.
- (ii) A petition by majority shareholders complaining oppression by minority shareholders.

Give your answer according to the provisions of the Companies Act, 2013.

Ans.: The term 'oppression' is not defined in the Companies Act, 2013. Oppression, according to the dictionary meaning of the word, is any act exercised in a manner burdensome, harsh and wrongful.

- (i) The oppression dealt with by Section 241 is only oppression of members in their character as such; and it is only in that character they can involve Section 241. The harsh treatment, for instance, of a member who is a director or other officer or employee, by the Board of directors or management does not come within Section 241. It has been held in *Re. Bellador Silk Ltd.* that if the majority of the Board of directors overrides the minority directors the latter cannot resort to Section 241 and hence the minority directors will not succeed in getting relief from CLB on the ground of oppression.
- (ii) According to Section 241, the right to apply for relief under Section 241 read with Section 244 is given to 100 members or 10% of the total number of members of the company. There is nothing in this section which suggests even indirectly that unless the application is made by minority shareholders it is not maintainable. The right to apply is, therefore, not confined to oppressed minority of the shareholders alone. It was held by Calcutta High Court in *Re. Sindhri Iron Foundry (P.) Ltd.* that the oppressed majority also might apply for relief under Section 241. Therefore, the petitioners are likely to succeed in getting relief provided.

Que. No. 12] (i) ABC Private Ltd. is a company in which there are 8 shareholders. Can a member holding less than 10% share capital of the company apply to the Tribunal for relief against oppression and mismanagement?

(ii) It is alleged by said member that the directors of the company have misused their position in making certain inter-corporate deposits which are against the interests of the company. Will the Tribunal entertain application containing such allegation in the case of a private company?

Give your answer according to the provisions of the Companies Act, 2013.

Ans.: Keeping in view the provisions of the Companies Act, 2013, answer to given problem is as follows:

- (i) As per Section 244, in the case of a company having share capital, 100 members or not less than 10% of the total number of members, whichever is less can apply for relief under Section 241. In the given case, since there are 8 shareholders. The condition of 10% of 8 i.e. 1 is satisfied. Therefore, a single member can present a petition to the Tribunal, regardless of the fact that he holds less than 10% of the company's share capital.
- (ii) As regards the proprietary rights in inter-corporate loans by a private company, they are not closely regulated by Company Law as in the case of public companies. Though the Board of Directors are the best to judge and to take a commercial decision in this regard, if it is *mala fide*, it should be looked into. Therefore, the Tribunal can look into the allegation lodged by the member.

Que. No. 13] XYZ Private Ltd. has two groups of directors. A dispute arose between the two groups out of which one group controlled the majority of shares. A very serious situation arose in the administration of the company's affairs when the minority group ousted the lawful board of directors from the possession and control of the management of the company's factory and workshop. Books of account and statutory records were held by the minority group and consequently the annual accounts could not be prepared for two years. The majority group applied to the Tribunal for relief under section 241 of the Companies Act, 2013. You are required to decide with reference to the provisions of the Companies Act, 2013, the following issues:

- (i) Can majority of shareholders apply to the Tribunal for relief against the oppression by the minority shareholders?
- (ii) Whether Tribunal can grant relief in such circumstances.

Ans.: Where the majority is prevented from protecting itself by controlling the directors at general body meetings, the majority becomes an artificial minority entitled to claim protection under Section 241 [V. Sebastian, Dr V City Hospital (Pvt.) Ltd. (1985) 57 Comp. Cas 453 (Ker)] Thus, the remedy u/s 241 is confined not to an oppressed minority of the shareholders alone; an oppressed majority may also apply to the Tribunal against their oppression from the side minority shareholders.

If the Tribunal finds that the company's interest is being seriously prejudiced by the activities of one or the other group of shareholders, that two different registered offices at two different addresses have been set up, that two rival boards are holding meetings, that the company's business property and assets have passed into hands of unauthorized persons who have taken wrongful possession and who claim to be the shareholders and directors, there is no reason why the Tribunal should not make appropriate orders to put an end to such matters.

The Tribunal may grant relief by passing appropriate order as per Section 242.

Que. No. 14] The issued, subscribed and paid-up capital of Supreme Chemicals Ltd. is ₹ 2 Crore consisting of 20,00,000 equity shares of ₹ 10 each. The said company has 800 members. For the purpose of relief against oppression and mismanagement, a petition was submitted before the Tribunal duly signed by 90 members holding 1,00,000 equity shares of the said company. Subsequently, 30 members, who signed the petition, withdrew their consent. Decide, under the provisions of the Companies Act, 2013 whether the said petition is maintainable?

Ans.: As per Section 244, in the case of a company having a share capital, 100 members of the company or 10% of the total number of members, whichever is less can apply for the relief u/s 241.

The shareholding pattern of the Supreme Chemicals Ltd. is ₹ 2 Crore equity share capital held by 800 members.

The petition alleging oppression and mismanagement has been made by the members as follows:

- (a) Number of members making the petition: 90
- (b) Amount of share capital held by members making the petition: ₹ 10,00,000

The petition shall be valid if it has been made by the lowest of the following:

- 100 members
- 80 members (being 10% of 800)

Members holding ₹ 20,00,000 share capital (being 10% of ₹ 2,00,00,000)

As it is evident, the petition made by 90 members meets the eligibility criteria specified under Section 244; therefore, the petition is maintainable.

The consent to be given by shareholder is reckoned at the beginning of the proceedings. The withdrawal of consent by shareholder during the course of proceedings does not affect the maintainability of the petition.

Thus, such petition shall remain valid despite the fact that 30 members, who signed the petition, have withdrawn their consent subsequently.

Que. No. 14A] A petition signed by 100 members of a company has been moved to Tribunal for prevention of mismanagement. Later on, half of the members (signatories) withdrew their consent after filing the petition. Examine whether the remaining applicants (petitioners/signatories) to the petition would be successful in their complaint to Tribunal.

CS (Executive) - June 2015 (4 Marks)

Ans.: Right to apply under section 241 [Section 244]: The following members of a company shall have the right to apply u/s 241, namely:

- (a) In the case of a company having a share capital: 100 members of the company or 10% of the total number of members, whichever is less. (The applicants must have paid all calls and other sums due on their shares. Thus, holders of partly paid-up shares cannot apply)
- (b) In the case of a company not having a share capital: 20% of the total number of members

However, the Tribunal may, on an application, waive all or any of the above requirements so as to enable the members to apply u/s 241.

Once the consent has been given by the requisite number of members by signing the application, the application may be made by one or more of them on behalf and for the benefit of all of them. It has been held by the Supreme Court that if some of the consenting members have,

subsequent to the presentation of the application, withdrawn their consent, it would not affect the right of the applicant to proceed with the application. [*Rajahmundry Electric Supply Co. v. Nageshwara Rao* AIR 1956 SC 213]

Obtaining of consent is a condition precedent to the making of the application and hence a consent obtained subsequent to the application is ineffective. [*Makhan Lal Jain v. The Amrit Banaspati Co. Ltd.*, I.L.R. (1954) I All. 131]

A person who had disposed off his shares will not be allowed to apply. [*In L. Chandramurthy v. K.L. Kapsi* (2005) 48 SCL 294 CLB]

As per facts given in case, required number of applicants had applied for relief u/s 241 and even if some of the applicants/signatories withdraw their consent, the petition can be entertained by the Tribunal.

Que. No. 15] Certain Members of MDV Ltd. having share capital feel that the affairs of the company are being mismanaged by Directors. Members therefore, decide to move the Tribunal, complaining the mismanagement of company affairs by Directors of the Company. Examine the provisions of the Companies Act, 2013 and state:

- (i) Whether members are entitled to complain the Tribunal.
- (ii) Whether the following acts of the board of directors amount to mismanagement:
 - (a) Continuation of directors in their office after expiry of their tenure and infighting continues among them.
 - (b) Non-declaration of dividend when it does not lead to devaluation of shares.

Ans.: Section 241 provides that a requisite number of members of the company as laid down in Section 244 may apply to Tribunal for appropriate relief on the ground of oppression and mismanagement of the company.

Continuation of directors in their office after the expiry of their term and infighting among them has been held to be the act of mismanagement. [*Ranjan Dutta vs. Bhola Nath Paper House Ltd.* (1983)]

Non-declaration of dividend when it does not lead to devaluation of shares is not an act of mismanagement. [*V.J. Thomas Vettom vs. Kuttanad Rubber Co. Ltd.* (1984)]

Que. No. 16] Mere lack of confidence between the majority shareholder and minority shareholder would not be enough to order for relief under Section 241.

CS (Executive) – Dec 2013 (4 Marks)

State some of the circumstances which must exist before filing a petition under Section 241 of the Companies Act, 2013 for prevention of oppression.

Ans.: Some of the circumstances which must exist before filing a petition under Section 241 for prevention of oppression are as follows:

- (i) An application u/s 241 can be made only by the members. In the case of a company having share capital of minimum 100 members or 10% or members holding 10% of the paid up capital can file such petition. In case of a company not having share capital, 20% of the total number of members is required for the purpose.
- (ii) It must be established that the affairs of the company are being conducted in a manner
 - (a) oppressive to any member/members of the company or
 - (b) prejudicial to public interest.

- (iii) The oppression complained of must affect a person in his capacity as a member of the company. Rights and interests as a member of a company can only be agitated and not in relation to any commercial relation that a member has with the company as was decided in the case of *Anil Gupta vs. Mirai Auto Industries Ltd.* [(2003)113 Comp. Cas.63].
- (iv) The acts complained of must be continuing acts of oppression. The acts constituting oppression must continue till the date of making the application. Mere isolated act do not amount to oppression.
- (v) The applicant must make out a *prima facie* case that the degree of oppression is so severe that there is just and equitable ground for winding up of the company. But at the same time, it must also be established that the winding up of the company would unfairly prejudice the applicant.
- (vi) Mere lack of confidence between majority and minority shareholder would not enough unless lack of confidence springs from oppression of majority in the management of company's affairs.

Que. No. 16A] Oppression need not be continuous. Discuss.

CS (Executive) – Dec 2009 (5 Marks)

Ans.: Oppression must be a continuous process. This is suggested by the words, "are being conducted in a manner....." used in Section 241. Hence, isolated acts of oppression or mismanagement will not give rise to an action under Section 241 of the Act.

Thus, the acts complained of must be continuing acts of oppression. The acts constituting oppression must continue till the date of making the application. Mere isolated act do not amount to oppression. [*Shanti Prasad vs. Kalinga Tubes*, (1965) 35 Comp. Cas 351]

Que. No. 17] What are the consequences of termination or modification of agreements by order passed by Tribunal in cases of oppression and mismanagement?

Ans.: Consequence of termination or modification of certain agreements [Section 243]: Where an order made u/s 242 terminates, sets aside or modifies an agreement referred to in u/s 242(2):

- (a) Such order shall not give rise to any claims by any person for damages or for compensation for loss of office or in any other respect
- (b) No managing director or other director or manager whose agreement is so terminated or set aside shall be appointed for a period of 5 years from the date of the order without the leave of the Tribunal

Any person who knowingly acts as a managing director or other director or manager of a company in contravention order of Tribunal shall be punishable with imprisonment for a term which may extend to 6 months or with fine which may extend to ₹ 5,00,000 or with both.

Que. No. 18] State the provisions relating to class action as provided under the Companies Act, 2013.

Ans.: **Meaning of Class Action:** In case of large companies many investors and depositors are small and they do not have time, money and energy to fight for their rights. In such cases, some of investors and depositors can take action on behalf all those who are affected. This is known as class action.

Class Action [Section 245(1)]: Such number of member(s) or depositor(s) as are indicated in Section 245(3), if they are of the opinion that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company or its members or depositors, may file an application before the Tribunal for seeking following orders, namely:

- (a) To restrain the company from committing *ultra vires* acts and breach of any provision of the company's MOA or AOA
- (b) To declare a resolution altering the MOA or AOA as void if the resolution was passed by suppression of material facts or obtained by mis-statement
- (c) To restrain the company and its directors from acting on such resolution;
- (d) To restrain the company from doing an act which is contrary to the provisions of the Act or any other law
- (e) To restrain the company from taking action contrary to any resolution passed by the members
- (f) To claim damages or compensation or demand any other suitable action from or against -
 - The company or its directors for any fraudulent, unlawful or wrongful act or omission
 - The auditor for any improper or misleading statement of particulars made in his audit report or for any fraudulent, unlawful or wrongful act or conduct or
 - Any expert or advisor or consultant or any other person for any incorrect or misleading statement or for any fraudulent, unlawful or wrongful act or conduct
- (g) To seek any other appropriate remedy.

Joint liability of auditors [Section 245(2)]: Where the members or depositors seek any damages or compensation or demand any other suitable action against an audit firm, the liability shall be of the firm as well as of each partner who was involved in making any improper or misleading statement.

Who can apply Tribunal for class action [Section 245(3)]: The requisite number of members provided in Section 245(1) shall be as under:

- (a) **In the case of a company having a share capital:** 100 members or prescribed percentage of the total members, whichever is less. *(The applicants must have paid all calls and other sums due on their shares. Thus, holders of partly paid-up shares cannot apply)*
- (b) **In the case of a company not having a share capital:** 20% of the total number of its members.

In case of depositors class action can be taken by 100 depositors or prescribed percentage of the total number of depositors, whichever is less.

Matters to be considered by Tribunal [Section 245(4)]: In considering an application under Section 245(1), the Tribunal shall take into account following -

- (a) Whether the member or depositor is acting in good faith
- (b) Whether there is any evidence of involvement of any person other than directors or officers of the company
- (c) Whether the cause of action is one which the member or depositor could pursue in his own right rather than through an order under class action (i.e. individual action)
- (d) Views of the members or depositors who have no personal interest, direct or indirect, in the matter being proceeded under the class action
- (e) Where the act or omission could be or likely to be authorized or ratified by the company before it occurs.

Procedure to be followed by the Tribunal [Section 245(5)]: If class application is admitted by the Tribunal, then following procedure should be followed:

- (a) **Public Notice:** Public notice shall be served to all the members or depositors of the class in prescribed manner.
- (b) **Clubbing of similar applications:** All similar applications prevalent in any jurisdiction should be consolidated into a single application.
- (c) **No parallel proceedings:** Two class action applications for the same cause of action shall not be allowed.
- (d) **Cost or expenses connected with application:** The cost or expenses connected with the application for class action shall be defrayed by the company or any other person responsible for any oppressive act.

To whom order passed by Tribunal will bind [Section 245(6)]: Any order passed by the Tribunal shall be binding on the company and all its members, depositors and auditor including audit firm or expert or consultant or advisor or any other person associated with the company.

Punishment [Section 245(7)]: Any company which fails to comply with an order passed by the Tribunal shall be punishable with fine which shall not be less than ₹ 5,00,000 but which may extend to ₹ 25,00,000 and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 3 years and with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 1,00,000.

Penalty for frivolous or vexatious applications. [Section 245(8)]: Where any application filed before the Tribunal is found to be frivolous or vexatious, it shall reject the application after recording reasons in writing and make an order that the applicant shall pay to the opposite party such cost, not exceeding ₹ 1,00,000.

No class actions against banking company [Section 245(9)]: Nothing contained in Section 245 shall apply to a banking company.

Reimbursement the cost of litigation [Section 125(3)(d)]: Legal expenses incurred in pursuing the class action can be reimbursed from Investor Education & Protection Fund, if sanctioned by Tribunal.

CHAPTER 26

PRODUCER COMPANIES

This Chapter Covers:

- Concept of producer companies
- Formation and registration of producer company
- Membership and voting rights of members.
- Memorandum of Association, Articles of Association and their content.
- Conversion of inter-state co-operative society into Producer Company.
- Appointment of directors, vacation of office, liability of directors, their committee.
- Secretary of Producer Company.
- Annual general meetings.
- Share capital, transferability of shares and surrender, issue of bonus shares.

Important Note: Section 465(1) of the Companies Act, 2013 provides that the provisions of Part IX A of the Companies Act, 1956 shall be applicable *mutatis mutandis* to a Producer Company in a manner as if the Companies Act, 1956 has not been repealed until a Special Act is enacted for Producer Companies.

The Companies Act, 2013 does not make any provisions in respect of producer companies. Any new producer company cannot be incorporated under the Companies Act, 2013.

The Companies Act, 1956 continues to be applicable to them, until a special Act is enacted for the producer companies.

Hence, in this chapter all the provisions of the Companies Act, 1956 as applicable to producer companies has been discussed.

Que. No. 1] Explain the concept of producer company. CS (Inter) – June 2006 (4 Marks)

Ans.: Producer Company [Section 581A(1)]: A producer company means a body corporate, having objects or activities specified in Section 581B and registered as producer company.

Hence, the objectives for which producer companies may be formed are laid down in Section 581B.

Every producer company shall deal primarily with the produce of its active members for carrying out any of its specified objects. This means there is an obligation on the producer company to deal primarily with the active members in conducting its activities.

Que. No. 1A] Distinguish between: 'Investment Company' & 'Producer Company'

CS (Executive) – June 2014 (4 Marks)

Ans.: Investment Company: An investment company is a company, the principal business of which consists in acquiring, holding and dealing in shares and securities. The word 'investment', no doubt, suggests only the acquisition and holding of shares and securities and thereby earning income by way of interest or dividend etc. But investment companies in actual practice earn their income not only through the acquisition and holding but also by dealing in shares and securities i.e. to buy with a view to sell later on at higher prices and to sell with a view to buy later on at lower prices.

If a company is engaged in any other business to an appreciable extent, it will not be treated as an investment company.

Producer Company [Section 581A(1)]: A producer company means a body corporate, having objects or activities specified in Section 581B and registered as producer company.

Hence, the objectives for which producer companies may be formed are laid down in Section 581B.

Every producer company shall deal primarily with the produce of its active members for carrying out any of its specified objects. This means there is an obligation on the producer company to deal primarily with the active members in conducting its activities.

Que. No. 2] State the provisions relating to formation and registration of producer company.

Ans.: Formation of Producer Company & its registration [Section 581C(1)]: Specified number of person desirous of forming a producer company having its objects specified in Section 581B and complying with the requirements in respect of registration, may form an incorporated company as a producer company.

Specified person are as follows:

- ◆ Any 10 or more individuals being a producer or
- ◆ Any 2 or more producer institutions, or
- ◆ A combination of 10 or more individuals and producer institutions

Issue of certificate of registration [Section 581C(2)]: If the Registrar is satisfied that all the requirements with in respect of registration and matters precedent and incidental thereto have been complied with, he will issue within 30 days of the receipt of the documents required for registration, a certificate of incorporation.

Liability of Members [Section 581C(3)]: A producer company so formed shall have the liability of its members limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them and be termed a company limited by shares.

Reimbursement of promotion cost to the promoters [Section 581C(4)]: The producer company may reimburse to its promoters all other direct costs associated with the promotion and registration of the company including registration, legal fees, printing of a memorandum and articles and the payment thereof shall be subject to the approval at its first general meeting of the Members.

Producer Company shall be a private company [Section 581C(5)]: On registration, the Producer Company shall become a body corporate as if it is a private limited company. However,

any limit to the number of members is not applicable. Thus, the producer company is a private company without any limit as to number of members.

Que. No. 3] A group of 8 individuals together with a producer institution approached the Registrar for incorporation of a producer company under Section 581 of the Companies Act, 1956. Can the Registrar go ahead with the registration and incorporation? Discuss.

CA (Final) - Nov 2014 (4 Marks)

Ans.: As per Section 581C(1), specified number of person desirous of forming a producer company having its objects specified in Section 581B and complying with the requirements in respect of registration, may form an incorporated company as a producer company.

Specified person are as follows:

- ◆ Any 10 or more individuals being a producer or
- ◆ Any 2 or more producer institutions, or
- ◆ A combination of 10 or more individuals and Producer institutions

Thus, group of 8 individuals together with a producer institution cannot be registered as producer company.

Que. No. 4] What are the provisions relating to 'membership' and 'voting rights' of members of producer company

Ans.: Voting rights when only individuals are members [Section 581D(1)(a)]: Every member shall have a single vote irrespective of the number of shares held.

Voting rights when only producer institutions are members [Section 581D(1)(b)]: The voting rights shall be determined on the basis of their participation in the business in the previous year, as may be specified by articles. However, during the first year of registration, the voting rights shall be determined on the basis of the shareholding by producer institutions.

Voting rights when individuals and producer institutions are members [Section 581D(1)(c)]: Every member shall have a single vote.

Conditions for membership [Section 581D(2)]: The articles of any producer company may provide for the conditions, subject to which a member may continue to retain his membership, and the manner in which voting rights shall be exercised by the members.

Restriction on voting rights [Section 581D(3)]: Producer Company may, if so authorized by its articles, restrict the voting rights to active members, in any special or general meeting.

Restriction on membership [Section 581D(4)]: No person, who has any business interest which is in conflict with business of the Producer Company, shall become a Member of that Company.

Cessation of membership [Section 581D(5)]: A member, who acquires any business interest which is in conflict with the business of the producer company, shall cease to be a member of that company and be removed as a member in accordance with articles.

Que. No. 5] What are the provisions of the Companies Act, 1956 relating to "benefits to members" of the producers companies?

Ans.: **Benefits to members [Section 581E(1)]:** Every member shall initially receive only such value for the produce or products pooled and supplied as the board of producer company may determine. The withheld price may be disbursed later in cash or in kind or by allotment of equity shares, in proportion to the produce supplied to the producer company during the financial year to such extent and in such manner and subject to such conditions as may be decided by the board.

As per Section 581A(n), withheld price means part of the price due and payable for goods supplied by any member to the producer company and as withheld by the producer company for payment on a subsequent date.

Return and bonus [Section 581E(2)]: Every member shall, on the share capital contributed, receive only a limited return. However, every such member may be allotted bonus shares in accordance with the provisions contained in Section 581ZJ.

As per Section 581A(c), limited return means the maximum dividend as may be specified by the articles.

Disbursement of patronage bonus [Section 581E(3)]: The surplus if any, remaining after making provision for payment of limited return and reserves as per Section 581ZL, may be disbursed as patronage bonus amongst the members in proportion to their participation in the business of the producer company, either in cash or by way of allotment of equity shares, or both, as may be decided by the members at the general meeting.

As per Section 581A(h), patronage means the use of services offered by the producer company to its members by participation in its business activities.

As per Section 581A(i), patronage bonus means payments made by a producer company out of its surplus income to the Members in proportion to their respective patronage.

Que. No. 6] State the provisions relating to MOA & AOA of the producer company.

Ans.: **Memorandum of Producer Company [Section 581F]:** The memorandum of association of every producer company shall state: -

1. The name of the company with "Producer Company Ltd." as the last words of the name
2. The State in which the registered office is to situate
3. The main objects as specified in Section 581B
4. The names and addresses of the persons who have subscribed to the memorandum
5. The amount of share capital with which it is to be registered and division into shares of a fixed amount
6. The names, addresses and occupations of the subscribers being producers, who shall act as the first directors
7. That the liability of its members is limited
8. Opposite to the subscriber's name the number of shares each subscriber takes (*no subscriber shall take less than one share*)
9. In case the objects are not confined to one State, the States to whose territories the objects extend.

MOA and AOA to be submitted at the time of registration [Section 581G(1)]: There shall be presented, for registration to the Registrar of the State to which the registered office of the producer company is, stated by the MOA, to be situate:

- (a) MOA of the Producer Company
- (b) Its AOA duly signed by the subscribers to the memorandum.

Contents of AOA [Section 581G(2)]: The articles shall contain the mutual assistance principles as given in Section 581G(2).

Que. No. 7] A producer company wants to amend its MOA and AOA. The director of the company approaches you for advice in this regard. Advise the directors about the procedure to be followed for amending MOA and AOA of the company.

CA (Final) - Nov 2008 & Nov 2012 (6 Marks)

Ans.: Amendments in MOA [Section 581H]: A producer company can alter the conditions contained in its MOA only as per provision is made in the Companies Act, 1956.

A producer company may, by special resolution alter its objects specified in its memorandum. A copy of the amended MOA, together with a copy of the special resolution duly certified by 2 directors, shall be filed with the Registrar within 30 days from the date of adoption of any resolution.

However, in the case of transfer of the registered office from the jurisdiction of one Registrar to another, certified copies of the special resolution certified by 2 directors shall be filed with both the ROC within 30 days and thereupon the ROC from whose jurisdiction the office is transferred, shall forthwith forward to the other ROC all documents relating to the company.

The alteration of the provisions of MOA relating to the change of the place of its registered office from one State to another shall not take effect unless it is confirmed by the Tribunal on petition.

Amendment of Articles [Section 581-I]: Any amendment of the articles shall be proposed by not less than 2/3rd of the elected directors or by not less than 1/3rd of the members of the producer company, and adopted by the members by a special resolution.

A copy of the amended articles together with the copy of the special resolution, both duly certified by two directors, shall be filed with the Registrar within 30 days from the date of its adoption.

Que. No. 8] XYZ Dairy Products Producer Company Ltd. proposes to shift its registered office from Hosur in Tamil Nadu to Bangalore in Karnataka. Explain the requirements under the Companies Act, 1956 to give effect to his proposal.

CA (Final) - Nov 2006 (7 Marks)

Ans.: The registered office of XYZ Dairy Products Producers Company Ltd. from Hosur in Tamil Nadu to Bangalore in Karnataka requires amendment to the MOA.

According to Section 581H, a producer company may, by special resolution alter its objects specified in its memorandum. A copy of the amended MOA, together with a copy of the special resolution duly certified by 2 directors, shall be filed with the Registrar within 30 days from the date of adoption of any resolution.

The alteration of the provisions of MOA relating to the change of the place of its registered office from one State to another shall not take effect unless it is confirmed by the Tribunal on petition.

Thus, after complying the above provisions, XYZ Dairy Products Producer Company Ltd. can shift its registered office from Hosur in Tamil Nadu to Bangalore in Karnataka.

Que. No. 9] An existing society seeks your advice as to its eligibility to be registered as a producer company under the Companies Act, 1956 and the procedure to be followed for such registration. Advise explaining the relevant provisions of the Companies Act, 1956.

CA (Final) - Nov 2005 & May 2006 (5 Marks)

Ans.: Option to inter-state co-operative societies to become producer companies [Section 581J]:

- (1) Any inter-State co-operative society with objects not confined to one State may make an application to the Registrar for registration as producer company.

- (2) Every application shall be accompanied by -

- (a) A copy of the special resolution, of not less than 2/3rd of total members of inter-State co-operative society, for its incorporation as a producer company
- (b) A statement showing -
 - Names and addresses or the occupation of the directors and Chief Executive, if any, of such co-operative and
 - List of members of such inter-State co-operative society
- (c) A statement indicating that the inter-state co-operative society is engaged in any one or more of the objects specified in Section 581B
- (d) A declaration by 2 or more directors of the inter-state co-operative society certifying that particulars given in clauses (a) to (c) are correct.

- (3) When an inter-state co-operative society is registered as a producer company, the words "Producer Company Ltd." shall form part of its name with any word or expression to show its identity preceding it.
- (4) On compliance with the above requirements, the Registrar shall, within a period of 30 days of the receipt of application, certify that the inter-state co-operative society is incorporated as a producer company.
- (5) A co-operative society formed by producers, by federation or union of co-operative societies of producers or co-operatives of producers, registered under any law for the time being in force which has extended its objects outside the State, either directly or through a union or federation of co-operatives of which it is a constituent, as the case may be, and any federation or unions of such co-operatives, which has so extended any of its objects or activities outside the State, shall be eligible to make an application and to obtain registration as a producer company.
- (6) The inter-state co-operative society shall, upon registration, stand transformed into a producer company, and there-after shall be governed by the provisions of Companies Act, 1956 as applicable to producer company.
- (7) Upon registration as a producer company, the ROC who registers the company shall forthwith intimate the Registrar with whom the erstwhile inter-state co-operative society was earlier registered for appropriate deletion of the society from its register.

Effect of incorporation of producer company [Section 581K]: Every shareholder of the inter-State co-operative society immediately before the date of registration of producer company shall be deemed to be registered on and from that date as a shareholder of the producer company to the extent of the face value of the shares held by such shareholder.

MANAGEMENT OF PRODUCER COMPANY

Que. No. 10] What is minimum and maximum number of directors that can be appointed in producer company?

Ans.: Number of directors [Section 581-O]: Every producer company shall have at least 5 and not more than 15 directors. However, in the case of an inter-state co-operative society incorporated as a producer company, such company may have more than 15 directors for a period of 1 year from the date of its incorporation as a producer company.

Que. No. 11] State the provisions relating to appointment of directors in Producer Company.

Ans.: Appointment of directors [581P]:

- (1) The members who sign the MOA and AOA may designate the Board of directors who shall govern the affairs of the producer company until the directors are elected in accordance with the provisions of this section.
- (2) The election of directors shall be conducted within a period of 90 days of the registration of the producer company. However, in the case of an inter-state co-operative society which has been registered as a producer company the election of directors shall be conducted within a period of 365 days date of registration as producer company.
- (3) Every person shall hold office of a director for a period not less than 1 year but not exceeding 5 years as may be specified in the articles.
- (4) Every director, who retires in accordance with the articles, shall be eligible for re-appointment as a director.
- (5) The directors of the Board shall be elected or appointed by the members in the AGM.
- (6) The Board may co-opt one or more expert directors or an additional director not exceeding $1/5^{\text{th}}$ of the total number of directors. The expert directors shall not have the right to vote in the election of the Chairman but shall be eligible to be elected as Chairman, if so provided by its articles. The maximum period, for which the expert director or the additional director holds office, shall not exceed such period as may be specified in the articles.

Que. No. 12] State the provisions relating to "vacation of office by directors" for the Producer Company.

Ans.: Vacation of office by directors [Section 581Q]: The office of the director of a producer company shall become vacant if-

- (a) He is convicted by a Court of any offence involving moral turpitude and sentenced in respect thereof to imprisonment for not less than 6 months;
- (b) The producer company, in which he is a director, has made a default in repayment of any advances or loans taken from any company or institution or any other person and such default continues for 90 days;
- (c) He has made a default in repayment of any advances or loans taken from the producer company in which he is a director;
- (d) The producer company, in which he is a director -
 - (i) has not filed the annual accounts and annual return for any continuous three financial years or
 - (ii) has failed to, repay its deposit or withheld price or patronage bonus or interest thereon on due date, or pay dividend and such failure continues for 1 year or more;
- (e) Default is made in holding election for the office of director, in the producer company in which he is a director;
- (f) The AGM or EOGM of the producer company, in which he is a director, is not called in accordance with the provisions of the Act except due to natural calamity or such other reason.

The provisions shall, as far as may be, apply to the director of a producer institution which is a member of a producer company.

Que. No. 13] Under provisions of Companies Act, 1956, relating to producer company, examine whether the office of director of such company shall fall vacant in the following circumstances:

- (i) X a director of ABC Producer Company Ltd., has made a default in payment of loan taken from a company and default continues for 60 days.
- (ii) Z a director of the above company could not call the AGM for the company due to some natural calamity occurred three days before the Schedule date.

CA (Final) - Nov 2010 (4 Marks)

Ans.: Keeping in view the provisions of the Section 581Q relating to vacation of office of director of producer companies, answers to given problem is as follows:

- (i) The office of the director of a producer company shall become vacant if the producer company, in which he is a director, has made a default in repayment of any advances or loans taken from any company or institution or any other person and such default continues for 90 days.

Since Mr. X has made default in payment of loan for 60 days, his office is not vacated. However, if default continues for 90 days or more he will vacate the office of director.

- (ii) The office of the director of a producer company shall become vacant if the AGM or EOGM of the producer company, in which he is a director, is not called in accordance with the provisions of the Act except due to natural calamity or such other reason.

Mr. Z could not call the AGM for the company due to some natural calamity and hence he does not vacate the office of director.

Que. No. 14] State the powers and functions of the board of directors of a producer company as enumerated in the Companies Act, 1956.

Ans.: Powers and functions of board [Section 581R]: The Board of directors of a producer company shall exercise all such powers and to do all such acts and things, as that company is authorized so to do. Such powers may include all or any of the following matters:

- (a) determination of the dividend payable;
- (b) determination of the quantum of withheld price and recommend patronage to be approved at general meeting;
- (c) admission of new members;
- (d) pursue and formulate the organizational policy, objectives, establish specific long-term and annual objectives, and approve corporate strategies and financial plans;
- (e) appointment of a Chief Executive and other officers as may be specified in the articles;
- (f) exercise superintendence, direction and control over Chief Executive and other officers appointed by it;
- (g) cause proper books of account to be maintained; prepare annual accounts to be placed before the annual general meeting with the auditor's report and the replies on qualifications, if any, made by the auditors;
- (h) acquisition or disposal of property of the producer company in its ordinary course of business;
- (i) investment of the funds of the producer company in the ordinary course of its business;
- (j) sanction any loan or advance, in connection with the business activities of the Producer Company to any Member, not being a director or his relative;
- (k) take such other measures or do such other acts as may be required in the discharge of its functions or exercise of its powers.

All the powers specified above shall be exercised by the Board, by means of resolution passed at its meeting on behalf of the Producer Company.

Explanation: A director or a group of directors, who do not constitute the Board, shall not exercise any of the powers exercisable by it.

Que. No. 15] Which powers can be exercised by board of directors of a producer company only by means of resolutions passed at the annual general meeting of the company?

Ans.: Matters to be transacted at general meeting [Section 581S]: The board of directors of a producer company shall exercise the following powers only by means of resolutions passed at the AGM:

- Approval of budget and adoption of annual accounts
- Approval of patronage bonus
- Issue of bonus shares
- Declaration of limited return and distribution of patronage
- Specify the conditions and limits of loans to any director
- Approval of any transaction of the nature as is to be reserved in the articles for approval by the members.

Que. No. 16] Write a short note on: Liability of directors of producer company

Ans.: Liability of directors [Section 581T]: When the directors vote for a resolution, or approve by any other means, does anything in contravention of the provisions of the Act or any other law for the time being in force or articles, they shall be jointly and severally liable to make good any loss or damage suffered by the producer company.

The Producer Company shall have the right to recover from its director -

- Profit made by contravention of any provisions of the Act
- Loss or damage as a result of the contravention any provisions of the Act

The liability imposed under this section shall be *in addition to and not in derogation of* a liability imposed on a director under the Act or any other law for the time being in force.

Que. No. 17] State the power of board of directors of the producer company to constitute committees of directors? Can committee of directors co-opt any other person as member of committee?

Ans.: Committee of directors [Section 581U]: The Board may constitute such number of committees as it may deem fit for the purpose of assisting the Board in the efficient discharge of its functions. However, the Board shall not delegate any of its powers or assign the powers of the Chief Executive, to any committee.

A committee of directors may, with the approval of the Board, co-opt such number of persons as it deems fit as members of the committee.

The Chief Executive or a director of the producer company shall be a member of such committee. Every such committee shall function under the general superintendence, direction and control of the Board, for such duration, and in such manner as the Board may direct.

The fee and allowances to be paid to the members of the committee shall be such as may be determined by the Board.

The minutes of each meeting of the committee shall be placed before the Board at its next meeting.

Que. No. 18] As a Company Secretary of the Producer Company advise the board of director on following matters:

- Number of board meeting to be held in year and time gap between two meetings
- Notice of board meeting
- Quorum for board meeting
- Fees and allowances for attendance of board meeting

Ans.: Meetings of board and quorum [Section 581V]:

- A meeting of the board shall be held not less than once in every 3 months and at least 4 board meetings shall be held in every year.
- Notice of every meeting of the board of directors shall be given in writing to every director for the time being in India, and at his usual address in India to every other director.
- The Chief Executive shall give notice as aforesaid not less than 7 days prior to the date of the meeting of the board and if he fails to do so, he shall be punishable with fine which may extend to ₹ 1,000. However, a meeting of the board may be called at shorter notice and the reasons thereof shall be recorded in writing by the board.
- The quorum for a meeting of the board shall be $\frac{1}{3}^{\text{rd}}$ of the total strength of directors, subject to a minimum of 3.
- Directors including the co-opted director, may be paid fees and allowances for attendance at the meetings of the Board, as may be decided by the members in the general meeting.

Que. No. 19] State the provisions relating to appointment of Chief Executive by producer company? Also state the powers and functions that can be exercised by the Chief Executive by producer company.

Ans.: Chief Executive and his functions [581W]:

- Every producer company shall have a full time Chief Executive, by whatever name called, to be appointed by the board from amongst persons other than members.
- The Chief Executive shall be *ex-officio* director of the board and such director shall not retire by rotation.
- The qualifications, experience and the terms and conditions of service of the Chief Executive shall be such as may be determined by the board.
- The Chief Executive shall be entrusted with substantial powers of management as the board may determine.
- The Chief Executive may exercise the powers and discharge the functions, namely:
 - do administrative acts of a routine nature including managing the day-to-day affairs
 - operate bank accounts or authorize any person to operate the bank account
 - make arrangements for safe custody of cash and other assets
 - sign documents authorized by the board
 - maintain proper books of account; prepare annual accounts and audit; place the audited accounts before the board and in the AGM
 - furnish members with periodic information to appraise them of the operation and functions of the producer company
 - make appointments to posts in accordance with the powers delegated to him
 - assist the board in the formulation of goals, objectives, strategies, plans and policies

- (i) advise the board with respect to legal and regulatory matters concerning the proposed and ongoing activities and take necessary action in respect thereof
 - (j) exercise necessary powers in the ordinary course of business
 - (k) discharge other functions and exercise other powers as may be delegated by the board.
- (6) The Chief Executive shall manage the affairs of the producer company under the general superintendence, direction and control of the board and be accountable for the performance of the producer company.

Que. No. 20] Is it obligatory for every producer company to appoint whole time Company Secretary under the Companies Act, 1956?

Ans.: Secretary of producer company [Section 581X]: Every producer company having an average annual turnover exceeding ₹ 5 Crore in each of 3 consecutive financial years shall have a whole-time secretary. A person possessing membership of the ICSI can only be appointed as whole-time secretary.

GENERAL MEETINGS OF PRODUCER COMPANY

Que. No. 21] What is the quorum for the general meetings of the producer company?

Ans.: Quorum [Section 581Y]: Unless the articles require a larger number, 1/4th of the total membership shall constitute the quorum at a general meeting.

Que. No. 22] State the provisions relating to voting rights of members in general meeting of the producer company?

Ans.: Voting Rights [Section 581Z]: Every member shall have one vote and in the case of equality of votes, the Chairman or the person presiding shall have a casting vote except in the case of election of the Chairman.

Que. No. 23] State the provisions relating to Annual General Meetings of the producer company?

Ans.: Annual General Meetings [Section 581ZA]:

- (1) Every producer company shall in each year, hold, in addition to any other meetings, a general meeting, as its AGM and shall specify the meeting as such in the notices calling it, and not more than 15 months shall elapse between the date of one AGM and that of the next. However, the Registrar may, for any special reason, permit extension of the time for holding any AGM (not being the first AGM) by a period up to 3 months.
- (2) A producer company shall hold its first AGM within a period of 90 days from the date of its incorporation.
- (3) The members shall adopt the articles of the producer company and appoint directors of its Board in the AGM.
- (4) The notice calling the AGM shall be accompanied by the following documents, namely:
 - (a) The agenda of the AGM
 - (b) The minutes of the previous AGM or the EOGM
 - (c) The names of candidates for election to the office of director including a statement of qualifications of each candidate
 - (d) The audited balance-sheet and profit and loss accounts and its subsidiary, if any, together with a board report of such company with respect to -

- (i) state of affairs of the producer company
 - (ii) amount proposed to be carried to reserve
 - (iii) amount to be paid as limited return on share capital
 - (iv) amount proposed to be disbursed as patronage bonus
 - (v) material changes and commitments affecting the financial position of the producer company and its subsidiary, which have occurred in between the date of the annual accounts to which the balance sheet relates and the date of the report of the Board
 - (vi) any other matter of importance relating to energy conservation, environmental protection, expenditure or earnings in foreign exchanges
 - (vii) any other matter which is required to be, or may be, specified by the Board
- (e) Text of the draft resolution for appointment of auditors
- (f) The text of any draft resolution proposing amendment to the memorandum or articles to be considered at the general meeting, along with the recommendations of the Board.
- (5) The Board of directors on the requisition made by 1/3rd of the members shall proceed to call an EOGM.
 - (6) Every AGM shall be called during business hours, on a day that is not a public holiday and shall be held at the registered office or at some other place within the city, town or village in which the registered office is situated.
 - (7) A general meeting shall be called by giving not less than 14 days prior notice in writing.
 - (8) The notice of the general meeting indicating the date, time and place of the meeting shall be sent to every member and auditor.
 - (9) One-fourth of the total number of members shall be the quorum for its AGM.
 - (10) The proceedings of every AGM along with the Directors Report, the audited balance sheet and the profit and loss account shall be filed with the Registrar within 60 days of the date on which the AGM is held, with an annual return along with the filing fees.
 - (11) If a producer company is formed by producer institutions, such institutions shall be represented in the general body through the Chairman or the Chief Executive who shall be competent to act on its behalf.

SHARE CAPITAL & MEMBERS RIGHTS

Que. No. 24] Which type of shares can be issued or allotted by the producer companies under Companies Act, 1956?

Ans.: Share Capital [Section 581ZB]: The share capital of a producer company shall consist of equity shares only. The shares held by a member in a producer company, shall as far as may be, be in proportion to the patronage of that company.

Que. No. 25] Write a short note on: Special user rights of member of producer company

Ans.: Special user rights [Section 581ZC]: The producers, who are active members may, if so provided in the articles, have special rights and the producer company may issue appropriate instruments to them in respect of such special rights.

Such instruments issued shall, after obtaining approval of the Board in that behalf, be transferable to any other active member of that producer company.

Explanation: "Special right" means any right relating to supply of additional produce by the active member or any other right relating to his produce which may be conferred upon him by the board.

As per **Section 581A (a)**, active member means a member who fulfils the quantum and period of patronage of the producer company.

Que. No. 26] State the provisions relating to 'transfer of shares' by members of producer companies.

Ans.: Transferability of shares and attendant rights [Section 581ZD]:

- (1) The shares of a member of a producer company shall not be transferable.
- (2) A member of a producer company may, after obtaining the previous approval of the board, transfer the whole or part of his shares along with any special rights, to an active member at par value.
- (3) Every member shall, within 3 months of his becoming a member in the producer company, nominate a person to whom his shall vest in the event of his death.
- (4) On the death of the member, the nominee shall become entitled to all the rights in the shares and the board shall transfer the shares of the deceased member to his nominee. However, in a case nominee is not a producer, the board shall direct the surrender of shares together with special rights, to the producer company at par value or such other value as may be determined by the Board.
- (5) Where the board of a producer company is satisfied that -
 - (a) any member has ceased to be a primary producer or
 - (b) any member has failed to retain his qualifications to be a member as specified in articles, the Board shall direct the surrender of shares together with special rights, if any, to the producer company at par value or such other value as may be determined by the Board

The Board shall not direct such surrender of shares unless the member has been served with a written notice and given an opportunity of being heard.

FINANCE, ACCOUNTS & AUDIT

Que. No. 27] Which types of books of account are required to be kept by the Producer Company under the Companies Act, 1956?

Ans.: Books of account [Section 581ZE]: Every Producer Company shall keep at its registered office proper books of account with respect to -

- (a) All sums of money received and expended
- (b) All sales and purchase of goods
- (c) The instruments of liability executed
- (d) The assets and liabilities
- (e) In case of a producer company engaged in production, processing and manufacturing, the particulars relating to utilization of materials or labour or other items of costs.

The balance sheet and profit and loss accounts of the producer company shall be prepared in accordance with the provisions contained in Section 211 of the Companies Act, 1956.

Que. No. 28] Write a short note on: Internal Audit by Producer Company

Ans.: Internal Audit [Section 581ZF]: Every producer company shall have internal audit of its accounts carried out at specified manner at prescribed interval by a Chartered Accountant.

Que. No. 29] Write a short note on: Duties of auditor of Producer Company

Ans.: Duties of auditor [Section 581ZG]: The auditor shall report on the following additional matters relating to the producer company:

- (i) Amount of debts due along with particulars of bad debts
- (ii) Verification of cash balance and securities
- (iii) Details of assets and liabilities
- (iv) All transactions which appear to be contrary to the provisions applicable to producer companies
- (v) Loans given by the producer company to the directors
- (vi) Donations or subscriptions given
- (vii) Any other matter as may be considered necessary by the auditor.

Que. No. 30] For what purposes a producer company can make donation or subscriptions? Also state the limit on such donation or subscriptions. Can it make donation or subscriptions to political parties?

Ans.: Donations or subscription by producer company [Section 581ZH(1)]: A producer company may, by special resolution, make donation or subscription to any institution or individual for the purposes of -

- (a) Promoting the social and economic welfare of producer members or producers or general public or
- (b) Promoting the mutual assistance principles

However, the aggregate amount of donation and subscription in any financial year shall not exceed 3% of the net profit of the preceding financial year.

Prohibition of political contribution [Section 581ZH(2)]: No producer company shall make directly or indirectly to any political party or for any political purpose to any person any contribution or subscription or make available any facilities including personnel or material.

Que. No. 31] XYZ Producer Company was incorporated on 1st April, 2003. At present it has 200 members and 10 members in its board. It intends to donate ₹ 10,000 to the political party. Advice in this regard.

CA (Final) - May 2004 (4 Marks)

Ans.: According to Section 581ZH(2), no producer company shall make directly or indirectly to any political party or for any political purpose to any person any contribution or subscription or make available any facilities including personnel or material.

Hence, XYZ Producer Company cannot donate ₹ 10,000 to political party.

Que. No. 31A] A three-year old producer company wants to donate some amount. Advise the company as to how and for what purposes such donation can be made. What are the monetary restrictions in this regard? In this context you are also informed that the net profit of the producer company for the last accounting year was ₹ 12 lakh.

CS (Executive) - Dec 2016 (4 Marks)

Ans.: As per Section 581ZH(1) of the Companies Act, 1956, a producer company may, by special resolution, make donation or subscription to any institution or individual for the purposes of -

- (a) Promoting the social and economic welfare of producer members or producers or general public or
- (b) Promoting the mutual assistance principles

However, the aggregate amount of donation and subscription in any financial year shall not exceed 3% of the net profit of the preceding financial year.

As per facts given in case net profit of the company is ₹ 12,00,000. Thus, it can donate ₹ 36,000 for the purposes mentioned above.

Que. No. 32] Write a short note on: Creation of general reserve by producer company

Ans.: General and other reserves [Section 581ZI]: Every producer company shall maintain a general reserve in every financial year, in addition to any reserve maintained by it as may be specified in articles.

In a case where the producer company does not have sufficient funds in any financial year for transfer to maintain the reserves as may be specified in articles, the contribution to the reserve shall be shared amongst the members in proportion to their patronage in the business of that company in that year.

Que. No. 33] State the provisions relating to issue of bonus shares by producer companies.

Ans.: Issue of bonus shares [Section 581ZJ]: Any producer company may, upon recommendation of the Board and passing of resolution in the general meeting, issue bonus shares by capitalization of amounts from general reserves in proportion to the shares held by the members on the date of the issue of such shares.

LOANS TO MEMBERS & INVESTMENTS

Que. No. 34] Can a producer company make a loan to its members? What conditions need to be complied in this regard?

Ans.: Loan, etc., to members [Section 581ZK]: The Board may, subject to the provisions made in articles, provide financial assistance to the members of the producer company by way of -

- Credit facility, to any member, in connection with the business of the producer company, for a period not exceeding 6 months
- Loans and advances, against security specified in articles to any member, repayable within a period exceeding 3 months but not exceeding 7 years from the date of disbursement of such loan or advances.

However, any loan or advance to any director or his relative shall be granted only after the approval by the members in general meeting.

Que. No. 35] What are the modes of investment available to Producer company registered under the Companies Act, 1956?

Ans.: Investment in other companies, formation of subsidiaries, etc. [Section 581ZL]:

- The general reserves of any producer company shall be invested to secure the highest returns available from approved securities, fixed deposits, units, bonds issued by the Government or co-operative or scheduled bank or in prescribed mode.
- Any producer company may, for promotion of its objectives acquire the shares of another producer company.
- Any producer company may subscribe to the share capital in formation of its subsidiary company, joint venture or in any other manner with any body corporate, for the purpose of promoting the objects of the producer company by special resolution.
- Any producer company or together with its subsidiaries may subscribe, purchase shares in any other company, other than a producer company for an amount not exceeding 30% of the aggregate of its paid-up capital and free reserves. However, a producer company

may, by passing special resolution and with prior approval of the Central Government, invest in excess of the limits specified in this section.

- All investments by a producer company may be made if such investments are consistent with the objects of the producer company.
- The Board of a producer company may, with the previous approval of members by a special resolution, dispose of any of its investments.
- Every producer company shall maintain a register containing particulars of all the investments, showing the names of the companies in which shares have been acquired, number and value of shares; the date of acquisition and the manner and price at which any of the shares have been subsequently disposed of.
- The register of investments shall be kept at the registered office of the producer company and the same shall be open to inspection by any Member who may take extracts.

Que. No. 36] Southern India Sugar Producer Company Ltd. having paid-up capital of ₹ 5 lakh and free reserves of ₹ 3 lakh, propose to make the following loans and investments:

- Loan of ₹ 2 lakh to Mr. Ram, a member of the company, for a period of 1 year and a loan of ₹ 1 lakh to Mr. Shekhar, director of the company for a period of 6 months
- Investment of ₹ 3 lakh in the equity shares of XYZ Marketing Ltd.

State the restrictions, if any, in this regard and also the legal requirements to be complied with by the company under the provisions of the Companies Act, 1956.

CA (Final) – May 2013 (8 Marks)

Ans.: As per Section 581ZK, the Board may, subject to the provisions made in articles, provide financial assistance to the members of the producer company by way of -

- Credit facility, to any member, in connection with the business of the producer company, for a period not exceeding 6 months
- Loans and advances, against security specified in articles to any member, repayable within a period exceeding 3 months but not exceeding 7 years from the date of disbursement of such loan or advances.

However, any loan or advance to any director or his relative shall be granted only after the approval by the members in general meeting.

Thus, Southern India Sugar Producer Company Ltd. can give loan to Mr. Ram, a member of the company for the period of 1 year.

Whereas in respect of Mr. Shekhar, a director, company may give the loan only after the approval by the members in general meeting.

As per Section 581ZL, any producer company may subscribe, purchase shares in any other company, other than a producer company for an amount not exceeding 30% of the aggregate of its paid-up capital and free reserves. However, a producer company may, by passing special resolution and with prior approval of the Central Government, invest in excess of the limits specified in this section.

Thus, according to the above provision, the Southern India Sugar Producer Company Ltd. cannot invest an amount exceeding 30% of the aggregate of its paid-up capital and free reserves i.e. ₹ 2,40,000 (i.e. 30% of 8,00,000) in XYZ Marketing Ltd. However, the company may invest in excess of the limits (more than 2,40,000) by special resolution passed in its general meeting and with prior approval of the Central Government.

CHAPTER

27

OFFENCES, PENALTIES & COMPOUNDING

This Chapter Covers:

- Officers in default
- Cognizance of offence
- Compounding of Offences
- Procedure for Compounding
- Mediation & Conciliation Panel
- Company Prosecutor
- Punishments
- Adjudication of Penalties
- Power of Court to grant relief in certain cases

OFFICER WHO IS IN DEFAULT

Que. No. 1] Write a short note on: Officer who is in default

CS (Inter) – Dec. 2002 (5 Marks)

CS (Executive) – Dec. 2014 (4 Marks)

Ans.: Many provisions of the Companies Act, 2013 use the word 'officer' and 'officer in default'. Thus, it is essential to know the meaning of these words.

Officer [Section 2(59)]: Officer includes any director, manager or KMP or any person in accordance with whose directions or instructions the board of directors or any one or more of the directors is or are accustomed to act.

Officer who is in default [Section 2(60)]: Officer who is in default, for the purpose of any provision in the Act which enacts that an officer of the company who is in default shall be liable to any penalty or punishment by way of imprisonment, fine or otherwise, means any of the following officers of a company, namely:

- (i) Whole-time director
- (ii) Key managerial personnel (KMP)
- (iii) Where there is no KMP, director(s) as specified by the board and who has or have given consent in writing, or all the directors, if no director is so specified
- (iv) Any person who is charged with any responsibility including maintenance, filing or distribution of accounts or records, authorizes, actively participates in, knowingly permits, or knowingly fails to take active steps to prevent, any default
- (v) Any person in accordance with whose advice, directions or instructions the board of directors of the company is accustomed to act (*However, a person who gives advice to the board in a professional capacity will not be treated as officer in default*)
- (vi) Every director, who is aware of contravention of any provisions of the Act or where such contravention had taken place with his consent or connivance
- (vii) In respect of the issue or transfer of any shares of a company, the share transfer agents, registrars and merchant bankers to the issue or transfer.

If any person is authorized u/s 2(60)(iv), return shall be filed in Form No. GNL 3. It may be noted that even if such person is appointed and authorized, MD and KMP are still liable as officer in default.

Person can be officer in default even if he retires: It was held that director can be held liable even after he retires, in case default during his tenure. [*Anita Chudha vs. ROC (1998) 18 SCL 304 (Del.)*]

However, if a person had ceased as director or employee on the date of default/omission, no offence can be taken to have been committed by him. [*Jayesh R More vs. State of Gujarat (2000) 38 CLA 30 (Guj.)*]

Que. No. 2] Abhay Ltd. committed default by failing to file balance sheet and profit and loss account. Proceedings have been initiated against a non-executive director. However, he contended that he had resigned before the date of default. Whether the contention of the ex-director can be taken into account? Give reasons.

CS (Executive) – Dec 2010 (4 Marks)

Ans.: If a person had ceased as director or employee on the date of default/omission, no offence can be taken to have been committed by him. [*Jayesh R More vs. State of Gujarat (2000) 38 CLA 30 (Guj.)*]

As per facts given in case, a non-executive director had resigned before the date of default and hence he cannot be held liable and his contention that he had resigned before the date of default can be taken into account.

SPECIAL COURTS

Que. No. 3] State the provisions relating to establishment of Special Courts under the Companies Act, 2013.

Ans.: **Establishment of Special Courts [Section 435]:** The Central Government may, for the purpose of providing speedy trial of offences, by notification, establish or designate as many Special Courts as may be necessary.

A Special Court shall consist of –

- (a) A single judge holding office as Session Judge or Additional Session Judge, in case of offences punishable under this Act with imprisonment of 2 years or more and

- (b) A Metropolitan Magistrate or a Judicial Magistrate of the First Class, in the case of other offences, who shall be appointed by the Central Government with the concurrence of the Chief Justice of the High Court within whose jurisdiction the judge to be appointed is working."

Application of Code to proceedings before Special Court [Section 438]: The provisions of the Code of Criminal Procedure, 1973 shall apply to the proceedings before a Special Court. The Special Court shall be deemed to be Court of Session or the Court of Metropolitan Magistrate or a Judicial Magistrate of the First Class, as the case may be. The person conducting a prosecution before a Special Court shall be deemed to be a Public Prosecutor.

COGNIZANCE OF OFFENCE & COMPOUNDING OF OFFENCES

Que. No. 4] Offence under the Companies Act, 2013 are cognizable or non-cognizable? On whose complaint the Court can take the cognizance of any offence under the Act?

Ans.: Offences to be non-cognizable [Section 439(1)]: Every offence except the offences referred to in Section 212(6) (i.e. *offence relating to investigation by SFIO*) shall be deemed to be non-cognizable (bailable).

Cognizance of offence [Section 439(2)]: Court shall not take cognizance of any offence except on the complaint in writing of the Registrar, a shareholder or member of the company, or of a person authorized by the Central Government in that behalf. The Court may take cognizance of offences relating to issue and transfer of securities and non-payment of dividend, on a complaint by a person authorized by the SEBI.

Personal presence of ROC not required [Section 439(3)]: Where the complainant is the Registrar or a person authorized by the Central Government, the presence of such officer before the Court shall not be necessary unless the Court requires his personal attendance at the trial.

Que. No. 5] What is compounding of offences? Who has got such powers? State the procedure for compounding of offences.

CS (Inter) – June 2006 (8 Marks), Dec. 2007 (7 Marks)

CS (Executive) – June 2011 (4 Marks)

Ans.: What is compounding: Instead of going to Court, the offender may agree to pay composition amount and in return administrator of enactment agrees not to prosecute the person who has committed an offence. This is called as compounding. Generally offences which are of private nature and relatively not serious are made compoundable. After payment of composition amount, prosecution will not be launched or if already launched, it will be withdrawn.

Following offences are compoundable:

- ✓ Offences punishable with fine only
- ✓ Offences punishable with fine or imprisonment
- ✓ Offences punishable with fine or imprisonment or both.

Following offences are not compoundable:

- ✗ Offences punishable with imprisonment only
- ✗ Offences punishable with fine and imprisonment

Compounding of certain offences [Section 441(1)]: Any offence punishable under the Act with fine only can be compounded by the Tribunal if amount of fine exceeds ₹ 5,00,000.

If the amount of fine does not exceeds ₹ 5,00,000 compounding can be done by Regional Director or the officer authorized by the Central Government.

If the offence is punishable with imprisonment or fine or both, compounding can be done with the permission of Special Court.

The sum specified for compounding shall not exceed the maximum amount of the fine which may be imposed for the offence so compounded.

In specifying the amount payable for compounding, additional fee paid u/s 403(2) for late filing of documents shall be taken into account.

If the investigation against company has been initiated or is pending under the Act, such offence shall not be compounded.

No compounding if similar offence is committed within period of 3 years [Section 442(2)]: Once an offence is compounded, similar offence committed within period of 3 years cannot be compounded. Thus, similar offence can be compounded only once in 3 years.

Procedure for compounding [Section 442(3)]: Every application for the compounding of an offence shall be made to the Registrar who shall forward the same, together with his comments, to the Tribunal or Regional Director or officer authorized by the Central Government.

Application for compounding shall be submitted electronically in **e-Form No. 61**. This form will be forwarded by ROC to Tribunal/Regional Director as applicable.

If any offence is compounded, intimation shall be given by the company to the Registrar within 7 days from the date on which the offence is so compounded.

If offence is compounded, no prosecution shall be instituted either by the Registrar or by any shareholder or by any person authorized by the Central Government against the offender whose offence is so compounded.

If compounding is made after the institution of any prosecution, such compounding shall be brought by the ROC to the notice of the Special Court in which the prosecution is pending and on such, company or its officer shall be discharged.

Return etc. to be filed if compounding was for offence for not filing the same [Section 441(4) & (5)]:

If compounding of offence relates to not filing of any return, account or other document, then compounding authority may require the offender to file same with fee or additional fee.

Any officer or other employee of the company who fails to comply with above order shall be punishable with imprisonment for a term which may extend to 6 months, or with fine not exceeding ₹ 1,00,000 or with both. (*This offence is also compoundable*)

Que. No. 5A] Write a short note on: Lesser penalties for OPC or small companies

Ans.: Lesser penalties for OPC or small companies [Section 446B]: If OPC or a small company fails to comply with the provisions of Section 92(5), Section 117(2)(c), Section 137(3), such company and officer in default of such company shall be punishable with fine or imprisonment or fine and imprisonment, as the case may be, which shall not be more than one-half of the fine or imprisonment or fine and imprisonment, as the case may be, of the minimum or maximum fine or imprisonment or fine and imprisonment, as the case may be, specified in such sections.

MEDIATION & CONCILIATION PANEL

Que. No. 6] Write a short note on: Mediation and Conciliation Panel

Ans.: Constitution of Mediation and Conciliation Panel [Section 442(1)]: The Central Government shall maintain a panel of experts to be called as the Mediation & Conciliation Panel.

Mediation & Conciliation Panel shall consist of prescribed number of experts having prescribed qualifications.

Any proceedings may be referred to Mediation & Conciliation Panel, if such proceedings are pending before:

- Central Government or
- Tribunal or
- Appellate Tribunal

Application for mediation [Section 442(2)]: Any of the parties to the proceedings may at any time during the proceedings may apply in prescribed form along with prescribed fees to the Central Government or Tribunal or Appellate Tribunal or mediation. On receiving such application the Central Government or Tribunal or Appellate Tribunal shall appoint one or more expert form the Mediation & Conciliation Panel.

Suo motu reference [Section 442(3)]: The Central Government or Tribunal or Appellate Tribunal may, *suo motu*, refer any matter to experts from the Mediation & Conciliation Panel.

Fees and other terms and conditions [Section 442(4)]: The fee and other terms and conditions of experts of the Mediation and Conciliation Panel shall be such as may be prescribed.

Procedure to be followed by Mediation & Conciliation Panel [Section 442(5)]: The Mediation & Conciliation Panel shall follow prescribed procedure and dispose of the matter referred to it within a period of 3 months and forward its recommendations to the Central Government or Tribunal or Appellate Tribunal, as the case may be.

Right of aggrieved party to file objection [Section 442(6)]: Any party aggrieved by the recommendation of the Mediation & Conciliation Panel may file objections to the Central Government or Tribunal or Appellate Tribunal, as the case may be.

COMPANY PROSECUTOR

Que. No. 7] Write a short note on: Power of Central Government to appoint company prosecutors

Ans.: Power of Central Government to appoint company prosecutors [Section 443]: The Central Government may appoint one or more persons, as company prosecutors for the conduct of prosecutions arising out of the Act. The persons appointed as company prosecutors shall have all the powers and privileges u/s 24 of the Code of Criminal Procedure, 1973.

Appeal against acquittal [Section 444]: The Central Government may direct company prosecutor or authorize any other person, to present an appeal from an order of acquittal passed by any court, other than a High Court.

PUNISHMENTS

Que. No. 8] Write a short note on: Punishment for fraud

Ans.: Punishment for Fraud [Section 447]: Without prejudice to any liability including repayment of any debt, any person who is found to be guilty of fraud involving an amount of at least ₹ 10 lakh or 1% of the turnover of the company, whichever is lower shall be punishable -

- With imprisonment for a term which shall not be less than 6 months but which may extend to 10 years and
- With 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.

However, where the fraud in question involves public interest, the term of imprisonment shall not be less than 3 years.

Where the fraud involves an amount **less than ₹ 10 lakh or 1% of the turnover** of the company, whichever is lower, and does not involve public interest, any person guilty of such fraud shall be punishable

- With imprisonment for a term which may extend to 5 years or
- With fine which may extend to ₹ 20 lakh or
- With both.

Explanation: For the purposes of this section -

- (i) "Fraud" in relation to affairs of a company or any body corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss.
- (ii) "Wrongful gain" means the gain by unlawful means of property to which the person gaining is not legally entitled.
- (iii) "Wrongful loss" means the loss by unlawful means of property to which the person losing is legally entitled.

Que. No. 9] Write a short note on: Punishment for false statement

Ans.: Punishment for false statement [Section 448]: If in any return, report, certificate, financial statement, prospectus, statement or other document required by, or for, the purposes of any of the provisions of the Act or the rules made there under, any person makes a statement, -

- (a) which is false in any material particulars, knowing it to be false or
- (b) which omits any material fact, knowing it to be material, he shall be liable under section 447.

Que. No. 10] Write a short note on: Residual penalty under the Companies Act, 2013

Ans.: Punishment where no specific penalty or punishment is provided [Section 450]: Normally most of the Sections prescribe the penalty for contravention of that section or offence under that particular section. However, if no specific penalty is has been prescribed, general punishment is ₹ 10,000. In addition, in case of continuing default fine up to ₹ 1,000 can be levied for every day till offence continues.

Que. No. 10A] Sweet (Pvt.) Ltd. has committed a default which is in violation of the provisions of the Companies Act, 2013. No specific penalty or punishment is provided in the Act for the said default. Decide the quantum of punishment for contravention where no specific penalty or punishment is provided under the Companies Act, 2013.

CS (Executive) - June 2016 (4 Marks)

Ans.: As per Section 450, if no specific penalty has been prescribed, general punishment is ₹ 10,000. In addition, in case of continuing default fine up to ₹ 1,000 can be levied for every day till offence continues.

Thus, Sweet (Pvt.) Ltd. is liable to residual penalty as stated above.

Que. No. 11] Write a short note on: Punishment in case of repeated default

Ans.: Punishment in case of repeated default [Section 451]: If a company or an officer of a company commit the same offence for the second or subsequent occasions within a period of 3 years, then, that company and every officer thereof who is in default shall be punishable with twice the amount of fine for such offence in addition to any imprisonment provided for that offence.

WRONGFUL WITHHOLDING OF PROPERTY

Que. No. 12] What are the powers of the Court in case the property of the Company is wrongfully withheld by an officer or employee of the company?

Ans.: Punishment for wrongful withholding of property [Section 452]: If any officer or employee of a company is liable for punishment for –

- Wrongfully obtaining possession of any property, including cash of the company or
- Having in possession such property, wrongfully withholds it or knowingly applies it for the purposes other than those expressed or directed in the articles and authorized by the Act

Such officer or employee shall be punishable with fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 5,00,000.

Complaint under this section can also be made by any member or creditor or contributory of the company.

Maximum cases under this section are where the employee or officer has not vacated the accommodation after his retirement/resignation. The Court has consistently held that an employee cannot continue occupation and he is punishable u/s 452 of the 2013 Act.

Judicial Views:

- ◆ **Ex-employees are liable:** The Supreme Court has held that the term officer or employee of a company applied not only to existing officers or employees of a company but also to past officers or employees of the company. Hence, even ex-employees are liable under this section. [*Baldev Krishna Sahi vs. Shipping Corporation of India* (1987) AIR 1987 SC 2245]
- ◆ **Employee is not sub-tenant:** Employee cannot claim sub-tenancy of premises, in absence of formal resolution of board of directors. [*Automobiles Products of India Ltd. vs. Cedric Allosins Santos* (1990) 3 CLA 154 Bom]
- ◆ **Heirs & legal representatives are covered:** Section 452 applies to heirs & legal representatives of deceased officer or employee of a company. [*Gopika Chandrabhushan Sarani & Anr. vs. XLO India Ltd. & Anr.* (2009) 148 Comp. Cas. 130 (SC)]
- ◆ **Offence is continuing offence:** Offence u/s 452 is continuing offence. Thus, complaint can be lodged at any time. [*Beguram vs. Jaipur Udyog Ltd.* (1987) 61 Comp Cas 900 Guj HC DB]
- ◆ **Prosecution even if civil litigation pending:** Prosecution can be launched even if civil litigation is pending. The Criminal Court need not wait till decision of Civil Court. [*Atul Matur vs. Atul Kabra* 1989 (4) SCC 541]
- ◆ **Property covers mortgage, leasehold rights also:** It was held that, the term property used in Section 452 does not signify only ownership, but also covers mortgage, leasehold rights. Thus, company can make the complaint even if it not the owner of the property but has mortgage, leasehold rights. [*Textile Labour Association vs. Official Liquidator of Amruta Mills*, (2005) 58 SCL 452 (Guj HC)]
- ◆ **It was held that the retirement benefits of an employee cannot be withheld by a company on the employee's failure to surrender possession of the flat allotted to him.** The Court observed that pension being the incidence of service which an employee earns after a lifelong service rendered by the employee, this right cannot be frittered as the very livelihood of the employee depends upon receiving his retirement benefits. [*Dr. S.K. Ghosh Alias Dr. S.N. Gupta vs. Siemens India Ltd.*]

Que. No. 13] Mountbay Company Ltd. decided to terminate the services of Mr. Gopal who was employed as Sales Manager. The Company, however, feels that the Sales Manager may not vacate the company's flat at Delhi. What action can be taken by the company under the Companies Act, 2013 to regain possession of the flat? Is it necessary to take such action before terminating the services of Mr. Gopal? Will it make any difference, if the flat is not owned by the company, but taken on lease?

Ans.: The Company can take action u/s 452 if the sales manager refuses to vacate the premises provided by the company.

According to Section 452, if any officer or employee of a company is liable for punishment for –

- Wrongfully obtaining possession of any property, including cash of the company or
- Having in possession such property, wrongfully withholds it or knowingly applies it for the purposes other than those expressed or directed in the articles and authorized by the Act

Such officer or employee shall be punishable with fine which shall not be less than ₹ 1,00,000 but which may extend to ₹ 5,00,000.

Further the Court may also order such officer or employee to deliver to the company any such property wrongly obtained or wrongfully withheld within a time fixed by the Court.

So the company can file a complaint under Section 630 as it provides speedy relief.

Section 452 covers either existing as well as past officers or employees. Thus, action may also be initiated after termination of the services of Mr. Gopal.

It is not necessary that the property in question should be owned by the company. Even if the company exercises only a leasehold right, the provisions of Section 452 can be invoked.

Que. No. 14] What is the punishment under the Companies Act, 2013 for misusing the words "Ltd." or "Private Ltd."?

Ans.: Punishment for improper use of "Ltd." or "Private Ltd." [Section 453]: The words "Ltd." or "Private Ltd." can be used by only incorporated company under the Act. Any person misusing the these words is punishable with fine which shall not be less than ₹ 500 per day but which may extend to ₹ 2,000 per day for every day for which that name or title has been used.

ADJUDICATION OF PENALTIES

Que. No. 15] State the provisions relating to adjudication of penalties under the Companies Act, 2013.

Ans.: Adjudication of penalties [Section 454]: The Central Government may appoint officers as adjudicating officers for adjudging penalty under the Act. Registrar of Companies (ROC) has been appointed as 'adjudicating authority' by issuing notification.

The adjudicating officer may impose the penalty on the company and the officer who is in default stating any non-compliance or default under the relevant provision of the Act.

The adjudicating officer shall give a reasonable opportunity of being heard to the company and the officer who is in default.

Any person aggrieved by an order of the adjudicating may prefer an appeal to the Regional Director.

Every appeal shall be filed in prescribed form along with prescribed form fees within 60 days from the date on which the copy of the order made by the adjudicating officer is received by the aggrieved person.

The Regional Director may, after giving the parties to the appeal an opportunity of being heard, pass such order as he thinks fit, confirming, modifying or setting aside the order appealed against. If the company does not pay the penalty imposed within a period of 90 days from the date of the receipt of the copy of the order, the company shall be punishable with fine of ₹ 25,000 but which may extend to ₹ 5,00,000.

If an officer of a company who is in default does not pay the penalty within a period of 90 days, such officer shall be punishable with imprisonment which may extend to 6 months or with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 5,00,000, or with both.

Que. No. 16] Can company take any legal action against the person appointed by the Central Government for excising any act as directed by the Central Government?

Ans.: Protection of action taken in good faith [Section 456]: No suit, prosecution or other legal proceeding shall lie against the Government or any officer of the Government in respect of anything which is in good faith done or intended to be done in pursuance of the Act or of any rules or orders made there under.

POWER OF COURT TO GRANT RELIEF IN CERTAIN CASES

Que. No. 17] Explain the power of Court to grant relief where an officer of the company is liable in respect of negligence or breach of duty?

Ans.: Section 463 gives the Court the power to relieve a director of any liability which he may incur under the law. The object of the section is to provide *protection against undue hardship in deserving cases*. For getting the relief, the section provides that the Court must be satisfied that the defaulting director acted *honestly and reasonably* and that having regard to all the circumstances of the case he ought fairly to be excused.

Power of Court to grant relief in certain cases [Section 463]:

Relief where proceedings are pending: In any proceeding for negligence, default, breach of duty, misfeasance or breach of trust against an officer of a company, the Court may relieve from liability wholly or partly, if it appears to the Court hearing the case that

- He is or may be liable in respect of the negligence, default, breach of duty, misfeasance or breach of trust,
- He has acted honestly and reasonably and
- Having regard to all the circumstances of the case, including those connected with his appointment, he ought fairly to be excused.

Relief by way of preventive action: Where any officer has reason to apprehend that any proceeding will or might be brought against him in respect of any negligence, default, breach of duty, misfeasance or breach of trust, he may apply to the High Court for relief and the High Court on such application shall have the same power to relieve him as it would have had if it had been a Court before which a proceedings had been brought.

No Relief: The Court may grant relief from any civil liability only. The Court cannot grant relief from criminal liability. In criminal proceeding, the Court cannot grant relief from even civil liability.

Relief subject to condition: The Court may grant relief on such terms and condition as it may think fit. Such relief may be complete or partial.

Notice to Registrar: Court shall not grant any relief to any officer unless it serves notice in specified manner to the Registrar and such other person, if any, as it thinks necessary, to show cause why such relief should not be granted.

Judicial Views:

The Supreme Court has held that the relief u/s 463 cannot be extended in respect of any liability under any Act other than the Companies Act, 2013. [*Rabindra Chamarla vs. Registrar of Companies*, C.A. No. 3012 of 1990 decided on 19.11.1991]

Que. No. 18] Gulmohar Ltd., a registered company owns a factory at Kolkata, wherein it manufactures jute products. By notification of the State Government, issued during October, 2014 due strike and lock out it was declared as relief undertaking. After four months in February 2015 the lockout was lifted. However, during the said period the company's director defaulted in payment of provident fund and other ancillary dues. During the month of December, 2015, the Regional PF Commissioner initiated proceedings against the company and its directors under the Employees Provident Fund & Miscellaneous Provisions Act, 1952, for default and delay in payment of PF dues.

Immediately the directors of the company applied the High Court for relief under the Companies Act, 2013, praying relief from liability under the PF Law. The petition is now pending before single Judge. The company and its directors desires to know from you, as the tenability of their claim for relief at the High Court, and as to whether they would be excused and exonerated by the High Court, in respect of the Contravention committed under the PF Law.

CA (Final) - Nov. 1998 (4 Marks)

Ans.: Section 463 gives the Court the power to relieve a director of any liability which he may incur under the law. The object of the section is to provide *protection against undue hardship in deserving cases*. For getting the relief, the section provides that the Court must be satisfied that the defaulting director acted *honestly and reasonably* and that having regard to all the circumstances of the case he ought fairly to be excused.

However, the Supreme Court in *Rabindra Chamarla vs. Registrar of Companies* has held that the relief u/s 463 cannot be extended in respect of any liability under any Act other than the Companies Act, 2013. Further, relief under Section 463 is available to the officer or director and not the company.

Therefore, Gulmohar Ltd. cannot claim any relief from High Court under Section 463.

Que. No. 19] One of the directors of the company has been prosecuted for non-payment of sales tax by the company. He intends to obtain relief under the Companies Act, 2013. Will he succeed?

CA (Final) - May 2008 (3 Marks)

Ans.: Section 463 gives the Court the power to relieve a director of any liability which he may incur under the law. The object of the section is to provide *protection against undue hardship in deserving cases*. For getting the relief, the section provides that the Court must be satisfied that the defaulting director acted *honestly and reasonably* and that having regard to all the circumstances of the case he ought fairly to be excused.

However, the Supreme Court in *Rabindra Chamarla vs. Registrar of Companies* has held that the relief u/s 463 cannot be extended in respect of any liability under any Act other than the Companies Act, 2013.

In given case a director of the company has been prosecuted under Sales Tax Act. Since the relief u/s 463 is available only against Companies Act, 2013, the Court cannot grant any relief to the director.

CHAPTER 28

WINDING-UP OF COMPANIES

This Chapter Covers:

- Introduction
- Winding up and Dissolution
- Modes of winding up
- Winding up by the Court
- Voluntary winding up
- Commencement of winding up
- Winding up of unregistered companies

WINDING-UP AND DISSOLUTION & MODES OF WINDING-UP

Que. No. 1] What do you understand by winding-up of companies?

Ans.: Winding-up of a company is the last stage of putting an end to the life of a company when other revival strategies do not work. It is a proceeding by means of which a company is dissolved and in the course of such dissolution its assets are collected, its debts are paid off out of the assets of the company or from contributions by its members. If surplus is still left, it is distributed among the members in accordance with their rights.

A liquidator is appointed for administration of properties and he takes control of the company, collects its debts and finally distributes any surplus among the members in accordance with their rights. Thus, winding-up is the process by which management of a company's affairs is taken out of its directors hands, its assets are realized by a liquidator and its debts are discharged out of proceeds of realization. Any surplus of assets which remains after such discharge is returned to its members or shareholders.

The main purpose of winding up of a company is to realize the assets and pay the debts of the company expeditiously and fairly in accordance with the law.

Que. No. 2] Distinguish between: Winding-up and Insolvency

CS (Executive) - June 2010 (4 Marks)

Ans.: Following are the main points of distinction between insolvency and winding-up:

| Points | Winding-up | Insolvency |
|------------------------------|---|---|
| Meaning | Winding-up is a proceeding by means of which a company is dissolved and in the course of such dissolution its assets are collected, its debts are paid off out of the assets or from contributions by its members. If surplus is still left, it is distributed among the members. | Insolvency is inability of a debtor to pay debts as they fall due. A person is said to be insolvent when his liabilities exceeds his assets and against whom Court makes an order of adjudication. |
| Law | The law relating to winding-up is contained in Companies Act, 2013. | The law relating to insolvency in India is contained two statutes: 1. The Presidency Towns Insolvency Act, 1909 which applies to presidency towns of Mumbai, Kolkata and Chennai. 2. The Provisional Insolvency Act, 1920 which applies to the rest of India. |
| Person | A company cannot be adjudged as insolvent. | Only individual can be adjudged as insolvent. |
| When | A company can be wound-up even if is financially sound. e.g. voluntary winding-up. | A person can be adjudged insolvent only when he is unable to pay his liabilities. |
| Vesting of assets | In winding-up, the property remains vested in the company, but the administration is taken over by the liquidator. | In insolvency proceedings, the assets of a person vested in Official Assignee or Official Receiver. |
| Effect of proceedings | After completion of winding-up proceedings, the company is dissolved. | After completion of insolvency proceedings, the insolvent person is discharged from all his liabilities. |

Que. No. 3] Distinguish between: Winding-up and Dissolution

CS (Executive) - June 2010 (5 Marks), Dec 2010 (5 Marks)

CS (Executive) - Dec 2012 (5 Marks), Dec 2014 (4 Marks)

Ans.: The entire procedure for bringing about a lawful end to the life of a company is divided into two stages - 'winding-up' and 'dissolution'. Winding up is the first stage in the process whereby assets are realized, liabilities are paid off and the surplus, if any, distributed among its members. Dissolution is the final stage whereby the existence of the company is withdrawn by the law. Following are the main points of distinction between winding-up and dissolution:

| Points | Winding-up | Dissolution |
|----------------|---|---|
| Meaning | Winding-up is a proceeding by means of which a company is dissolved and in the course of such dissolution its assets are collected, its debts are paid off out of the assets or from contributions by its members. If surplus is still left, it is distributed among the members. | Dissolution brings an end to the company's legal existence. |
| Stage | Winding-up precedes the dissolution. In other words first winding-up of state of affairs occurs and after winding-up and all other proceeding company is dissolved. | Dissolution is the final stage which leads to corporate death of the company. |
| Effect | In winding-up, the assets are realized and liabilities are paid but, the corporate status of the company continues. | After dissolution the corporate status of the company does not continue. |

| Points | Winding-up | Dissolution |
|-----------------------|--|--|
| Liquidator | The liquidator can present the company in winding-up proceedings. | Once the order of dissolution is made, the liquidator cannot represent the company |
| Proceedings | Any person can proceed against the company which is being wound-up. | No proceedings can be started against the company which has been dissolved. |
| Order of Court | Winding-up proceedings can be started without the intervention of Court. | Order of Court is essential for the dissolution of the company. |

Que. No. 4] Write a short note on: Modes of winding-up

CS (Executive) - June 2009 (4 Marks)

Ans.: Under the Companies Act, 2013, the company may be wound up by any of the following modes:

1. By the NCLT i.e. compulsory winding-up
2. Voluntary winding-up
3. Winding-up by the Central Government under summary procedure.

WINDING UP BY THE NCLT

Que. No. 5] Explain the cases in which a company is compulsory wound-up by the Court. Write a short note: Winding-up on the ground of inability to pay debt.

CS (Final) - Dec 1994 (5 Marks)

Ans.: Circumstances in which company may be wound up by the Court [Section 271(1)]: A company may, on a petition, be wound up by the Tribunal, —

- (a) If the company is unable to pay its debts.
- (b) If the company has, by special resolution, resolved that the company be wound up by the Tribunal.
- (c) If the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality.
- (d) If the Tribunal has ordered the winding up of the company.
- (e) If on an application made by the Registrar or any other person authorized by the Central Government by notification under this Act, the Tribunal is of the opinion that the affairs of the company have been conducted in a fraudulent manner or the company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company be wound up.
- (f) If the company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years.
- (g) If the Tribunal is of the opinion that it is just and equitable that the company should be wound up.

Judicial Views:

- ◆ Where a company having many business, discontinue one of them, it cannot be said to have suspended its business. For invoking Section 271(1) it must be shown that the entire business of the company has been suspended. [*Paramjit Lal Badwar vs. Prem Spg. & Wvg. Mills Ltd. (1986) 60 Comp Cas 420*]
- ◆ If the delay for non-commencement of business is sufficiently explained and it is shown that the company intends to carry on business, an order for winding-up will not be made. [*Malbar Iron & Steel Works Ltd. vs. ROC (1963) 33 Comp Cas 886 (Ker.)*]
- ◆ Where in spite of repeated demands by a creditor, the company neglects to pay the debt, is *prima facie* evidence of its inability to pay debts. [*Re, Gold Hill Mines (1883) 23 Ch. D 210*]
- ◆ Where a debt is *bona fide* disputed by the company and Tribunal is satisfied with the company's defence, there is no 'neglect to pay' and therefore winding-up order cannot be made. [*Piura Singh vs. S.H.R. Properties Ltd. (1993) 10 CLA 83*]

Que. No. 6] State the reasons where Tribunal have ordered winding-up under Section 271(1) i.e. the 'just & equitable clause'

Ans.: Some reasons where Tribunal have ordered winding-up under Section 271(1) i.e. the 'just & equitable clause' are as follows:

- ◆ When substratum of the company has disappeared, i.e. original object become impossible to attain.
- ◆ It is impossible to carry on business except at a loss and there is no reasonable hope of making profits.
- ◆ If the object for which it is formed is illegal or becomes illegal by change in law.
- ◆ Deadlock in management due to serious difference among rival groups and disagreement cannot be resolved in general meeting or board meetings.
- ◆ If the company is 'bubble' i.e. it does not have any real business.
- ◆ Oppression of members which cannot be resolved by any other means.
- ◆ It is in public interest that company be wound-up.

Que. No. 7] When company is deemed to be unable to pay its debts under Section 271(2) of the Companies Act, 2013?

Ans.: Unable to pay its debts [Section 271(2)]: A company shall be deemed to be unable to pay its debts —

- (a) if a creditor, by assignment or otherwise, for an amount exceeding ₹ 1 lakh, has served demand at its registered office, by registered post or otherwise, requiring the company to pay the amount and the company has failed to pay the sum within 21 days after the receipt of demand or to provide adequate security or re-structure or compound the debt to the reasonable satisfaction of the creditor;
- (b) if any execution or other process issued on a decree or order of any Court or Tribunal in favour of a creditor of the company is returned unsatisfied in whole or in part; or
- (c) if it is proved to the satisfaction of the Tribunal that the company is unable to pay its debts.

In determining whether a company is unable to pay its debts, the Tribunal shall take into account the *contingent* and *prospective liabilities* of the company.

Que. No. 8] State with reasons, whether the following are debts for the purpose of Section 433(e) of the Companies Act, 1956:

- (i) Contingent or conditional liability
- (ii) Non-payment of dividend declared
- (iii) Non-payment of salary of an employee
- (iv) Non-payment to creditor of a disputed liability CS (Final) - June 2001 (4 Marks)

Ans.: Under Section 271(1)(a), a company can be wound up by the Tribunal if it is unable to pay its debts. Section 271(2) prescribes the circumstances in which the company shall be deemed to be unable to pay its debts.

- (i) **Contingent or conditional liability:** A debt must be a definite sum of money payable immediately or at a future date. A contingent or conditional liability is not debt, unless the contingency or condition has already happened. Since, contingent or conditional liability is not debt, winding-up petition on the ground that company is unable to pay debt cannot be entertained by the Tribunal.
- (ii) **Non-payment of dividend declared:** A dividend when declared becomes a debt. Thus, if company fails to pay declared dividend and the amount of dividend exceeds ₹ 1,00,000 winding-up petition on the ground that company is unable to pay debt can be entertained by the Tribunal.
- (iii) **Non-payment of salary of an employee:** Non-payment of salary of an employee is debt for the purpose of Section 271(1). The word debt includes the sum which is to be recovered from a person who is obliged to make the payment and accordingly unpaid salary is a debt. Thus, winding-up petition on the ground that company is unable to pay debt can be entertained by the Tribunal.
- (iv) **Non-payment to creditor of a disputed liability:** Where a debt is *bona fide* disputed by the company and Tribunal is satisfied with the company's defence, there is no 'neglect to pay' and therefore winding-up order cannot be made.

Que. No. 9] The ROC, Mumbai filed a petition in Tribunal for compulsory winding-up of Constant Overtrading Ltd. on the ground that a perusal of the Balance Sheet of the company revealed that its liabilities far exceeded the assets and consequently the company is unable to pay its debts. Examine with reference to the provisions of the Companies Act, 2013, the various factors the Tribunal will take into account before the company is ordered to be wound up compulsorily and whether there is any justification in the present case for the Tribunal to order winding up of the company.

CA (Final) - May 2011 (5 Marks)

Ans.: In the case law *ROC Punjab vs. Ajanta Lucky Scheme & Investment Co. Private Ltd.*, the ROC filed a petition for the winding up of the respondent company on the ground that the company was unable to pay its debts and that its liabilities exceeded its assets. In the said case it was held by the Tribunal that for determining the company's ability or otherwise to pay its debts, it was to be considered whether the company was able to meet its liability as and when they accrued due.

The mere fact that the company's liabilities being in excess of its assets could not *ipso facto* be a ground for putting the company into liquidation. The test would be that the company should be commercially solvent *i.e.*, the company ought to be in a position to meet its liabilities as and when they arose.

Thus, in the present case, the Tribunal may not order the winding-up of the company, merely because its liabilities far exceeded the assets of the company.

Que. No. 10] ZYZ Ltd. owes a sum of ₹ 5,00,000 to Mr. S, who assigns this debt to his two creditors viz.

Mr. R: to extent of ₹ 4,60,000 and

Mr. M: to the extent of ₹ 40,000.

Mr. M makes a demand for his money from the company by giving legal notice. The company could not meet his demand or otherwise satisfy him till the expiry of 4 weeks from the date of notice. Mr. M therefore moves to the Tribunal a petition for winding-up of the company. Referring to the provisions of the Companies Act, 2013 decide whether Mr. M's petition can be accepted by the Tribunal and can company be wound up.

CA (Final) - Nov 1997 (5 Marks)

Ans.: Under Section 271(1)(a), a company can be wound up by the Tribunal if it is unable to pay its debts. Section 271(2) prescribes the circumstances in which the company shall be deemed to be unable to pay its debts.

A company shall be deemed to be unable to pay its debts if a creditor for more than ₹ 1,00,000 has served a notice demanding his debt at the registered office and the company fails to pay or secure or compound the sum to the satisfaction of the creditor within 21 days.

In given case the company is indebted to the Mr. M only to the extent of ₹ 40,000 less than ₹ 1,00,000. Since, the requirement of Section 271(2) could not be satisfied, the non-payment by the company cannot be said to be the inability of the company to pay debts. Thus, Mr. M's petition for winding-up of the company cannot be accepted by the Tribunal.

Que. No. 11] Write a short note on: Jurisdiction of Court for entertaining winding-up petition

Ans.: In *GTC Industries Ltd. vs. Parasrampur Trading (1999) 34 CLA 380 (All HC)*, it was held that only Tribunal has jurisdiction in winding up, even if there was agreement between parties that dispute between parties will be resolved before Court where registered office is situated. Regardless of where agreement is executed, Tribunal have the jurisdiction to entertain a petition for winding up.

Que. No. 12] Who can present the petition for winding-up?

CS (Executive) - Dec 2011 (6 Marks)

Ans.: **Petition for winding-up [Section 272(1)]:** An application for the winding up of a company can be presented by following:

- ◆ Company itself
- ◆ Any creditor or creditors, including any contingent or prospective creditor or creditors
- ◆ Any contributory or contributories
- ◆ Any combination of company, creditors or contributories
- ◆ Registrar of companies
- ◆ Any person authorized by the Central Government
- ◆ Central Government or State Government.

Que. No. 13] A company passed a special resolution for winding-up of the company to the Tribunal and made the necessary petition to the Tribunal. In spite of the opposition of the workers, the company was ordered to be wound-up. The workers filed an appeal against the winding-up order. It is contended by the company that workers have no right to appeal as they have neither any right to present a petition for the winding-up, nor to be heard in winding-up proceedings. Is the contention of the company correct? Cite case law.

CS (Final) - June 1996 (8 Marks)

Ans.: The right to file petition for winding-up of the company is given by Section 272. The said section does not authorize the workers to file winding-up petition. [*National Textile Workers vs. P. R. Ramakrishnan* (1983) Comp Cas 184]

However, there is nothing in Companies Act, 2013 which expressly prohibits workers from being heard in a winding-up petition. Accordingly the workers will be entitled to be heard as interveners and not as parties. Also, after winding-up order is made, the workers may appeal against it. But, once the order becomes final, the workers shall not participate in any further proceeding. [*National Textile Workers vs. P. R. Ramakrishnan* (1983) Comp Cas 184]

The Tribunal shall take into account not only the interest of the shareholders and creditors but also public interest and the interest of workers and employees of the company.

Thus, contention of the company that workers have no right to appeal nor to be heard in winding-up proceedings is not correct.

VOLUNTARY WINDING-UP

Que. No. 14] Under what circumstances a company may be wound up voluntarily? When does such a winding-up commence? What is the effect of voluntary winding-up upon the status of the company?

Ans.: The companies are usually wound up voluntarily as it is an easier process of winding-up than compulsory winding-up by the Tribunal. In voluntary winding up the company and its creditors are left to settle their affairs without going to Tribunal, although they may apply to the Tribunal for directions or orders, as and when necessary.

Circumstances in which company may be wound up voluntarily [Section 304]: A company may be wound up voluntarily if the company in general meeting passes a resolution requiring the company to be wound up voluntarily:

- as a result of the expiry of the period for its duration fixed by its articles or
- on the occurrence of any event in respect of which the articles provide that the company should be dissolved or
- the company passes a special resolution that the company be wound up voluntarily.

Declaration of Solvency [Section 305]: Discussed in next question.

Meeting of Creditors [Section 306]: The company shall along with the calling of meeting of the company at which the resolution for the voluntary winding up is to be proposed, cause a meetings of its creditors either on same day or on the next day. The company shall cause a notice of the meeting to be sent by registered post to the creditors with the notice of the meeting of the company.

The Board of Directors of the company shall –

- (a) cause to be presented a full statement of the position of the affairs of the company together with a list of creditors, copy of declaration u/s 305 and the estimated amount of the claims before such meeting; and
- (b) appoint one of the directors to preside at the meeting.

Where two-thirds in value of creditors of the company are of the opinion that –

- (a) it is in the interest of all parties that the company be wound up voluntarily, the company shall be wound up voluntarily; or
- (b) the company may not be able to pay for its debts in full from the proceeds of assets sold in voluntary winding up and pass a resolution that it shall be in the interest of all parties if the company is wound up by the Tribunal, the company shall within fourteen days thereafter file an application before the Tribunal.

The notice of any resolution passed at the meeting of creditors shall be given by the company to the Registrar within **10 days** of the passing thereof.

Publication of resolution to wind-up voluntarily [Section 307]: Where a company has passed a resolution for voluntary winding up and a resolution by creditors is passed, it shall within 14 days of the passing of the resolution give notice of the resolution by advertisement in the Official Gazette and also in a newspaper which is in circulation in the district where the registered office or the principal office of the company is situate.

Commencement of voluntary winding up [section 308]: A voluntary winding up shall be deemed to commence on the date of passing of the resolution for voluntary winding up.

Effect of voluntary winding up [section 309]: In the case of a voluntary winding up, the company shall from the commencement of the winding up cease to carry on its business except as far as required for the beneficial winding up of its business. The corporate state and corporate powers of the company shall continue until it is dissolved.

Que. No. 15] Explain the provisions of the Companies Act, 2013 in regard to preparation and filing of 'declaration of solvency' in case of member's voluntary winding-up.

Ans.: **Declaration of Solvency [Section 305(1)]:** In case of a proposed voluntary winding up, majority of directors (not less than two), shall make a declaration at a Board meeting verified by an affidavit that they have made full inquiry into the affairs of the company and they have formed an opinion that the company has no debt or whether it will be able to pay its debts in full from the proceeds of assets sold in voluntary winding up.

Conditions for Declaration of Solvency [Section 305(2)]: This declaration shall have effect only if:

- (a) it is made within **5 weeks** immediately preceding the date of the passing of the resolution for winding up the company and it is delivered to the Registrar for registration before that date;
- (b) it contains a declaration that the company is not being wound up to defraud any person or persons;
- (c) it is accompanied by a copy of the report of the auditors of the company on the profit and loss account of the company for the period commencing from the date up to which the last such account was prepared and ending with the latest practicable date immediately before the making of the declaration and the balance sheet of the company made out as on that date which would also contain a statement of the assets and liabilities of the company on that date; and
- (d) where there are any assets of the company, it is accompanied by a report of the valuation of the assets of the company prepared by a registered valuer.

Unreasonable Declaration [Section 305(3)]: Where the company is wound up in pursuance of a resolution passed within a period of 5 weeks after the making of the declaration, but its debts are not paid or provided for in full, it shall be presumed, until the contrary is shown, that the director or directors did not have reasonable grounds for their opinion while making declaration of solvency.

Punishment for wrong declaration [Section 305(4)]: Any director of a company making a declaration without having reasonable grounds for the opinion that the company will be able to pay its debts in full from the proceeds of assets sold in voluntary winding up shall be punishable

- with imprisonment for a term which shall not be less than 3 years but which may extend to 5 years or
- with fine which shall not be less than ₹ 50,000 but which may extend to ₹ 3,00,000 or
- with both.

Judicial View:

It was held that where the declaration of solvency is not made in accordance with the law, the resolution for winding up and all subsequent proceedings will be null and void. [*Shri Raja Mohan Manucha vs. Lakshminath Sainal* (1963) 33 Comp. Cas. 719].

Que. No. 16] Write a short note on: Creditors voluntary winding-up

Ans.: Where a company is solvent, the declaration of solvency is not made by the directors and therefore the voluntary winding-up is called as creditors winding-up. In creditors voluntary winding-up, the dominant control over the winding-up proceedings remain in control of creditors of the company. *There is no provision relating to 'creditors voluntary winding-up' under the Companies Act, 2013. Hence, question is not relevant for June 2017 and onward examinations.*

Que. No. 17] Distinction between: Member's voluntary winding-up and Creditor's voluntary winding-up
CS (Executive) - Dec 2013 (4 Marks)

Ans.: *There is no provision relating to 'creditors voluntary winding-up' under the Companies Act, 2013. Hence, question is not relevant for June 2017 and onward examinations.*

COMMENCEMENT OF WINDING UP

Que. No. 19] Write a short note on: Commencement of winding-up

Ans.: Section 441 provides for the provisions relevant to commencement of winding up.

The winding-up of a company by the Court is deemed to commence at the time of the presentation of the petition for winding up. But where, before the presentation of the petition a resolution has been passed by the company, for voluntary winding up, the winding up shall be deemed to have commenced at the time of the passing of the resolution.

Where an order is made by the Court on more than one petition the commencement of the winding up dates from the earliest petition. [*Kent vs. Freehold Land Co.* (1868) 3 Ch. App. 493]

It may be noted here that voluntary winding up shall be deemed to commence at the time when resolution for voluntary winding up is passed [Section 486].

It was held that the words "shall be deemed to have commenced" clearly show the intention of legislature that although the winding-up of a company does not in fact commence at the time of presentation itself, but it shall be presumed to commence from that stage. [*Rishabh Agro Industries Ltd. vs. PNB Capital Services Ltd.* (2000) AIR SCW 1753]

CHAPTER 29

STRIKING OFF NAME OF COMPANIES

This Chapter Covers:

- > Meaning of "striking off"
- > Procedure for striking off a company.
- > Striking-off by Registrar of his own motion
- > Striking-off on company's application
- > Ministry of Corporate Affairs (MCA) Circulars
- > Rights of person aggrieved by company having been struck off the register
- > Restoration of names strike off
- > Effect of restoration order.
- > Mode of sending letter/notice
- > Who can apply for restoration of name?

Que. No. 1] What is meant by striking the name of company under Section 248 of the Companies Act, 2013? CS (Executive) - June 2011 (2 Marks), June 2012 (4 Marks)

CS (Executive) - June 2013 (2 Marks)

Ans.: "Striking-off" implies removal. Where the Registrar has reasonable cause to believe that a company is not carrying on business or in operation, the Registrar can, on his own, exercise the power conferred upon him by Section 248 and remove the company from his Register of Companies. Despite the striking-off, the liability, if any, of every director, manager or other officer who was exercising any power of management, and of every member of the company, shall continue and may be enforced as if the company had not been dissolved.

Que. No. 2] Write a short note on: Provisions and procedure for striking off the name of the company. CS (Executive) - Dec 2010 (4 Marks)

Ans.: Power of Registrar to remove name of company from register of companies [Section 248(1)]: Where the Registrar has reasonable cause to believe that –

- (a) A company has failed to commence its business within one year of its incorporation;
- (b) The subscribers to MOA have not paid the subscription within a period of 180 days from the date of incorporation and a declaration to this effect has not been filed within 180 days of its incorporation; or
- (c) A company is not carrying on any business or operation for a period of 2 immediately preceding financial years and has not made any application within such period for obtaining the status of a dormant company,

he shall send a notice to the company and all the directors of the company, of his intention to remove the name of the company from the register of companies and requesting them to send their representations along with copies of the relevant documents, within a period of 30 days from the date of the notice.

Removal of name on application of company [Section 248(2)]: A company may, after extinguishing all its liabilities, by a special resolution or consent of 75% members in terms of paid-up share capital, file an application in the prescribed manner to the ROC for removing the name of the company from the register of companies on all or any of the grounds above. The Registrar shall, on receipt of such application, cause a public notice to be issued in the prescribed manner.

However, in the case of a company regulated under a special Act, approval of the regulatory body constituted or established under that Act shall also be obtained and enclosed with the application.

Provisions of this section shall not apply to section 8 companies.

A notice shall be published in the prescribed manner and also in the Official Gazette for the information of the general public.

At the expiry of the time mentioned in the notice, the ROC may strike off its name from the register of companies, and shall publish notice thereof in the Official Gazette. On the publication in the Official Gazette of this notice, the company shall stand dissolved.

Before passing an order, the ROC shall satisfy himself that sufficient provision has been made for the realization of all amount due to the company and for the payment or discharge of its liabilities and obligations by the company within a reasonable time and, if necessary, obtain necessary undertakings from the managing director, director or other persons in charge of the management of the company.

The assets of the company shall be made available for the payment or discharge of all its liabilities and obligations even after the date of the order removing the name of the company from the register of companies.

The liability, if any, of every director, manager or other officer who was exercising any power of management, and of every member of the company dissolved, shall continue and may be enforced as if the company had not been dissolved.

Nothing in this section shall affect the power of the Tribunal to wind up a company the name of which has been struck off from the register of companies.

Que. No. 3] State the provisions relating to restrictions on making application for removal of name of company.

Ans.: Restrictions on making application u/s 248 in certain situations [Section 249]: An application u/s 248 on behalf of a company shall not be made if, at any time in the previous 3 months, the company—

- (a) has changed its name or shifted its registered office from one State to another;
- (b) has made a disposal for value of property or rights held by it, immediately before cesser of trade or otherwise carrying on of business, for the purpose of disposal for gain in the normal course of trading or otherwise carrying on of business;
- (c) has engaged in any other activity except the one which is necessary or expedient for the purpose of making an application under that section, or deciding whether to do so or concluding the affairs of the company, or complying with any statutory requirement;
- (d) has made an application to the Tribunal for the sanctioning of a compromise or arrangement and the matter has not been finally concluded; or
- (e) is being wound up whether voluntarily or by the Tribunal.

An application filed shall be withdrawn by the company or rejected by the Registrar as soon as conditions are brought to his notice.

Que. No. 4] What is the effect when company is notified as dissolved u/s 248 of the Companies Act, 2013?

Ans.: Effect of company notified as dissolved [Section 250]: Where a company stands dissolved u/s 248, it shall on and from the date mentioned in the notice cease to operate as a company and the Certificate of Incorporation issued to it shall be deemed to have been cancelled from such date except for the purpose of realizing the amount due to the company and for the payment or discharge of the liabilities or obligations of the company.

Que. No. 5] What are the consequences of making fraudulent application for removal of name?

Ans.: Fraudulent application for removal of name [Section 251]: Where it is found that an application by a company u/s 248 has been made with the object of evading the liabilities of the company or with the intention to deceive the creditors or to defraud any other persons, the persons in charge of the management of the company shall—

- (a) be jointly and severally liable to any person or persons who had incurred loss or damage as a result of the company being notified as dissolved; and
- (b) be punishable for fraud in the manner as provided in Section 447.

The Registrar may also recommend prosecution of the persons responsible for the filing of an application u/s 248.

Que. No. 6] Write a detailed note on: Fast Track Exit (FTE) mode by MCA – striking-off the name of the companies

Ans.: Fast Track Exit (FTE) mode is introduced by Ministry of Corporate Affairs for giving opportunity to non-operating companies for getting their names struck off from the records of Ministry of Corporate Affairs. FTE mode is an easy mode of closing non-operating companies at cheaper cost with lesser formalities.

Provisions relating to FTE are contained in the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016.

Removal of name of company on suo motu basis [Rule 3]: The Registrar of Companies may remove the name of a company from the register of companies Section 248(1).

However, name of following types of companies shall not be removed:

- (1) Listed companies.
- (2) Companies that have been delisted due to non-compliance of listing regulations or listing agreement or any other statutory laws.
- (3) Vanishing companies.
- (4) Companies where inspection or investigation is ordered and being carried out or actions on such order are yet to be taken up or were completed but prosecutions arising out of such inspection or investigation are pending in the Court.
- (5) Companies where notices u/s 234 of the Companies Act, 1956 or Section 206 or Section 207 have been issued by the RoC or Inspector and reply thereto is pending or report u/s 208 has not yet been submitted or follow up of instructions on report u/s 208 is pending or where any prosecution arising out of such inquiry or scrutiny, is pending with the Court.
- (6) Companies against which any prosecution for an offence is pending in any Court.
- (7) Companies whose application for compounding is pending before the competent authority for compounding the offences committed by the company or any of its officers in default.
- (8) Companies, which have accepted public deposits which are either outstanding or the company is in default in repayment of the same.
- (9) Companies having charges which are pending for satisfaction and
- (10) Section 8 companies (*i.e. non-profit making companies*).

Vanishing Company: Vanishing company means a registered company and listed with Stock Exchange which has failed to file its returns with the ROC and Stock Exchange for a consecutive period of 2 years and is not maintaining its registered office at the address notified with the ROC or Stock Exchange and none of its directors are traceable.

Notice by ROC: The ROC shall give a notice in writing in **Form STK-1** which shall be sent to all the directors of the company at the addresses available on record, by registered post with acknowledgement due or by speed post.

The notice shall contain the reasons on which the name of the company is to be removed from the register of companies and shall seek representations against the proposed action from the company and its Directors along with the copies of relevant documents within a period of 30 days from the date of the notice.

Application for removal of name of company [Rule 4]: An application for removal of name of the company shall be made in **Form STK-2** along with the fee of ₹ 5,000.

Every application shall accompany no objection certificate from appropriate Regulatory Authority in respect of following companies:

- (a) Companies which have conducted or conducting non-banking financial and investment activities as referred to in the RBI Act, 1934 or rules and regulations thereunder.
- (b) Housing finance companies as referred to in the Housing Finance Companies (National Housing Bank) Directions, 2010.
- (c) Insurance companies as referred to in the Insurance Act, 1938.
- (d) Companies in the business of capital market intermediaries as per SEBI Act, 1992 or rules and regulations thereunder.
- (e) Companies engaged in Collective Investment Schemes (CIS) as per SEBI Act, 1992 or rules and regulations thereunder.

(f) Asset Management Companies (AMC) as per SEBI Act, 1992 or rules and regulations thereunder.

(g) Any other company which is regulated under any other law for the time being in force.

Documents to be attached to Form STK-2: The application in Form STK-2 shall be accompanied by -

- (1) Indemnity bond duly notarized by every director in **Form STK-3**.
- (2) A statement of accounts containing assets and liabilities of the company made up to a day, not more than 30 days before the date of application and certified by a CA.
- (3) An affidavit in **Form STK-4** by every director of the company.
- (4) A copy of the special resolution duly certified by each of the directors of the company or consent of 75% of the members of the company in terms of paid up share capital as on the date of application.
- (5) A statement regarding pending litigations, if any, involving the company.

Manner of filing of application [Rule 5]: The application in Form STK-2 shall be signed by a director duly authorized by the Board in their behalf. Where the director concerned does not have a registered digital signature certificate, a physical copy of the form duly filled in shall be signed manually by the director duly authorized in that behalf and shall be attached with the Form STK-2 while uploading the form.

Form to be certified [Rule 6]: The Form STK-2 shall be certified by CS or CA in whole time practice may be.

Manner of publication of notice [Rule 7]: The notice u/s 248 shall be in **Form STK-5** or **Form STK-6** be-

- (a) placed on the official website of the MCA on a separate link established on such website in this regard
- (b) published in the Official Gazette
- (c) published in English language in a leading English newspaper and at least once in vernacular language in a leading vernacular language newspaper, both having wide circulation in the State in which the registered office of the company is situated.

Notice under Rule 7(c) should be in Form No. STK-SA.

In case of any application made under Section 248(2), the company shall also place the application on its website, if any, till the disposal of the application.

The Registrar of Companies shall, simultaneously intimate the concerned regulatory authorities regulating the company, *viz.* the Income-tax authorities, central excise authorities and service-tax authorities having jurisdiction over the company, about the proposed action of removal or striking off the names of such companies and seek objections, if any, to be furnished within a period of thirty days from the date of issue of the letter of intimation and if no objections are received within 30 days from the respective authority, it shall be presumed that they have no objections to the proposed action of striking off or removal of name.

Manner of notarization, apostilisation or consularisation of indemnity bond and declaration in case of foreign nationals or non-resident Indians [Rule 8]: If the person is a foreign national or non-resident Indian, the indemnity bond, and declaration shall be notarised or apostilised or consularised.

Notice of striking off and dissolution of company [Rule 9]: The ROC shall cause a notice u/s 248(5) of striking off the name of the company from the register of companies and its dissolution to be published in the Official Gazette in **Form STK-7** and the same shall also be placed on the official website of the Ministry of Corporate Affairs.