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STUDY MATERIAL

EXECUTIVE PROGRAMME

# COMPANY LAW

MODULE 1

PAPER 2



**THE INSTITUTE OF  
Company Secretaries of India**

**भारतीय कम्पनी सचिव संस्थान**

**IN PURSUIT OF PROFESSIONAL EXCELLENCE**

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Laser Typesetting by Delhi Computer Services, Dwarka, New Delhi  
Printed at M. P. Printers/May 2018

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## EXECUTIVE PROGRAMME COMPANY LAW

In view of increasing emphasis on adherence to norms of good corporate governance, Company Law assumes an added importance in the corporate legislative milieu, as it deals with structure, management, administration and conduct of affairs of Companies. Paper on Company Law is divided into three parts:- Part I deals with Company Law, Principles & Concepts, Part II deals with Company Administration and Meetings – Law and Practices and Part III deals with Company Secretary as a Profession.

Part I emphasises on principles and legal fundamentals with respect to the raising of capital through various sources, allotment of securities, maintaining of records, disclosure and transparency, members and their shareholding, concerns of stakeholders. This also guides on the secretarial and strategic work involved in above stated matters.

Part II relates to the fundamental role that a board of directors play in supporting, guiding the management team in generating long term added value for the shareholders and society at large and to account to the shareholders for companies long term performance. Right decision making is important for company's growth, board meetings leads to greater strategic decision making whereas the shareholder meetings leads to greater transparency and accountability. Company secretary plays a vital role in preparation, convene and conduct of the meetings.

A key expectation of members of self-governing professions is that they accept legal and ethical responsibility for their work and hold the interest of the public and society as paramount. One of the essential traits of a profession is to be subject to strict codes of conduct enshrining rigorous ethical and moral obligations. In a self regulated regime, Company Secretary subjected to a strict code of conduct is looked upon by the regulators, as ethical and trustworthy professional whose professional judgment and competence has made a mark in the corporate sector. It is a moral duty of all of us as Company Secretaries to strictly abide by the Code of Conduct laid down by the Council of the Institute. Part III relates to conduct of company secretaries, discusses brief about Secretarial Standards Board and future of professional practice i.e. mega firms.

This study material is published to aid the students in preparing the paper on Company Law for Executive Programme. It is part of the educational kit and takes the students step by step through each phase of preparation emphasizing key concepts, principles, pointers and procedures. Company Secretaryship being a professional course, the examination standards are set very high, with focus on knowledge of concepts, their application, procedures and case laws, for which sole reliance on the contents of this study material may not be enough. This study material may, therefore, be regarded as the basic material and must be read along with the Bare Acts, Rules, Regulations, Case Law.

The legislative changes made upto May 09, 2018 have been incorporated in the study material. The students to be conversant with the amendments to the laws made upto six months preceding the date of examination. It may happen that some developments might have taken place during the printing of the study material and its supply to the students. The students are therefore advised to refer to the updations at the Regulator's website, Supplement relevant for the subject issued by ICSI and ICSI Journal Chartered Secretary and other publications for updation of study material.

In the event of any doubt, students may write to the Directorate of Professional Development, Perspective Planning & Studies of the Institute for clarification at [academics@icsi.edu](mailto:academics@icsi.edu).

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Although due care has been taken in publishing this study material, the possibility of errors, omissions and/or discrepancies cannot be ruled out. This publication is released with an understanding that the Institute shall not be responsible for any errors, omissions and/or discrepancies or any action taken in that behalf.

Should there be any discrepancy, error or omission noted in the study material, the Institute shall be obliged if the same is brought to its notice for issue of corrigendum in the e-bulletin 'Student Company Secretary'.



## EXECUTIVE PROGRAMME

### COMPANY LAW

This study material is divided into three parts with following weightage of marks:

Part I - Company Law, Principles & Concepts (50 Marks)

Part II - Company Administration and Meetings – Law and Practices (40 Marks)

Part III- Company Secretary as a Profession (10 Marks)

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#### **Part I- Company Law, Principles & Concepts**

Company Law is the collection of various legal aspects that govern the formation, running and winding up of a Company. The Companies Act 2013 is about improving corporate governance which revolves around the Board of Directors, Senior Management of the Company, their roles, responsibility and accountability, Rights and equitable treatment of stakeholders, prompt disclosures, transparency, the legal and regulatory compliances and appropriate risk management measures to protect and enhance interest of all stakeholders.

This part of the study deals with the evolution of company law whether indian or international, sources of funding the company, shareholders, shareholding, responsibility & accountability of the company with respect to transparency and disclosures, secretarial and strategic work involved.

Company Secretaries, over a period of time, have developed themselves as professionals having core competence in compliances and corporate governance, moving from their traditional role of Company Secretary of the Company. Company law is the core area of practice for the company secretary professionals whether in practice or employment. This part imparts expert knowledge of the various provisions of the Companies Act, its schedules, rules, notifications, circulars including secretarial practice & case laws.

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#### **Part II - Company Administration and Meetings – Law and Practices**

Company directors are responsible for the management of their companies. They must act in a way most likely to promote the success of the business and benefit its shareholders. The board of directors has an essential role in company governance and setting the strategic direction of the business. The right board of directors brings your company specialist knowledge and expertise in key business areas, such as management, finance or technology. They also have responsibilities to the company's employees, its trading partners, and the state. Companies use board meetings to create and improve key business strategies. Hence from company secretary point of view meeting preparation is vital: from setting up right papers, circulating meeting papers in advance to providing all kinds of supplementary support to the meeting. A collection of resources on company administration including company filing, company records, company meetings and the responsibilities of company secretaries.

- The company secretary acts as the chief governance officer of the company, and shares various responsibilities with the directors under the Companies Act.

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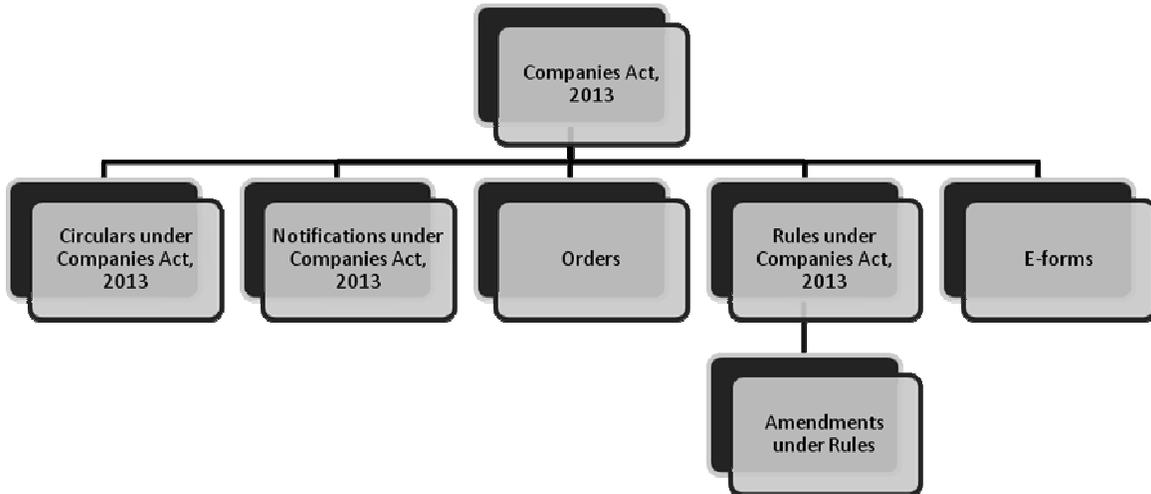
- According to Section 205 of the Companies Act, 2013 the Company Secretary shall discharge following functions and duties, this is the first time that the duties of the company secretary have been specified in the company law:
    - To report to the Board about the compliance with the provisions of this Act.
    - To ensure that the company complies with the applicable secretarial standards.
    - To provide to the directors of the company the guidance they require in discharging their duties, responsibilities and powers.
    - To facilitate the convening of meetings and attend Board, committee and general meetings and maintain the minutes of these meetings.
    - To obtain approvals from the Board, general meeting, the government and such other authorities as required under the provisions of the Act.
    - To assist the Board in the conduct of the affairs of the company.
    - To assist and advise the Board in ensuring good corporate governance and in complying with the corporate governance requirements and best practices.
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### **Part III- Company Secretary as a Profession**

A Professional is a person who has completed formal education and training in a profession. A Professional is subject to strict codes of conduct enshrining rigorous ethical and moral obligations. A Professional is an interface between business and society. Professionals are expected to conduct themselves in such a manner so as to uphold the grace, dignity and professional standing of their respective institutes. Any commitment to complete a particular assignment as agreed by the person himself should be completed in a professional manner. This section gives an overview of the code of conduct that applies on the professional conduct of company secretaries, discusses brief about Secretarial Standards Board and future of professional practice i.e. mega firms.

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## LEGAL FRAMEWORK OF COMPANY LAW



**EXECUTIVE PROGRAMME**  
**Module 1**  
**Paper 2**  
**Company Law (Max Marks 100)**

**SYLLABUS**

**Objectives**

To impart expert knowledge of the various provisions of the Companies Act, its schedules, rules, notifications, circulars including secretarial practice, case laws and Secretarial Standards.

**Detailed Contents**

**Part I : Company Law, Principles & Concepts (50 Marks)**

- 1. Introduction to Company Law:** Jurisprudence of Company Law; Meaning, Nature, Features of a company; Judicial acceptance of the company as a separate legal entity; Concept of Corporate Veil, Applicability of Companies Act; Definitions and Key Concepts.
- 2. Shares and Share Capital:** Meaning and types of Capital; Concept of issue and allotment; Issue of Share certificates; Further Issue of Share Capital; Issue of shares on Private and Preferential basis; Rights issue and Bonus Shares; Sweat Equity Shares and ESOPs; Issue and Redemption of preference shares; Transfer and Transmission of securities; Buyback of securities; dematerialization and rematerialization of shares; Reduction of Share Capital.
- 3. Members and Shareholders:** How to become a member; Register of Members; Declaration of Beneficial Interest; Rectification of Register of Members; Rights of Members; Variation of Shareholders' rights; Shareholders Democracy; Shareholder agreement, Subscription Agreements, Veto powers.
- 4. Debt Instruments:** Issue and redemption of Debentures and Bonds; creation of security; Debenture redemption reserve; debenture trust deed; conversion of debentures into shares; Overview of Company Deposits.
- 5. Charges:** Creation of Charges; Registration, Modification and Satisfaction of Charges; Register of Charges; Inspection of charges; Punishment for contravention; Rectification by Central Government in Register of charges.
- 6. Distribution of Profits:** Profit and Ascertainment of Divisible Profits; Declaration and Payment of Dividend; Unpaid Dividend Account; Investor Education and Protection Fund; Right to dividend; rights shares and bonus shares to be held in abeyance.
- 7. Corporate Social Responsibility:** Applicability of CSR; Types of CSR Activities; CSR Committee and Expenditure; Net Profit for CSR; Reporting requirements.
- 8. Accounts, Audit and Auditors:** Books of Accounts; Financial Statements; National Financial Reporting Authority; Auditors-Appointment, Resignation and Procedure relating to Removal,

Qualification and Disqualification; Rights, Duties and Liabilities; Audit and Auditor's Report; Cost Audit; Secretarial Audit; Special Audit; Internal Audit.

9. **Transparency and Disclosures:** Board's Report; Annual Return; Annual Report; Website disclosures; Policies.
10. **An overview of Inter-Corporate Loans, Investments, Guarantees and Security, Related Party Transactions.**
11. **Registers and Records:** Maintenance and Disposal.
12. **An overview of Corporate Reorganization:** Introduction of Compromises, Arrangement and amalgamation, Oppression and Mismanagement, Liquidation and winding-up; Overview of Registered Valuers; Registration Offices and Fees; Companies to furnish information and statistics.
13. **Introduction to MCA 21 and filing in XBRL.**
14. **Global Trends and Developments in Company Law. Case Laws, Case Studies and Practical Aspects.**

#### **Part II: Company Administration and Meetings – Law and Practices (40 Marks)**

15. **Board Constitution and its Powers:** Board composition; Restriction and Powers of Board; Board Committees- Audit Committee, Nomination and Remuneration Committee, Stakeholder relationship Committee and other Committees.
16. **Directors:** DIN requirement, Types of Directors; Appointment/ Reappointment, Disqualifications, Vacation of Office, Retirement, Resignation and Removal, and Duties of Directors; Rights of Directors; Loans to Directors; Disclosure of Interest.
17. **Key Managerial Personnel (KMP's) and their Remuneration:** Appointment of Key Managerial Personnel; Managing and Whole-Time Directors, Manager, Chief Executive Officer and Chief Financial Officer; Company Secretary – Appointment, Role and Responsibilities, Company Secretary as a Key Managerial Personnel; Functions of Company Secretary; Officer who is in default; Remuneration of Managerial Personnel.
18. **Meetings of Board and its Committees:** Frequency, Convening and Proceedings of Board and Committee meetings; Agenda Management; Management Information System; Meeting Management; Resolution by Circulation; Types of Resolutions; Secretarial Standard – 1; Duties of Company Secretaries before, during and after Board/ Committee Meeting.
19. **General Meetings:** Annual General Meeting; Extraordinary general Meetings; Other General Meetings; Types of Resolutions; Notice, Quorum, Poll, Chairman, Proxy; Meeting and Agenda; Process of conducting meeting; Voting and its types-vote on show of hands, Poll, E-Voting, Postal ballot; Circulation of Members' Resolutions etc.; Signing and Inspection of Minutes; Secretarial Standard – 2; Duties of Company Secretaries before, during and after General Meeting.
20. **Virtual Meetings:** Technological Advancement in conduct of Board Committee & General Meetings; e-AGM.

**Case Laws, Case Studies and Practical Aspects.**

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**Part III: Company Secretary as a Profession (10 Marks)**

- 21. Legal framework governing Company Secretaries:** The Company Secretaries Act, 1980 along with Rules and Regulations; Disciplinary Mechanism and Penalties for Professional Misconduct; Ethics in Profession, Professional Liabilities.
- 22. Secretarial Standards Board:** Secretarial Standards Board of ICSI; Process of making Secretarial Standards; Need and Scope of Secretarial Standards.
- 23. Mega Firms:** Concept of mega firms; Benefits of mega firms, Eligibility criteria for partner, Agreement between partners; management of Firm; Collective multidisciplinary expertise; Public Relation and Brand Building.

**Case Laws, Case Studies and Practical Aspects**

## LESSON WISE SUMMARY

### Company Law

#### Lesson 1: Introduction to Company Law

A Company is a legal entity, allowed by legislation, which permits a group of people, as shareholders, to apply to the regulators for an independent organization to be created, which can then focus on pursuing set objectives, and empowered with legal rights which are usually only reserved for individuals, such as to sue and be sued, own property, hire employees or loan and borrow money. These distinct fundamental legal features and characteristics of a company makes it more advantageous over other forms of business like sole proprietorship, Hindu undivided family, partnership, Limited Liability Partnership, etc. The Lesson gives an insight of the distinct features of the company and advantages otherwise.

A company is regarded as a distinct legal entity and is said to cast a veil between the company and its human constituents, 'the corporate veil'. This veil can be pierced for the purpose of imposing some form of liability on a company's shareholders and / or directors. There are many court cases and exceptions to this which have been discussed in detail in this Lesson.

To understand a piece of legislation it is important to understand what was the need of this legislation?, what practices were being followed?, what were the expectation of the stakeholders?, what led to creation of legislation?

Company Legislation in India owes its origin to the English Company Law. The Companies Acts passed from time to time in India have been following the English Companies Acts, with certain modifications. Even the Companies Act, 1956, was based on the U.K. Companies Act, 1948.

The first legislative enactment for registration of Joint Stock Companies in India was passed in the year 1850 which was based on the English Companies Act, 1844. This Act recognised companies as distinct legal entities but did not introduce the concept of limited liability. The concept of limited liability, in India, was recognised for the first time by the Companies Act, 1857 closely following the English Companies Act, 1856 in this regard. Till 1956, the business companies in India were regulated by this Act of 1913. Based on Bhabha committee report Companies Act 1956 was introduced.

As the business evolved need was felt to introduce the Company Law in a fresh manner considering the changes in the systems and procedures worldwide. Companies Act, 2013 was passed after decade long deliberations with stakeholders.

This Lesson gives an overview of the developments of company law and discusses the features of a company form of business.

#### Lesson 2: Shares and Share Capital

Importantly share capital refers to the funds that a company raises in exchange for issuing an ownership interest in the company in the form of shares. "Share capital" may also describe the number and types of shares that compose a company's share structure. There are two general types of share capital, which are equity and preference shares.

For running a company it is important to understand the options available to fund the projects of the company. The Company Law permits various options which can be availed to generate funds. There are various ways to raise capital which include preferential allotment, employee stock option, issue of rights shares and issue of shares with differential voting rights. It involves various approvals, disclosures, filings, maintenance of records, etc. which are prescribed under Chapter IV of the Companies Act, 2013 read with Companies (Share Capital and Debentures) Rules, 2014.

There are several compliances that need be done pre and post the securities are issued such as issue of share certificates, dematerialization, register of members, allotment of securities. The Lesson also introduces to the basic modalities of issue of securities and allotment thereunder.

The shares of a company are freely transferable. The shareholding can either be maintained in physical form or demat form. The law is very clear with the procedure to be followed to transfer the shares, still there remain many practical issues in transfer of shares. The law also makes a provision for rectification of register of members. This Lesson gives an insight on this.

Buy back of shares is not reduction of capital. Buy-Back is a corporate action in which a company buys back its shares from the existing shareholders usually at a price higher than market price. Reduction of capital by a company is always subject to confirmation by the Tribunal on an application made by the company.

As a prospected company secretary understanding of processes involved in raising of capital, issuance of securities, reduction of share capital, buy-back is of utmost importance. This Lesson provides an overview on the subject covering both theory and practical aspects.

### **Lesson 3: Members and Shareholders**

Members may come and members may go but the company goes on for ever.

A person whose name is entered in the register of members of a company becomes a member of that company. The register includes every single detail about the member like name, address, occupation, date of becoming a member, etc. It also includes every person who holds company's shares and whose name is entered as the beneficial owners in depository records. An individual who owns the share of a public or a private company is known as a 'Shareholder.'

The terms shareholders and members are commonly used as synonyms, as one can become a member of the company, except by way of holding shares. In this way, a member is a shareholder and a shareholder is a member. The statement is true but not completely, as it is subject to certain exceptions, i.e. a person can become the holder of shares through transfer, but is not a member, until the transfer is entered in the register of members.

This Lesson gives an insight on secretarial practices expected to be known by the prospected company secretaries on maintaining register of members, shareholder agreement etc.

### **Lesson 4: Debt Instruments**

An issue of debenture plays a great role in long-term planning and decision-making. In modern competitive business era, every company needs fund for any business opportunity. This financing can be fulfilled only by issuing owner's capital and debt capital. The issue of debenture, in one side creates the obligation for the payment of interest at a fixed rate and in another side, it causes an increase in 'earning per share' due to comparatively less number of shares issued.

Companies need to follow certain procedures for issue of debentures to raise money. These have been

elaborated under Companies Act, 2013 and have been discussed in this Lesson.

Deposits have been defined under the Companies Act, 2013 ("2013 Act") to include any receipt of money by way of deposit or loan or in any other form by a company. However what shall not constitute deposits has been prescribed under law in consultation with the Reserve Bank of India. The Lesson provides an overview of the same.

## **Lesson 5: Charges**

A charge is a right created by any person including a company referred to as "the borrower" on its assets and properties, present and future, in favour of a financial institution or a bank, referred to as "the lender", which has agreed to extend financial assistance.

Section 2(16) of the Companies Act, 2013 defines charges so as to mean an interest or lien created on the property or assets of a company or any of its undertakings or both as security and includes a mortgage. The following are the essential features of the charge which are as under:

1. There should be two parties to the transaction, the creator of the charge and the charge holder.
2. The subject-matter of charge, which may be current or future assets and other properties of the borrower.
3. The intention of the borrower to offer one or more of its specific assets or properties as security for repayment of the borrowed money together with payment of interest at the agreed rate should be manifested by an agreement entered into by him in favour of the lender, written or otherwise.

Companies Act, 2013 details the procedure for creation, modification and satisfaction of a charge. As a prospected company secretary you are expected to advise the management on the subject and ensure compliance to the same.

## **Lesson 6: Distribution of profits**

Profit or a portion of profit that can be legally distributed as a dividend to the shareholders is known as Divisible Profit. Considering the small shareholders and their concerns with regard to failure to transfer the dividend to the shareholders the Companies Act, 2013 provides for elaborate mechanism where the shareholders can claim the shares through an authority constituted for the purpose i.e. Investor Education and Protection Fund (IEPF).

The Act clearly enunciates the procedure for transfer of unpaid dividend to separate account and thereafter after particular time period to the authority. The company has to mandatorily comply with the legal requirement, failure may attract penal provisions, as well as this may also be reflected in the Board's report.

A company secretary is also an investor relation officer of the company, he acts as a bridge between the shareholder and company management. This Lesson shall enable the readers to understand the procedures and implement the same while practically operating.

## **Lesson 7: Corporate Social Responsibility**

The concept of Corporate Social responsibility (CSR) has been introduced for the first time in India through Companies Act, 2013. With the enactment of the Companies Act, 2013, India has become the forerunner to mandate spend on Corporate Social Responsibility (CSR) activities through a statutory provision. India has a tradition of corporate philanthropy, while many corporate houses like TATA, Birlas have been traditionally engaged in doing CSR activities voluntarily, the new CSR provisions has put a greater responsibility on companies in India to set out clear CSR framework.

The Act mandates the spending of atleast 2 % of the net profits towards CSR activities within the defined parameters. The Board has been held responsible to ensure compliance with the provision. Non-compliance of the provision has to be reflected in the Board's report and may not be taken well by the investors.

This Lesson details the framework that the company has to comply with right from the constitution of the committee, to its role and manner in which a company can carry out its CSR activities, and CSR reporting. As a company secretary you have to guide the Board on the subject.

## **Lesson 8: Accounts, Audit and Auditors**

Maintaining of company Book of Accounts is mandatory for all types of companies under the Companies Act, 2013. Private Limited Company, One Person Company and Limited Company including Small Companies are required to maintain proper book of accounts. Further, the Books of Accounts of a Company is the basis on which financial statements of a Company are prepared for company annual return filing. Therefore, maintenance of proper company account is both mandatory and necessary.

According to the Companies Act, 2013, a Company's Book of Accounts is considered to be maintained properly if it satisfies the following two conditions:

- Books which are necessary to give a true and fair view of the state of affairs of the company is kept along with the documents required to explain the transactions.
- Books are kept on accrual basis and according to the double entry system of accounting.

Having an effective audit system is important for a company because it enables it to pursue and attain its various corporate objectives. Business processes need various forms of internal control to facilitate supervision and monitoring, prevent and detect irregular transactions, measure ongoing performance, maintain adequate business records and to promote operational productivity.

Auditing is a means of evaluating the effectiveness of a company's internal controls. Maintaining an effective system of internal controls is vital for achieving a company's business objectives, obtaining reliable financial reporting on its operations, preventing fraud and misappropriation of its assets, and minimizing its cost of capital. Both internal and independent auditors contribute to a company's audit system in different but important ways.

The Lesson details the maintenance of accounts in the company and how the auditors have to be appointed, role of auditors and legal provisions relating to the same.

A company has to undertake secretarial audit, cost audit, statutory audit as per the threshold requirement under law.

As a company secretary this is an important area and must be well understood by the readers.

## **Lesson 9: Transparency and Disclosures**

Transparency and disclosure are fundamental to the way businesses are conducted. Transparency and disclosure are essential elements of a robust corporate governance framework as they provide the base for informed decision making by shareholders, stakeholders and potential investors in relation to capital allocation, corporate transactions and financial performance monitoring. The new concept of transparency has put more responsibilities on the corporation by imposing to disclose true and fair picture to every stakeholder and different stakeholder groups.

A company has to make disclosures in Board 's Report under various enactments. Companies Act, 2013,

SEBI (Listing obligations and Disclosure Requirement) Regulations, 2015 and, Sexual Harassment of Women at Workplace (Prevention, Prohibition and Redressal) Act, 2013 have mandated disclosures at many places.

The Lesson also discusses the disclosures to be made by the company on the website, through its Annual report and Annual return. SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015 requires listed entities to maintain various policies. This Lesson gives an overview of the same.

As an important part of secretarial practice this Lesson shall enable prospected company secretaries to understand the various disclosures required and would help them to guide the Board and management not only on the legal parameters but also in terms of financial and non-financial benefits derived all kinds of true and fair disclosures.

### **Lesson 10: An overview of Inter Corporate Loans, Investments, Guarantees and security, Related Party transactions**

Inter corporate loans and investments play a vital role in the growth of Industries since they result in flow of funds to group companies or other companies in need of funds. The Companies Act, 2013 (Act) has come up with a change in the concept of 'Loan and Investment by Company'. The new Act provides that inter-corporate investments not to be made through more than two layers of investment companies.

Transactions with related parties are a basic human instinct. This applies both for personal & commercial transactions. Such transactions are sometimes influenced by consideration other than commercial. There is a possibility that such transactions might have not occurred on 'arm's length' consideration. Related party transactions adopted by the companies could be a possible tool for corporate abuse. Transfer of economic resources to the related party at less than arm's length price is necessitated for host of reasons ranging from evasion/avoidance of tax liability to siphon-off the resources. That's why various laws and regulations stipulate the deeper scrutiny and the greater disclosures of such transactions. The Companies Act, 2013 does provide for a framework for transactions in which directors, etc., are interested with a view to avoid situation of conflict of interest

The lesson examines the legal provisions with respect to related party transaction; inter corporate loans, investments, guarantees and security. This Lesson enables the students to understand the legal framework and guide the board members and shareholders in future.

### **Lesson 11: Register and Records**

The Companies Act, 2013 and the rules made there under lays down that every company incorporated under the Act has to maintain Statutory Registers.

The Registers need to maintained and updated eventually and should be kept at the registered office of the company. Some of the Registers are required to be kept open for inspection by directors, members, creditors and by other persons. A company is required to provide the extracts from the registers, if demanded by directors, members, creditors and by other persons on payment of specified fees.

The registers and records are to be preserved for certain period for some or the other reason. This is of absolute importance for the secretarial practice whether by company secretary in employment or in practice. This Lesson covers all the registers to be maintained by the company under the Act and shall enable the understanding of the same.

### **Lesson 12: An overview of corporate reorganization**

Corporate reorganization requires compliances of not only Companies Act, 2013, SEBI (Listing

Obligations & Disclosure Requirements) Regulations, 2015, Indian Stamp Act 1899, income Tax Act, 1961 etc.

Apart from complying with the rules and regulations of an organisation, the company secretary also plays a pivotal role in corporate restructuring exercises.

This Lesson gives an overview of the legal and procedural requirement to be complied by the company. As a prospected company secretary you are expected to guide the Board and management on the proper restructuring model, legal and procedural technicalities etc. this Lesson would enable you to gain knowledge of the subject.

### **Lesson 13: Introduction to MCA21 and filing in XBRL**

A very important area of work of company secretaries relate to secretarial practice. MCA 21 is a portal which facilitates the electronic filing under Companies Act, 2013. This Lesson highlights the basic technicalities of the portal and discusses certain details of various forms to be submitted to MCA.

### **Lesson 14: Global Trends and Developments in Company Law**

Indian Company Law is based on various best practices from around the world. This is a theory based Lesson which gives you an idea of how the developments across various nations have impacted the country's corporate law. This Lesson covers salient features of company law emerged/ emerging in the following countries:

- ♣ United Kingdom
- ♣ The United States of America
- ♣ Australia
- ♣ Canada
- ♣ Hong Kong
- ♣ Singapore

### **Lesson 15: Board Constitution and its Powers**

The Board of director is the ultimate decision – making body and determines the delegation of powers throughout the company; it is considered to be the primary organ of the company..

The role of the Board is summarized as:

- Providing entrepreneurial leadership
- Setting strategy
- Ensuring the human and financial resources are available to achieve objectives
- Reviewing management performance
- Setting up company's values and standards
- Ensuring robustness of financial controls and risk management

This Lesson guides on the constitution of the Board, its powers and restrictions. Board committees are constituted in accordance with Companies Act, 2013 and SEBI (Listing Obligations & Disclosure

Requirements) Regulations, 2015, the Lesson discusses the same and the major role assigned to them under law.

### **Lesson 16: DIRECTORS**

The directors play a very important role in the day to day functioning of the company. It is the board, who is responsible for the company's overall performance. Only individuals can be appointed as directors of a company. The subscribers to the memorandum who are individuals are deemed to be the first directors of the company. Thereafter the shareholders or in many cases the board of directors appoint the directors.

The Act has brought in many new provisions such as appointment of women director, resident director, independent director by certain class of companies. The Lesson discusses the procedure for appointing the various types of directors, the rights, duties of a director.

As a company secretary you should be in know of the subject.

### **Lesson 17: Key Managerial Personnel and their Remuneration**

The Companies Act 2013 has introduced a new concept for appointment of the Key Managerial Personnel at top level of the organizational structure. In the new Act the position of company secretary has been enhanced multifold, from record keeper to key managerial personnel. A present day company secretary is expected to do statutory, administrative, managerial and strategic functions.

This Lesson guides on the appointment, procedure for appointment and role to be undertaken as KMP.

### **Lesson 18: Meetings of the Board and its Committees**

Under Companies Act, 2013 the Board has to meet atleast four times in a year and not more one hundred and twenty days shall intervene between two consecutive Board meetings. The committees have to meet in accordance with the terms of reference of the committee. As a company secretary you need to guide the members on the conduct of affairs of the company and facilitate the convening of meetings and attend Board and Committee meetings and maintain minutes of these meetings.

This Lesson gives the basic idea of holding a meeting of the board or committee.

### **Lesson 19: General Meetings**

A company may have many kinds of meetings; general meetings are one among them. In very simple terms, a meeting of general body may be called general meeting. General meeting comprises of all general members of an recognized n that is company in our case.

A general meeting may be Annual General Meeting (AGM), Extra – ordinary General Meeting (EGM) and class meetings.

A company secretary plays a critical role in preparation, convening, holding and conducting a meeting. This Lesson gives an overall idea of not only legal framework but also secretarial work involved in conducting a meeting.

### **Lesson 20: Virtual meetings**

The new Act permits for meeting of Board of directors through video conferencing or audio conferencing. The Lesson discusses the broad parameters of holding such meetings and the restrictions thereat.

E-voting at a general meeting has now been practiced and well recognized by the law but the concept E-AGM is still not practiced in India.

### **Lesson 21: Legal framework governing Company secretaries**

Professionals are expected to conduct themselves in such a manner so as to uphold the grace, dignity and professional standing of their respective Institutes. Any commitment to complete a particular assignment as agreed by the person himself should be completed in a professional manner.

The purpose of this Lesson is to explain to the students, expectation as a member with respect to various aspects of the ethical conduct. This lesson has been designed to assist in defining appropriate personal and professional conduct, to provide guidance in the identification and resolution of ethical issues, and to help the students (the future members) of the Institute to maintain the culture of honesty, integrity, transparency and accountability.

### **Lesson 22: Secretarial Standards Board**

A company needs to comply with the mandatory requirement of compliance with the Secretarial Standards. A company secretary in whole time employment is required to guide the Board of Directors of the company on the compliances of the secretarial standards. On the other hand a practicing company secretary while conducting secretarial audit has to ensure the compliance. This Lesson shall give the readers a broader perspective of how the standards are formulated and developed.

### **Lesson 23: Mega Firms**

In a rapidly changing economy, industrial environment and emergence of the need for corporate governance and ethical business practices of voluntary disclosures, role of a practicing company secretary has also changed swiftly. Company Secretary in Practice has become a crucial player. The stakeholders are becoming vigilant towards the compliances. It is the prime duty of a professional to meet the expectations of the stakeholders at any given point of time.

Company Secretary in practice may face technical, time and knowledge constraint after certain point of time in profession. There comes the need of having a practicing firm, mega firms. Keeping in view of the present needs of the corporate and multi dimensional growth of CS profession especially in the areas of practicing in the areas of Corporate Laws, Labour laws, RBI/ FEMA, acting as Secretarial Audit, Resolution Professional Insolvency Bankruptcy Code, GST Practitioner there is a need to structure and build the mega firms.

This chapter gives an overview of benefits, challenges of constituting mega firms.



## LIST OF RECOMMENDED BOOKS

### Paper 2: COMPANY LAW

#### Readings:

1. Dr. Avtar Singh : Company Law; Eastern Book Company, 34, Lalbagh, Lucknow – 226 001
2. C.R. Datta : Datta on the Company Law; Lexis Nexis, Butterworths Wadhwa, Nagpur
3. A. Ramaiya : Guide to the Companies Act; Lexis Nexis, Butterworths Wadhwa, Nagpur
4. K.C. Garg, R.C. Chawla, Vijay Gupta : Company Law; Kalyani Publishers, 1/1, Rajinder Nagar, Civil Lines, Ludhiana – 141 001.
5. A.K. Majumdar, Dr. G.K. Kapoor, Sanjay Dhamija : Company Law and Practice; Taxmann, 59/32, New Rohtak Road, New Delhi-110 005.
6. D.K. Jain : Company Law Ready Reckoner; Bharat Law House Pvt. Ltd.; T-1/95, Mangolpuri Industrial Area, Delhi-110083.
7. R. Suryanarayanan : Company Law Ready Reckoner; Commercial Law Publishers, 151, Rajinder Market, Opp. Tis Hazari Court, Delhi-110054.
8. L.C.B. Gower : Principles of Modern Company Law; Stevens & Sons Ltd., London.
9. Taxmann's : Circulars & Clarifications on Company Law; Taxmann, 59/32, New Rohtak Road, New Delhi-110 005.
10. Bare Act : Corporate Laws; Taxmann, 59/32, New Rohtak Road, New Delhi-110 005.
11. Video : Primer on Company Law by ICSI (<https://www.youtube.com/user/icsicompaniesact2013>)

#### Journals:

1. Chartered Secretary : ICSI, New Delhi
2. Student Company Secretary : ICSI, New Delhi
3. Corporate Law Adviser : Corporate Law Advisers, 613, Metro View Apt., Sector 13, Pocket B, Dwarka, New Delhi-110075.
4. Company Law Journal : Company Law Journal (India) Pvt. Ltd., 53/15, Old Rajinder Nagar, Post Box No. 2844, New Delhi-110060.

**Note:** The latest edition of all the books referred to above should be read.

## ARRANGEMENT OF STUDY LESSONS

### Module-1 Paper-2 COMPANY LAW

#### PART I: Company Law, Principles & Concepts

<b>Sr. No.</b>	<b>Lesson Title</b>
1	Introduction to Company Law
2	Shares and Share Capital
3	Members and Shareholders
4	Debt Instruments
5	Charges
6	Distribution of Profits
7	Corporate Social Responsibility
8	Accounts, Audit and Auditors
9	Transparency and Disclosures
10	An overview of Inter-Corporate Loans, Investments, Guarantees and Security, Related Party Transactions
11	Registers and Records
12	An overview of Corporate Reorganization
13	Introduction to MCA 21 and filing in XBRL
14	Global Trends and Developments in Company Law

#### Part II: Company Administration and Meetings – Law and Practices

<b>Lesson No.</b>	<b>Chapter Title</b>
15	Board Constitution and its Powers
16	Directors
17	Key Managerial Personnel (KMP's) and their Remuneration
18	Meetings of Board and its Committees
19	General Meetings
20	Virtual Meetings

**Part III : Company Secretary as a Profession Secretaries**

<b>Lesson No.</b>	<b>Chapter Title</b>
21	Legal framework governing Company Secretary
22	Secretarial Standards Board
23	Mega Firms

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# Lesson 1

## Introduction to Company Law

### LESSON OUTLINE

- Introduction
- History and development of Company Law in India
  - The Companies Act, 1956
  - Concept Paper on Company Law, 2004 & JJ Irani Report
  - Companies Bill 2012
  - Companies Act, 2013
- Meaning and definition of Company
- Nature and characteristics of a Company
- Company *vis-a-vis* other forms of business
- Doctrine of lifting of or piercing the corporate veil
- Applicability of Companies Act, 2013 and Key Concepts
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

The concept of 'Company' or 'Corporation' in business is not new, but was dealt with, in 4<sup>th</sup> century BC itself, at the time of 'Arthashastra'. It has evolved over time according to the needs of society and business dynamics. The word Company is made of two Latin words "Com" meaning "coming together" and "panis" meaning "bread". Company originally referred to group of people who took their meal together.

It is important for the students as future Company Secretaries to understand the concept and legal provisions of Company Law very well as this forms as major part of working in future whether in practice or employment.

This chapter introduces the reader with the background and evolution of corporate legislation in India, the distinct features of Company, other forms of business, concepts under new law etc.

## **INTRODUCTION- JURISPRUDENCE OF COMPANY LAW**

Company Law in India, is the cherished child of the English parents. Our various Companies Acts have been modelled on the English Acts. Following the enactment of the Joint Stock Companies Act, 1844 in England, the first Companies Act was passed in India in 1850. It provided for the registration of the companies and transferability of shares. The Amending Act of 1857 conferred the right of registration with or without limited liability. Subsequently this right was granted to banking and insurance companies by an Act of 1860 following the similar principle in Britain. The Companies Act of 1856 repealed all the previous Acts. This Act covered aspects of incorporation, regulation and winding up of companies and other associations. This Act was recast in 1882, embodying the amendments which were made in the Company Law in England upto that time. In 1913 a consolidating Act was passed, and major amendments were made to the consolidated Act in 1936. In the meantime England passed a comprehensive Companies Act in 1948. In 1951, the Indian Government promulgated the Indian Companies (Amendment) Ordinance under which the Central Government and the Court assumed extensive powers to intervene directly in the affairs of the company and to take necessary action in the interest of the company. The ordinance was replaced by an Amending Act of 1951.

## **HISTORY AND DEVELOPMENT OF THE CONCEPT OF COMPANY LAW IN INDIA**

### **The Companies Act, 1956 – Based on Bhabha Committee Recommendations**

At the end of 1950, the Government of independent India appointed a Committee under the Chairmanship of H.C. Bhabha to go into the entire question of the revision of the Indian Companies Act, with particular reference to its bearing on the development of Indian trade and industry. This Committee examined a large number of witnesses in different part of the country and submitted its report in March 1952.

Based largely on the recommendations of the Company Law Committee, a Bill to enact the present legislation, namely, the Companies Act, 1956 was introduced in Parliament. This Act, once again largely followed the English Companies Act, 1948.

The Companies Act, 1956 was enacted with a view to consolidate and amend the earlier laws relating to companies and certain other associations. The Act came into force on 1st April, 1956. This Companies Act was based largely on the recommendations of the Bhabha Committee. This Act was the longest piece of legislation ever passed by our Parliament. Amendments have been made in this Act periodically. The Companies Act, 1956 consisted of 658 Sections and 15 Schedules.

Full and fair disclosure of various matters in prospectus; detailed information of the financial affairs of company to be disclosed in its account; provision for intervention and investigation by the Government into the affairs of a company; restrictions on the powers of managerial personnel; enforcement of proper performance of their duties by company management; and protection of minority shareholders were some of the main features of the Companies Act, 1956.

The Companies Act, 1956 was enacted with the object to amend and consolidate the law relating to companies. This Act provided the legal framework for corporate entities in India and was a mammoth legislation. As the corporate sector grew in numbers and size of operations, the need for streamlining this Act was felt and as many as 24 amendments had taken place since then.

The Companies Act, 1956 had undergone changes by amendments in 1960, 1962, 1963, 1964, 1965, 1966, 1967, 1969, 1971, 1977, 1985, 1988, 1996, 1999, 2000, 2002 and 2006. The provisions of Companies (Second Amendment) Act, 2002 were not enforced except that of definitions and the constitution of NCLT (National Company Law Tribunal). The Companies Act, 1956 was also amended pursuant to the enactment

of the Depositories Act, 1996. Unsuccessful attempts were made in 1993 and 1997 to replace the present Act with a new law. Companies (Amendment) Bill, 2003 containing important provisions relating to Corporate Governance and aimed at achieving competitive advantage was also introduced.

<b>Brief of major amendments to Companies Act, 1956</b>	
<b>Amendment</b>	<b>Particulars</b>
The Companies (Amendment) Act, 1960	Based on the recommendations of Shastri Committee, this introduced several new provisions relating to various aspects of company management which were overlooked in the 1956 Act.
The Companies (Amendment) Act, 1963	This provided for the appointment of a Companies Tribunal and constitution of the Board of Company Law Administration. It also empowered the Central Government to remove managerial personnel involved in cases of fraud, etc.
The Companies (Amendment) Act, 1965	Based on the recommendations of the Vivian Bose Commission, this introduced some major changes, such as clear definition of the main and subsidiary objects of a company in its Memorandum of Association; Strengthening the provisions relating to investigation into the affairs of the company, etc. The Companies Act was further amended twice in 1966.
The Companies (Amendment) Act, 1969	Two important changes were introduced through this. The institutions of managing agents and secretaries and treasurers were abolished with effect from April 3, 1970. Secondly, contributions by companies to any political party or for any political purpose were prohibited.
The Companies (Amendment) Act, 1974	This introduced some important and major changes in the Companies Act, 1956. The object of the Amendment Act was to inject an element of public interest in the working of the corporate sector.
The Companies (Amendment) Act of 1977	This brought about certain changes in Sections 58A, 220, 293, 620 and 634A of 1956 Act.
The Companies (Amendment) Act, 1985	The amending Act substituted Section 293A of Companies Act, 1956 with a new section permitting Non-Government companies to make political contributions, directly or indirectly.  With a view that legitimate dues of workers rank <i>pari passu</i> with secured creditors in the event of closure of the company and rank above even the dues to Government, Sections 529 and 530 of the Companies Act, 1956, were amended and a new Section 529A was introduced.
The Companies (Amendment) Act, 1988	Based on the recommendations made by the Expert Committee (Sachar Committee), the Companies (Amendment) Act, 1988 substantially amended the Companies Act, 1956 in order to streamline some of the existing provisions of the Companies Act, 1956 and to ensure better working and administration of the Act. <i>The important</i>

	<p><i>changes introduced by the Amendment Act of 1988 were:</i></p> <p>(a) Definition of Secretary brought in line with the definition of 'Company Secretary' in the Company Secretaries Act, 1980 and includes an individual possessing the prescribed qualifications.</p> <p>(b) The concept of company secretary in practice was introduced for the first time in the Companies Act. The Amended Act, among other things, also set up an independent Company Law Board to exercise such judicial and quasi-judicial functions, earlier being exercised either by the Court or the Central Government.</p>
The Depositories Act, 1996	Dematerialization of securities was introduced by the Depositories Act, 1996 and accordingly amendments were made to register of members and several other consequential things were incorporated.
The Companies (Amendment) Act, 1999	<p>The following major changes to the Companies Act, 1956:-</p> <ol style="list-style-type: none"> <li>a) Companies allowed to issue Sweat Equity shares and to buy-back their own securities.</li> <li>b) Facility for nomination provided for the benefit of share/debenture/deposit holders.</li> <li>c) An Investor Education and Protection Fund to be established.</li> <li>d) National Advisory Committee on Accounting Standards for companies to be established.</li> <li>e) Prior approval of Central Government not required for inter-corporate investment/lending proposals subject to certain conditions.</li> </ol>
The Companies (Amendment) Act, 2000	<p>The following major amendments were introduced:</p> <ol style="list-style-type: none"> <li>a. Private Companies and Public Companies to have a minimum paid-up capital of Rupees one lakh and five lakh respectively.</li> <li>b. Provisions relating to deemed public companies became inoperative and a new provision relating to conversion of a public company to a private company inserted in the Companies Act, 1956.</li> <li>c. SEBI given powers regarding issue and transfer of securities and non-payment of dividend by listed public companies.</li> <li>d. Every listed company making initial public offer of any security for a sum of Rupees ten crores or more will have to issue the same only in a dematerialised form.</li> </ol>
The Companies (Amendment) Act, 2002 and Companies (Second	<p>The following changes to the Companies Act, 1956:-</p> <ol style="list-style-type: none"> <li>a) New Part IXA consisting of Section 581A to 581ZT relating to Producer Companies inserted</li> <li>b) The existing Company Law Board was proposed to be dissolved and in its</li> </ol>

Amendment) Act, 2002 (not enforced)	place a National Company Law Tribunal (Tribunal) was to be constituted. c) The Board for Industrial and Financial Reconstruction was to be abolished and SICA was proposed to be repealed.
The Companies (Amendment) Act, 2006	This inserted new Sections 610B, 610C, 610D and 610E and also certain sections pertaining to Director Identification Number (DIN). With the advent of new technologies this amendment introduced electronic filing, DIN, maintenance of electronic records in consistency with Information Technology Act, 2000.

### CONCEPT PAPER ON COMPANY LAW, 2004 & J.J. IRANI REPORT

To frame a law that enables companies to achieve global competitiveness in a fast changing economy, the Government had taken up a fresh exercise for a comprehensive revision of the Companies Act, 1956, albeit through a consultative process. As the first step in this direction, a Concept Paper on Company Law drawn up in the legislative format was exposed for public viewing on the electronic media so that all interested parties may not only express their opinions on the concepts involved but may also suggest formulations on various aspects of Company Law.

The response to the concept paper on Company Law was tremendous. The Government, therefore, felt it appropriate that the proposals contained in the Concept Paper and suggestions received thereon be put to merited evaluation by an independent Expert Committee. A Committee was constituted on 2nd December, 2004 under the Chairmanship of Dr. J J Irani, the then Director, Tata Sons, with the task of advising the Government on the proposed revisions to the Companies Act, 1956 with the objective to have a simplified compact law that will be able to address the changes taking place in the national and international scenario, enable the adoption of internationally accepted best practices as well as provide adequate flexibility for timely evolution of new arrangements in response to the requirements of ever-changing business models. The Committee submitted its report to the Government on 31st May 2005.

Dr. J J Irani Expert Committee on Company Law had submitted its report charting out the road map for a flexible, dynamic and user-friendly new company law. The Committee had taken a pragmatic approach keeping in view the ground realities, and had sought to address the concerns of all the stakeholders to enable adoption of internationally accepted best practices. As one wades through the report, one finds an arduous zeal to ensure that flexibility is coupled with accountability and transparency. Be it the role of directors in the management of the company or the role of promoters at the time of incorporation or the responsibility of professionals in ensuring better governance, the report had made very dynamic and balanced recommendations. The Report of the Committee had also sought to bring in multifarious progressive and visionary concepts and endeavored to recommend a significant shift from the “Government Approval Regime” to a “Shareholder Approval and Disclosure Regime”.

The Expert Committee had recommended that private and small companies need to be given flexibilities and freedom of operations and compliance at a low cost. Companies with higher public interest should be subject to a stricter regime of Corporate Governance. Further, Government companies and public financial institutions should be subject to similar parameters with respect to disclosures and Corporate Governance as other companies are subjected to.

To attune the Indian Company Law with the global reforms taking place in the arena, the Report of the Committee had sought to bring in multifarious visionary concepts, which if accepted and acted upon would really simplify the voluminous and cumbersome Companies Act in the country.

## **Companies Bill, 2012**

The Government considered the recommendations of Irani Committee and also had detailed discussions and deliberations with various stakeholders viz Industry Chambers, Professional Institutes, Government Departments, Legal Experts and Professionals etc. Thereafter, the Companies Bill, 2009 was introduced in the Lok Sabha on 3rd August, 2009, The Bill laid greater emphasis on self regulation and minimization of regulatory approvals in managing the affairs of the company. The Bill promised greater shareholder democracy, vesting the shareholders with greater powers, containing stricter corporate governance norms and requiring greater disclosures.

The Companies Bill, 2009 after introduction in Parliament was referred to the Parliamentary Standing Committee on Finance for examination which submitted its report to Parliament on 31st August, 2010. Certain amendments were introduced in the Bill in the light of the report of the Committee and a revised Companies Bill, 2011 was introduced. This version was also referred to the Hon'ble Committee, which suggested certain further amendments. The amended Bill was passed by the Lok Sabha on 18th December, 2012 and by the Rajya Sabha on 8th August, 2013. The Bill was retitled as Companies Bill, 2012.

## **Companies Act, 2013**

The Companies Bill, 2012 finally became the Companies Act, 2013. It received the assent of the President on August 29, 2013 and was notified in the Gazette of India on 30.08.2013.

Companies Act, 2013 has undergone amendments four times so far. Companies (Amendment) Act, 2015 and Companies (Amendment) Act, 2017 aimed at enhancing efficiency and promoting ease of doing business. The Act was also amended by The Insolvency and Bankruptcy Code, 2016 and Finance Act, 2017. The Insolvency and Bankruptcy Code, 2016 led to omission of various sections i.e. section 253 to section 269, section 289, section 304 to section 323 and section 325. The Finance Act, 2017 amended section 182 with regard to prohibitions and restrictions regarding political contributions. So far Ministry has come out with several circulars, notifications, Orders and various amendment rules to facilitate better and smooth implementation of the Act.

The Companies Act 2013 introduced new concepts supporting enhanced disclosure, accountability, better board governance, better facilitation of business and so on. It includes associate company, one person company, small company, dormant company, independent director, women director, resident director, special court, secretarial standards, secretarial audit, class action, registered valuers, rotation of auditors, vigil mechanism, corporate social responsibility, E-voting etc.

## **MEANING AND DEFINITION OF A COMPANY**

Lets' now understand what is a company and how it is positioned.

The word 'company' is derived from the Latin word (Com=with or together; panis =bread), and it originally referred to an association of persons who took their meals together. In the leisurely past, merchants took advantage of festive gatherings, to discuss business matters. Nowadays, the company form of organization has assumed great importance. In popular parlance, a company denotes an association of likeminded persons formed for the purpose of carrying on some business or undertaking. A company is a corporate body and a legal person having status and personality distinct and separate from the members constituting it.

It is called a body corporate because the persons composing it are made into one body by incorporating it according to the law and clothing it with legal personality. The word 'corporation' is derived from the Latin term 'corpus' which means 'body'. Accordingly, 'corporation' is a legal person created by a process other than natural birth. It is, for this reason, sometimes called artificial legal person. As a legal person, a corporate is capable of enjoying many rights and incurring many liabilities of a natural person.

An incorporated company owes its existence either to a Special Act of Parliament or to company law. Public corporations like Life Insurance Corporation of India, SBI etc., have been brought into existence through special Acts of Parliament, whereas companies like Tata Steel Ltd., Reliance Industries Limited have been formed under the Company law i.e. Companies Act, 1956 which is replaced by the Companies Act, 2013.

In the legal sense, a company is an association of both natural and artificial persons and is incorporated under the existing law of a country.

In terms of the Companies Act, 2013 (Act No. 18 of 2013) a **“company” means a company incorporated under this Act or under any previous company law [Section 2(20)].**

In common law, a company is a “legal person” or “legal entity” separate from, and capable of surviving beyond the lives of its members. A company is rather a legal device for the attainment of social and economic end. It is, therefore, a combined political, social, economic and legal institution. Thus, the term company has been described in many ways. “It is a means of cooperation and organisation in the conduct of an enterprise”. It is “an intricate, centralised, economic and administrative structure run by professional managers who hire capital from the investor(s)”.

Lord Justice Lindley has defined a company as “an association of many persons who contribute money or money’s worth to a common stock and employ it in some trade or business and who share the profit and loss arising therefrom. The common stock so contributed is denoted in money and is the capital of the company. The persons who contributed in it or form it, or to whom it belongs, are members. The proportion of capital to which each member is entitled is his “share”. The shares are always transferable although the right to transfer them may be restricted.”

## NATURE AND CHARACTERISTICS OF A COMPANY

Since a corporate body (i.e. a company) is the creation of law, it is not a human being, it is an artificial juridical person (i.e. created by law) and it is clothed with many rights, obligations, powers and duties prescribed by law.

The most striking characteristics of a company are discussed below:

### ***(i) Corporate personality***

A company incorporated under the Act is vested with a corporate personality so it bears its own name, acts under name, has a seal of its own and its assets are separate and distinct from those of its members. It is a different ‘person’ from the members who compose it. Therefore it is capable of owning property, incurring debts, borrowing money, having a bank account, employing people, entering into contracts and suing or being sued in the same manner as an individual. Its members are its owners however they can be its creditors simultaneously. A shareholder cannot be held liable for the acts of the company even if he holds virtually the entire share capital.

The shareholders are not the agents of the company and so they cannot bind it by their acts. The company does not hold its property as an agent or trustee for its members and they cannot sue to enforce its rights, nor can they be sued in respect of its liabilities. Thus, ‘incorporation’ is the act of forming a legal corporation as a juristic person. A juristic person is in law also conferred with rights and obligations and is dealt in accordance with law. In other words, the entity acts like a natural person but only through a designated person, whose acts are processed within the ambit of law [*Shiromani Gurdwara Prabandhak Committee v. Shri Sam Nath Dass* AIR 2000 SCW 139].

## CASE EXAMPLE

### The case of *Salomon v. Salomon and Co. Ltd.*, (1897) A.C. 22

*The above case has clearly established the principle that once a company has been validly constituted under the Companies Act, it becomes a legal person distinct from its members and for this purpose it is immaterial whether any member holds a large or small proportion of the shares, and whether he holds those shares as beneficially or as a mere trustee.*

*In the case, Salomon had, for some years, carried on a prosperous business as a leather merchant and boot manufacturer. He formed a limited company consisting of himself, his wife, his daughter and his four sons as the shareholders, all of whom subscribed to 1 share each so that the actual cash paid as capital was £7. Salomon sold his business (which was perfectly solvent at that time), to the Company formed by him for the sum of £38,782. The company's nominal capital was £40,000 in £1 shares. In part payment of the purchase money for the business sold to the company, debentures of the amount of £10,000 secured by a floating charge on the company's assets were issued to Salomon, who also applied for and received an allotment of 20,000 £ 1 fully paid shares. The remaining amount of £8,782 was paid to Salomon in cash. Salomon was the managing director and two of his sons were other directors.*

*The company soon ran into difficulties and the debentureholders appointed a receiver and the company went into liquidation. The total assets of the company amounted to £6050, its liabilities were £10,000 secured by debentures, £8,000 owing to unsecured trade creditors, who claimed the whole of the company's assets, viz., £6,050, on the ground that, as the company was a mere 'alias' or agent for Salomon, they were entitled to payment of their debts in priority to debentures. They further pleaded that Salomon, as a principal beneficiary, was ultimately responsible for the debts incurred by his agent or trustee on his behalf.*

*Their Lordships of the House of Lords observed:*

*"...the company is a different person altogether from the subscribers of the memorandum; and though it may be that after incorporation the business is precisely the same as before, the same persons are managers, and the same hands receive the profits, the company is not, in law, their agent or trustee. The statute enacts nothing as to the extent or degree of interest, which may, be held by each of the seven or as to the proportion of interest, or influence possessed by one or majority of the shareholders over others. There is nothing in the Act requiring that the subscribers to the memorandum should be independent or unconnected, or that they or any of them should take a substantial interest in the undertakings, or that they should have a mind or will of their own, or that there should be anything like a balance of power in the constitution of company."*

## CASE EXAMPLE

### The case of *Lee v. Lee's Air Farming Ltd.* (1961) A.C. 12 (P.C.),

*The above case illustrates the application of the principles established in Salomon's case (supra). In this case, a company was formed for the purpose of aerial top-dressing. Lee, a qualified pilot, held all but one of the shares in the company. He voted himself the managing director and got himself appointed by the articles as chief pilot at a salary. He was killed in an air crash while working for the company. His widow claimed compensation for the death of her husband in the course of his employment. The company opposed the claim on the ground that Lee was not a worker as the same person could not be the employer and the employee. The Privy Council held that Lee and his company were distinct legal persons which had entered into contractual relationships under which he became the chief pilot, a servant of the company. In his capacity of managing director he could, on behalf of the company, give himself orders in his other capacity of pilot, and the relationship between himself, as pilot and the company, was that of servant and master. Lee*

was a separate person from the company he formed and his widow was held entitled to get the compensation. In effect the magic of corporate personality enabled him (Lee) to be the master and servant at the same time and enjoy the advantages of both.

The decision of the Calcutta High Court in *Re. Kondoli Tea Co. Ltd.*, (1886) ILR 13 Cal. 43, recognised the principle of separate legal entity even much earlier than the decision in *Salomon v. Salomon & Co. Ltd.* case. Certain persons transferred a Tea Estate to a company and claimed exemptions from ad valorem duty on the ground that since they themselves were also the shareholders in the company, it was nothing but a transfer from them in one name to themselves under another name. While rejecting this Calcutta High Court observed: "The company was a separate person, a separate body altogether from the shareholders and the transfer was as much a conveyance, a transfer of the property, as if the shareholders had been totally different persons.

### CASE EXAMPLE

*New Horizons Ltd. v. Union of India*, (AIR 1994, Delhi 126)

The experience of a shareholder of a company can be regarded as experience of a company. The tender of the company, New Horizons Ltd., for publication of telephone directory was not accepted by the Tender Evaluation Committee on the ground that the company had nothing on record to show that it had the technical experience required to be possessed to qualify for tender. On appeal the rejection of tender was upheld by the Delhi High Court.

The judgement of the Delhi High Court was reversed by the Supreme Court which observed as under:

"Once it is held that NHL (New Horizons Ltd.) is a joint venture, as claimed by it in the tender, the experience of its various constituents namely, TPI (Thomson Press India Ltd.), LMI (Living Media India Ltd.) and WML (World Media Ltd.) as well as IIPL (Integrated Information Pvt. Ltd.) had to be taken into consideration, if the Tender Evaluation Committee had adopted the approach of a prudent business man."

"Seeing through the veil covering the face of NHL, it will be found that as a result of re-organisation in 1992 the company is functioning as a joint venture wherein the Indian group (TPI, LMI and WML) and Mr. Aroon Purie hold 60% shares and the Singapore based company (IIPL) holds 40% shares. Both the groups have contributed towards the resources of the joint venture in the form of machines, equipment and expertise in the field. The company is in the nature of partnership between the Indian group of companies and Singapore based company who have jointly undertaken this commercial enterprise wherein they will contribute to the assets and share the risk. In respect of such a joint venture company, the experience of the company can only mean the experience of the constituents of the joint venture i.e. the Indian group of companies (TPI, LMI and WML) and the Singapore based company (IIPL) (*New Horizons Ltd. and another v. Union of India* (1995) 1 Comp. LJ 100 SC).

#### **(ii) Company as an artificial person**

A Company is an artificial person created by law. It is not a human being but it acts through human beings. It is considered as a legal person which can enter into contracts, possess properties in its own name, sue and can be sued by others etc. It is called an artificial person since it is invisible, intangible, existing only in the contemplation of law. It is capable of enjoying rights and being subject to duties.

### CASE EXAMPLE

*Union Bank of India v. Khader International Construction and Other* [(2001) 42 CLA 296 SC]

In this case, the question which arose before the Court was whether a company is entitled to sue as an indigent (poor) person under Order 33, Rule 1 of the Civil Procedure Code, 1908. The aforesaid Order permits persons to file suits under the Code as pauper/indigent persons if they are unable to bear the cost of litigation. The appellant in this case had objected to the contention of the company which had sought permission to sue as an indigent person. The point of contention was that, the appellant being a public limited company, it was not a 'person' within the purview of Order 33, Rule 1 of the Code and the 'person' referred to only a natural person and not to other juristic persons. The Supreme Court held that the word 'person' mentioned in Order 33, Rule 1 of the Civil Procedure Code, 1908, included any company as association or body of individuals, whether incorporated or not. The Court observed that the word 'person' had to be given its meaning in the context in which it was used and being a benevolent provision, it was to be given an extended meaning. Thus a company may also file a suit as an indigent person.

#### ***(iii) Company is not a citizen***

The company, though a legal person, is not a citizen under the Citizenship Act, 1955 or the Constitution of India. In *State Trading Corporation of India Ltd. v. C.T.O.*, A.I.R. 1963 S.C. 1811, the Supreme Court held that the State Trading Corporation though a legal person, was not a citizen and can act only through natural persons. Nevertheless, it is to be noted that certain fundamental rights enshrined in the Constitution for protection of "person", e.g., right to equality (Article 14) etc. are also available to company. Section 2(f) of Citizenship Act, 1955 expressly excludes a company or association or body of individuals from citizenship.

### CASE EXAMPLE

In *R.C. Cooper v. Union of India*, AIR 1970 SC 564

In this case, the Supreme Court held that where the legislative measures directly touch the company of which the petitioner is a shareholder, he can petition on behalf of the company, if by the impugned action, his rights are also infringed. In that case, the court entertained the petition under Article 32 of the Constitution at the instance of a director as shareholder of a company and granted relief. It is, therefore, to be noted that an individual's right is not lost by reason of the fact that he is a shareholder of the company.

### CASE EXAMPLE

***Bennet Coleman Co. v. Union of India*, AIR 1973 SC 106**

In this case, the Supreme Court stated that:

"It is now clear that the Fundamental Rights of shareholders as citizens are not lost when they associate to form a company. When their Fundamental Rights as shareholders are impaired by State action, their rights as shareholders are protected. The reason is that the shareholders' rights are equally and necessarily affected if the rights of the company are affected."

#### ***(iv) Company has Nationality and Residence***

Though it is established through judicial decisions that a company cannot be a citizen, yet it has nationality, domicile and residence. In *Gasque v. Inland Revenue Commissioners*, (1940) 2 K.B. 88, Macnaghten. J. held that a limited company is capable of having a domicile and its domicile is the place of its registration and

that domicile clings to it throughout its existence. He observed in this case:

“It was suggested that a body corporate has no domicile. It is quite true that a body corporate cannot have a domicile in the same sense as an individual. But by analogy with a natural person the attributes of residence, domicile and nationality can be given to a body corporate.”

In *Tulika v. Parry and Co.*, (1903) I.L.R. 27 Mad. 315, Kelly C.B. observed:

**“A joint stock company resides where its place of incorporation is, where the meetings of the whole company or those who represent it are held and where its governing body meets in bodily presence for the purposes of the company and exercises the powers conferred upon it by statute and by the Articles of Association.”**

### **(v) Limited Liability**

“The privilege of limited liability for business debts is one of the principal advantages of doing business under the corporate form of organisation.” The company, being a separate person, is the owner of its assets and bound by its liabilities. The liability of a member as shareholder, extends to the contribution to the capital of the company up to the nominal value of the shares held and not paid by him. Members, even as a whole, are neither the owners of the company’s undertakings, nor liable for its debts. In other words, a shareholder is liable to pay the balance, if any, due on the shares held by him, when called upon to pay and nothing more, even if the liabilities of the company far exceed its assets. This means that the liability of a member is limited. For example, if A holds shares of the total nominal value of 1,000 and has already paid Rs.500/- (or 50% of the value) as part payment at the time of allotment, he cannot be called upon to pay more than Rs. 500/-, the amount remaining unpaid on his shares. If he holds fully-paid shares, he has no further liability to pay even if the company is declared insolvent. In the case of a company limited by guarantee, the liability of members is limited to a specified amount of the guarantee mentioned in the memorandum.

Buckley, J. in *Re. London and Globe Finance Corporation*, (1903) 1 Ch.D. 728 at 731, has observed: ‘The statutes relating to limited liability have probably done more than any legislation of the last fifty years to further the commercial prosperity of the country. They have, to the advantage of the investor as well as of the public, allowed and encouraged aggregation of small sums into large capitals which have been employed in undertakings of “great public utility largely increasing the wealth of the country”’.

### **Exceptions to the principle of limited liability**

- Members are severally liable in certain cases- if at any time the number of members of a company is reduced, in the case of a public company, below seven, in the case of a private company, below two, and the company carries on business for more than six months while the number of members is so reduced, every person who is a member of the company during the time that it so carries on business after those six months and is cognisant of the fact that it is carrying on business with less than seven members or two members, as the case may be, shall be severally liable for the payment of the whole debts of the company contracted during that time, and may be severally sued therefor.[Section 3A]
- When the company is incorporated as an Unlimited Company under Section 3(2)(c) of the Act
- Where a company has been got incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants, direct that liability of the members of such company shall be unlimited. [Section 7(7)(b)]

- Further under section 339(1), where in the course of winding up it appears that any business of the company has been carried on with an intent to defraud creditors of the company or any other persons or for any fraudulent purpose, the Tribunal may declare the persons who were knowingly parties to the carrying on of the business in the manner aforesaid as personally liable, without limitation of liability, for all or any of the debts/liabilities of the company.[Section 339]
- Under Section 35(3), where it is proved that a prospectus has been issued with intent to defraud the applicants for the securities of a company or any other person or for any fraudulent purpose, every person who was a director at the time of issue of the prospectus or has been named as a director in the prospectus or every person who has authorised the issue of prospectus or every promoter or a person referred to as an expert in the prospectus shall be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by any person who subscribed to the securities on the basis of such prospectus.
- As per section 75(1), where a company fails to repay the deposit or part thereof or any interest thereon referred to in section 74 within the time specified or such further time as may be allowed by the Tribunal and it is proved that the deposits had been accepted with intent to defraud the depositors or for any fraudulent purpose, every officer of the company who was responsible for the acceptance of such deposit shall, without prejudice to other liabilities, also be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by the depositors.
- Section 224(5) states that where the report made by an inspector states that fraud has taken place in a company and due to such fraud any director, key managerial personnel, other officer of the company or any other person or entity, has taken undue advantage or benefit, whether in the form of any asset, property or cash or in any other manner, the Central Government may file an application before the Tribunal for appropriate orders with regard to disgorgement of such asset, property, or cash, and also for holding such director, key managerial personnel, officer or other person liable personally without any limitation of liability.

#### ***(vi) Perpetual Succession***

An incorporated company never dies, except when it is wound up as per law. A company, being a separate legal person is unaffected by death or departure of any member and it remains the same entity, despite total change in the membership. Perpetual succession, means that the membership of a company may keep changing from time to time, but that shall not affect its continuity.

The membership of an incorporated company may change either because one shareholder has sold/transferred his shares to another or his shares devolve on his legal representatives on his death or he ceases to be a member under some other provisions of the Companies Act. Thus, perpetual succession denotes the ability of a company to maintain its existence by the succession of new individuals who step into the shoes of those who cease to be members of the company. Professor L.C.B. Gower rightly mentions, "Members may come and go, but the company can go on forever. During the war all the members of one private company, while in general meeting, were killed by a bomb, but the company survived — not even a hydrogen bomb could have destroyed it".

#### ***(vii) Separate Property***

A company being a legal person and entirely distinct from its members, is capable of owning, enjoying and disposing of property in its own name. The company is the real person in which all its property is vested, and by which it is controlled, managed and disposed off. Their Lordships of the Madras High Court in *R.F.*

*Perumal v. H. John Deavin*, A.I.R. 1960 Mad. 43 held that “no member can claim himself to be the owner of the company’s property during its existence or in its winding-up”. A member does not even have an insurable interest in the property of the company.

### CASE EXAMPLE

#### ***Mrs. Bacha F. Guzdar v. The Commissioner of Income Tax, Bombay, A.I.R. 1955 S.C. 74***

The Supreme Court in this case held that, though the income of a tea company is entitled to be exempted from Income-tax up to 60% being partly agricultural, the same income when received by a shareholder in the form of dividend cannot be regarded as agricultural income for the assessment of income-tax. It was also observed by the Supreme Court that a shareholder does not, as is erroneously believed by some people, become the part owner of the company or its property; he is only given certain rights by law, e.g., to receive notice of or to attend or vote at the meetings of the shareholders. The court refused to identify the shareholders with the company and reiterated the distinct personality of the company.

#### ***(viii) Transferability of Shares***

The capital of a company is divided into parts, called shares. The shares are said to be movable property and, subject to certain conditions, freely transferable, so that no shareholder is permanently or necessarily wedded to a company. When the joint stock companies were established, the object was that their shares should be capable of being easily transferred. Section 44 of the Companies Act, 2013 enunciates the principle by providing that the shares held by the members are movable property and can be transferred from one person to another in the manner provided by the articles. If the articles do not provide anything for the transfer of shares and the Regulations contained in Table “F” in Schedule I to the Companies Act, 2013, are also expressly excluded, the transfer of shares will be governed by the general law relating to transfer of movable property.

A member may sell his shares in the open market and realise the money invested by him. This provides liquidity to a member (as he can freely sell his shares) and ensures stability to the company (as the member is not withdrawing his money from the company). The Stock Exchanges provide adequate facilities for the sale and purchase of shares.

Further, as of now, in most of the listed companies, the shares are also transferable through Electronic mode i.e. through Depository Participants in dematerialised form instead of physical transfers.

However there are restrictions with respect to transferability of shares of a Private Limited Company.

#### ***(ix) Capacity to Sue and Be Sued***

A company being a body corporate, can sue and be sued in its own name. To sue, means to institute legal proceedings against (a person) or to bring a suit in a court of law. All legal proceedings against the company are to be instituted in its name. Similarly, the company may bring an action against anyone in its own name. A company’s right to sue arises when some loss is caused to the company, i.e. to the property or the personality of the company. Hence, the company is entitled to sue for damages in libel or slander as the case may be [*Floating Services Ltd. v. MV San Fransceco Dipalao* (2004) 52 SCL 762 (Guj)]. A company, as a person distinct from its members, may even sue one of its own members.

A company has a right to seek damages where a defamatory material published about it, affects its business. Where video cassettes were prepared by the workmen of a company showing, their struggle against the company’s management, it was held to be not actionable unless shown that the contents of the cassette would be defamatory. The court did not restrain the exhibition of the cassette. [*TVS Employees Federation v.*

*TVS and Sons Ltd., (1996) 87 Com Cases 37].* The company is not liable for contempt committed by its officer. [*Lalit Surajmal Kanodia v. Office Tiger Database Systems India (P) Ltd., (2006) 129 Com Cases 192 Mad*].

### **(x) Contractual Rights**

A company, being a legal entity different from its members, can enter into contracts for the conduct of the business in its own name. A shareholder cannot enforce a contract made by his company; he is neither a party to the contract, nor be entitled to the benefit derived from of it, as a company is not a trustee for its shareholders. Likewise, a shareholder cannot be sued on contracts made by his company. The distinction between a company and its members is not confined to the rules of privity but permeates the whole law of contract. Thus, if a director fails to disclose a breach of his duties towards his company, and in consequence a shareholder is induced to enter into a contract with the director on behalf of the company which he would not have entered into had there been disclosure, the shareholder cannot rescind the contract.

Similarly, a member of a company cannot sue in respect of torts committed against the company, nor can he be sued for torts committed by the company. Therefore, the company as a legal person can take action to enforce its legal rights or be sued for breach of its legal duties. Its rights and duties are distinct from those of its constituent members.

### **(xi) Limitation of Action**

A company cannot go beyond the power stated in its Memorandum of Association. The Memorandum of Association of the company regulates the powers and fixes the objects of the company and provides the edifice upon which the entire structure of the company rests. The actions and objects of the company are limited within the scope of its Memorandum of Association. In order to enable it to carry out its actions without such restrictions and limitations in most cases, sufficient powers are granted in the Memorandum of Association. But once the powers have been laid down, it cannot go beyond such powers unless the Memorandum of Association, itself altered prior to doing so.

### **(xii) Separate Management**

As already noted, the members may derive profits without being burdened with the management of the company. They do not have effective and intimate control over its working and they elect their representatives as Directors on the Board of Directors of the company to conduct corporate functions through managerial personnel employed by them. In other words, the company is administered and managed by its managerial personnel.

### **(xiii) Voluntary Association for Profit**

A company is a voluntary association for profit. It is formed for the accomplishment of some stated goals and whatsoever profit is gained is divided among its shareholders or saved for the future expansion of the company. Only a Section 8 company can be formed with no profit motive.

### **(xiv) Termination of Existence**

A company, being an artificial juridical person, does not die a natural death. It is created by law, carries on its affairs according to law throughout its life and ultimately is effaced by law. Generally, the existence of a company is terminated by means of winding up. However, to avoid winding up, sometimes companies adopt strategies like reorganisation, reconstruction and amalgamation.

To sum up, “a company is a voluntary association for profit with capital divisible into transferable shares with limited liability, having a distinct corporate entity and a common seal with perpetual succession”.

### COMPANY VIS-A-VIS OTHER FORMS OF BUSINESS

Though there are a number of similarities between a limited company and other forms of associations, there are a great number of dissimilarities as well. In the following paragraphs, a limited company is distinguished from a partnership firm, a Hindu Undivided Family (HUF) business and a LLP.

### Distinction between Partnership Firm and Company

The principal points of distinction between a partnership firm and a company are as follows:

Partnership Firm	Company
A partnership firm is not distinct from the several persons who form the partnership.	A company is a distinct legal person.
In a partnership, the property of the firm is the property of the individuals comprising it.	In a company, it belongs to the company and not to the individuals who are its members.
Creditors of a partnership firm are creditors of individual partners and a decree against the firm can be executed against the partners jointly and severally.	The creditors of a company can proceed only against the company and not against its members.
Partners are the agents of the firm. A partner can dispose of the property and incur liabilities as long as he acts in the course of the firm's business.	Members of a company are not its agents. A member of a company cannot dispose of the property and incur liabilities in the course of the company's business.
A partner cannot contract with his firm.	A member can contract with his company.
A partner cannot transfer his share and make the transferee a member of the firm without the consent of the other partners.	A company's share can ordinarily be transferred
A partner's liability is always unlimited.	The liability of shareholder may be limited either by shares or a guarantee.
The death or insolvency of a partner dissolves the firm, unless otherwise provided.	A company has perpetual succession, i.e. the death or insolvency of a shareholder or all of them does not affect the life of the company.
The accounts of a firm are audited at the discretion of the partners.	A company is required to have its accounts audited annually by a chartered accountant.
A partnership firm, on the other hand, is the result of an agreement and can be dissolved at any time by agreement among the partners.	A company, being a creation of law, can only be dissolved as laid down by law.

### Distinction between a Hindu Undivided Family Business and a Company

Hindu Undivided Family Business	Company
A Hindu Undivided Family Business consists of homogenous (unvarying) members since it consists of members of the joint family itself.	A company consists of heterogeneous (varied or diverse) members.
In a Hindu Undivided Family business the <i>Karta</i> (manager) has the sole authority to contract debts for the purpose of the business, other coparceners cannot do so.	There is no such system in a company.
A person becomes a member of a Hindu Undivided Family business by virtue of birth.	There is no provision to that effect in the company.
No registration is compulsory for carrying on business for gain by a Hindu Undivided Family even if the number of members exceeds twenty [ <i>Shyamal Roy v. Madhusudan Roy</i> , AIR 1959 Cal. 380 (385)].	Registration of a company is compulsory.

### Distinction between Limited Liability Partnership (LLP) and a Company

LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership. LLP can continue its existence irrespective of changes in partners. It is capable of entering into contracts and holding property in its own name. LLP is a separate legal entity, is liable to the full extent of its assets but liability of the partners is limited to their agreed contribution in the LLP.

Further, no partner is liable on account of the independent or un-authorized actions of other partners, thus individual partners are shielded from joint liability created by another partner's wrongful business decisions or misconduct.

Mutual rights and duties of the partners within a LLP are governed by an agreement between the partners or between the partners and the LLP as the case may be. The LLP, however, is not relieved of the liability for its other obligations as a separate entity.

Since LLP contains elements of both 'a corporate structure' as well as 'a partnership firm structure' LLP is called a hybrid between a company and a partnership.

LLP is a body corporate and a legal entity separate from its partners, having perpetual succession. LLP form is a form of business model which :(i) is organized and operates on the basis of an agreement.(ii) provides flexibility without imposing detailed legal and procedural requirements (iii) enables professional/technical expertise and initiative to combine with financial risk taking capacity in an innovative and efficient manner.

A basic difference between an LLP and a company lies in that the internal governance structure of a company is regulated by statute (i.e. Companies Act) whereas for an LLP it would be by a contractual agreement between partners.

The management-ownership divide inherent in a company is not there in a limited liability partnership. LLP have more flexibility as compared to a company. LLP have lesser compliance requirements as compared to a company.

## DOCTRINE OF LIFTING OF OR PIERCING THE CORPORATE VEIL

The separate personality of a company is a statutory privilege and it must be used for legitimate business purposes only. Where a fraudulent and dishonest use is made of the legal entity, the individuals concerned will not be allowed to take shelter behind the corporate personality. The Court will break through the corporate shell and apply the principle/doctrine of what is called as “lifting of or piercing the corporate veil”. The Court will look behind the corporate entity and take action as though no entity separate from the members existed and make the members or the controlling persons liable for debts and obligations of the company.

The corporate veil is lifted when in defence proceedings, such as for the evasion of tax, an entity relies on its corporate personality as a shield to cover its wrong doings. [*BSN (UK) Ltd. v. Janardan Mohandas Rajan Pillai* [1996] 86 Com Cases 371 (Bom).]

However, the shareholders cannot ask for the lifting of the veil for their purposes. This was held in *Premlata Bhatia v. Union of India* (2004) 58 CL 217 (Delhi) wherein the premises of a shop were allotted on a licence to the individual licensee. She set up a wholly owned private company and transferred the premises to that company without Government consent. She could not remove the illegality by saying that she and her company were virtually the same person.

### Statutory Recognition of Lifting of Corporate Veil

The Companies Act, 2013 itself contains some provisions [Sections 7(7), 251(1) and 339] which lift the corporate veil to reach the real forces of action. Section 7(7) deals with punishment for incorporation of company by furnishing false information; Section 251(1) deals with liability for making fraudulent application for removal of name of company from the register of companies and Section 339 deals with liability for fraudulent conduct of business during the course of winding up.

### Lifting of Corporate Veil under Judicial Interpretation

Ever since the decision in *Salomon v. Salomon & Co. Ltd.*, (1897) A.C. 22, normally Courts are reluctant or at least very cautious to lift the veil of corporate personality to see the real persons behind it. Nevertheless, Courts have found it necessary to disregard the separate personality of a company in the following situations:

- (a) **Where the corporate veil has been used for commission of fraud or improper conduct. In such a situation, Courts have lifted the veil and looked at the realities of the situation.**

## CASE EXAMPLE

### In *Jones v. Lipman*, (1962) 1 W.L.R. 832

A agreed to sell certain land to B. Pending completion of formalities of the said deal, A sold and transferred the land to a company which he had incorporated with a nominal capital of £100 and of which he and a clerk were the only shareholders and directors. This was done in order to escape a decree for specific performance in a suit brought by B. The Court held that the company was the creature of A and a mask to avoid recognition and that in the eyes of equity A must complete the contract, since he had the full control of the limited company in which the property was vested, and was in a position to cause the contract in question to be fulfilled.

**(b) Where a corporate facade is really only an agency instrumentality.**

### CASE EXAMPLE

In *Re. R.G. Films Ltd.* (1953) 1 All E.R. 615

An American company produced a film in India technically in the name of a British Company, 90% of whose capital was held by the President of the American company which financed the production of the film. Board of Trade refused to register the film as a British film which stated that English company acted merely as the nominee of the American corporation.

**(c) Where the conduct conflicts with public policy, courts lifted the corporate veil for protecting the public policy.**

### CASE EXAMPLE

In *Connors Bros. v. Connors* (1940) 4 All E.R. 179

The principle was applied against the managing director who made use of his position contrary to public policy. In this case the House of Lords determined the character of the company as "enemy" company, since the persons who were *de facto* in control of its affairs, were residents of Germany, which was at war with England at that time. The alien company was not allowed to proceed with the action, as that would have meant giving money to the enemy, which was considered as monstrous and against "public policy".

**(d) Further, In *Daimler Co. Ltd. v. Continental Tyre & Rubber Co.*, (1916) 2 A.C. 307, it was held that a company will be regarded as having enemy character, if the persons having de facto control of its affairs are resident in an enemy country or, wherever they may be, are acting under instructions from or on behalf of the enemy.**

**(e) Where it was found that the sole purpose for which the company was formed was to evade taxes the Court will ignore the concept of separate entity and make the individuals concerned liable to pay the taxes which they would have paid but for the formation of the company.**

### CASE EXAMPLE

*Re. Sir Dinshaw Maneckjee Petit*, A.I.R. 1927 Bombay 371

The facts of the case are that the assessee was a wealthy man enjoying large dividend and interest income. He formed four private companies and agreed with each to hold a block of investment as an agent for it. Income received was credited in the accounts of the company but the company handed back the amount to him as a pretended loan. This way he divided his income in four parts in a bid to reduce his tax liability.

But it was held "the company was formed by the assessee purely and simply as a means of avoiding super-tax and the company was nothing more than the assessee himself. It did no business, but was created simply as a legal entity to ostensibly receive the dividends and interests and to hand them over to the assessee as pretended loans". The Court decided to disregard the corporate entity as it was being used for tax evasion.

### Vodafone case

One of the most recent and also a landmark case of the Supreme Court, is its decision in the case of *Vodafone International Holdings B.V. v. Union of India & Another* [S.L.P. (C) No. 26529 of 2010]. In judgment,

the Supreme Court set aside the Bombay High Court's judgment directing Vodafone International Holdings BV ("Vodafone"), to pay INR 110 billion, as withholding tax in a transaction that took place off-shore.

The facts, as briefly put, are that in May 2007, Vodafone, incorporated in the Netherlands, acquired from Hong Kong based Hutchison Group, the entire share capital of CGP Investments (Holdings) Limited ("CGP"), a company incorporated in the Cayman Islands, which in turn controlled a 67% interest in Hutchison-Essar Limited ("HEL"), Hutchison's Indian mobile business. The Indian income tax authorities contended that capital gains were made by Hutchison in India and that Vodafone was therefore liable to pay withholding tax thereon, amounting to approximately INR 110 billion (the sale price being USD 11.2 billion).

Vodafone challenged the tax demand in the Bombay High Court, which ruled in favour of the income tax authorities, holding that the essence of the transaction was a change in the controlling interest in HEL, which constituted a source of income in India. Vodafone appealed to the Supreme Court, which overruled the High Court and held that the transaction fell outside India's territorial tax jurisdiction and was hence not taxable.

The judgment was not only important in the context of taxation, but also covers other issues of corporate law. One of these is in the context of the principle of the corporate veil, and the circumstances under which it may be lifted, particularly in the context of commercial cross-border transactions and tax avoidance.

The Court recognised the fundamental principle of the corporate veil by noting that, "The approach of both the corporate and tax laws, particularly in the matter of corporate taxation, generally is founded on the abovementioned separate entity principle, i.e., treat a company as a separate person. The Indian Income Tax Act, 1961, in the matter of corporate taxation, is founded on the principle of the independence of companies and other entities subject to income-tax." It observed in the context of parent / subsidiary relationships, that it is generally accepted that the group parent company would give guidance to group subsidiaries, but that by itself would not justify piercing the veil or imply that the subsidiaries are to be deemed residents of the State in which the parent company resides, and that "a subsidiary and its parent are totally distinct tax payers".

Six factors that may be considered to determine whether the transaction is a bogus and whether in a specific case, the corporate veil may be lifted, are: "(i) the concept of participation in investment, (ii) the duration of time during which the Holding Structure exists; (iii) the period of business operations in India; (iv) the generation of taxable revenues in India; (v) the timing of the exit; and (vi) the continuity of business on such exit."

In the final analysis, the Supreme Court decided against lifting the corporate veil in Vodafone, as the tax authorities failed to establish that the transaction was a bogus or tax avoidance scheme.

**(f) Avoidance of welfare legislation is as common as avoidance of taxation and the approach in considering problems arising out of such avoidance has necessarily to be the same and, therefore, where it was found that the sole purpose for the formation of the new company was to use it as a device to reduce the amount to be paid by way of bonus to workmen, the Supreme Court upheld the piercing of the veil to look at the real transaction.**

### CASE EXAMPLE

*The Workmen Employed in Associated Rubber Industries Limited, Bhavnagar v. The Associated Rubber Industries Ltd., Bhavnagar and another, A.I.R. 1986 SC 1.*

The facts of the case were that a new company was created wholly by the principal company with no assets of its own except those transferred to it by the principal company, with no business or income of its own except

receiving dividends from shares transferred to it by the principal company i.e. only for the purpose of splitting the profits into two hands and thereby reducing the obligation to pay bonus. The Supreme Court of India held that the new company was formed as a device to reduce the gross profits of the principal company and thereby reduce the amount to be paid by way of bonus to workmen. The amount of dividends received by the new company should, therefore, be taken into account in assessing the gross profit of the principal company.

**(g) Another instance of corporate veil arrived at by the Court arose in *Kapila Hingorani v. State of Bihar*.**

### CASE EXAMPLE

*Kapila Hingorani v. State of Bihar*, 2003(4) Scale 712

In this case, the petitioner had alleged that the State of Bihar had not paid salaries to its employees in PSUs etc. for long periods resulting in starvation deaths. But the respondent took the stand that most of the undertakings were incorporated under the provisions of the Companies Act, 1956, hence the rights etc. of the shareholders should be governed by the provisions of the Companies Act and the liabilities of the PSUs should not be passed on to the State Government by resorting to the doctrine of lifting the corporate veil. The Court observed that the State may not be liable in relation to the day-to-day functioning of the PSUs but its liability would arise on its failure to perform the constitutional duties and the functions of these undertakings. It is so because, "life means something more than mere ordinal existence. The inhibition against deprivation of life extends to all those limits and faculties by which life is enjoyed".

**(h) Where it is found that a company has abused its corporate personality for an unjust and inequitable purpose, the court would not hesitate to lift the corporate veil. Further, the corporate veil could be lifted when acts of a corporation are allegedly opposed to justice, convenience and interests of revenue or workmen or are against public interest.**

Thus, in appropriate cases, the Courts disregard the separate corporate personality and look behind the legal person or lift the corporate veil.

### Lifting the Corporate Veil of Small Scale Industry

Where small scale industries were given certain exemptions and the company owning an industry was controlled by some group of persons or companies, it was held that it was permissible to lift the veil of the company to see whether it was the subsidiary of another company and, therefore, not entitled to the proposed exemptions. [*Inalsa Ltd. v. Union of India*, (1996) 87 Com Cases 599 (Delhi).]

### Use of Corporate Veil for Hiding Criminal Activities

Where the defendant used the corporate structure as a device or facade to conceal his criminal activities (evasion of customs and excise duties payable by the company), the Court could lift the corporate veil and treat the assets of the company as the realisable property of the shareholder.

For example, in a case, there was a prima facie case that the defendants controlled the two companies, the companies had been used for the fraudulent evasion of excise duty on a large scale, the defendant regarded the companies as carrying on a family business and that they had benefited from companies' cash in substantial amounts and further no useful purpose would have been served by involving the companies in the criminal proceedings. In all these circumstances it was therefore appropriate to lift the corporate veil and treat the stock in the companies' warehouses and the companies' motor vehicles as realisable property held by the defendants. The court said that the excise department is not to be criticized for not charging the companies. The more complex commercial activities become, the more vital it is for prosecuting authorities to be selective in whom and what they charge, so that issues can be presented in as clear and short form as possible. In the

present case, it seemed that no useful purpose would have been served by initiating criminal proceedings. [*H. and Others (Restraint Order : Realisable Property), Re, (1996) 2 BCLC 500 at 511, 512 (CA).*]

## APPLICABILITY OF COMPANIES ACT, 2013 AND KEY CONCEPTS

### (A) Applicability

According to section 1 of the Companies Act, 2013, the Act extends to whole of India and the provisions of the Act shall apply to the following:-

- (a) companies incorporated under this Act or under any previous company law;
- (b) insurance companies, except in so far as the said provisions are inconsistent with the provisions of the Insurance Act, 1938 (4 of 1938) or the Insurance Regulatory and Development Authority Act, 1999 (41 of 1999);
- (c) banking companies, except in so far as the said provisions are inconsistent with the provisions of the Banking Regulation Act, 1949 (10 of 1949);
- (d) companies engaged in the generation or supply of electricity, except in so far as the said provisions are inconsistent with the provisions of the Electricity Act, 2003 (36 of 2003);
- (e) any other company governed by any special Act for the time being in force, except in so far as the said provisions are inconsistent with the provisions of such special Act; and
- (f) such body corporate, incorporated by any Act for the time being in force, as the Central Government may, by notification, specify in this behalf, subject to such exceptions, modifications or adaptation, as may be specified in the notification.

Companies Act, 2013 is not applicable to unincorporated companies. An unincorporated company, association or partnership consisting of large number of persons has been declared illegal.

By virtue of section 464 of the Companies Act, 2013, no association or partnership consisting of more than such number of persons as may be prescribed shall be formed for the purpose of carrying on any business that has for its object the acquisition of gain by the association or partnership or by the individual members thereof, unless it is registered as a company under this Act or is formed under any other law for the time being in force. Rule 10 of Companies( Miscellaneous) Rules, 2014 prescribes 50 persons in this regard. The maximum number of persons which may be prescribed under this section shall not exceed 100.

Section 464 of the Act does not apply to the case of a Hindu undivided family carrying on any business whatever may be the number of its members. However, this section is also not applicable to an association or partnership, if it is formed by professionals who are governed by special Acts.

### B. Key Concepts

The 2013 Act has introduced several new concepts and has also tried to streamline many of the requirements by introducing new definitions. Some of the concepts are discussed here in brief.

#### 1. Companies

- 1.1 One-person company: The 2013 Act introduces a new type of entity to the existing list i.e. apart from forming a public or private limited company, the Act enables the formation of a new entity a 'one-person company' (OPC). An OPC means a company with only one person as its member (section 3(1)).
- 1.2. Private company: The 2013 Act introduces a change in the definition for a private company,

inter-alia, the new requirement increases the limit of the number of members from 50 to 200. [section 2(68).

- 1.3. Small company: A small company has been defined as a company, other than a public company.
- (i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees; and
  - (ii) turnover of which as per profit and loss account for the immediately preceding financial year does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than one hundred crore rupees:
- Provided** that nothing in this clause shall apply to—
- (A) a holding company or a subsidiary company;
  - (B) a company registered under section 8; or
  - (C) a company or body corporate governed by any special Act; (section 2(85)).
- 1.4 Dormant company: A company formed and registered under this 2013 for a future project or to hold an asset or intellectual property and has no significant accounting transaction such a company or an inactive company may make an application to the Registrar for obtaining the status of a dormant company. (Section 455)
- 1.5 Nidhi company: Nidhi Company means a company which has been incorporated as a Nidhi with the object of cultivating the habit of thrift and savings amongst its members, receiving deposits from, and lending to, its members only, for their mutual benefit, and which complies with such rules as are prescribed by the Central Government for regulation of such class of companies. (section 406)

## 2. Roles and responsibilities

- 2.1 Officer: The definition of officer has been extended to include promoters and key managerial personnel (section 2(59)).
- 2.2 Key managerial personnel: The term 'key managerial personnel' has been defined in the Act which 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; and
  - (vi) such other officer as may be prescribed (section 2(51)).

The role and liability have been defined at various places under the Act.

- 2.3. Promoter: The term 'promoter' means a person—
- (a) who has been named as such in a prospectus or is identified by the company in the annual return; or
  - (b) who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or

(c) in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act:

Provided that nothing in sub-clause (c) shall apply to a person who is acting merely in a professional capacity. (section 2(69))

2.4 Independent Director: The term 'Independent Director' has been defined in the Act, along with several new requirements relating to their appointment, role and responsibilities. Further some of these requirements are not in line with the corresponding requirements under the equity listing agreement (section 2(47), 149(5)).

### 3. Audit and auditors

3.1 Mandatory auditor rotation and joint auditors: The Act mandates the rotation of auditors after the specified time period. (Section 139).

3.2. Secretarial audit: The Act mandates Secretarial Audit for the following:

- (a) Listed companies
- (b) every public company having a paid-up share capital of fifty crore rupees or more;
- (c) every public company having a turnover of two hundred fifty crore rupees or more.

The Secretarial Audit Report is required to be annexed to the Board's Report (Sec 204)

3.3 Secretarial Standards: The Act requires every company to observe secretarial standards specified by the Institute of Company Secretaries of India with respect to general and board meetings (Section 118 (10)).

4. Corporate Social Responsibility- The Act introduces the culture of corporate social responsibility (CSR) in Indian corporates by requiring companies to formulate a corporate social responsibility policy and at least incur a given minimum expenditure on social activities.

5. Class action suits- The Act introduces a new concept of class action suits which can be initiated by shareholders against the company and auditors.

## FORMATION AND INCORPORATION OF COMPANIES

Section 3(1) states that a company may be formed for any lawful purpose by—

- (a) seven or more persons, where the company to be formed is to be a public company;
- (b) two or more persons, where the company to be formed is to be a private company; or
- (c) one person, where the company to be formed is to be One Person Company that is to say, a private company by subscribing their names or his name to a memorandum and complying with the requirements of this Act in respect of registration.

A company formed under Section 3(1) may be either—

- (a) a company limited by shares; or
- (b) a company limited by guarantee; or
- (c) an unlimited company.

Section 7(1) of the Act provides for the detailed procedure for incorporation of company.

*(Note: For details on Types of Companies and Formation of Companies - you may refer Paper 3 of Module 1 i.e. "Setting up of Business Entities and Closure")*

## LESSON ROUND-UP

- The word 'company' is derived from the Latin word (Com = with or together; panis = bread), and it originally referred to an association of persons who took their meals together.
- The main characteristics of a company are corporate personality, limited liability, perpetual succession, separate property, transferability of shares, capacity to sue and be sued, contractual rights, limitation of action, separate management, termination of existence etc.
- The company, though a legal person, is not a citizen under the Citizenship Act, 1955 or the Constitution of India. Though it has established through judicial decisions that a company cannot be a citizen, yet it has nationality, domicile and residence.
- In India after independence, the Companies Act, 1956 was enacted with a view to consolidate and amend the earlier laws relating to companies and certain other associations.
- The Companies Act, 2013 has replaced the Companies Act, 1956. Further the Act has been amended four times.
- Where a fraudulent and dishonest use is made of the legal entity, the individuals concerned will not be allowed to take shelter behind the corporate personality. The Court may break through the corporate shell and apply the principle of what is known as "lifting of or piercing the corporate veil".

## GLOSSARY

Jurisprudence	The study of law and the principles on which law is based
Ordinance	Ordinances are temporary laws that are promulgated by the President of India on the recommendation of the Union Cabinet. Article 123 of Constitution of India provide for power of President to promulgate Ordinances during recess of Parliament. They enable the government to take immediate legislative action. Ordinances cease to operate either if Parliament does not approve of them within six weeks of reassembly, or if disapproving resolutions are passed by both Houses. It is also compulsory for a session of Parliament to be held within six months of passing an ordinance.
Bill	A bill is proposed legislation under consideration by a legislature. A bill does not become law until it is passed by the legislature. Once a bill has been enacted into law, it is called an act of the legislature, or a statute.

## SELF-TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

1. Answer on the following:
  - (a) Four persons are the only members of a private company. All of them go for a pleasure trip in a car and due to an accident all the four die. Does the private company exist?
  - (b) The members of a private limited company consist of 'A' and 'B' who are also its directors. On 4th August, 2015 'A' left India for a foreign business tour and on 28th August, 2015 he died

abroad. On 1st September, 2015 'B' purchased on credit ₹10,000 worth of goods from 'C' on behalf of the company. 'C' now proposes to make 'B' personally liable for the payment of the debt. Is 'B' liable?

2. (a) What types of associations are prohibited by the Companies Act, and what are the disabilities of such associations?
  - (b) "Members of a Limited Company may nevertheless have unlimited liability." Comment.
  - (c) What do you understand by corporate veil and when is it disregarded?
3. State the consequences in each of the following cases giving reasons for your answers:
  - (a) A Private Company has 210 members in total of which 10 are the employees of the company. 5 of these employees leave the employment of the company.
  - (b) A private firm has 20 partners, including a private company which is having 30 shareholders.
4. "The fundamental attribute of corporate personality is that the company is a legal entity distinct from the members." Elucidate the above statement.
5. What are the advantages of an incorporated company compared to partnership firms and unincorporated companies?
6. Write short notes on:
  - (a) Perpetual succession
  - (b) Transferability of shares
  - (c) Limited liability
  - (d) Corporate personality
  - (e) One man company.
7. Examine the following and say whether they are correct or wrong:
  - (a) A company being an artificial person cannot own property and cannot sue or be sued.
  - (b) Members are the owners of the company's undertaking.
  - (c) The term "body corporate" connotes a wider meaning than the term "company".
  - (d) Every member of an illegal association shall be personally liable for all liabilities incurred in carrying on the business.
  - (e) A company is a juristic legal person.



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# Lesson 2

## Share Capital

### LESSON OUTLINE

- Meaning and types of Capital
- Concept of issue and allotment
- Issue of Share certificates
- Further Issue of Share Capital
- Issue of shares on Private and Preferential basis
- Rights issue and Bonus Shares
- Sweat Equity Shares and ESOPs
- Issue and Redemption of preference shares
- Transfer and Transmission of securities
- Buyback of securities
- Dematerialization and Rematerialization of shares
- Reduction of Share Capital
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

Share is a share in the share capital of the company.

Share capital refers to the funds that a company raises in exchange for issuing an ownership interest in the company in the form of shares. "share capital" may also describe the number and types of shares that compose a company's share structure. There are two general types of share capital, which are common stock and preferred stock.

There are various ways to raise capital which include preferential allotment, employee stock option, issue of rights shares and issue of shares with differential voting rights. It involves various approvals, disclosures, filings, maintenance of records, etc. which are prescribed under Chapter IV of the Companies Act, 2013 read with Companies (Share Capital and Debentures) Rules, 2014.

The chapter also introduces the manner of issue of securities and allotment thereunder.

The chapter is divided into six parts for easy understanding

PART A: Meaning and types of share capital

PART B: Concept of Issue and Allotment

PART C – Issue of Securities

Part D- Buy Back of Securities

Part E- Reduction of share capital

Part F- Transferability- A Brief on Provisions of Companies Act, 2013

A company secretary should be well versed with the technicalities of the subject. This chapter will aid understanding in complete legal and practical knowledge on the subject

## PART A: Meaning and Types of Share Capital

### MEANING OF THE TERM 'CAPITAL'

The term 'Capital' has a variety of meanings. It may mean one thing to an economist, another to an accountant, while another to a businessman or a lawyer. A layman views capital as the money, which a company has raised by issue of its shares. It uses this money to meet its requirements by way of acquiring business premises and stock-in-trade, which are called the fixed capital and the circulating capital respectively.

The phrase "loan or borrowed capital" is sometimes used to mean money borrowed by the company and secured by issuing debentures and other securities. This, however, is not the proper use of the word 'capital'.

In relation to a company limited by shares, the word 'capital' means the share capital *i.e.*, the capital in terms of rupees divided into specified number of shares of a fixed amount each. For example share capital of a company is ₹1,00,000 which can be divided into 10,000 shares of ₹10 each or 1,000 shares of ₹100 each, whichever is feasible to the company.

### Classification of Share Capital

In Company Law, Capital is the share capital of a company, which is classified as:



S. No.	Type of Capital	Section under Companies Act, 2013	Definition
(a)	<b>Nominal, Authorised or Registered Capital</b>	2(8)	Such capital as is authorised by the memorandum of a company to be the maximum amount of share capital of the company.
(b)	<b>Issued Capital</b>	2(50)	Such capital as the company issues from time to time for subscription. It is that part of the authorised or nominal capital which the company issues for the time being for public subscription and allotment. This is computed at the face or nominal value.
(c)	<b>Subscribed Capital</b>	2(86)	Such part of the capital which is for the time being subscribed by the members of a company. It is that portion of the issued capital at face value which has been subscribed for or taken up by the subscribers of

			shares in the company. It is clear that the entire issued capital may or may not be subscribed.
(d)	<b>Called-up Capital</b>	2(15)	Such part of the capital, which has been called for payment. It is that portion of the subscribed capital which has been called up or demanded on the shares by the company.
(e)	<b>Paid-up Share Capital</b>	2(64)	Such aggregate amount of money credited as paid-up as is equivalent to the amount received as paid-up in respect of shares issued and also includes any amount credited as paid-up in respect of shares of the company, but does not include any other amount received in respect of such shares, by whatever name called.
(f)	<b>Equity Preference Share Capital (Discussed later)</b> &	Explanation under Section 43	<p><b>“equity share capital”</b>, with reference to any company limited by shares, means all share capital which is not preference share capital;</p> <p><b>“preference share capital”</b>, with reference to any company limited by shares, means that part of the issued share capital of the company which carries or would carry a preferential right with respect to—</p> <ol style="list-style-type: none"> <li>payment of dividend, either as a fixed amount or an amount calculated at a fixed rate, which may either be free of or subject to income-tax; and</li> <li>repayment, in the case of a winding up or repayment of capital, of the amount of the share capital paid-up or deemed to have been paid-up, whether or not, there is a preferential right to the payment of any fixed premium or premium on any fixed scale, specified in the memorandum or articles of the company;</li> </ol>

### PUBLICATION OF AUTHORISED, SUBSCRIBED AND PAID-UP CAPITAL

It is provided under section 60 of the Act that where any notice, advertisement or other official publication, or any business letter, billhead or letter paper of a company contains a statement of the amount of the authorised capital of the company, such notice, advertisement or other official publication, or such letter, billhead or letter paper shall also contain a statement, in an equally prominent position and in equally conspicuous characters, of the amount of the capital which has been subscribed and the amount paid-up.

In case of failure in complying with the afore mentioned requirements, the company shall be liable to pay a penalty of ten thousand rupees and every officer of the company who is in default shall be liable to pay a penalty of five thousand rupees, for each default.

### SHARE AND TYPES OF SHARE CAPITAL

As defined earlier a share means “a share in the share capital of a company, and includes stock except where a distinction between stock and shares is expressed or implied.”

## Nature of a Share

- (a) A share is a right to a specified amount of the share capital of a company, carrying with it certain rights and liabilities while the company is a going concern and in its winding up. (Halsbury's Laws of England)
- (b) A share is a right to participate in the profits made by a company, while it is a going concern.
- (c) Section 44 of the Companies Act, 2013 provides that a share or other interest of any member in a company is a movable property transferable in the manner provided by the articles of the company.
- (d) In India, a share is regarded as goods. According to the Sale of Goods Act, 1930, "Goods" means any kind of movable property other than actionable claim and money, and includes stock and shares.
- (e) According to Section 45 of the Companies Act, 2013 every share in a company having a share capital shall be distinguished by its distinctive number but this provision shall not apply to a share held by a person whose name is entered as holder of beneficial interest in such share in the records of a depository.

## Share Capital

### Preference Share Capital

### Equity Share Capital

Share capital is of two kinds- Preference and equity share capital (definitions stated above). A Preference share, which receive dividends before ordinary shares but which have no voting rights, it must satisfy the following conditions:

- As regards dividends, it must carry a preferential right to fixed amount or amount calculated at a fixed rate and
- As regards the capital, in the event of a winding up or other arrangement to repayment of capital, there must be a preferential right to be repaid the amount of the capital paid up on such share. A Preference share capital may or may not carry such other rights as specified.

All share capital, not falling within the above description of preference capital, is equity share capital, which has no guaranteed amount of dividend but carries voting rights.

Some illustrative rights attached to the equity shareholding are as under:

- Right to vote
- Right to receive dividends
- Right to transfer freely without any restriction. The Equity share capital is sub-divided into shares with equal voting rights and shares with differential voting rights as to dividend, voting or otherwise.

Equity capital is also known as "Common Stock" or common share capital that represents ownership in a company. Common share capital is generally divided into units known shares. These unit holders are called equity shareholders. They are the real owners of the company and policy makers of the company. However, they do not have access to the day to day affairs of the company. They appoint their representatives called board of directors to look after the affairs of the company. Equity shareholders are entitled to vote on

resolutions of the company, get a return by way of dividend if declared and take part in surplus in assets of the company at time of winding-up.

**Part B: Concept of Issue and Allotment**

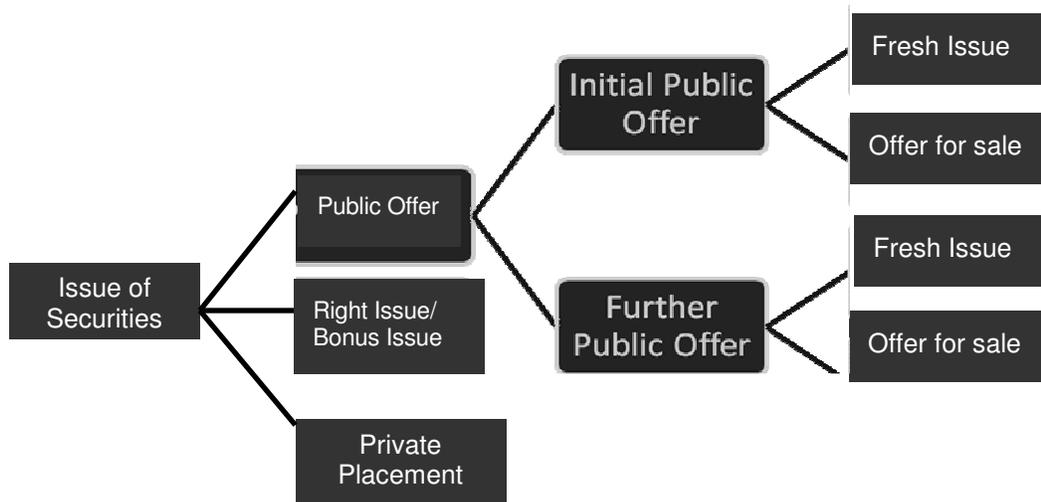
Financial markets have an important relationship with economic development. A company decides to issue securities for different reasons; the main reason being raising capital to meet its financial requirements may be for starting a venture, repaying debts, expansion and diversification. This actually reflects indulgence of enormous investor wealth for the sublime reason of economic development. This economic dependence of the corporate sector is a compelling rationale for an orderly regulated environment that boosts investor confidence and assures conformity with prescribed norms. It helps in creating conducive ownership base and wide capacities to create an impact on the national economy. When an investor buys securities he is enabling the company to carry on its business using those funds.

In India a company planning to issue securities shall abide by relevant provisions of

- (a) Securities Contracts (Regulation) Act, 1956,
- (b) Securities Contracts (Regulation) Rules, 1957,
- (c) Companies Act, 2013 (hereinafter referred to as the Act),
- (d) Securities and Exchange Board of India Act, 1992 and the rules and regulations made thereunder.

**OVERVIEW OF ISSUE OF SECURITIES**

Primarily, issues can be classified as a Public, Rights or preferential issues (also known as private placements). While public and rights issues involve a detailed procedure, private placements or preferential issues are relatively simpler.



Chapter III of the Companies Act, 2013 deals with “Prospectus and allotment of securities”, the chapter is divided into two parts, Part I deals with Public Offer and Part II deals with Private Placement.

Section 23 of the Companies Act, 2013 provides that a company whether public or private may issue securities. A public company may issue securities:

- (a) to public through prospectus ("public offer") by complying with the provisions of Part I of Chapter III of the Act; or
- (b) through private placement by complying with the provisions of Part II of Chapter III of the Act; or
- (c) through a rights issue or a bonus issue in accordance with the provisions of this Act and in case of a listed company or a company which intends to get its securities listed also with the provisions of the SEBI Act, 1992 and the rules and regulations made thereunder.

For a private company the section provides that a private company may issue securities (a) by way of rights issue or bonus issue in accordance with the provisions of this Act; or (b) through private placement by complying with the provisions of Part II Chapter III of the Act.

The section deals with issue of securities, which is a wider term not restricted to equity, preference or debentures. Securities has been defined under section 2(81) to mean the securities as defined in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956. The relevant section lays that securities include:-

As per Section 2(h) of the Securities Contracts (Regulation) Act, 1956, 'securities' include—

- (i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;
  - (ia) derivative;
  - (ib) units or any other instrument issued by any collective investment scheme to the investors in such schemes;
  - (ic) security receipt as defined in clause (zg) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
  - (id) units or any other such instrument issued to the investors under any mutual fund scheme;
  - (ie) any certificate or instrument (by whatever name called), issued to an investor by any issuer being a special purpose distinct entity which possesses any debt or receivable, including mortgage debt, assigned to such entity, and acknowledging beneficial interest of such investor in such debt or receivable including mortgage debt, as the case may be;
- (ii) Government securities;
  - (iia) such other instruments as may be declared by the Central Government to be securities; and
- (iii) rights or interests in securities.

*Thus, the word 'securities' includes shares and other instruments.*

A public company may issue any of the aforesaid securities by way of a public offer or rights/ bonus issue or private placement. Public Offer here includes initial public offer (IPO) or further public offer (FPO) of securities to the public by a company, or an offer for sale (OFS) of securities to the public by an existing shareholder, through issue of a prospectus.

Public offer has been defined for the first time Explanation to Section 23 states that "public offer" includes initial public offer or further public offer of securities to the public by a company, or an offer for sale of securities to the public by an existing shareholder, through issue of a prospectus.

To increase the accountability of companies and enhance protection to small investors the term private

placement has been defined for the first time in the Act. Explanation I to Section 42 defines private placement as any offer or invitation to subscribe or issue of securities to a select group of persons by a company (other than by way of public offer) through private placement offer-cum-application, which satisfies the conditions specified in this section.

## GOVERNING LAWS

Issue of Securities is governed in the following manner:

In the case of a Public Company, which is a listed entity or is desirous of listing its securities on the recognized stock exchange in India, the issue of securities is governed by the Companies Act, Securities Contract Regulation Act, 1956, the SEBI Act, 1992 and the Issue of Capital and Disclosure Requirements (Regulations), 2009.

In the case of all issues by Private Companies, the same is governed by the Companies Act and the power of administration is exercised by the Central Government, the Tribunal or the Registrar of Companies as the case may be.

Section 24 of the Act empowers the SEBI to regulate the matters relating to issue and transfer of securities and non-payment of dividend by listed companies or those companies which intend to get their securities listed. All powers relating to prospectus return of allotment, redemption of preference shares and any other matter specifically provided in the Act shall be exercised by the Central Government, the tribunal or the Registrar of Companies as the case may be. Further the power relating to forward dealing and insider trading has been delegated to SEBI for listed companies or the companies which intend to get their securities listed.

## PROSPECTUS

In general parlance prospectus refers to an information booklet or offer document on the basis of which an investor invests in the securities of an issuer company. It has been defined under section 2(70) so as to mean any document described or issued as a prospectus and includes a red herring prospectus referred to in section 32 or shelf prospectus referred to in section 31 or any notice, circular, advertisement or other document inviting offers from the public for the subscription or purchase of any securities of a body corporate.

Red herring Prospectus under Explanation to section 32 has been referred to mean a prospectus which does not include complete particulars of the quantum or price of the securities included therein.

Shelf Prospectus under Explanation to section 31 has been referred to mean a prospectus in respect of which the securities or class of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus.

The definition clarifies that any notice, circular, advertisement or any other document inviting offers from public for the subscription or purchase of securities shall be included in the definition of Prospectus.

### ***Matters to be stated in the prospectus***

Every Prospectus shall state such information and set out such reports on financial information as may be specified by the Securities and Exchange Board in consultation with the Central Government:

Provided that until the Securities and Exchange Board specifies the information and reports on financial information under this sub-section, the regulations made by the Securities and Exchange Board under the Securities and Exchange Board of India Act, 1992, in respect of such financial information or reports on

financial information shall apply.

## **SHELF PROSPECTUS**

Shelf Prospectus means a prospectus in respect of which the securities or class of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus. In simple terms Shelf Prospectus is a single prospectus for multiple public. Issuer is permitted to offer and sell securities to the public without a separate prospectus for each act of offering for a certain period.

Under the Act any class or classes of companies, as the Securities and Exchange Board (SEBI) may provide by regulations in this behalf, may file a shelf prospectus with the Registrar. Such prospectus is to be submitted at the stage of the first offer of securities which shall indicate a period not exceeding one year as the period of validity of such prospectus. The validity period shall commence from the date of opening of the first offer of securities under that prospectus, and in respect of a second or subsequent offer of such securities issued during the period of validity of that prospectus, no further prospectus is required.

An information memorandum is required to be filed by a company filing a shelf prospectus which shall contain all material facts relating to

- new charges created,
- changes in the financial position of the company as have occurred between the first offer of securities or the previous offer of securities and the succeeding offer of securities and
- such other changes as may be prescribed,

with the Registrar within the prescribed time, prior to the issue of a second or subsequent offer of securities under the shelf prospectus. According to the rules the information memorandum shall be prepared in Form PAS-2 and filed with the Registrar along with the fee as provided in the Companies (Registration Offices and Fees) Rules, 2014 within one month prior to the issue of a second or subsequent offer of securities under the shelf prospectus.

The section also provides a benefitting provision for the investors, the proviso provides that where a company or any other person has received applications for the allotment of securities along with advance payments of subscription before the making of any such change, the company or other person shall intimate the changes to such applicants and if they express a desire to withdraw their application, the company or other person shall refund all the monies received as subscription within fifteen days thereof.

## **RED HERRING PROSPECTUS**

Red herring Prospectus means a prospectus which does not include complete particulars of the quantum or price of the securities included therein. In simple terms a red herring prospectus contains most of the information pertaining to the company's operations and prospects, but does not include key details of the issue such as its price and the number of shares offered.

According to section 32 a company proposing to make an offer of securities may issue a red herring prospectus prior to the issue of a prospectus. Such company proposing to issue a red herring prospectus shall file it with the Registrar at least three days prior to the opening of the subscription list and the offer.

A red herring prospectus shall carry the same obligations as are applicable to prospectus and any variation between the red herring prospectus and a prospectus shall be highlighted as variations in the prospectus.

Upon the closing of the offer of securities under this section, the prospectus stating therein the total capital raised, whether by way of debt or share capital, and the closing price of the securities and any other details as are not included in the red herring prospectus shall be filed with the Registrar and the Securities and Exchange Board.

## ABRIDGED PROSPECTUS

According to section 2(1) of the Act “abridged prospectus” means a memorandum containing such salient features of a prospectus as may be specified by the Securities and Exchange Board by making regulations in this behalf.

Section 33 of the Act provides that no form of application for the purchase of any of the securities of a company shall be issued unless such form is accompanied by an abridged prospectus. A copy of the prospectus shall, on a request being made by any person before the closing of the subscription list and the offer, be furnished to him.

Nothing aforesaid shall apply if it is shown that the form of application was issued—

- (a) in connection with a bona fide invitation to a person to enter into an underwriting agreement with respect to such securities; or
- (b) in relation to securities which were not offered to the public.

The penal provisions provide that a company which makes any default in complying with the provisions shall be liable to a penalty of fifty thousand rupees for each default.

## OFFER FOR SALE

Public Offer includes or an offer for sale (OFS) of securities to the public by an existing shareholder, through issue of a prospectus.

Under section 25 of the Act where a company allots or agrees to allot any securities of the company with a view to all or any of those securities being offered for sale to the public, any document by which the offer for sale to the public is made shall, for all purposes, be deemed to be a prospectus issued by the company. In simple terms any document by which the offer or sale of shares or debentures to public is made shall for all purposes be treated as prospectus. The document “Offer for sale” is an invitation to the general public to purchase the shares of a company through an intermediary, such as an issuing house or a merchant bank. A company may allot or agree to allot any shares or debentures to an “Issue house” without there being any intention on the part of the company to make shares or debentures available directly to the public through issue of prospectus. The issue house in turn makes an “Offer for sale” to the public.

All enactments and rules of law as to the contents of prospectus and as to liability in respect of mis-statements, in and omissions from, prospectus, or otherwise relating to prospectus, shall apply to Offer for sale. Following additional information to the matters required to be stated in a prospectus:

- (a) the net amount of the consideration received or to be received by the company in respect of the securities to which the offer relates; and
- (b) the time and place at which the contract where under the said securities have been or are to be allotted may be inspected;

According to the section in order to construe “Offer for Sale” either of the following conditions needs to be

fulfilled:

- (a) "Offer for sale" to the public was made within six months after the allotment or agreement to allot; or
- (b) at the date when the offer was made, the whole consideration to be received by the company in respect of the securities had not been received by it.

As for the signing of the Prospectus the section provides that where a person making an offer to which this section relates is a company or a firm, it shall be sufficient if the Offer document is signed on behalf of the company by two directors of the company and in case of a firm by not less than one-half of the partners in the firm, as the case may be.

### **OFFER OF SALE OF SHARES BY CERTAIN MEMBERS OF A COMPANY**

Section 28 of the Act permits certain members of a company, in consultation with Board of directors, to offer the whole or a part of their holdings of shares to the public. The document by which the offer of sale to the public is made shall, for all purposes, be deemed to be a prospectus issued by the company.

All laws and rules made hereunder as to the contents of the prospectus and as to liability in respect of mis-statements in and omission from prospectus or otherwise relating to prospectus shall apply as if this is a prospectus issued by the company.

The section lays that the members, whether individuals or bodies corporate or both, whose shares are proposed to be offered to the public, shall collectively authorise the company, whose share were offered for sale to the public, to take all actions in respect of offer of sale for and on their behalf and they shall reimburse the company all expenses incurred by it on this matter.

The rules in this context provide that the provisions of Part I of Chapter III namely "Prospectus and Allotment of Securities" and rules made there under shall be applicable to an offer of sale referred to in section 28 except for the following, namely:-

- (a) the provisions relating to minimum subscription;
- (b) the provisions for minimum application value;
- (c) the provisions requiring any statement to be made by the Board of directors in respect of the utilization of money; and
- (d) any other provision or information which cannot be compiled or gathered by the offeror, with detailed justifications for not being able to comply with such provisions.

Further the rules provide that such offer document or prospectus issued under the section shall disclose the name of the entity bearing the cost of making the offer for sale along with reasons.

### **ISSUE OF SECURITIES AT A PREMIUM**

- A company may issue securities at a premium when it is able to sell them at a price above par or above nominal value. The Companies Act, 2013, does not stipulate any conditions or restrictions regulating the issue of securities by a company at a premium. However, the Companies Act does impose conditions regulating the utilization of the amount of premium collected on securities.

### **Share Premium to be transferred to 'Securities Premium Account'**

- Section 52(1) states that when a company issues shares at a premium, whether for cash or otherwise, an amount equal to the aggregate amount of the premium received on those shares shall be transferred to a "securities premium account" and the provisions of this Act relating to reduction of share capital of a company shall, except as provided in this section, apply as if the securities premium account were the paid-up share capital of the company.

### Utilisation of Securities premium

In accordance with the provisions of Section 52(2) of the Act, the securities premium can be utilised only for:

- (a) issuing fully paid bonus shares to members;
- (b) writing off the balance of the preliminary expenses of the company;
- (c) writing off commission paid or discount allowed, or the expenses incurred on issue of shares or debentures of the company;
- (d) for providing for the premium payable on redemption of any redeemable preference shares or debentures of the company; or
- (e) for the purchase of its own shares or other securities under section 68.

Section 52(3) further states that the securities premium account may, notwithstanding anything contained in sub-sections (1) and (2), be applied by such class of companies, as may be prescribed and whose financial statement comply with the accounting standards prescribed for such class of companies under section 133,—

- (a) in paying up unissued equity shares of the company to be issued to members of the company as fully paid bonus shares; or
- (b) in writing off the expenses of or the commission paid or discount allowed on any issue of equity shares of the company; or
- (c) for the purchase of its own shares or other securities under section 68.

Firstly, the premium cannot be treated as profit and as such the amount of premium is not available for distribution as dividend. Secondly, the amount of premium whether received in cash or in kind must be kept in a separate account, known as the “Securities Premium Account”. Thirdly, the amount of premium is to be maintained with the same sanctity as the share capital.

Where a company issues shares at a premium, even though the consideration may be other than cash, a sum equal to the amount or value of the premium must be transferred to the securities premium account. [*Head (Henry) & Co. Ltd. v. Ropner Holding Ltd.* (1951) 2 All ER 994: (152) Ch 124 (Ch D)].

Any premium paid does not give the shareholder any preferential rights in case of a winding up. Monies in the securities premium account cannot be treated as free reserves, as they are in the nature of capital reserve [See Departmental Circular No. 3/77 dated 15.4.1977].

### PROHIBITION TO ISSUE THE SHARES AT DISCOUNT

- Section 53 states that except as provided in section 54 (i.e. issue of sweat equity shares), a company shall not issue shares at a discount. Any share issued by a company at a discount shall be void.
- A company may issue shares at a discount to its creditors when its debt is converted into shares in pursuance of any statutory resolution plan or debt restructuring scheme in accordance with any guidelines or directions or regulations specified by the Reserve Bank of India under the Reserve Bank of India Act, 1934 or the Banking (Regulation) Act, 1949.
- When a company contravenes the provisions of this section, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees and every officer who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees, or with both.

**Let us Remember!**

1. Issue of shares at discount is prohibited except by issue of sweat equity.
2. Share premium amount is not available for distribution of dividend.

**CONCEPT OF ALLOTMENT OF SECURITIES**

Section 39 of Companies Act, 2013 deals with Allotment of Securities

*Allotment*

- Allotment of any securities of a company offered to the public for subscription shall be made only when the amount stated in the prospectus as the minimum amount has been subscribed and the sums payable on application for the amount so stated have been paid to and received by the company by cheque or other instrument.
- Whenever a company having a share capital makes any allotment of securities, it shall file with the Registrar a return of allotment, within thirty days thereafter, in Form PAS-3, along with the fee as specified in the Companies (Registration Offices and Fees) Rules, 2014.
- Alongwith Form PAS-3 a certified list of allottees stating their names, address, occupation, if any, and number of securities allotted to each of the allottees, shall be attached.
- Further, in the case of securities (not being bonus shares) allotted as fully or partly paid up for consideration other than cash, a copy of the contract, duly stamped, pursuant to which the securities have been allotted together with any contract of sale if relating to a property or an asset, or a contract for services or other consideration shall be attached to the Form PAS-3.
- When a contract is not reduced to writing, the company shall furnish along with the Form PAS-3 complete particulars of the contract stamped with the same stamp duty as would have been payable if the contract had been reduced to writing and those particulars shall be deemed to be an instrument within the meaning of the Indian Stamp Act, 1899 (2 of 1899), and the Registrar may, as a condition of filing the particulars, require that the stamp duty payable thereon be adjudicated under section 31 of the Indian Stamp Act, 1899. Further a report of a registered valuer in respect of valuation of the consideration shall also be attached along with the contract of sale if relating to property or an asset or a contract for services, as the case may be.
- In the case of issue of bonus shares, a copy of the resolution passed in the general meeting authorizing the issue of such shares shall be attached to the Form PAS-3.
- The amount payable on application on every security shall not be less than five per cent of the nominal amount of the security or such other percentage or amount, as may be specified by the SEBI by making regulations in this behalf.

*Refund of money*

In cases where the stated minimum amount has not been subscribed and the sum payable on application is not received within a period of thirty days from the date of issue of the prospectus, or such other period as may be specified by the SEBI, the amount received as above shall be returned. The application money shall be repaid within a period of fifteen days from the closure of the issue and if any such money is not so repaid within such period, the directors of the company who are officers in default shall jointly and severally be liable to repay that money with interest at the rate of fifteen percent per annum.

*Penalty for default [Section 39(5)]*

In case of any default, the company and its officer who is in default shall be liable to a penalty, for each default, of one thousand rupees for each day during which such default continues or one lakh rupees, whichever is less.

**Let us remember!**

*Whenever a company having a share capital makes any allotment of securities, it shall file with the Registrar a return of allotment in Form PAS-3 within thirty days from the date of allotment.*

**CASE LAWS****Judicial Pronouncement relating to return of allotment**

- (A) In *Sri Gopal Jalan & Co. v. Calcutta Stock Exchange Association Ltd.* 1963-(033)-Com Cases-0862-SC, the Supreme Court held that the exchange was not liable to file any return of the forfeited shares under Section 75(1) of the Companies Act, 1956 [Corresponds to section 39 of the Companies Act, 2013] when the same were re-issued. The Court observed that when a share is forfeited and re-issued, there is no allotment, in the sense of appropriation of shares out of the authorised and unappropriated capital and approved the observations of Harries C.J. in *S.M. Nandy's* case that: "On such forfeiture all that happened was that the right of the particular shareholder disappeared but the shares considered as a unit of issued capital continued to exist and was kept in suspense until another shareholder was found for it";
- (B) *Alote Estate v. R.B. Seth Hiralal Kalyanmal Kasliwal* [1970] 40 Com Cases 1116 (SC). In case of inadequacy of consideration, the shares will be treated as not fully paid and the shareholder will be liable to pay for them in full, unless the contract is fraudulent;
- (C) *Harmony and Montage Tin and Copper Mining Company; Spargo's case* (1873) 8 Ch. App. 407. Any payment which is presently enforceable against the company such as consideration payable for property purchased, will constitute payment in cash;
- (D) *Chokkalingam v. Official Liquidator* AIR 1944 Mad. 87. Allotment of shares against promissory notes shall not be valid.

**GENERAL PRINCIPLES REGARDING ALLOTMENT**

"Allotment" of shares means the act of appropriation by the Board of directors of the company out of the previously un-appropriated capital of a company of a certain number of shares to persons who have made applications for shares (In *Re Calcutta Stock Exchange Association*, AIR 1957 Cal. 438). It is on allotment that shares come into existence.

The following general principles should be observed with regard to allotment of securities:

- (1) **The allotment should be made by proper authority.** The proper authority may be the Board Directors of the company, or a committee authorised to allot securities on behalf of the Board.
- (2) **Allotment of securities must be made within a reasonable time** (As per Section 6 of the Indian Contract Act, 1872, an offer must be accepted within a reasonable time). What is reasonable time is a question of fact in each case. An applicant may refuse to take securities if the allotment is made after a long time. (As per Section 56 within a period of two months from the date of allotment in the case of allotment of any of its shares.)

- (3) **The allotment should be absolute and unconditional.** Securities must be allotted on same terms on which they were applied for and as they are stated in the application for securities. Allotment of securities subject to certain conditions is also not valid. Similarly, if the number of securities allotted is less than those applied for, it cannot be termed as absolute allotment.
- (4) **The allotment must be communicated.** As mentioned earlier posting of letter of allotment or allotment advice will be taken as a valid communication even if the letter is lost in transit.
- (5) **Allotment against application only.** Section 2(55) of the Act requires that a person should agree in writing to become a member.
- (6) **Allotment should not be in contravention of any other law.** If securities are allotted on an application of a minor, the allotment will be void.

## CASE LAWS

### Judicial Pronouncement relating to allotment

- (A) An allotment may be valid even if some defect was there in the appointment of directors but which was subsequently discovered. (Section 290 and the Rule in *Royal British Bank v. Turquand* (1856) 6 E & B 327 : (1843-60) All ER Rep 435);
- (B) An allotment by a Board irregularly constituted may be subsequently ratified by a regular Board [*Portugese Consolidated Copper Mines*, (1889) 42 Ch. D 160 (CA)];
- (C) A director who has joined in an allotment to himself will be estopped from alleging the invalidity of the allotment [*Yark Tramways Co. v. Willows*, (1882) 8 QBD 685 (CA)];
- (D) Grant applied for certain shares in a company, the company dispatched letter of allotment to him which never reached him. It was held that he was liable for the balance amount due on the shares. [*Household Fire And Carriage Accident Insurance Co. Ltd. v. Grant* (1879) 4 E.D. 216]
- (E) There can be no proper allotment of shares unless the applicant has been informed of the allotment [*British and American Steam Navigation Co. Re.* (1870) LR 10 Eq 659].

### What is a share certificate?

A share certificate is a certificate issued to the members by the company, specifying the number of shares held by him and the amount paid on each share. According to Section 45 of the Companies Act, 2013 each share of the share capital of the company shall be distinguished with a distinct number for its individual identification. However, such distinction shall not be required, as per proviso to Section 45, if the shares are held by a person whose name is entered as holder of beneficial interest in such share in the records of a depository.

In terms of Section 46(1) of the Act, a certificate under the common seal, if any, of the company or signed by two directors or by a director and the company secretary, wherever, the company has appointed a Company Secretary, *is prima facie* evidence of the title of the person to the shares specified therein. The certificate is the only documentary evidence of title in the possession of the shareholder. But it is not a warranty of title by the company issuing it.

### When can a company issue Duplicate Share Certificate?

Section 46 (2) states that a duplicate certificate of shares may be issued, if such certificate —

- (a) is proved to have been lost or destroyed; or

(b) has been defaced, mutilated or torn and is surrendered to the company.

**Manner of issuing share certificates/ Duplicate Share Certificates**

Section 46(3) states that notwithstanding anything contained in the articles of a company, the manner of issue of a certificate of shares or the duplicate thereof, the form of such certificate, the particulars to be entered in the register of members and other matters shall be such as may be prescribed.



ISSUE OF SHARE CERTIFICATE	ISSUE OF RENEWED OR DUPLICATE SHARE CERTIFICATE
Board Resolution be passed and Letter of allotment or fractional coupons of requisite value, must be surrendered to company. In case the letter of allotment is lost or destroyed the Board may impose reasonable terms	Renewal to be made only on surrender of old certificate.
Certificate shall be issued in Form No. SH-1 and shall specify the name of person in whose favour the certificate is issued, shares to which it relates and the amount paid-up thereon.	Company may charge fee for duplicate share certificate as the board decides but not exceeding Rs. 50 per certificate.
<p>Every certificate shall specify the shares to which it relates and the amount paid-up thereon and shall be signed by two directors or by a director and the CS, wherever the company has appointed CS.</p> <p>In case the company has a common seal it shall be affixed in the presence of persons required to sign the certificate.</p> <p>In case of an One Person Company, it shall be sufficient if the certificate is signed by a director and the CS or any other person authorised by the Board for the purpose.</p>	<p>Company shall not issue any duplicate share certificate in lieu of those lost or destroyed without the prior consent of Board</p> <p>If the company is listed then the duplicate share certificates shall be issued within 45 days and if the company is unlisted it shall issue the certificates within 3 months from the date of submission of complete documents with the company</p>

<p>a director shall be deemed to have signed the share certificate if his signature is printed thereon as facsimile signature by means of any machine, equipment or other mechanical means such as engraving in metal or lithography or digitally signed, but not by means of rubber stamp, provided that the director shall be personally responsible for permitting the affixation of his signature thus and the safe custody of any machine, equipment or other material used for the purpose.</p>	
<p>Particulars of shares certificates to be entered in the Register of Members</p>	<p>The particulars of renewed and duplicate share certificate to be entered in Register of Renewed and Duplicate Share Certificates maintained in Form No. SH.2.</p>
	<p>The register to be kept at registered office of the company in the custody of the Company Secretary of the company or any other person authorised by the Board.</p>
	<p>On fraudulent issue the company shall be punishable with: fine which shall not be less than five times the face value of shares involved which may extend to ten times or rupees 10 crore whichever is higher.</p>
	<p>Officer in default shall be liable under section 447.</p>

**Maintenance of share certificate forms and related books and documents [Rule 7 of Companies(Prospectus and Allotment of Securities) Rules, 2014]**

- (1) All blank forms to be used for issue of share certificates shall be printed and the printing shall be done only on the authority of a resolution of the Board and the blank form shall be consecutively machine-numbered and the forms and the blocks, engravings, facsimiles and hues relating to the printing of such forms shall be kept in the custody of the secretary or such other person as the Board may authorise for the purpose; and the company secretary or other person aforesaid shall be responsible for rendering an account of these forms to the Board.
- (2) The following persons shall be responsible for the maintenance, preservation and safe custody of all books and documents relating to the issue of share certificates, including the blank forms of share certificates referred above, namely:—
  - (a) the committee of the Board, if so authorized by the Board or where the company has a Company Secretary, the Company Secretary; or
  - (b) where the company has no Company Secretary, a Director specifically authorised by the Board for such purpose.
- (3) All books mentioned above shall be preserved in good order not less than thirty years and in case of

disputed cases, shall be preserved permanently, and all certificates surrendered to a company shall immediately be defaced by stamping or printing the word “cancelled” in bold letters and may be destroyed after the expiry of three years from the date on which they are surrendered, under the authority of a resolution of the Board and in the presence of a person duly appointed by the Board in this behalf:

The above mentioned provisions shall not apply to cancellation of the certificates of securities, under sub-section (2) of section 6 of the Depositories Act, 1996 (22 of 1996), when such certificates are cancelled in accordance SEBI (Depositories and Participants) Regulations, 1996.

### **Record of depository is prima facie evidence for shares in depository form**

Section 46(4) states that where a share is held in depository form, the record of the depository is the *prima facie* evidence of the interest of the beneficial owner.

### **Issuing duplicate share certificates to defraud**

According to Section 46(5), if a company with an intention to defraud, issues a duplicate certificate of shares, the company shall be punishable with fine which shall not be less than five times the face value of the shares involved in the issue of the duplicate certificate but which may extend to ten times the face value of such shares or rupees ten crores whichever is higher and every officer of the company who is in default shall be liable for action under section 447, for fraud.

### **Time of issue of Certificate of Securities**

Under Section 56(4) of the Act, every company, unless prohibited by any provision of law or any order of any Court, Tribunal or other authority must deliver the certificates of all securities allotted, transferred or transmitted:-

- (a) within a period of two months from the date of incorporation, in the case of subscribers to the memorandum;
- (b) within a period of two months from the date of allotment, in the case of any allotment of any of its shares;
- (c) within a period of one month from the date of receipt by the company of the instrument of transfer or, as the case may be, of the intimation of transmission, in the case of a transfer or transmission of securities;
- (d) within a period of six months from the date of allotment in the case of any allotment of debenture.

*However, where the securities are dealt with in a depository, the company shall intimate the details of allotment of securities to depository immediately on allotment of such securities. [Proviso to Section 56(4)]*

Where any default is made in complying with the above provisions, the company shall be punishable with fine which shall not be less than Rs 25,000 but which may extend to Rs. 5 Lakh and every officer of the company who is in default shall be punishable with fine which shall not be less than Rs 10,000 but which may extend to Rs.1,00,000. [Section 56(6)]

### **Significance of Share Certificate**

A certificate of shares is evidence to the effect that the allottee is holding a certain number of shares of the company showing their nominal and paid-up value and distinctive numbers. This certificate is a *prime facie* evidence of title to the shares in the possession of shareholders. [*Society Generale De Paris v. Walker,*

(1885) 11A AC 20, 29].

Moreover, when the company issues a certificate, it holds that the facts contained therein are true. Any person acting on the faith of the share certificate of the company, can compel the company to pay compensation for any damage caused by reason of any misstatement in the share certificate as the company is bound by any statements made in the certificate.

Share certificate is the only documentary evidence of title and that the share certificate is a declaration by the company that the person in whose name the certificate is issued is a shareholder in the company. [*Ghanshyam Chhaturbuj v. Industrial Ceramics (Pvt.) Ltd. (1995) 4 Com LJ 51*].

Also the company cannot dispute the amount mentioned on the certificate as already paid. [*Bloomenthal v. Ford (1897) AC 156 (HL)*].

### **Damages against Company and Directors for wrong certificates**

As already mentioned, a person acting on the share certificate issued by the company may recover compensation for the damages suffered by him. The measure of damage is the value of the shares at the time of the refusal by the company to recognise him as a shareholder together with interest from that date. [*Bahla and San Francisco Rly. Co., (1868) LR 3 QB 584*].

Where directors issue a certificate of title of shares which the company has no power to issue, they may be held personally liable to damages on an implied warranty of authority to any person who acts on such certificate.

### **Split Certificate**

A split certificate means a separate certificate claimed by a shareholder for a portion of his holding. The advantages of a split certificate are that the shareholder may benefit in case of a transfer by way of sale or mortgage in small lots and the right to multiply the certificates into as many shares held by the shareholder.

### **Purpose and Form of Share Certificate**

With the help of a share certificate a member of a company may deal with his shares in the market whether it is one of sale, mortgage or pledge by showing a good prima facie marketable title to the shares. A share certificate is a documentary evidence of title to shares in the possession of the shareholder. It is a *prima facie* evidence of his title to the shares.

Section 46(4) provides that where a share is held in depository form, the record of the depository is the *prima facie* evidence of the interest of the beneficial owner.

### **Let us remember!**

*Every certificate of share or shares shall be in Form No. SH.1 or as near thereto as possible.*

*The particulars of every share certificate issued shall be entered forthwith in a Register of Renewed and Duplicate Share Certificates maintained in Form No. SH.2.*

### **Whether Share Certificate an Official Publication**

The question whether a share certificate is an official publication within the meaning of Section 12(3)(c) was considered by the Department of Company Affairs (Now, Ministry of Corporate Affairs) and the Department has clarified *vide* Circular No. 3/73[8/10(47)]/72-CL-V dated 3.2.1973 as follows:

“It will be seen that in terms of Section 82 [Corresponds to section 44 of the Companies Act, 2013], the shares in a company are movable property transferable in the manner provided in the articles of the company.

Section 84 [Corresponds to section 46 of the Companies Act, 2013] provides that a certificate under the common seal of the company specifying any share held by any member shall be prima facie evidence of the title of the member to such share. [With the Companies (Amendment) Act, 2015 coming into force the common seal is no more mandatory. The implications and signatories have been discussed earlier.]

Thus, shares are movable property transferable in the manner provided in the articles of the company and that the share certificates are certificates of title and are movable property but are not publications in the nature of prospectus, balance sheet, profit and loss account, notice or advertisement.

*The conclusion reached, therefore, is that the share certificate is not an official publication within the meaning of Section 12(3)(c) of Companies Act, 2013.*

### Legal Effect of Share Certificate

We have already stated that a share certificate is prima facie evidence to the title of the person whose name is entered on it. It means that the share certificate is a statement by the company that the moment when it was issued, the person named in it was the legal owner of the shares specified in it, and those shares were paid-up to the extent stated. It does not constitute title but it is merely evidence of title. It is, however a statement of considerable importance, for it is made with the knowledge that other persons may act upon it in the belief that it is true and this fact brings into operation the doctrine of estoppel. As a result, a share certificate once issued by the company binds it in two ways, namely:

- (a) by estoppel as to title, and
- (b) by estoppel as to payment.

**Estoppel as to Title:** A share certificate once issued binds the company in two ways. In the first place, it is a declaration by the company to the entire world that the person in whose name the certificate is made out and to whom it is given is a shareholder in the company. In other words the company is estopped from denying his title to the shares.

**Estoppel as to Payment:** If the certificate states that on each of the shares full amount has been paid, the company is estopped as against a *bona fide* purchaser of the shares, from alleging that they are not fully paid.

If a person knows that the statements in a certificate are not true, he cannot claim an estoppel against the company *Barrow case* (1880) 14 Ch D 432: 42LT 891CA.

Despite everything, a certificate must be issued by someone who has the authority. For example, where the secretary forged the signature of two directors in a company, the company had refused to register the holder of shares as a member. Further a certificate is not evidence as to the equitable interest in shares. Also, where an individual is aware of the false statements in a certificate, he will not be entitled to claim an estoppel.

### Personation of Shareholders [Section 57]

Where any person deceitfully personates as an owner of any security or interest in a company, or of any share warrant or coupon issued in pursuance of this Act, and

- (1) thereby obtains or attempts to obtain any such security or interest or any such share warrant or

coupon, or

- (ii) receives or attempt to receive any money due to any such owner;

He shall be punishable with imprisonment for a term which shall not be less than 1 year but which may extend to 3 years and with fine which shall not be less than 1 lakh rupees but which may extend to 5 lakh rupees.

To 'personate' means to pretend to be someone else, especially for fraudulent purpose such as casting a vote in another person's name. Personation and impersonation imply the same thing.

## Part C: Issue of Securities

### EQUITY SHARES WITH DIFFERENTIAL VOTING RIGHTS

While Section 43 enables companies to issue equity shares with differential rights as to dividend, voting rights etc. Rule 4 of Companies (Share Capital and Debentures) Rules, 2014 states the following conditions regarding shares with differential voting rights.

#### ***Conditions for issuing shares with differential rights (Rule 4) Companies (Share Capital and Debentures) Rules, 2014***

Only a company limited by shares can issue equity shares with differential rights as to dividend, voting or otherwise. Such company has to comply with the following conditions, namely:-

- (a) the articles of association of the company authorizes the issue of shares with differential rights;
- (b) the issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders. When the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot. (Though with Companies (Amendment) Act, 2017 coming into force, Any item of business required to be transacted by means of postal ballot, may be transacted at a general meeting by a company which is required to provide the facility to members to vote by electronic means under section 108).
- (c) the shares with differential rights shall not exceed twenty-six percent of the total post-issue paid up equity share capital including equity shares with differential rights issued at any point of time;
- (d) the company having consistent track record of distributable profits for the last three years;
- (e) the company has not defaulted in filing financial statements and annual returns for three financial years immediately preceding the financial year in which it is decided to issue such shares;
- (f) the company has no subsisting default in the payment of a declared dividend to its shareholders or repayment of its matured deposits or redemption of its preference shares or debentures that have become due for redemption or payment of interest on such deposits or debentures or payment of dividend;
- (g) the company has not defaulted in payment of the dividend on preference shares or repayment of any term loan from a public financial institution or State level financial institution or scheduled Bank that has become repayable or interest payable thereon or dues with respect to statutory payments relating to its employees to any authority or default in crediting the amount in Investor Education and Protection Fund to the Central Government;

A company may issue equity shares with differential rights upon expiry of five years from the end of the financial year in which such default was made good.

- (h) the company has not been penalized by Court or Tribunal during the last three years of any offence under the RBI Act, 1934, the SEBI Act, 1992, the Securities Contracts Regulation Act, 1956, the Foreign Exchange Management Act, 1999 or any other special Act, under which such companies being regulated by sectoral regulators.

***Disclosures in the explanatory statement to the notice of the meeting***

While taking a decision it is important that all information is provide with regard to the matter, hence rule 4(2) of Companies (Share Capital and Debentures) Rules, 2014 requires that the explanatory statement shall be annexed to the notice of the general meeting or of a postal ballot. The explanatory statement shall contain the following particulars, namely:-

- (a) the total number of shares to be issued with differential rights;
- (b) the details of the differential rights ;
- (c) the percentage of the shares with differential rights to the total post issue paid up equity share capital including equity shares with differential rights issued at any point of time;
- (d) the reasons or justification for the issue;
- (e) the price at which such shares are proposed to be issued either at par or at premium;
- (f) the basis on which the price has been arrived at;
- (g) (i) in case of private placement or preferential issue-
  - (a) details of total number of shares proposed to be allotted to promoters, directors and key managerial personnel;
  - (b) details of total number of shares proposed to be allotted to persons other than promoters, directors and key managerial personnel and their relationship if any with any promoter, director or key managerial personnel;
- (ii) in case of public issue - reservation, if any, for different classes of applicants including promoters, directors or key managerial personnel;
- (h) the percentage of voting right which the equity share capital with differential voting right shall carry to the total voting right of the aggregate equity share capital;
- (i) the scale or proportion in which the voting rights of such class or type of shares shall vary;
- (j) the change in control, if any, in the company that may occur consequent to the issue of equity shares with differential voting rights;
- (k) the diluted Earning Per Share pursuant to the issue of such shares, calculated in accordance with the applicable accounting standards;
- (l) the pre and post issue shareholding pattern along with voting rights as per Regulation 31 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

***Conversion of existing equity share capital into differential voting rights and vice-versa not possible***

The company shall not convert its existing equity share capital with voting rights into equity share capital carrying differential voting rights and *viceversa*.

### ***Disclosures in the Boards' Report***

The Board of Directors are required to disclose the details of the issue of equity shares with differential rights in the Board's Report for the financial year in which was completed. The details are given in Chapter "Transparency and Disclosure", later in this study.

### ***Rights of holders of equity shares with differential voting rights***

The holders of the equity shares with differential rights enjoys all other rights such as bonus shares, rights shares etc., which the holders of equity shares are entitled to, subject to the differential rights with which such shares have been issued.

### ***Register of Members to contain the details of equity shareholders having differential voting rights***

When a company issues equity shares with differential rights, the Register of Members maintained under section 88 shall contain all the relevant particulars of the shares so issued along with details of the shareholders.

## **Procedure for Issue of Equity Shares with Differential Voting Rights**

1. Check whether the Articles of Association of the company authorizes issue of equity shares with differential rights and if not, the name and the Articles of Association of the company.
2. Hold the Board meeting to issue the notice of general meeting fo issuance of equity share with differential rights.
3. Before issuing equity shares with differential rights as to dividend, voting or otherwise, ensure that the conditions of issue are fully satisfied
4. If the company is listed with any of the recognized stock exchange, then within15 minutes of the closure of the aforesaid Board Meeting intimate to the concerned Stock Exchange about the decision taken at the Board Meeting.
5. Pass the ordinary resolution in the general meeting or through Postal Ballot under section 110 of the Act.
6. Once the company makes any allotment, then it shall, within 30 days thereafter, file with the Registrar a return allotment in **Form PAS-3**, along with the fees as specified in the Companies (Registration Offices and Fees) Rules, 2014.
7. The company shall not convert its existing equity share capital with voting rights into equity share capital carrying differential voting rights and *vice-versa*.
8. In case of listed company, send copies of the notice and a copy of the proceedings of the general meeting to the stock exchange within 24 hours of the occurrence of event. [Regulation 30 (6) of SEBI (Listing Obligations and Disclosure Requirements), 2015]
9. Complete all other proceedings for the issue of certificate of shares with differential voting rights making necessary entries in various registers. In case of a company whose shares are dematerialized form, inform the depositories about the same for credit to the respective accounts.
11. Intimate the details of allotment of shares to the Depository immediately on allotment of such shares.

12. Maintain the Register of Members under section 88 containing all the relevant particulars of the shares so issued along with details of the shareholders.

## ISSUE AND REDEMPTION OF PREFERENCE SHARES

### Company cannot issue irredeemable preference shares or redeemable preference shares with the redemption period beyond 20 years

Section 55 (1) states that no company limited by shares shall issue any preference shares which are irredeemable. Section 55(2) further states that a company limited by shares may, if so authorised by its articles, issue preference shares which are liable to be redeemed within a period not exceeding twenty years from the date of their issue subject to such conditions as may be prescribed.

#### **Exceptions**

##### *Issue and redemption of preference shares by company in infrastructure projects*

A company engaged in the setting up and dealing with of infrastructural projects may issue preference shares for a period exceeding twenty years but not exceeding thirty years, subject to the redemption of a minimum ten percent of such preference shares per year from the twenty first year onwards or earlier, on proportionate basis, at the option of the preference shareholders.

The term “infrastructure projects” means the infrastructure projects specified in Schedule VI.

##### *Other conditions attached*

Proviso to Section 55(2) states that

- (a) Preference Shares shall be redeemed out of the profits of the company which would otherwise be available for dividend or out of the proceeds of a fresh issue of shares made for the purposes of such redemption;
- (b) Such shares shall be redeemed only if they are fully paid;
- (c) where such shares are proposed to be redeemed out of the profits of the company, there shall, out of such profits, be transferred, a sum equal to the nominal amount of the shares to be redeemed, to a reserve, to be called the Capital Redemption Reserve Account.
- (d) (i) in case of such class of companies, as may be prescribed and whose financial statement comply with the accounting standards prescribed for such class of companies under section 133, the premium, if any, payable on redemption shall be provided for out of the profits of the company, before the shares are redeemed. Premium, if any, payable on redemption of any preference shares issued by any such company shall be provided for out of the profits of the company or out of the company's securities premium account, before such shares are redeemed.
- (ii) in a case not falling under sub-clause (i) above, the premium, if any, payable on redemption shall be provided for out of the profits of the company or out of the company's securities premium account, before such shares are redeemed.

Section 55 (3) when a company is not in a position to redeem any preference shares or to pay dividend, if any, on such shares in accordance with the terms of issue (such shares hereinafter referred to as unredeemed preference shares), it may, with the consent of the holders of three-fourths in value of such preference shares and with the approval of the Tribunal on a petition made by it in this behalf, issue further

redeemable preference shares equal to the amount due, including the dividend thereon, in respect of the unredeemed preference shares, and on the issue of such further redeemable preference shares, the unredeemed preference shares shall be deemed to have been redeemed.

The issue of further redeemable preference shares or the redemption of preference shares under this section shall not be deemed to be an increase or, as the case may be, a reduction, in the share capital of the company.

The capital redemption reserve account may, notwithstanding anything in this section, be applied by the company, in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares.

### **Prescriptions under Companies (Share Capital and Debentures) Rules, 2014 with regard to issue and redemption of Preference shares (Rule 9)**

#### ***Conditions***

A company having a share capital may, if so authorised by its articles, issue preference shares subject to the following conditions, namely:-

- (a) the issue of such shares has been authorized by passing a special resolution in the general meeting of the company
- (b) the company, at the time of such issue of preference shares, has no subsisting default in the redemption of preference shares issued earlier or in payment of dividend due on any preference shares.

#### ***Resolution authorising preference shares to set out certain particulars***

A company issuing preference shares shall set out in the resolution, particulars in respect of the following matters relating to such shares, namely:-

- (a) the priority with respect to payment of dividend or repayment of capital vis-a-vis equity shares;
- (b) the participation in surplus fund;
- (c) the participation in surplus assets and profits, on winding-up which may remain after the entire capital has been repaid;
- (d) the payment of dividend on cumulative or non-cumulative basis.
- (e) the conversion of preference shares into equity shares.
- (f) the voting rights;
- (g) the redemption of preference shares.

#### ***Explanatory statement to special resolution to set out certain particulars***

While taking a decision it is important that all information is provide with regard to the matter, hence rule 9(3) states that the explanatory statement to be annexed to the notice of the general meeting which shall provide the material facts concerned with and relevant to the issue of such shares, including-

- (a) the size of the issue and number of preference shares to be issued and nominal value of each share;
- (b) the nature of such shares i.e. cumulative or non - cumulative, participating or non - participating,

- convertible or non - convertible
- (c) the objectives of the issue;
  - (d) the manner of issue of shares;
  - (e) the price at which such shares are proposed to be issued;
  - (f) the basis on which the price has been arrived at;
  - (g) the terms of issue, including terms and rate of dividend on each share, etc.;
  - (h) the terms of redemption, including the tenure of redemption, redemption of shares at premium and if the preference shares are convertible, the terms of conversion;
  - (i) the manner and modes of redemption;
  - (j) the current shareholding pattern of the company;
  - (k) the expected dilution in equity share capital upon conversion of preference shares.

***Register of Members to contain the particulars of preference share holder(s)***

When a company issues preference shares, the Register of Members maintained under section 88 shall contain the particulars in respect of such preference share holder(s).

***Redemption of preference shares***

Rule 9(6) states that a company may redeem its preference shares only on the terms on which they were issued or as varied after due approval of preference shareholders under section 48 of the Act and the preference shares may be redeemed:-

- (a) at a fixed time or on the happening of a particular event;
- (b) any time at the company's option; or
- (c) any time at the shareholder's option

**Procedure to issue and redemption of Preference Shares**

- (1) For issue of preference shares the articles of the company should authorize for it, if not then amendment in the articles of the company is required. Also ensure that there is no subsisting defaults in redemption of preference shares earlier or in payment of dividend due on any preference shares.
- (2) Ensure that the resolution for issuing preference shares contains all the relevant particulars as mentioned above
- (3) Issue the notice of general meeting along with the explanatory statement, to provide the required details.

In the case of listed entity, intimate the stock exchange at least two working days in advance of the date of board meeting (Refer Regulation 29 of Listing Regulations)

- (4) Pass special resolution and file with the registrar **Form MGT-14** along with the fee so specified in the Companies (Registration of Offices and Fees) Rules, 2014 within 30 days of passing the resolution

*Note:* in case of One Person Company for the purpose of passing of ordinary and special resolution in general meeting, any business which is required to be transacted at an annual general meeting or

other general meeting of accompany by means of an ordinary or special resolution, it shall be sufficient if the resolution is communicated by the member to the company and entered in the minutes book and signed and dated by the member and such date shall be deemed to be the date of meeting for all purpose under this act.

- (5) Within 30 days of allotment file with the registrar the Return of allotment in **Form PAS-3** along with fee as specified in companies (Registration of Offices and Fees), Rules 2014
- (6) Update the register of members maintained under section 88 after issue of preference shares
- (7) The company may redeem the preference shares only on the terms on which they were issued or as varied after due approval of preference shareholders
- (8) The preference shares may be redeemed as given below:
  - a. At affixed time or happening of a particular event
  - b. Any time at the company's option
  - c. Any time at the shareholders option
- (9) The notice of redemption of preference shares shall be filed by the company with the Registrar in **Form SH-7** along with altered MOA with the fee as specified in Companies (Registration of Offices and Fees), Rules, 2014 within 30 days of redemption of preference shares.
- (10) Once the allotment is made, the company shall within 30 days of allotment, file with the Registrar are turn of allotment in **Form PAS.3**, along with the fee as specified in Companies (Registration of Offices and Fees) Rules, 2014.
- (11) Deliver the share certificates of allotted shares within a period of 2 months from the date of allotment.
- (12) Intimate the details of allotment of shares to the Depository immediately on allotment of such shares

**FURTHER ISSUE OF SHARE CAPITAL**

**FURTHER ISSUE OF SHARE CAPITAL**  
**Section 62**

Where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered to—

(A)  
Holders of Equity Shares  
[u/s 62(1)(a)](Rights Issue)

(B)  
EMPLOYEES  
[u/s 62(1)(b)]Employee Stock Options)

(C)  
ANY PERSONS  
[u/s 62(1)(c)](Preferential Basis)

(A) <b>PERSONS</b>	(B) <b>EMPLOYEES</b>	(C) <b>ANY PERSONS</b>
<b>[u/s 62(1)(a)]</b>	<b>[u/s 62(1)(b)]</b>	<b>[u/s 62(1)(c)]</b>
Who, at the date of the offer,	Under a Scheme Of Employees'	Whether or not those persons

<p>are holders of equity shares of the company                  In proportion to the paid-up share capital on those shares                  By sending a letter of offer  <i>Subject to such conditions as may be prescribed.</i></p>	<p>Stock Option                  Subject to special resolution passed by company  <i>Subject to such conditions as may be prescribed.</i></p>	<p>include the persons referred to in (A) or (B)                  If it is authorised by a special resolution                  Either for cash or for a consideration other than cash, if the price of such shares is determined by the valuation report of a registered valuer  <i>Subject to such conditions as may be prescribed.</i></p>
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**CONDITIONS FOR FURTHER ISSUE OF SHARES TO EQUITY HOLDERS RIGHTS ISSUE [u/s 62(1)(a)]**

The offer shall be made by notice:

- specifying the number of shares offered and
- limiting a time not being less than 15 days and not more than 30 days from the date of the offer within which the offer, if not accepted, shall be deemed to have been declined
- The offer shall be deemed to include right of renunciation
- unless the articles of the company otherwise provide; and

the notice referred above shall contain a statement of this right;

- If the offer is rejected by the equity shareholders
- after the expiry of the time specified in the notice aforesaid, or
- on receipt of earlier intimation from the person to whom such notice is given that he declines to accept the shares offered,
- the Board of Directors may dispose of them in such manner which is not dis-advantageous to the shareholders and the company.

The said notice shall be dispatched through registered post or speed post or through electronic mode or courier or any other mode having proof of delivery to all the existing shareholders at least three days before the opening of the issue.

Unless the articles of the company otherwise provide, the directors must state in the notice of offer of rights shares the fact that the shareholder has also the right to renounce the offer in whole or in part, in favour of some other persons. However in case of a private company case ninety per cent of the members of a private company have given their consent in writing or in electronic mode, the periods lesser than those specified in the said sub-clause or subsection shall apply.

Accordingly, time limit for acceptance of offer by existing shareholders may be less than 15 days, if 90% of the members of a private limited company have given their consent either in writing or through electronic mode.

If a shareholder has neither renounced in favour of another person nor accepted the shares, the Board of directors may dispose of the shares so declined in such manner which is not dis-advantageous to the

shareholders and the company.

The provisions of section 62 are applicable to all types of companies except the Nidhi companies.

The restrictions contained in Section 62 of the Act regarding issue of further shares do not apply to:-

- (a) Increase of the subscribed capital of a company caused by the exercise of an option as a term attached to the debentures issued or loans raised by the company to convert such debentures or loans into shares in the company [Section 62(3)].

The terms of issue of such debentures or loan containing such an option have been approved before the issue of such debentures or the raising of loans by a special resolution passed by the company in the general meeting.

- (b) conversion of part or whole of the debentures issued to or loans obtained from any Government in shares of the company in pursuance of a direction issued by that Government in public interest on such terms and conditions as appear to be fair and reasonable to the Government even if the terms of issue of such debentures or loans do not contain a term providing for an option for such conversion.[Section 62(4)].

Where the terms and conditions of such conversion are not acceptable to the company, it may, within sixty days from the date of communication of such order, appeal to the Tribunal which shall after hearing the company and the Government pass such order as it deems fit.

In determining the terms and conditions of conversion under section 62(4), the Government shall have due regard to the financial position of the company, the terms of issue of debentures or loans, as the case may be, the rate of interest payable on such debentures or loans and such other matters as it may consider necessary. [Section 62(5)]

Where the Government has, by an order made under section 62(4), directed that any debenture or loan or any part thereof shall be converted into shares in a company and where no appeal has been preferred to the Tribunal under section 62(4) or where such appeal has been dismissed, the memorandum of such company shall, where such order has the effect of increasing the authorised share capital of the company, stand altered and the authorised share capital of such company shall stand increased by an amount equal to the amount of the value of shares which such debentures or loans or part thereof has been converted into. [Section 62(6)]

## CASE LAWS

### Judicial Pronouncement relating to further issue of shares by a company

- (A) *Nanalal Zaver v. Bombay Life Assurance Co. Ltd., AIR 1950 SC 172: (1950) 20 Com Cases 179:*** Section 81 (Corresponding to section 62 of the Companies Act, 2013) is intended to cover cases where the directors decide to increase the capital by issuing further shares within the authorised limit, because it is within that limit that the directors can decide to issue further shares, unless, of course, they are precluded from doing that by the Articles of Association of the company. Accordingly, the section becomes applicable only when the directors decide to increase the capital within the authorised limit, by issue of further shares.

The above judgement was followed by the Supreme Court in *Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.* (1981) 51 Com Cases 743 at 816: AIR 1981 SC 1298: (1982) 1 Comp LJ1. The Court pointed out that the directors of a company must exercise their powers for the benefit of the company. The directors are in a fiduciary position and if they does not

exercise powers for the benefit of the company but simply and solely for personal aggrandisement and to the detriment of the company, the court will interfere and prevent the directors from doing so;

- (B) See ***Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.*** The power to issue shares need not be used only when there is a need to raise additional capital. The power can be used to create a sufficient number of shareholders to enable a company to exercise statutory powers or to enable it to comply with statutory requirements.

The Department of Company Affairs, now Ministry of Corporate Affairs has clarified that 'one year' specified in the section is to be counted from the date on which the company has allotted any share for the first time;

- (C) ***Balkrishan Gupta v. Swadeshi Polytex Ltd. (1985) 58 Com Cases 563: AIR 1985 SC 520***. Although the term 'holders of the equity shares' is used in Sub-section (1)(a) and 'members' in Sub-section (1A)(b) of Section 81 (Corresponding to section 62 of the Companies Act, 2013), the two terms are synonymous and mean persons whose names are entered in the register of members;
- (D) In ***Worldwide Agencies (P) Ltd. v. Margaret T. Desor, (1990) 67 Com Cases 607: AIR 1990 SC 737***, it was held that persons who have become entitled to the shares of a deceased member can exercise all the membership rights of the deceased irrespective of the fact whether their name is in the register of members or not
- (E) ***Mathalone (R) v. Bombay Life Assurance Co. Ltd. AIR 1953 SC 385: (1954) 24 Com Cases 1***. The Court held that the transferor could not be compelled by the transferee to take up on his behalf the rights shares offered to the transferor and all that he could require the transferor to do was to renounce the rights issue in the transferee's favour.

### Procedure for issue of Right Shares

- (i) Check whether the rights issue results in increase of authorized capital.,
- (ii) If so call a board meeting to approve the notice of General meeting to pass necessary special resolutions at the general meeting to amend Memorandum/Articles of Association
- (iii) Convene the general Meeting and obtain shareholders' approval through special Resolution.
- (iv) he offer should be made by notice, specifying the number of shares offered and limiting a time not being less than fifteen days and not exceeding thirty days from the date of the offer within which the offer, if not accepted, shall be deemed to have been declined. This notice shall be dispatched through Registered post or speed post or through electronic mode to all the existing shareholders at least three days before the opening of the issue. However, in case of private companies in case 90% of members have given their consent in writing or in electronic mode, the lesser period than the specified period shall apply.
- (v) Check the copy of form SH7, MGT14 filed with ROC.
- (vi) The shares declined by the existing shareholder can be disposed off by the company in manner which is not disadvantageous to the shareholders and the company.
- (vii) Once the allotment is made, the company shall within 30 days of allotment, file with the Registrar are turn of allotment in Form PAS.3, along with the fee as specified in Companies (Registration of Offices and Fees) Rules, 2014.
- (viii) Deliver the share certificates of allotted shares within a period of 2 months from the date of allotment.
- (ix) Intimate the details of allotment of shares to the Depository immediately on allotment of such shares

## EMPLOYEE STOCK OPTION SCHEME

The term '*Employee Stock Option*' (ESOP) has been defined under sub-section (37) of Section 2 of the Companies Act, 2013, according to which "employees' stock option" means the option given to the directors, officers or employees of a company or of its holding company or subsidiary company or companies, if any, which gives such directors, officers or employees, the benefit or right to purchase, or to subscribe for, the shares of the company at a future date at a pre-determined price.

As discussed earlier, Section 62(1)(b) provides that a company may issue further shares to its employees under a scheme of employees' stock option, subject to special resolution passed by company and subject to such conditions as may be prescribed. In case of private company special resolution has been substituted by ordinary resolution.

### Rule 12 of Companies (Share Capital and Debentures) Rules, 2014

A company, other than a listed company, which is not required to comply with Securities and Exchange Board of India Employee Stock Option Scheme Guidelines shall not offer shares to its employees under a scheme of employees' stock option (hereinafter referred to as "Employees Stock Option Scheme"), unless it complies with the following requirements, namely:-

- (i) the issue of Employees Stock Option Scheme has been approved by the shareholders of the company by passing a special resolution (exception in case of private company where ordinary resolution is required).

#### ***Who is an employee for the purpose of Section 62(1)(b)***

- (a) a permanent employee of the company who has been working in India or outside India; or
- (b) a director of the company, whether a whole time director or not but excluding an independent director; or
- (c) an employee as defined in clauses (a) or (b) of a subsidiary, in India or outside India, or of a holding company of the company but does not include-
- (d) an employee who is a promoter or a person belonging to the promoter group; or
- (e) a director who either himself or through his relative or through any body corporate, directly or indirectly, holds more than ten percent of the outstanding equity shares of the company.

#### ***Details in explanatory statement***

While taking a decision it is important that all information is provide with regard to the matter, hence *rule 12(2)* states that the company shall make the following disclosures in the explanatory statement annexed to the notice for passing of the resolution –

- (a) total number of stock options to be granted;
- (b) identification of classes of employees entitled to participate in the Employees Stock Option Scheme;
- (c) the appraisal process for determining the eligibility of employees to the Employees Stock Option Scheme;
- (d) the requirements of vesting and period of vesting;
- (e) the maximum period within which the options shall be vested;
- (f) the exercise price or the formula for arriving at the same;

- (g) the exercise period and process of exercise;
- (h) the Lock-in period, if any ;
- (i) the maximum number of options to be granted per employee and in aggregate;
- (j) the method which the company shall use to value its options;
- (k) the conditions under which option vested in employees may lapse e.g. in case of termination of employment for misconduct;
- (l) the specified time period within which the employee shall exercise the vested options in the event of a proposed termination of employment or resignation of employee; and
- (m) a statement to the effect that the company shall comply with the applicable accounting standards.

***Free pricing in conformity with accounting policies***

The companies granting option to its employees pursuant to Employees Stock Option Scheme will have the freedom to determine the exercise price in conformity with the applicable accounting policies, if any.

***Separate resolution for granting options to employees of holding/subsidiary companies etc in certain cases***

*Rule 12(4)* states that the approval of shareholders by way of separate resolution shall be obtained by the company in case of –

- (a) grant of option to employees of subsidiary or holding company; or
- (b) grant of option to identified employees, during any one year, equal to or exceeding one percent of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant of option.

***Varying the terms of ESOP requires special resolution***

*Rule 12(5)* the company may by special resolution, vary the terms of Employees Stock Option Scheme not yet exercised by the employees provided such variation is not prejudicial to the interests of the option holders. The notice for passing special resolution for variation of terms of Employees Stock Option Scheme shall disclose full of the variation, the rationale therefor, and the details of the employees who are beneficiaries of such variation.

***Minimum one year vesting period***

*Rule 12 (6)(a)* states that there shall be a minimum period of one year between the grant of options and vesting of option. In a case where options are granted by a company under its Employees Stock Option Scheme in lieu of options held by the same person under an Employees Stock Option Scheme in another company, which has merged or amalgamated with the first mentioned company, the period during which the options granted by the merging or amalgamating company were held by him shall be adjusted against the minimum vesting period required under this clause.

***Company has freedom to specify lock-in period***

*Rule 12(6)(b)* states that the company shall have the freedom to specify the lock-in period for the shares issued pursuant to exercise of option.

***No right of dividend or voting till exercise of option***

*Rule 12(6)(c)* states that the Employees shall not have right to receive any dividend or to vote or in any

manner enjoy the benefits of a shareholder in respect of option granted to them, till shares are issued on exercise of option.

### ***Forfeiture/refund***

*Rule 12(7)* states that the the amount, if any, payable by the employees, at the time of grant of option –

- (a) may be forfeited by the company if the option is not exercised by the employees within the exercise period; or
- (b) the amount may be refunded to the employees if the options are not vested due to non-fulfillment of conditions relating to vesting of option as per the Employees Stock Option Scheme.

### ***Conditions***

*Rule 12(8)* states the following conditions:

- The option granted to employees shall not be transferable to any other person.
- The option granted to the employees shall not be pledged, hypothecated, mortgaged or otherwise encumbered or alienated in any other manner.
- No person other than the employees to whom the option is granted shall be entitled to exercise the option.

### ***Death/permanent disability/resignation of employees who were granted with options***

*Rule 12(8)* states that in the event of the death of employee while in employment, all the options granted to him till such date shall vest in the legal heirs or nominees of the deceased employee.

In case the employee suffers a permanent incapacity while in employment, all the options granted to him as on the date of permanent incapacitation, shall vest in him on that day.

In the event of resignation or termination of employment, all options not vested in the employee as on that day shall expire. However, the employee can exercise the options granted to him which are vested within the period specified in this behalf, subject to the terms and conditions under the scheme granting such options as approved by the Board.

### ***Disclosure in the Board's Report***

*Rule 12(9)* states that the Board of directors, shall, *inter alia*, disclose in the Directors' Report for the year, the following details of the Employees Stock Option Scheme issued during the year. The details are given in chapter "Transparency and Disclosures", later in this study.

### ***Maintenance of Register***

*Rule 12(10)* states that the company shall maintain a Register of Employee Stock Options in Form No. SH.6 and shall forthwith enter therein the particulars of option granted under clause (b) of sub-section (1) of section 62.

The Register of Employee Stock Options shall be maintained at the registered office of the company or such other place as the Board may decide. The entries in the register shall be authenticated by the company secretary of the company or by any other person authorized by the Board for the purpose.

### ***Listed companies has to comply with the SEBI guidelines***

Where the equity shares of the company are listed on a recognized stock exchange, the Employees Stock

Option Scheme shall be issued, in accordance with the regulations made by the Securities and Exchange Board of India in this behalf.

### **Procedure for issue of securities to employees through “Employees Stock Option Scheme”**

- (1) Convene a Board Meeting to approve the notice of the General meeting along with special resolution, explanatory statement etc., to be approved by the shareholders through special resolution.

In case of private company, it is sufficient that they obtain ordinary resolution.

- (2) Ensure that the company has made the following disclosures in the explanatory statement annexed to the notice for passing of the resolution-

Ensure that the special resolution is filled with ROC in MGT 14 within 30 days of passing the resolution.

- (3) The companies granting option to its employees pursuant to Employees Stock Option Scheme will have the freedom to determine the exercise price in conformity with the applicable accounting policies, if any.

- (4) The approval of shareholders by way of separate resolution shall be obtained by the company in case of-

- (a) Grant of option to employees of subsidiary or holding company; or

- (b) Grant of option to identified employees, during any one year, equal to or exceeding one per cent of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant of option.

- (5) (a) The company may by special resolution, vary the terms of Employees Stock Option Scheme not yet exercised by the employees provided such variation is not prejudicial to the interests of the option holders.

- (b) The notice for passing special resolution for variation of terms of Employees Stock Option Scheme shall disclose full of the variation, the rationale therefore, and the details of the employees who are beneficiaries of such variation.

- (6) (a) There shall be a minimum period of one year between the grant of options and vesting of option.

Provided that in a case where options are granted by a company under its Employees Stock Option Scheme in lieu of options held by the same person under an Employees Stock Option Scheme in another company, which has merged or amalgamated with the first mentioned company, the period during which the options granted by the merging or amalgamating company were held by him shall be adjusted against the minimum vesting period required under this clause;

- (b) The company shall have the freedom to specify the lock-in period for the shares issued pursuant to exercise of option.

- (c) The Employees shall not have right to receive any dividend or to vote or in any manner enjoy the benefits of a shareholder in respect of option granted to them, till shares are issued on exercise of option.

- (7) The amount, if any, payable by the employees, at the time of grant of option-

- (a) Maybe forfeited by the company if the option is not exercised by the employees within the exercise period; or
  - (b) The amount may be refunded to the employees if the options are not vested due to non-fulfillment of conditions relating to vesting of option as per the Employees Stock Option Scheme.
- (8) (a) The option granted to employees shall not be transferable to any other person.
- (b) The option granted to the employees shall not be pledged, hypothecated, mortgaged or otherwise encumbered or alienated in any other manner.
  - (c) No person other than the employees to whom the option is granted shall be entitled to exercise the option.
  - (d) In the event of the death of employee while in employment, all the options granted to him till such date shall vest in the legal heirs or nominees of the deceased employee.
  - (e) In case the employee suffers a permanent incapacity while in employment, all the options granted to him as on the date of permanent incapacitation, shall vest in him on that day.
  - (f) In the event of resignation or termination of employment, all options not vested in the employee as on that day shall expire. However, the employee can exercise the options granted to him which are vested within the period specified in this behalf, subject to the terms and conditions under the scheme granting such options as approved by the Board.
- (9) The details to be disclosed in Board of directors should be ensured. ,
- (10) (a) The company shall maintain a Register of Employee Stock Options in **Form No. SH.6** and shall enter therein the particulars of option. Such registrar shall be maintained at the registered office of the company or such other place as the Board may decide.
- (b) The entries in the register shall be authenticated by the company secretary of the company or by any other person authorized by the Board for the purpose.
- (11) Once the allotment is made, the company shall within 30 days of allotment, file with the Registrar are turn of allotment in **Form PAS.3**, along with the fee as specified in Companies (Registration of Offices and Fees) Rules, 2014.
- (12) Deliver the share certificates of allotted shares within a period of 2 months from the date of allotment.
- (13) Intimate the details of allotment of shares to the Depository immediately on allotment of such shares
- (14) Where the equity shares of the company are listed on a recognized stock exchange, the Employees Stock Option Scheme shall be issued, in accordance with the regulations made by the Securities and Exchange Board of India in this behalf.

## ISSUE OF SHARES ON PREFERENTIAL BASIS

As discussed earlier, section 62(1)(c) deals with issue of shares to persons other than existing shareholders and provides that a company can issue further shares to persons other than existing shareholders either for cash or for a consideration other than cash, if —

- (a) The company in General Meeting passes a special resolution to this effect; and
- (b) The price of such shares is determined by the valuation report of a registered valuer, subject to the compliance with the applicable provisions of Chapter III and any other conditions as may be prescribed.

**RULE 13 OF COMPANIES (SHARE CAPITAL AND DEBENTURES) RULES, 2014****Preferential offer [Rule 13(1)]**

The expression '*Preferential Offer*' means an issue of shares or other securities, by a company to any select person or group of persons on a preferential basis and does not include shares or other securities offered through a public issue, rights issue, employee stock option scheme, employee stock purchase scheme or an issue of sweat equity shares or bonus shares or depository receipts issued in a country outside India or foreign securities.

**Preferential offer by unlisted companies to comply with the rules [Rule 13(2) & (3)]**

When the preferential offer of shares or other securities is made by a company whose share or other securities are listed on a recognized stock exchange, such preferential offer shall be made in accordance with the provisions of the Act and regulations made by the SEBI, and if they are not listed, the preferential offer shall be made in accordance with the provisions of the Act and rules made hereunder and subject to compliance with the under mentioned requirements:

- (a) The issue is authorized by its articles of association;
- (b) The issue has been authorized by a special resolution of the members;
- (d) While taking a decision it is important that all information is provide with regard to the matter, hence the company shall make the following disclosures in the explanatory statement to be annexed to the notice of the general meeting:
  - (i) The objects of the issue;
  - (ii) The total number of shares or other securities to be issued;
  - (iii) The price or price band at/within which the allotment is proposed;
  - (iv) Basis on which the price has been arrived at along with report of the registered valuer;
  - (v) Relevant date with reference to which the price has been arrived at;
  - (vi) The class or classes of persons to whom the allotment is proposed to be made;
  - (vii) Intention of promoters, directors or key managerial personnel to subscribe to the offer;
  - (viii) The proposed time within which the allotment shall be completed;
  - (ix) The names of the proposed allottees and the percentage of post preferential offer capital that may be held by them;
  - (xi) The change in control, if any, in the company that would occur consequent to the preferential offer;
  - (xii) The number of persons to whom allotment on preferential basis have already been made during the year, in terms of number of securities as well as price;
  - (xiii) The justification for the allotment proposed to be made for consideration other than cash together with valuation report of the registered valuer.
  - (xiv) The pre issue and post issue shareholding pattern of the company in the prescribed format
- (e) the allotment of securities on a preferential basis shall be completed within a period of twelve months from the date of passing of the special resolution.

- (f) If the allotment of securities is not completed within twelve months from the date of passing of the special resolution, another special resolution shall be passed for the company to complete such allotment thereafter.
- (g) The price of the shares or other securities to be issued on a preferential basis, either for cash or for consideration other than cash, shall be determined on the basis of valuation report of a registered valuer;
- (h) where convertible securities are offered on a preferential basis with an option to apply for and get equity shares allotted, the price of the resultant shares pursuant to conversion shall be determined-
  - (i) either upfront at the time when the offer of convertible securities is made, on the basis of valuation report of the registered valuer given at the stage of such offer, or
  - (ii) at the time, which shall not be earlier than thirty days to the date when the holder of convertible security becomes entitled to apply for shares, on the basis of valuation report of the registered valuer given not earlier than sixty days of the date when the holder of convertible security becomes entitled to apply for shares:

The company should take a decision on sub-clauses (i) or (ii) at the time of offer of convertible security itself and make such disclosure in explanatory statement;

- (i) Where shares or other securities are to be allotted for consideration other than cash, the valuation of such consideration shall be done by a registered valuer who shall submit a valuation report to the company giving justification for the valuation;
- (j) Where the preferential offer of shares is made for a non-cash consideration, such non-cash consideration shall be treated in the following manner in the books of account of the company-
  - (i) where the non-cash consideration takes the form of a depreciable or amortizable asset, it shall be carried to the balance sheet of the company in accordance with the accounting standards; or
  - (ii) where clause (i) is not applicable, it shall be expensed as provided in the accounting standards.

Until a registered valuer is appointed in accordance with the provisions of the Act, the valuation report shall be made by an independent merchant banker who is registered with the Securities and Exchange Board of India or an independent Chartered Accountant in practice having a minimum experience of ten years.

According to Rule 13(3), the price of shares or other securities to be issued on preferential basis shall not be less than the price determined on the basis of valuation report of a registered valuer.

*(Further in case of listed companies the price of shares to be issued on a preferential basis is not required to be determined by the valuation report of a registered valuer).*

*In case the preferential offer is made by a company to one or more existing members only, few provisions relating to private placement in PAS-5 & offer letter in PAS-4 shall not apply.*

### **Procedure for issue of shares on Preferential basis**

- (a) Check whether the issue is authorize by Articles. If not make necessary amendments to alter the articles of association, through special resolution passed at the shareholders' meeting.
- (b) Convene a Board Meeting to approve the notice of General Meeting and necessary special Resolution/s along with explanatory statements as required.

It is to be noted that preferential issue of share are required to comply with section 42 also which relates to private placement. However, in case of preferential offer to one or more existing members the aspects relating to letter offer as stated in rule14(1) and proviso to rule1 4(3) of Companies (Prospectus & Allotment of Securities) Rules, 2014 shall not apply.

- (c) The company shall ensure that all the disclosures in the explanatory statement are annexed to the notice of the general meeting pursuant to section102 of the Act:
- (d) Convene General Meeting and pass necessary Special Resolution/s.
- (e) Ensure to file Form MGT-14 with Registrar of Companies with in 30 days of passing the Resolution.
- (f) the allotment of securities on a preferential basis made pursuant to the special resolution passed shall be completed with in a period of 12 months from the date of passing of the special resolution. If the allotment of securities is not completed within 12 months from the date of passing of the special resolution, another special resolution shall be passed for the company to complete such allotment thereafter.
- (g) the price of the shares or other securities to be issued on a preferential basis, either for cash or for consideration other than cash, shall be determined on the basis of valuation report of a registered valuer; and when convertible securities are offered on a preferential basis with an option to apply for and get equity shares allotted, the price of the resultant shares pursuant to conversion shall be determined:
  - (i) either up front at the time when the offer of convertible securities is made on the basis of valuation report of the registered valuer given at the stage of such offer, or
  - (ii) at the time, which shall not be earlier than thirty days to the date when the holder of convertible security becomes entitled to apply for shares, on the basis of valuation report of the registered valuer given not earlier than sixty days of the date when the holder of convertible security becomes entitled to apply for shares.

The company shall take a decision on the above clause (i) and (ii) at the time of offer of convertible security itself and make such disclosure in the explanatory statement to be annexed to the notice.
- (h) Where shares or other securities are to be allotted for consideration other than cash, the valuation of such consideration shall be done by a registered valuer who shall submit a valuation report to the company giving justification for the valuation;
- (i) Where the preferential offer of shares is made for a non-cash consideration, such non-cash consideration shall be treated in the following manner in the books of account of the company-
  - (i) Where the non-cash consideration takes the form of a depreciable or a mortizable asset, it shall be carried to the balance sheet of the company in accordance with the accounting standards; or
  - (ii) Where clause (i) is not applicable, it shall be expensed as provided in the accounting standards.
- (j) Once the allotment is made, the company shall within 30 days of allotment, file with the Registrar a return of allotment in **Form PAS.3**, along with the fee as specified in Companies (Registration of Offices and Fees) Rules, 2014.
- (k) Deliver the share certificates of allotted shares within a period of 2 months from the date of allotment.
- (l) Intimate the details of allotment of shares to the Depository immediately on allotment of such shares

## **PRIVATE PLACEMENT OF SHARES**

As per Explanation I to Section 42(3), "private placement" means any offer or invitation to subscribe or issue of securities to a select group of persons by a company (other than by way of public offer) through private placement offer-cum-application, which satisfies the conditions specified in this section.

### **Private Placement Offer – cum Application**

Section 42(1) provides that a company may, subject to the provisions of this section, make a private placement of securities.

Section 42(3) reads, a company making private placement shall issue private placement offer and application in such form and manner as may be prescribed to identified persons, whose names and addresses are recorded by the company in such manner as may be prescribed. The private placement offer and application shall not carry any right of renunciation.

### **Maximum number of persons to whom offer can be made and other incidental matters**

As per section 42(2), a private placement shall be made only to a select group of persons who have been identified by the Board (herein referred to as "identified persons"), whose number shall not exceed fifty or such higher number as may be prescribed [excluding the qualified institutional buyers and employees of the company being offered securities under a scheme of employees stock option in terms of provisions of clause (b) of sub-section (1) of section 62], in a financial year subject to such conditions as may be prescribed.

"qualified institutional buyer" has been defined under the section to mean that the qualified institutional buyer as defined in the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009, as amended from time to time.

Accordingly any offer or invitation made to qualified institutional buyers, or to employees of the company under a scheme of employees stock option as per provisions of clause (b) of sub-section (1) of section 62 shall not be considered while calculating the number of identified persons.

Where a company, listed or unlisted, makes an offer to allot or invites subscription, or allots, or enters into an agreement to allot, securities to more than the prescribed number of persons, whether the payment for the securities has been received or not or whether the company intends to list its securities or not on any recognised stock exchange in or outside India, the same shall be deemed to be the public offer and shall be accordingly dealt.

### **Applying to private placement**

As per section 42(4) states that every identified person willing to subscribe to the private placement issue shall apply in the private placement and application issued to such person along with subscription money paid either by cheque or demand draft or other banking channel and not by cash:

Hence all the payments have to be made either by cheque or demand draft or other banking channel and not by cash.

However, a company shall not utilise monies raised through private placement unless allotment is made and the return of allotment is filed with the Registrar.

According to subsection (5) the company shall make any fresh offer or invitation with respect to private placement unless the allotments with respect to any offer or invitation made earlier have been completed or that offer or invitation has been withdrawn or abandoned by the company.

A company may, at any time, make more than one issue of securities to such class of identified persons as may be prescribed subject to the maximum number of identified persons as stated above.

#### **Time limit for allotment and payment of interest/refund of subscription money otherwise**

Section 42(6) states that a company making an offer or invitation under this section shall allot its securities within sixty days from the date of receipt of the application money for such securities and if the company is not able to allot the securities within that period, it shall repay the application money to the subscribers within fifteen days from the expiry of sixty days and if the company fails to repay the application money within the aforesaid period, it shall be liable to repay that money with interest at the rate of twelve per cent per annum from the expiry of the sixtieth day.

#### **Subscription money to be kept in a separate bank account**

Proviso to Section 42(6) states that monies received on application received by the company shall be kept in a separate bank account in a scheduled bank and shall not be utilised for any purpose other than—

- (a) for adjustment against allotment of securities; or
- (b) for the repayment of monies where the company is unable to allot securities.

#### **Offer to be made specifically addressing persons**

Section 42(7) states that no company issuing securities under this section shall release any public advertisements or utilise any media, marketing or distribution channels or agents to inform the public at large about such an issue.

#### **Return of allotment**

Section 42(8) states that a company making any allotment of securities, shall file with the Registrar a return of allotment within fifteen days from the date of the allotment in such manner as may be prescribed, including a complete list of all allottees, with their full names, addresses, number of securities allotted and such other relevant information as may be prescribed.

Where a company defaults in filing the return of allotment within the period mentioned above, the company, its promoters and directors shall be liable to a penalty for each default of one thousand rupees for each day during which such default continues but not exceeding twenty-five lakh rupees.

#### **Penalty**

According to section 42(10), if a company makes an offer or accepts monies in contravention of this section, the company, its promoters and directors shall be liable for a penalty which may extend to the amount raised through the private placement or two crore rupees, whichever is lower, and the company shall also refund all monies with interest to subscribers within a period of thirty days of the order imposing the penalty.

Section 42(11) states that notwithstanding anything contained in sub-section (9) and sub-section (10), any private placement issue not made in compliance of the provisions of the sub-section (2) shall be deemed to be a public offer and all the provisions of this Act and the Securities Contracts (Regulation) Act, 1956 and the Securities and Exchange Board of India Act, 1992 shall be applicable.

#### **BONUS SHARES**

A company may, if its Articles provide, capitalize its profits by issuing fully-paid bonus shares. The issue of bonus shares by a company is a common feature. When a company is prosperous and accumulates large

distributable profits, it converts these accumulated profits into capital and divides the capital among the existing members in proportion to their entitlements. Members do not have to pay any amount for such shares. They are given free. The bonus shares allotted to the members do not represent taxable income in their hands. Issue of bonus shares is bare machinery for capitalizing undistributed profits. The vesting of rights in bonus shares takes place when the shares are actually allotted; and not from any earlier date.

*Advantages of Issuing Bonus Shares:*

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

**Sources for issue of Bonus shares**

According to section 63(1), a company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of—

- (i) its free reserves;
- (ii) the securities premium account; or
- (iii) the capital redemption reserve account.

*No issue of bonus shares shall be made by capitalising reserves created by the revaluation of assets*

**Conditions for issue of Bonus Shares**

In terms of section 63(2), no company shall capitalise its profits or reserves for the purpose of issuing fully paid-up bonus shares, unless—

- (a) it is authorised by its articles;
- (b) it has, on the recommendation of the Board, been authorised in the general meeting of the company;
- (c) it has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it;
- (d) it has not defaulted in respect of the payment of statutory dues of the employees, such as, contribution to provident fund, gratuity and bonus;
- (e) the partly paid-up shares, if any outstanding on the date of allotment, are made fully paid-up.

**No Bonus shares in lieu of dividend**

The bonus shares shall not be issued in lieu of dividend. [Section 63(3)]

SEBI has issued regulations for Bonus Issue which are contained in Chapter IX of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 with regard to bonus issues by listed companies.

According to Rule 14 of Companies (Share Capital and Debentures) Rules, 2014 states that the company

which has once announced the decision of its Board recommending a bonus issue, shall not subsequently withdraw the same.

### Procedure for issue of Bonus share

1. Check whether the Article of Association authorizes issue of bonus share. If not, the name and the Articles of Association of the company by passing the Special Resolution.
2. Check whether the Bonus issue results in increase of authorized capital. If so, make necessary alterations in the Memorandum/Articles of Association by passing special Resolution.
3. In the case of listed entity, give prior intimation to the stock exchange at least two working days in advance of the date of Board Meeting excluding the date of intimation and the date of the meeting [Refer Regulation 29 of Listing Regulations]
4. Hold the Board Meeting and get the following proposal to be approved by the Board:
  - (i) To recommend the bonus issue;
  - (ii) To approve the resolution to be passed at a general meeting;
    - (a) To authorize the Bonus issue
    - (b) To approve requisite resolution for increase of the capital and consequential alteration of the Memorandum of Association/Articles of Association (if necessary)
    - (c) To enable the Articles to authorize the issue, if necessary.
5. Ensure that bonus issue has been made out of free reserves built out of the genuine profits or securities premium or capital redemption reserve account.
6. Ensure that reserves created by revaluation of assets are not capitalized.
7. Ensure that the company has not defaulted in payment of interest or principal in respect of fixed deposits and or debt securities issued by it or in respect of the payment of statutory dues of the employees such as contribution to provident fund, gratuity, bonus etc.
8. Ensure that the bonus issue is not made in lieu of dividend.
9. The company which has once announced the decision of its Board recommending a bonus issue shall not subsequently withdraw the same.
10. If there are any partly paid-up shares, ensure that these are made fully paid-up before the bonus issue is recommended by the Board of directors.
11. Hold the general meeting and get the resolution/s for issue of bonus shares passed by the members.
12. Once Special Resolution is passed file **Form MGT-14** along with the fees with the Registrar **with in 30 days** of passing of the resolution along with the altered article of association.
13. With in 30 days of allotment file with the registrar the Return of allotment in **Form PAS-3** along with fee as specified in Companies (Registration of Offices and Fees), Rules 2014.
14. All share certificates shall be delivered to the shareholders within two months from the date of allotment of bonus issue as required under section 56(4). In case of a Specified IFSC public and private company the share certificates shall be delivered within sixty days of allotment.

15. Intimate the details of allotment of shares to the Depository immediately on allotment of such shares.
16. In case of listed companies, the conditions prescribed under SEBI (LODR), Reg 2015 and SEBI (ICDR) Reg, 2009 are to be complied with.

## **SWEAT EQUITY SHARES**

### **Issue of Sweat Equity Shares**

According to section 2(88), sweat equity shares mean such equity shares issued by a company to its directors or employees at a discount or for consideration, other than cash for providing their know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

According to Explanation to Rule 8(1) of Companies (Share Capital and Debentures) Rules, 2014:

- (ii) the expression "Employee" means –
  - (a) a permanent employee of the company who has been working in India or outside India, for at least last one year; or
  - (b) a director of the company, whether a whole time director or not; or
  - (c) an employee or a director as defined in sub-clauses (a) or (b) above of a subsidiary, in India or outside India, or of a holding company of the company;
- (iii) the expression 'Value additions' means actual or anticipated economic benefits derived or to be derived by the company from an expert or a professional for providing know-how or making available rights in the nature of intellectual property rights, by such person to whom sweat equity is being issued for which the consideration is not paid or included in the normal remuneration payable under the contract of employment, in the case of an employee.

Section 54 permits issue of such equity shares to employees or directors in recognition of their contribution for providing know-how etc. as aforesaid. As the contribution made by employees/directors results in increased profits to the company for a number of years, sweat equity shares provide a new form of adequate return.

### **Conditions for Issue of Sweat Equity Shares**

Section 54(1) provides that notwithstanding anything contained in Section 53, a company can issue sweat equity shares, of a class of shares already issued, if the following conditions are satisfied:

- (i) the issue has been authorized by a special resolution passed by the company in the general meeting.
- (ii) the following are clearly specified in the resolution:
  - (a) number of shares;
  - (b) current market price;
  - (c) consideration, if any; and
  - (d) class or classes of directors or employees to whom such equity shares are to be issued.
- (iii) Where shares are listed on a recognized stock exchange, the company issuing sweat equity shares

should comply with the regulations made in this behalf by SEBI.

- (iv) a company whose shares are not so listed should issue sweat equity shares in compliance with the rules made in this behalf by the Central Government *i.e.*, Companies (Share Capital and Debentures) Rules, 2014.

### **Holders of Sweat Equity Shares to be ranked *pari passu* with other Equity shareholders**

Section 54(2) provides that the rights, limitations, restrictions and provisions as are for the time being applicable to equity shares shall be applicable to the sweat equity shares issued under this section and the holders of such shares shall rank *pari passu* with other equity shareholders.

### **Companies (Share Capital and Debentures) Rules, 2014**

#### ***Explanatory Statement to Special Resolution to contain certain particulars***

While taking a decision it is important that all information is provide with regard to the matter, hence rule 8(2) states that the explanatory statement to be annexed to the notice of the general meeting shall contain the following particulars, namely:-

- (a) the date of the Board meeting at which the proposal for issue of sweat equity shares was approved;
- (b) the reasons or justification for the issue;
- (c) the class of shares under which sweat equity shares are intended to be issued;
- (d) the total number of shares to be issued as sweat equity;
- (e) the class or classes of directors or employees to whom such equity shares are to be issued;
- (f) the principal terms and conditions on which sweat equity shares are to be issued, including basis of valuation;
- (g) the time period of association of such person with the company;
- (h) the names of the directors or employees to whom the sweat equity shares will be issued and their relationship with the promoter or/and Key Managerial Personnel;
- (i) the price at which the sweat equity shares are proposed to be issued;
- (j) the consideration including consideration other than cash, if any to be received for the sweat equity;
- (k) the ceiling on managerial remuneration, if any, be breached by issuance of such sweat equity and how it is proposed to be dealt with;
- (l) a statement to the effect that the company shall conform to the applicable accounting standards; and
- (m) diluted Earning Per Share pursuant to the issue of sweat equity shares, calculated in accordance with the applicable accounting standards.

#### ***Validity of Special Resolution authorizing sweat equity shares***

Rule 8(3) states the special resolution authorising the issue of sweat equity shares shall be valid for making the allotment within a period of not more than twelve months from the date of passing of the special resolution.

#### ***Limits on issue of sweat equity shares***

Rule 8(4) states that the company shall not issue sweat equity shares for more than fifteen percent of the

existing paid up equity share capital in a year or shares of the issue value of rupees five crores, whichever is higher. The issuance of sweat equity shares in the company shall not exceed twenty five percent, of the paid up equity capital of the company at any time.

### ***Sweat Equity Shares to be locked for three years***

The sweat equity shares issued to directors or employees shall be locked for a period of three years from the date of allotment and the fact that the share certificates are under lock-in and the period of expiry of lock in shall be stamped in bold or mentioned in any other prominent manner on the share certificate. [Rule 8(5)]

### ***Valuation aspects***

- *Rule 8(6)* states that the sweat equity shares to be issued shall be valued at a price determined by a registered valuer as the fair price giving justification for such valuation.
- *Rule 8(7)* states that the valuation of intellectual property rights or of know how or value additions for which sweat equity shares are to be issued, shall be carried out by a registered valuer, who shall provide a proper report addressed to the Board of directors with justification for such valuation.
- *Rule 8(8)* states that a copy of gist along with critical elements of the valuation report obtained under Rule 8 (6) and Rule 8 (7) shall be sent to the shareholders with the notice of the general meeting.

### ***Sweat equity shares for non-cash consideration***

Rule 9 states that when sweat equity shares are issued for a non-cash consideration on the basis of a valuation report in respect thereof obtained from the registered valuer, such non-cash consideration shall be treated in the following manner in the books of account of the company –

- (a) where the non-cash consideration takes the form of a depreciable or amortizable asset, it shall be carried to the balance sheet of the company in accordance with the accounting standards; or
- (b) where clause (a) is not applicable, it shall be expensed as provided in the accounting standards.

### ***Sweat equity shares forming part of managerial remuneration***

Rule 8(10) states that the amount of sweat equity shares issued shall be treated as part of managerial remuneration for the purposes of sections 197 and 198 of the Act, if the following conditions are fulfilled, namely –

- (a) the sweat equity shares are issued to any director or manager; and
- (b) they are issued for consideration other than cash, which does not take the form of an asset which can be carried to the balance sheet of the company in accordance with the applicable accounting standards.

### ***Sweat equity shares and compensation aspects***

- *If the sweat equity shares are not issued pursuant to acquisition of an asset*  
 Rule 8(11) states that in respect of sweat equity shares issued during an accounting period, the accounting value of sweat equity shares (*i.e.*, fair value by Registered valuer shall be treated as a form of compensation to the employee or the director in the financial statements of the company.
- *If the shares are issued pursuant to acquisition of an asset*  
 Rule 8(12) states that if the shares are issued pursuant to acquisition of an asset, the value of the asset, as determined by the valuation report, shall be carried in the balance sheet as per the

Accounting Standards and such amount of the accounting value of the sweat equity shares that is in excess of the value of the asset acquired, as per the valuation report, shall be treated as a form of compensation to the employee or the director in the financial statements of the company.

### **Board's Report to disclose the details of sweat equity shares**

According to rule 8(13) the details of issue during the year in which such shares are issued are to be disclosed in the Board's report of the company. The details are given in chapter "Transparency and Disclosures", later in this study.

### **Maintenance of Register**

Rule 8(14) states that the company shall maintain a Register of Sweat Equity Shares in Form No. SH.3 and shall forthwith enter therein the particulars of Sweat Equity Shares issued under section 54. The Register of Sweat Equity Shares shall be maintained at the registered office of the company or such other place as the Board may decide. The entries in the register shall be authenticated by the Company Secretary of the company or by any other person authorized by the Board for the purpose.

## **Part D: Buy Back of Securities**

### **BUY BACK OF SECURITIES (SECTION 68)**

#### **Sources**

According to Section 68(1) of the Companies Act, 2013 a company may purchase its own shares or other specified securities (hereinafter referred to as "buy-back") out of:

- (i) its free reserves; or
- (ii) the securities premium account; or
- (iii) the proceeds of the issue of any shares or other specified securities.

However, no buy-back of any kind of shares or other specified securities can be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.

Thus, the company must have at the time of buy-back, sufficient balance in any one or more of these accounts to accommodate the total value of the buy-back.

Free reserves has been defined under section 2(43) of the Act as such reserves which, as per the latest audited balance sheet of a company, are available for distribution as dividend: Further it has been provided that the following shall not be treated as free reserves:

- (i) any amount representing unrealised gains, notional gains or revaluation of assets, whether shown as a reserve or otherwise, or
- (ii) any change in carrying amount of an asset or of a liability recognised in equity, including surplus in profit and loss account on measurement of the asset or the liability at fair value, shall not be treated as free reserves.

#### **Authorisation [Section 68(2)]**

The primary requirement is that the articles of association of the company should authorise buyback. In case, such a provision is not available, it would be necessary to alter the articles of association to authorise buy-back. Buy-back can be made with the approval of the Board of directors at a board meeting and/or by a special resolution passed by shareholders in a general meeting, depending on the quantum of buy back. In

case of a listed company, approval of shareholders shall be obtained only by postal ballot.

### **Quantum [Section 68(2)]**

Board of directors can approve buy-back up to 10% of the total paid-up equity capital and free reserves of the company and such buy back by means of a resolution passed at the meeting.

Shareholders by a special resolution can approve buy-back up to 25% of the total paid-up capital and free reserves of the company, in respect of any financial year.

Board can authorise buy back upto 10% equity capital and free reserves in a resolution passed at its Meeting.

Shareholders can authorize buy back by special resolution upto 25% of the total paid-up capital and free reserves of the company in a financial year.

### **Special Resolution to be accompanied by Explanatory Statement [Section 68(3)]**

The notice of the meeting at which the special resolution is proposed to be passed shall be accompanied by an explanatory statement stating—

- a full and complete disclosure of all material facts;
- the necessity for the buy-back;
- the class of shares or securities intended to be purchased under the buy-back;
- the amount to be invested under the buy-back; and
- the time-limit for completion of buy-back.

### **Companies (Share Capital and Debentures) Rules, 2014**

#### ***Explanatory statement to contain certain disclosures [Rule 17(1)]***

*Explanatory statement to the special resolution authorising buy-back to be annexed to the notice of the general meeting pursuant to section 102 shall contain the following disclosures:*

- (a) the date of the board meeting at which the proposal for buy-back was approved by the board of directors of the company;
- (b) the objective of the buy-back;
- (c) the class of shares or other securities intended to be purchased under the buy-back;
- (d) the number of securities that the company proposes to buy-back;
- (e) the method to be adopted for the buy-back;
- (f) the price at which the buy-back of shares or other securities shall be made;
- (g) the basis of arriving at the buy-back price;
- (h) the maximum amount to be paid for the buy-back and the sources of funds from which the buy-back would be financed
- (i) the time-limit for the completion of buy-back;
- (j) (i) the aggregate shareholding of the promoters and of the directors of the promoter, where the

- promoter is a company and of the directors and key managerial personnel as on the date of the notice convening the general meeting;
- (ii) the aggregate number of equity shares purchased or sold by persons mentioned in (i) above during a period of twelve months preceding the date of the board meeting at which the buy-back was approved and from that date till the date of notice convening the general meeting;
  - (iii) the maximum and minimum price at which purchases and sales referred to in (ii) above were made along with the relevant date;
- (k) if the persons mentioned in sub-clause (i) of clause (j) intend to tender their shares for buy-back –
- (i) the quantum of shares proposed to be tendered;
  - (ii) the details of their transactions and their holdings for the last twelve months prior to the date of the board meeting at which the buy-back was approved including information of number of shares acquired, the price and the date of acquisition.
- (l) a confirmation that there are no defaults subsisting in repayment of deposits, interest payment thereon, redemption of debentures or payment of interest thereon or redemption of preference shares or payment of dividend due to any shareholder, or repayment of any term loans or interest payable thereon to any financial institution or banking company;
- (m) a confirmation that the Board of directors have made a full enquiry into the affairs and prospects of the company and that they have formed the opinion –
- (i) that immediately following the date on which the general meeting is convened there will be no grounds on which the company could be found unable to pay its debts;
  - (ii) as regards its prospects for the year immediately following that date, that, having regard to their intentions with respect to the management of the company's business during that year and to the amount and character of the financial resources which will in their view be available to the company during that year, the company will be able to meet its liabilities as and when they fall due and will not be rendered insolvent within a period of one year from that date; and
  - (iii) in forming their opinion for the above purposes, the directors have taken into account the liabilities (including prospective and contingent liabilities); as if the company were being wound up under the provisions of the Companies Act, 2013.
- (n) a report addressed to the Board of directors by the company's auditors stating that:
- (i) they have inquired into the company's state of affairs;
  - (ii) the amount of the permissible capital payment for the securities in question is in their view properly determined;
  - (iii) that the audited accounts on the basis of which calculation with reference to buy back is done is not more than six months old from the date of offer document, and
  - (iv) the Board of directors have formed the opinion as specified in clause (m) on reasonable grounds and that the company, having regard to its state of affairs, will not be rendered insolvent within a period of one year from that date;

***Letter of Offer to be Filed with Registrar of Companies before Buy-Back [Rule 17(2)]***

The company which has been authorized by a special resolution shall, before the buy-back of shares, file with the Registrar of Companies a letter of offer in Form No. SH. 8, along with the fee as prescribed. Such letter of offer shall be dated and signed on behalf of the Board of directors of the company by not less than

two directors of the company, one of whom shall be the managing director, where there is one.

***Dispatch of letter of offer to shareholders [Rule 17(4)]***

The letter of offer shall be dispatched to the shareholders or security holders immediately after filing the same with the Registrar of Companies but not later than 21 days from its filing with the Registrar of Companies.

***Period of offer for buy back [Rule 17(5)]***

The offer for buy-back shall remain open for a period of not less than 15 days and not exceeding 30 days from the date of dispatch of the letter of offer.

***Post buy-back debt-equity ratio [Section 68(2)(d)]***

The ratio of the aggregate of secured and unsecured debts owed by the company after buy-back is not more than twice the paid-up capital and its free reserves. However, the Central Government may, by order, notify a higher ratio of the debt to capital and free reserves for a class or classes of companies.

***Shares/Securities being Bought Back are to be Fully Paid-up [Section 68(2)]***

No company shall purchase its own shares or other specified securities unless all the shares or other specified securities for buy-back are fully paid-up.

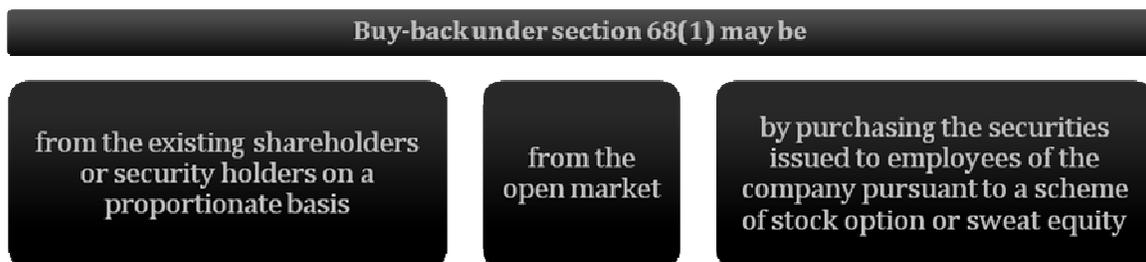
***Time gap between two buy-backs [Proviso to Section 68(2)(g)]***

No offer of buy-back under Section 68(2) shall be made within a period of one year reckoned from the date of the closure of the preceding offer of buy-back, if any.

***Time limit for completion of buy-back [Section 68(4)]***

Every buy-back shall be completed within a period of one year from the date of passing of the special resolution, or as the case may be, the resolution passed by the Board.

***Methods of buy-back [Section 68(5)]***



***Filing Declaration of Solvency with SEBI/ROC [Section 68(6) read with Rule 17(3)]***

When a company proposes to buy-back its own shares or other specified securities under this section in pursuance of a special resolution or board resolution as the case may be, it shall, before making such buy-back, file with the Registrar and the Securities and Exchange Board (in case of listed companies), a declaration of solvency signed by at least two directors of the company, one of whom shall be the managing

director, if any, in Form No. SH.9 and verified by an affidavit to the effect that the Board of Directors of the company has made a full inquiry into the affairs of the company as a result of which they have formed an opinion that it is capable of meeting its liabilities and will not be rendered insolvent within a period of one year from the date of declaration adopted by the Board.

***Extinguishment of securities bought back [Section 68(7)]***

When a company buys back its own shares or other specified securities, it shall extinguish and physically destroy the shares or securities so bought back within seven days of the last date of completion of buy-back.

***Prohibition of further issue of shares or securities [Section 68(8)]***

When a a company completes a buy-back of its shares or other specified securities it shall not make a further issue of the same kind of shares or other securities including allotment of new shares under clause (a) of sub-section (1) of section 62 or other specified securities within a period of six months except by way of a bonus issue or in the discharge of subsisting obligations such as conversion of warrants, stock option schemes, sweat equity or conversion of preference shares or debentures into equity shares.

***Register of buy-back [Section 68(9)]***

When a company buys back its shares or other specified securities under this section, it shall maintain a register of the shares or securities so bought, the consideration paid for the shares or securities bought back, the date of cancellation of shares or securities, the date of extinguishing and physically destroying the shares or securities and other particulars.

***Return of buyback [Section 68(10)]***

A company shall, after the completion of the buy-back under this section, file with the Registrar and the Securities and Exchange Board (in case of listed companies) a return containing such particulars relating to the buy-back within thirty days of such completion, as may be prescribed.

Rule 17(14) of Companies (Share Capital and Debentures) Rules, 2014 states that a certificate in Form No. SH.15 signed by two directors of the company including the managing director, if any, certifying that the buy-back of securities has been made in compliance with the provisions of the Act and the rules made there under shall be annexed to the return filed with the Registrar in Form No. SH.11.

***Punishments [Section 68(11)]***

If a company makes any default in complying with the provisions of this section or any regulation made by the Securities and Exchange Board, in case of listed companies, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees, or with both.

***Transfer to and application of Capital Redemption Reserve Account [Section 69]***

When a company purchases its own shares out of free reserves or securities premium account, a sum equal to the nominal value of the shares so purchased shall be transferred to the capital redemption reserve account and details of such transfer shall be disclosed in the balance sheet. The capital redemption reserve account may be applied by the company, in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares.

***Circumstances prohibiting buy-back [Section 70(1)]***

No company shall directly or indirectly purchase its own shares or other specified securities—

- through any subsidiary company including its own subsidiary companies;
- through any investment company or group of investment companies; or
- if a default, is made by the company, in the repayment of deposits accepted either before or after the commencement of this Act, interest payment thereon, redemption of debentures or preference shares or payment of dividend to any shareholder, or repayment of any term loan or interest payable thereon to any financial institution or banking company: However, the buy-back is not prohibited, if the default is remedied and a period of three years has lapsed after such default ceased to subsist. [Proviso to Section 70(1)]

No company shall, directly or indirectly, purchase its own shares or other specified securities in case such company has not complied with the provisions of sections 92 (Annual Return), section 123 (Declaration of Dividend), section 127 (punishment for failure to distribute dividend) and section 129 (Financial Statement).

## **Part E: Reduction of Share Capital**

### **Reduction of Share Capital (Section 66)**

#### **Approval by Special Resolution and confirmation by the Tribunal [Section 66(1)]**

Subject to confirmation by the Tribunal on an application by the company, a company limited by shares or limited by guarantee and having a share capital may, by a special resolution, reduce the share capital in any manner and in particular, may—

- (b) extinguish or reduce the liability on any of its shares in respect of the share capital not paid-up; or
- (c) either with or without extinguishing or reducing liability on any of its shares,—
  - (i) cancel any paid-up share capital which is lost or is unrepresented by available assets; or
  - (ii) pay off any paid-up share capital which is in excess of the wants of the company,
  - (iii) alter its memorandum by reducing the amount of its share capital and of its shares accordingly:

No Reduction of Capital would be allowed in case of Arrears in the Repayment of Deposits and Interest thereon [Proviso to Section 66(1)]

#### **Notice by Tribunal [Section 66(2)]**

The Tribunal shall give notice of every application made to it under sub-section (1) to:

- Central Government( Powers have been delegated to Regional Director),
- Registrar,
- the Securities and Exchange Board, in the case of listed companies, and
- the creditors of the company.

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

If no representation has been received from the Central Government, Registrar, the SEBI or the creditors

within the said period, it shall be presumed that they have no objection to the reduction. [Proviso to Section 66(2)]

### **Confirmation of Reduction of Capital [Section 66(3)]**

The Tribunal may, if it is satisfied that the debt or claim of every creditor of the company has been discharged or determined or has been secured or his consent is obtained, make an order confirming the reduction of share capital on such terms and conditions as it deems fit:

### **No sanction for reduction unless complied with accounting standards**

Proviso to Section 66(3) provides that no application for reduction of share capital shall be sanctioned by the Tribunal unless the accounting treatment, proposed by the company for such reduction is in conformity with the accounting standards specified in section 133 or any other provision of this Act and a certificate to that effect by the company's auditor has been filed with the Tribunal.

### **Publication of the order of the Tribunal [Section 66(4)]**

The order of confirmation of the reduction of share capital by the Tribunal under Section 66(3) shall be published by the company in such manner as the Tribunal may direct.

### **Deliver a copy of order of Tribunal to Registrar [Section 66(5)]**

The company shall deliver a certified copy of the order of the Tribunal under subsection (3) and of a minute (which means document submitted to Tribunal detailing the reduction and approved by the tribunal. Here the word minute has different meaning from the word minutes used for proceedings) approved by the Tribunal showing —

- (a) the amount of share capital;
- (b) the number of shares into which it is to be divided;
- (c) the amount of each share; and
- (d) the amount, if any, at the date of registration deemed to be paid-up on each share,

to the Registrar within thirty days of the receipt of the copy of the order, who shall register the same and issue a certificate to that effect.

### **DIMINUTION OF SHARE CAPITAL IS NOT A REDUCTION OF CAPITAL**

As per section 61(1)(e) of the Companies Act, 2013, diminution of capital is the cancellation of the unsubscribed part of the issued capital. It can be effected by an ordinary resolution provided articles of the company authorises to do so. According to section 61(2), cancellation of shares under section 61(1) shall not be deemed to be reduction of share capital. It does not need any confirmation of the Tribunal under section 66.

- (a) Redemption of redeemable preference shares.
- (b) Purchase of shares of a member by the Company on order of the Tribunal under Section 242 of Companies Act, 2013.
- (c) Buy-back of its own securities under Section 68.

In the following cases, the diminution of share capital is not to be treated as reduction of the capital:

- (i) Where the company cancels shares which have not been taken or agreed to be taken by any

person [Section 61(1)(e) Companies Act, 2013];

- (ii) Where redeemable preference shares are redeemed in accordance with the provisions of Section 55 [Explanation to section 55(3) Companies Act, 2013];
- (iii) Where any shares are forfeited for non-payment of calls and such forfeiture amounts to reduction of capital;
- (iv) Where the company buys-back its own shares under Section 68 of the Act [Section 66(6)];
- (v) Where the reduction of share capital is effected in pursuance of the order of the Tribunal sanctioning any compromise or arrangement under section 230.

In all these cases, the procedure for reduction of capital as laid down in Section 66 is not attracted.

## CASE LAWS

- (A) *SIEL Ltd., In re. [(2008) 144 Com Cases 469 (Del)]***, the view was that reduction of the share capital of a company is a domestic concern of the company and the decision of the majority would prevail. If the majority by special resolution decides to reduce the share capital of the company, it has the right to decide to reduce the share capital of the company and it has the right to decide how this reduction should be effected. While reducing the share capital, the company can decide to extinguish some of its shares without dealing in the same manner with all other shares of the same class. A selective reduction is permissible within the frame work of law for any company limited by shares.
- (B) *Indian National Press (Indore) Ltd., In re. (1989) 66 Com Cases 387, 392 (MP)***: The need for reducing capital may arise in various circumstances for example trading losses, heavy capital expenses and assets of reduced or doubtful value. As a result, the original capital may either have become lost or a capital may find that it has more resources than it can profitably employ. In either case, the need may arise to adjust the relation between capital and assets.
- (C) *Elpro International Ltd., In re [(2009) 149 Com Cases 646 (Bom.)]***, a company proposed to extinguish and cancel 8, 89,169 shares held by shareholders constituting 25 per cent of the issued and paid up share capital and return capital to such shareholders at Rs. 183 per equity share of Rs. 10 each so cancelled and extinguished in accordance with Section 100 of the Act (corresponds to section 66 of the Companies Act, 2013). According to the scheme as approved by the shareholders, the reducing of 25 percent of the issued and paid up capital was to take place from amongst 3,835 shareholders which included 112 shareholders who voted for the resolution, and 3,723 shareholders who did not object to the resolution. It was held that a selective reduction of share capital is legally permissible. The shareholders who did not cast their votes were those who had abstained from voting at the meeting. Moreover, there was no objection from any of the shareholders to the proposed reduction.
- (D) *British and American Trustee and Finance Corpn. v. Couper, (1894) AC 399, 403: (1991-4) All ER Rep 667***. The Act does not prescribe the manner in which the reduction of capital is to be effected. Nor is there any limitation of the power of the Court to confirm the reduction except that it must first be satisfied that all the creditors entitled to object to the reduction have either consented or been paid or secured.
- (E) *British and American Trustee Corpn. v. Couper, (1894) (ibid)*** When exercising its discretion, the Court must ensure that the reduction is fair and equitable. In short the Court shall consider the following, while sanctioning the reduction:

- (i) The interests of creditors must be safeguarded;
- (ii) The interests of shareholders must be considered; and
- (iii) Lastly, the public interest must be considered as well.

**(F) *Borough Commercial and Bldg. Society, (1893) 2 Ch 242. Reduction in shares capital of an unlimited company:*** An unlimited company to which Section 100 (corresponds to section 66 of the Companies Act, 2013) does not apply, can reduce its capital in any manner that its Memorandum and Articles of Association allow. It is not governed by Sections 61 and 66 of the Act (corresponds to section 27 and 30 of the Companies Act, 2013). Section 13 (corresponds to section 4 of the Companies Act, 2013) does not provide that its capital shall be stated in the Memorandum. However, even if its capital is stated in the Memorandum, the Companies Act impliedly gives power to the member to alter it.

**(G) *Great Universal Stores Ltd., Re (1960) 1 All ER 252: (1960)*** Reduction of capital when company is defunct: The Registrar of Companies has been empowered under Section 560 (corresponds to section 248 of the Companies Act, 2013) to strike off the name of the company from register on the ground of non-working. Therefore, where the company has ceased to trade and Registrar exercises his power under Section 560 (corresponds to section 248 of the Companies Act, 2013) a reduction of capital cannot be prevented.

**(H) *Marwari Stores Ltd. v. Gouri Shanker Goenka, (1936) 6 Com Cases 285.*** Equal Reduction of Shares of One Class: Where there is only one class of shares, prima facie, the same percentage should be paid off or cancelled or reduced in respect of each share, but where different amounts are paid-up on shares of the same class, the reduction can be effected by equalising the amount so paid-up. The same principle is to be followed where there are different classes of shares [*Bannatyne v. Direct Spanish Telegraph Co., (1886) 34 Ch D 287*].

**(I) *Asian Investments Ltd. Re, (1992) 73 Com Cases 517, 523 (Mad).*** It is, however, not necessary that extinguishment of shares in all cases should necessarily result in reduction of share capital. Accordingly where reduction is not involved Section 100 (corresponds to section 66 of the Companies Act, 2013) would not be attracted.

## REDUCTION OF SHARE CAPITAL WITHOUT SANCTION OF THE TRIBUNAL

The following are cases which amount to reduction of share capital and where no confirmation by the Tribunal is necessary:

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

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

- (a) Where forfeiture of such shares is justified; or

(b) When shares are surrendered in exchange for new shares of same nominal value.

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

**(b) Forfeiture of shares** — A company may if authorised by its articles, forfeit shares for non-payment of calls and the same will not require confirmation of the Tribunal.

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

### **Conclusiveness of certificate for reduction of capital**

Where the Registrar had issued his certificate confirming the reduction, the same was held to be conclusive although it was discovered later that the company had no authority under its articles to reduce capital [*Re Walkar & Smith Ltd.*, (1903) 88 LT 792 (Ch D)]. Similarly, in a case the special resolution for reduction was an invalid one, but the company had gone through with the reduction. It was held that the reduction was not allowed to be upset [*Ladies's Dress Assn. v. Pulbrook*, (1900) 2 QB 376].

## **Part F: Transferability – A Brief of Provisions of Companies Act, 2013**

### **TRANSFERABILITY- A BRIEF ON PROVISIONS OF COMPANIES ACT, 2013**

One of the most important characteristics of a company is that its shares are transferable. Section 44 of the Companies Act, 2013 states that the shares or debentures or other interest of any member in a company shall be movable property, transferable in the manner provided by the articles of the company.

As per section 58(2), the securities or other interest of any member in a public company shall be freely transferable. Proviso to section 58(2) provides that any contract or arrangement between two or more persons in respect of transfer of securities shall be enforceable as a contract. In terms of Section 2(68), a private company is required to restrict the right to transfer its shares by its articles. Section 56 of the Companies Act deals with transfer and transmission of securities.

### **TRANSFER OR TRANSMISSION OF SECURITIES**

#### **Free transferability of securities**

#### **PRIVATE COMPANIES**

Shares of a private company are not marketable securities due to restriction on right to transfer. Such shares by their very nature are not freely transferable in the market. The objective behind the right of restriction on the transfer of shares is to preserve the composition of the shareholding.

- The section 2(68) of the Companies Act 2013 restricts the right to transfer shares but does not prohibit the right to transfer shares. In case of transfer of shares of a private company, the provisions or restrictions contained in the Articles of Association should be duly complied with by the transferor and transferee.
- As per the provisions of section 44 of the companies Act, 2013, shares or debentures or other interest are movable property, transferable in the manner provided by the Articles of the company. Therefore, there cannot be an absolute prohibition on the right to transfer shares. The right to

transfer may be subjected to restrictions contained in the articles and there cannot be total prohibition or ban on transferability of shares. However, only permissible restriction on transferability may be contained in the Articles of association. Restrictions upon transfer of shares in private companies are not applicable in following cases:-

- (a) On the right of a member to transfer his/her shares in a case where the shares are to be transferred to his/her representative(s).
  - (b) In the event of death of a shareholder, legal representatives may require the registration of shares in the names of heirs, on whom the shares have been devolved.
  - (c) In respect of shares which are proposed to be issued on a right basis, existing members would have a right to renounce shares likely to be allotted to them. If the existing shareholders renounce their shares then these shares will be allotted to the renouces for the first time and therefore no transfer of shares will take place.
- Restriction on right to transfer shares is generally placed by using following two methods:
- (a) **Right of pre-emption:** If a member wishes to sell some or all of his shares, such shares shall first be offered to other existing members of the company at a price determined by the directors or by the auditor of the company or by the use of formula set out in the articles. If no existing member is determined to acquire shares, then shares can be transferred by the transferor to the proposed transferee. A member is not bound to sell his shares to other members under pre-emption clause unless any other member or members agree to buy all the shares proposed to be sold. The transfer between the members is outside the purview of pre-emption clause. The pre-emption clause cannot place a complete ban on right to transfer; they cannot completely prohibit the transfer.

**Valuation of Shares under Preemption clause:** Articles of Association of private company provide that the shares are to be sold under pre-emption clause at a fair price determined by the directors or the auditor of the company. It may also be provided that the fair price would be certified by the auditor of the company. If the pre-emption clause requires that the shares are required to be offered to other members at a price certified by the directors or auditor(s), the court are not in a position to enquire into the correctness of valuation, unless there is evidence that valuation was not correctly made. If the person who made the valuation has acted negligently and failed to take into account all the necessary factors for arriving at the value of share, in such case the transferor may sue for damages to the person who made the valuation for difference between the value of the share, as computed by the valuer, and the real value of shares

- (b) **Powers of directors to refuse registration of transfer of shares:** The Powers of directors to refuse registration of transfer of shares are specified in the articles of association of the company. This power is to be exercised by the Board of directors in good faith.

### ***PUBLIC COMPANY***

As per section 58(2), the securities or other interest of any member in a public company shall be freely transferable. The Board of directors of a Company or the concerned depository has no discretion to refuse or withhold transfer of any security. The transfer has to be effected by the company/depository automatically and immediately.

However, proviso to section 58(2) provides that any contract or arrangement between two or more persons in respect of transfer of securities shall be enforceable as a contract. It is now possible to contractually agree on terms such as right of first refusal, right of first offer, tag along, call option, put option, etc. in the shareholder agreements/ investment agreements, in the case of a public company as well. These terms would now be binding on the investors. Therefore, private arrangements or contracts between two or more

persons would be enforceable contracts.

***Instruments of transfer to be presented to the company***

A company, shall not register a transfer of securities of, the company, unless a proper instrument of transfer duly stamped, dated and executed by or on behalf of the transferor and the transferee has been delivered to the company by the transferor or transferee within a period of **sixty days** (irrespective of the nature of the company, whether listed or unlisted) from the date of execution along with the certificate relating to the securities, or if no such certificate is in existence, then along with the related certificate or letter of allotment of securities. In case of loss of the instrument, the company may register the transfer on terms as to indemnity.

Such instrument of transfer of securities held in physical form shall be in Form No. SH.4. Where a company not having share capital, the instrument of transfer herein should also be in Form No. SH.4 and other conditions be complied where the references therein to securities were references instead to the interest of the member in the company.

However, nothing in section 56(1) shall prejudice any power of the company to register, on receipt of an intimation of transmission of any right to securities by operation of law from any person to whom such right has been transmitted. [Section 56(2)]

***Registration of partly paid up shares – Notice to the transferee***

According to section 56(3), where an application is made by the transferor alone and relates to partly paid shares, the transfer shall not be registered, unless the company gives the notice in Form No. SH.5 to the transferee and the transferee gives 'no objection' to the transfer within two weeks from the receipt of the notice.

***Time Limit for Delivery of certificates***

Section 56(4) states that every company, unless prohibited by any provision of law or any order of Court, Tribunal or other authority, deliver the certificates of all securities allotted, transferred or transmitted:

- (i) Within a period of two months from the date of incorporation, in the case of subscribers to the memorandum;
- (ii) Within a period of two months from the date of allotment, in the case of any allotment of any of its shares;
- (iii) Within a period of one month in case of transfer or transmission of securities.
- (iv) Within a period of six months from the date of allotment in the case of any allotment of debentures.

***Intimation to depository***

Proviso to Section 56(4) states that where the securities are dealt with in a depository, the company shall intimate the details of allotment of securities to depository immediately on allotment of such securities. No transfer deed is required for transfer of shares, where the shares are held in dematerialized form.

***Transfer of securities by legal representative***

Section 56(5) of the Act provides that in case of death of holder of any security, the transfer of such security by the legal representative of the deceased shall be valid-

- Even though the legal representative is not the holder of such security;

- As if the legal representatives were the holder of such security.

### **Penalties**

According to 56(6), when any default is made in complying with the provisions of sub-sections (1) to (5), the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

### ***Transfer of shares by depository with an intent to defraud, is liable under Section 447 for fraud***

As per section 56(7), without prejudice to any liability under the Depositories Act, 1996, where any depository or depository participant, with an intention to defraud a person, has transferred shares, it shall be liable under section 447 for fraud.

### **Stamp duty payable and affixation/ cancellation of stamps at the time of transfer of shares**

Before the transfer is lodged with the company, it should be duly stamped. The transfer of securities attracts stamp duty under the Indian Stamp Act, 1899. Only the Central Government can levy stamp duty on share transfers. Stamps at the rate of twenty five paise for consideration of Rs. 100 or part thereof is payable. The duty chargeable shall, wherever necessary, be rounded off to the next five paise. [S.O. 130(E) dated 28.1.2004 issued by Department of Revenue].

The stamp duty payable on transfer of debentures is, however, governed by Article 62(b) of Schedule I to the Indian Stamp Act, 1899, and also varies from State to State. In this case, the duty would be:

- (i) The duty applicable where the deed is executed, or
- (ii) The duty applicable where the registered office of the company is situated, whichever is higher.

The amount of consideration is required to be mentioned in the share transfer deed as otherwise the companies cannot verify whether share transfer stamp duty has been correctly charged thereby attracting the penal provisions of the Stamp Act in case of a default. Thus, in case where question of consideration does not arise like in the case of a gift of shares, stamp duty will be paid on the basis of the market value of shares and in case of unquoted shares or where quotations are not available at the face value of the shares.

Under Section 56(1), a company cannot register the transfer of securities unless a proper instrument of transfer duly stamped, dated and executed by or on behalf of the transferor and the transferee has been delivered to the company along with the certificate relating to the securities in question.

The expression 'duly stamped' has not been defined in the Companies Act. Under Section 2(11) of the Indian Stamp Act, 1899, 'duly stamped' as applied to an instrument, means that the instrument bears an adhesive or impressed stamp of not less than the proper amount and that such stamp has been affixed or used in accordance with the law for the time being in force in India.

Under Section 12(1) of the Indian Stamp Act, 1899, whoever affixes an adhesive stamp to an instrument which has been executed by any person shall, when affixing such stamp, cancel the same so that it cannot be used again. Sub-section (2) thereof makes it clear that any instrument bearing an adhesive stamp which has not been cancelled so that it cannot be used again, shall, so far as such stamp is concerned, be deemed to be unstamped. Sub-section (3) thereof provides the manner in which the adhesive stamp can be cancelled and provides that the stamp be cancelled by writing on or across the stamp his name or initials or the name or initials of his firm. Section 17 of the Indian Stamp Act, 1899 makes it clear that all instruments chargeable with duty and executed shall be stamped before, or at the time of execution. Therefore, the legal requirement

is that the stamp must be cancelled either before or at the time of execution

It is necessary that the value of the consideration paid for a transfer must be determined as a part of the agreement because in the absence of such valuation it would not be possible to know whether stamp duty has been paid according to the value or not. A transfer form which does not indicate the value of the shares for the purposes of transfer would be void and not capable of being accepted.

The “value of the shares” means the price which the shares would fetch at the time of the transfer and not the face value of the shares. The consideration actually paid or agreed to be paid is the value of the shares. So long as there is nothing to indicate that the consideration was not truly stated in the transfer, the one mentioned therein should be accepted as the consideration that was paid. [*Union of India v. Kulu Valley Transport Ltd. (1958) 28 Com Cases 29 at 36 (P&H)*]

## CASE LAWS

A company cannot register transfer of shares unless the instrument of transfer is duly stamped and is delivered to the company. The expression “duly stamped” has to be construed with reference to the provisions of Section 2(11) of the Indian Stamp Act, 1899 and the document in question would be an invalid one if the stamp affixed thereon has not been cancelled. Under Section 108(1) of the Companies Act, 1956 [Corresponds to section 56(1) of the Companies Act, 2013] it is mandatory that the company shall not register the transfer of shares unless a properly executed instrument of transfer duly stamped has been delivered to the company [*Shri Parveen Sharda v. Chopsani Ice Aerated Water and Oils Mills Ltd., Appeal No. 1 of 1982 decided on 10.1.1983 (CLB)*].

In *Vardhaman Publishers Ltd. v. Mathrubhumi Printing & Publishing Co. Ltd. (1990)*, the Kerala High Court held that affixing stamps on a separate sheet of paper and attaching it to the transfer application or cancellation of stamps by drawing a line across the stamp was not improper and would not invalidate the said application. On the question of whether a newly added Article empowering the Board to reject transfer of shares would affect transactions of sale of shares entered into before the insertion of the Article, the Court held that the property in the shares passes on the date of transfer and the right to have the shares registered in the transferee’s name becomes crystallised on that day itself. Any alteration of articles will not affect concluded transactions and in respect of such transactions, the existing articles would prevail. So, if the original (unaltered) Articles as on the date of transfer permit free transfer of shares, the Board cannot refuse registration of the transfer.

### Procedure for transfer of shares as per the Companies Act, 2013

- (i) Obtain the transfer deed in the prescribed form i.e. **Form SH-4**, endorsed by the prescribed authority.
- (ii) The instrument of transfer may not be in the prescribed form in the following cases:-
  - Shares transferred by a director or nominee on behalf of another body corporate under section 187 of the Companies Act, 2013;
  - Shares transferred by a director or nominee on behalf of a corporation owned or controlled by the central or state Government;
  - Shares transferred by way of deposit as a security for repayment of any loan or advance if they are made with any of the following:-
    - (a) State Bank of India; or
    - (b) Any scheduled bank; or

- (c) Any other banking company; or
  - (d) Financial Institution; or
  - (e) Central Government; or
  - (f) State Government; or
  - (g) Any corporation owned or controlled by the Central or State Government; or
  - (h) Trustees who have filed the declarations.
- (iii) For transferring debentures, the instrument of transfer need not be in prescribed form but standard format can be used, being convenient to do so.
- (iv) Get the transfer deed duly executed either by the transferor and the transferee or on their behalf in accordance with section 56 of the Companies Act, 2013 and the Articles of Association, in case of shares, and also in accordance with trust deed in the case of debentures.

Requirement of execution of the transfer form by each of the joint shareholders cannot be met by execution of the transfer form by one of the shareholders even though between the shareholders inter se there is an agreement that one shareholder can sign on behalf of all other shareholders [Claude-Lila Parulekar v. Sakal Papers (P) Ltd. (2005) 124 Comp Cas 685(SC); (2005) 59SCL414 (SC)]

- (v) The transfer deed should bear stamps according to Indian Stamp Act and stamp duty notification in force in the state concerned. The present rate of transfer of shares is 25 paise for every one hundred rupees of the value of share or part thereof.
- (vi) See that stamp affixed on the transfer deed is cancelled at the time or before signing of the transfer deed.
- (vii) The signatures of the transferor and the transferee in the share/debentures transfer deed must be witnessed by a person giving his signature, name and address.
- (viii) Attach the relevant share or debenture certificate or allotment letter with the transfer deed and deliver the same to the company.
- (ix) Where the application is made by the transferor and relates to partly paid shares, the company has to give due notice of the amount due on shares/debentures to the transferee and the transferee shall raise objections, if any within two weeks from the date of receipt of the said notice.
- (x) If signed transfer deed has been lost, affix the same stamp on a written application. In such case, the

Board may, if it thinks fit to do so, register the transfer on such terms of indemnity as it thinks fit.

- (xi) If the shares of the company are listed in a recognized stock exchange, then the company cannot charge any fee for registration of transfers of shares and debentures.

### CHECKLIST FOR COMPANY SECRETARY

A company secretary is required to put up before the Board or the Share Transfer Committee of the company for consideration and approval, only those cases of registration of share transfers, which have been checked up by him and have been found to be strictly in accordance with the provisions of section 56 and other applicable provisions of the Companies Act, 2013 and the articles of association of the company. If the Instrument received is deficient in any respect, the same should be returned to the person who had

lodged the same with the company for making good the deficiency. The following checklist has been designed to help a company secretary in his work of processing of cases of share transfers:

- (1) Each column of transfer deed (SH-4) is properly and adequately filled in.
- (2) Date of execution is to be filled up properly.
- (3) Name of the company and its Corporate Identification Number (CIN) is correctly given.
- (4) Names of the recognized stock exchange, where dealt in, if any, have been given in the Instrument.
- (5) Description of shares, viz., equity, preference etc. is correctly given. Kind or class of securities, nominal value of each unit, amount called up and amount paid up, number of securities being transferred (both in figures and words) and consideration received (both in figures and words) are to be mentioned clearly.
- (6) Distinctive numbers of the shares mentioned in the share certificate(s) are to be mentioned in the deed.
- (7) Corresponding share certificate numbers are to be entered in the transfer deed.
- (8) Folio number of the transferor as given in the enclosed share certificate(s) is to be correctly entered in the transfer deed.
- (9) Name and address of the witness to the signature(s) of the transferor(s) are legibly written in the transfer deed and the witness has signed the transfer deed.
- (10) Signature(s) of the transferor(s) must tally with the specimen signature available with the company.
- (11) In case of joint shareholdings, form shall be signed by all joint transferors.
- (12) Particulars of transferee viz. Name, Father's name, address, E-mail Id, occupation and existing folio number are to be correctly entered in the transfer deed.
- (13) The transferee(s) or the buyer(s) has/have signed the Instrument.
- (14) Relevant certificate(s) of shares or debentures or other securities is/are to be enclosed.
- (15) If certificate was not issued, letter of allotment is to be enclosed.
- (16) Share Transfer Stamps of appropriate value have been affixed on the Instrument and they have been properly cancelled by a rubber stamp or defaced otherwise. If the shares are listed, the valuation of the Share Transfer Stamps is to be determined based on their quoted value. At present the stamp duty on

Transfer of shares is at the rate of twenty five paise for every hundred rupees of value of the shares on the date of sale, or part thereof.

- (17) Where the transfer is proposed to be in the name of the minor(s), whether the articles of association of the company permit such registration of transfer and the shares are fully paid.
- (18) Whether the transferor(s) and/or transferee(s) is/are non-resident Indians and if so, whether the transfer is permitted under the Foreign Exchange Management Act, 1999, and if not, whether specific permission of the Reserve Bank of India has been obtained.
- (19) Where the transferor is a body corporate, whether board resolution of the transferor is passed to this effect and proper authority has been given by the Board of directors to the person signing as the transferor on behalf of the company.

- (20) In case of listed company, comply with the formalities of SEBI (LODR) Reg, 2015 and other SEBI Guidelines.
- (21) Check whether the shares under registration are subject to a lien of the company and if so, whether the company has lifted the lien.
- (22) The transfer of shares must not contravene the provisions of SEBI (Substantial Acquisition of Share and Takeovers) Regulations, 2011.

### ***Transmission of securities***

Where any person acquires any right to securities by operation of any law, the company may register the transmission of shares in favour of such person if the company receives intimation of transmission from such person, and in such a case no transfer deed shall be necessary.

According to Section 56(2), a company shall have power to register on receipt of an intimation of transmission of any right to securities by operation of law from any person to whom such right has been transmitted.

#### ***Let us remember !***

A company shall not register a transfer of partly paid shares, unless the company has given a notice in Form No. SH.5 to the transferee and the transferee has given no objection to the transfer within two weeks from the date of receipt of notice.

## **POWER OF BOARD TO REFUSE REGISTRATION**

### ***STATUTORY REMEDY AGAINST REFUSAL UNDER SECTION 58***

Section 58 of the Companies Act, 2013, deals with process of the company to be followed by on refusal to register the transfer of securities.

- (i) If a **private company** limited by shares refuses (whether in pursuance of any power of the company under its articles or otherwise), to register the transfer of, or the transmission of the right to any securities or interest of a member in the company, then the company shall send notice of the refusal to the transferor and the transferee or to the person giving intimation of such transmission, within a period of **thirty days** from the date on which the instrument of transfer, or the intimation of such transmission, was delivered to the company. Notice shall contain the reasons for refusal to register the transfer or transmission.
- (ii) The transferee may **appeal to the Tribunal** against the refusal within a period of **thirty days** from the date of receipt of the notice or in case no notice has been sent by the company, within a period of sixty days from the date on which the instrument of transfer or the intimation of transmission, was delivered to the company. **[Section 58(3)]**
- (iii) If a **public company** without sufficient cause refuses to register the transfer of securities within a period of **thirty days** from the date on which the instrument of transfer or the intimation of transmission, is delivered to the company, the transferee may, within a period of **sixty days** of such refusal or where no intimation has been received from the company, within **ninety days** of the delivery of the instrument of transfer or intimation of transmission, appeal to the Tribunal. **[Section 58(4)]**
- (iv) The **Tribunal**, while dealing with an appeal may, after hearing the parties, either dismiss the appeal,

or by order—

- (a) direct that the transfer or transmission shall be registered by the company and the company shall comply with such order within a period of **ten days** of the receipt of the order; or
- (b) direct rectification of the register and also direct the company to pay damages, if any, sustained by any party aggrieved. **[Section 58(5)]**
- (v) If a person contravenes the order of the Tribunal he shall be punishable with imprisonment for a term **not less than one year** but may extend to **three years** and with fine **not less than one lakh rupees** which may extend to **five lakh rupees**. **[Section 58(6)]**

## CASE LAWS

- (A) Refusal to register share transfer on suspicion that the employee if admitted as a member will attend general meetings of the company and may create nuisance by raising irrelevant issues and also obtain access to the records to the company as a shareholder is not a valid reason. **[Appeal to the CLB No. 27, of 1975 dated 17th August, 1976, *Shri Nirmal Kumar v. Jaipur Metal and Electrical Limited*].**
- (B) The mere attempts of a person to wind up a company more than once cannot be a ground for refusing to register transfer by the directors **[*Rangpur Tea Association Ltd. v. Makkan Lal Samaddar (1979)*, 43 Com Cases 58].**
- (C) The power to refuse registration of shares which is conferred on the directors by the articles, is a discretionary power and must be exercised reasonably, and in good faith for the benefit of the company. Unless the contrary is proved, the power is deemed to have been exercised properly. **[*Berry & Stewart v. Tottenham Hostpur Football and Athletic Co. Ltd., 1936, 3 A11 E.R. 554*]**
- (D) Where the articles of association of a company confers a discretion on the directors with regard to acceptance of transfers, this discretion is a fiduciary one to be exercised bona fide in what the Board considers to be in the interest of the company. If on a true construction of the articles, the directors are only given the powers to reject on certain prescribed grounds and it is proved that on these grounds the request for transfer was rejected, the Court cannot substitute the opinion of the Board. If the articles of association give an unfettered discretion, the court would interfere with it only on proof of bad faith. **[*M.J. Amrithalingam v. Gudiyatham Textiles Pvt. Ltd., (1972) 42 Com Cases 350*]**
- (E) The Supreme Court, in ***Bajaj Auto Limited v. N.K. Firodia, AIR 1971, S.C. 321***, observed, “discretion implies just and proper consideration of the proposal under the facts and circumstances of the case. In the exercise of that discretion, the directors will act in the paramount interest of the company and in the general interest of the shareholders because the directors are in a fiduciary position both towards the company and towards every shareholder. The directors are, therefore, required to act bona fide and not arbitrarily and not for any collateral motive”. It was observed further that where the articles permitted the directors to decline to register transfer of shares without stating reasons, the Court would not draw unfavourable inferences against the directors because they did not give reasons. The Court would assume that the directors acted reasonably and bona fide and those who allege to the contrary would have to prove and establish the same by evidence. However, if the directors gave reasons, the Court would consider whether they were legitimate and whether the directors proceeded on right or wrong principle. The Court has also laid down three tests to determine the proper exercise of power by the Board of directors. The tests are:
  1. Whether the directors acted in the interest of the company;

2. Whether they acted on a wrong principle; and
3. Whether they acted on oblique motive or for a collateral purpose.

If the directors have uncontrolled and absolute discretion in regard to declining registration of transfer of shares, the Court would consider whether the reasons were legitimate or the directors acted on a wrong principle, or from corrupt motive. If the reasons for refusal given by the directors were legitimate, the Court would not over-rule that decision merely on the ground that the court would not have come to the same conclusion. The discretion of the directors was to be tested as the opinion of any fair and sensible man in the interest of the company.

- (F) Where the appellant transferee and respondent company were in the same line of business and were rivals, the refusal on the ground of rivalry will be justified in terms of the decision rendered by the Supreme Court in the Bajaj Auto Case. Under these circumstances, the investment cannot be considered to have been made bona fide with the intention of making profits. The respondent company is entitled to refuse the registration even in the absence of an enabling provision in articles in view of the provisions of Section 111(2) [Corresponds to section 58(3) and 58(4) of the Companies Act, 2013] [*Modi Carpets Ltd. v. Trans-Asia Carpets Ltd., Appeal No. 2 of 1980 decided on 26.12.1981 (CLB)*].
- (G) In *Shri T.N. Kuriakos v. Premier Tyres Ltd., decided on 13.6.1983 (CLB)*, the appeal against the refusal by the respondent company to register transfer of shares was allowed by the Company Law Board (Now Tribunal) on the ground that the refusal of the respondent to register transfer of shares in favour of the appellant was based on the decision of the Transfer Committee, a sub-committee of the Board of directors and not that of the Board of directors as such, and, therefore, the said decision was not a valid and legal decision.

## RECTIFICATION OF REGISTER OF MEMBERS (SECTION 59)

Section 59 of the Companies Act, 2013 provides the procedure for the rectification of register of members after the transfer of securities. The provision states that –

### (1) Remedy to the aggrieved for not carrying the changes in the register of members:

**Grounds of appeal:** If, without sufficient cause –

- (i) The name of any person is entered in the register of members; or
- (ii) The name of any person having entered in the register of members is without sufficient cause omitted therefrom; or
- (iii) Default or unnecessary delay is being made in entering in the register, the fact of any person having become a member; or
- (iv) Default or unnecessary delay is being made in entering in the register, the fact of any person having ceased to be a member
- (v) the person aggrieved, or any member of the company, or the company may appeal in such form as may be prescribed, to the Tribunal. In case of foreign members or debenture holders residing outside India, the appeal shall be filed in a competent court outside India as may be specified by the Central Government by notification.

2. **Order of the Tribunal:** The Tribunal may, after hearing the parties to the appeal by order, either dismiss the appeal or direct that the transfer or transmission shall be registered by the company within a period of ten days of the receipt of the order, or direct rectification of the records of the depository or the

register and in the latter case, direct the company to pay damages, if any, sustained by the party aggrieved.

3. **Right to transfer not restricted:** Section 59 of the Act shall not restrict the right of a holder of securities, to transfer such securities. Any person acquiring such securities shall be entitled to voting rights unless the voting rights have been suspended by an order of the Tribunal.
4. **Contravention of provisions of the law:** Where the transfer of securities is in contravention of any of the provisions of the Securities Contracts (Regulation) Act, 1956, the Securities and Exchange Board of India Act, 1992 or this Act or any other law for the time being in force, the Tribunal may, on an application made by the depository, company, depository participant, the holder of the securities or the Securities and Exchange Board, direct any company or a depository to set right the contravention and rectify its register or records concerned.
5. **Default in complying with the order:** If any default is made in complying with the order of the Tribunal under this section, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees, or with both.
6. **Specific instances of rectification:**
  - (a) Rectification has been held to be permissible in the following cases:
  - (b) Applicant induced to take shares by misrepresentation;
  - (c) Shareholders' name removed under unlawful surrender of his shares;
  - (d) Irregular allotment;
  - (e) Name of nominee entered in register without his knowledge or consent;
  - (f) Allotment of shares to a non-resident without taking necessary permission for foreign exchange.
  - (g) Allotment in violation of memorandum of association of the company.
7. **Mutation of name in other Company's register of members:** The Company which has changed its name would be entitled to ask those companies in which it is holding shares to substitute a company's new name in their register of members in the place of old name. [*Sulphur Dyes v. Hickson & Dadajee Ltd. (1995) 83 Com Cases 533 (Bom)*]

(Note: Students may also see Chapter 3 in this context)

## LOST TRANSFER DEEDS

It is sometimes found that the transfer documents sent to companies are lost, say, in transit. In such a case, the proviso to section 56(1) of the Act provides that where the instrument of transfer has been lost or the instrument of transfer has not been delivered within the prescribed period (within 60 days from the date of execution of the instrument of transfer), the company may register the transfer on such terms as to indemnity as the Board may think fit.

The Board of directors of the company should be satisfied that the instrument of transfer signed by or on behalf of the transferor and by or on behalf of the transferee has been lost. The proof may be in the form of an affidavit from the transferor or the transferee and supported by the purchase or sale note of the broker and the registration receipt issued by the postal authorities.

In addition, the Board can take an **indemnity** on such terms as it may think fit to safeguard its position and after that company may register the transfer.

### DELEGATION OF POWERS FOR TRANSFER

It is the articles of the company which authorise the Board of directors to accept or refuse transfer of securities, at their discretion. The Board further have the power to delegate all or any of their powers to any of the directors of the company or any person even not in the employment of the company. Therefore, the articles of association should authorise the Board of directors to delegate the powers suitably. Only in the case of refusal to register a transfer, the directors are required to exercise their discretion.

### TRANSFER OF DEBENTURES

In case of transfer of debentures, a proper instrument of transfer duly stamped, dated and executed by or on behalf of the transferor and the transferee should be delivered to the company by the transferor or transferee within a period of **sixty days** from the date of execution along with the certificate relating to the debentures or if no such certificate is in existence with the letter of allotment of debentures.

Stamp duty is payable for transfer of debentures and the duty varies from State to State, as explained above.

After registering the transfer, the particulars thereof have to be recorded in the Debenture Transfer Register and should be initialed by the appropriate authority. After making appropriate endorsements, the debenture certificate may be sent to the party concerned.

### TRANSFER OF SHARES TO A MINOR

In India, a minor is not competent to enter into any contract, as under Section 11 of the Indian Contract Act, 1872, a person who has attained the age of majority is only competent to contract. Since a minor cannot enter into a contract or agreement except through a guardian, and since as per Section 153, no notice can be taken of the fact that the guardian holds a share in trust for a minor, it follows that his name cannot be entered in the Register of Members and therefore, he cannot become a member of a company. There is, however, no objection in law to the guardian of a minor entering into a contract on behalf of a minor, by virtue of the statutory right conferred on the guardian of a minor under Section 8 read with Section 4 to 6 of the Hindu Minority and Guardianship Act, 1956. Since Section 56 of the Companies Act, 2013 enables execution of transfer deed by or on behalf of the transferor or the transferee, the transfer deed can be executed by a minor through his natural guardian as transferee, and the contract so entered into by a minor through his natural guardian is a binding and valid contract under Section 8 of the Hindu Minority and Guardianship Act, 1956.

The articles of association of a company cannot impose a blanket ban prohibiting transfer of shares in favour of a minor, as such a restriction is unreasonable and not sustainable. Section 44 of the Companies Act, 2013 provides that shares in a company are movable property and are transferable in the manner provided by the Articles. The expression 'in the manner provided by the articles of association of the company' can only be interpreted to mean the procedure to be adopted for transfer and impose restrictions, which are meaningful and reasonable. In case, the restriction imposed on transfer to a minor is accepted, it would mean that the shares of a deceased member can never be inherited by the legal heir who might be a minor. This would lead to a highly unjust situation and cannot be accepted as tenable. Accordingly, if the shares can be transmitted in favour of a minor, there is no reason why the shares which are fully paid-up and in respect of which no financial liability devolves on the minor are to be held as not transferable merely because of the ban imposed in the articles of association [*Saroj v. Britannia Industries Ltd.*, Appeal No. 5/80 decided on 14.12.81 by CLB].

### TRANSFER OF SHARES TO PARTNERSHIP FIRM

A firm is not a person and as such is not entitled to apply for membership. The Department of Company Affairs (Now, Ministry of Corporate Affairs) has in its Circular No. 4/72 dated 9.2.1972 stated that a firm not being a person cannot be registered as a member of a company except where the company is licensed under Section 25 (Corresponds to section 8 of the Companies Act, 2013).

### TRANSFER OF SECURITIES TO A BODY CORPORATE

An incorporated body being a legal person can acquire securities in its own name. Where a company is a transferee, the following documents are required to be submitted to the company:

- (a) A certified true copy of the Board resolution and/or power of attorney authorizing the signatory of the instrument of transfer to execute the instruments;
- (b) A certified true copy of a Board resolution passed under Section 179(3)(e) of the Companies Act; and
- (c) A certified true copy of Memorandum and Articles of Association of a company.

### TRANSFER WITHOUT THE AUTHORITY OF THE OWNER

Shares in a company can be transferred either by registered owner or by anyone else with his authority. A sale by any unauthorized person will be void. Accordingly, the Supreme Court held that, transfer of shares by the husband of a lady owner without her authority was void and the transferee obtained no rights.

### POSITION OF TRANSFEROR

When a transferor makes a transfer, he makes an implied representation that the transfer will be registered by the company in the name of the transferee in the place of transferor. If the company refuses to register the transfer for no fault or default of the transferee, the transferor, by reason of the shares continuing to stand in his name, will, in cases where he has received consideration for the transfer, be treated as trustee for the transferee and bound to act in accordance with his direction and for his benefit in respect of the shares, unless the transferee rescinds the contract and seeks to recover his money on consideration which has failed.

However, after the transfer form has been executed the transferor cannot be compelled to undertake any financial burden in respect of the shares at the instance of transferee where, after the transfer of shares, but before the company had registered the transfer, the company offered rights shares to its members. The transferor could not be compelled by the transferee to take up on his behalf the rights shares offered to the transferor.

### TRANSFER IN VIOLATION OF ARTICLES

Where the article of a private company requires that transfers of the company shares should be made with the previous sanction of the company's Board of Directors, the Supreme Court held that any transfer without such approval would be invalid. *John Tinson & co. P. Ltd. v. Surjeet Malhan (Mrs.)* (1997) 88 Com Cases 750: AIR 1997 SC 1411.

Where a transfer was made in violation of a private company's articles requiring that shares must be first offered to existing members, it was held that the transferor was not the proper person to object.

### TRANSMISSION OF SECURITIES

Transmission of securities has not been defined by the Companies Act. 'Transmission by operation of law' is

not a transfer. It refers to those cases where a person acquires an interest in property by operation of any provision of law, such as by right of inheritance or succession or by reason of the insolvency or lunacy of the holder of securities or by purchase in a Court-sale.

Thus, transmission of securities takes place when the registered holder of securities dies or is adjudicated as an insolvent, or if the holder of securities is a company, it goes into liquidation. Because a deceased person cannot own anything, the ownership of all his property passes, after his death, to those who legally represent him. Similarly, when a person is declared insolvent, his entire property vests in the Official Assignee or Official Receiver. Upon the death of a sole registered holder of securities, so far as the company is concerned, the legal representatives of the deceased holder of securities are the only persons having title to the securities unless securities-holder had appointed a nominee, in which case he would be entitled to the exclusion of all others.

### ***Transmission in Case of Sole Owner***

On the death of a sole owner of shares, vesting of rights and liabilities goes in favor of the legal heirs. They are entitled to be registered as the holders of shares. [*Scott v. Scott (London) Ltd., (1940) Ch. 794; Safeguard Industrial Investments Ltd. v. National Westminster Bank Ltd., (1980) 3 All ER 849.*] But the legal heirs do not by itself become members of the company. The company cannot register them as members without their consent. [*Re, Cheshire Banking Co. Duff's Executor's case, (1886) 32 Ch D 301.*] A company cannot compel them to become member nor it is a duty to do so. [*State of Kerala v. West Coast Planters Agencies Ltd., (1958) 28 Com Cases 13 (Ker).*] The company can justifiably register them as members when they apply for it.

### ***Transmission of shares to widow***

If a widow applies for transmission of the shares standing in the name of her deceased husband without producing a succession certificate and if the articles of association of the company so authorises, the directors may dispense with the production of succession certificate, probate or letter of administration upon such terms as to indemnity as the directors may consider necessary, and transmit the shares to the widow of the deceased by obtaining an indemnity bond.

### ***Transmission of joint holdings***

In case some shares are registered in joint names and the articles of the company provide that the survivor shall be the only person to be recognised by the company as having any title to the shares, the company is justified in refusing to register the transmission of title by operation of law in favour of the son of the deceased holder even though he may obtain succession certificate from the Court.

Section 56(1) of the Companies Act, 2013 states that the transfer of securities must be effected by a proper instrument of transfer and that a provision in the articles of an automatic transfer of securities of a deceased securities-holder is illegal and void. Such transfer does not amount to transmission which takes place by operation of law. Section 56(2) of the Act provides that nothing in the sub-section(1) shall prejudice the powers of the company to register, on receipt of an intimation of transmission of any right to securities by operation of law from any person to whom such right has been transmitted. It follows that, for such transmission, instrument of transfer is not required, and, merely an application addressed to the company by the legal representative is sufficient.

Articles of companies generally provide for formalities to be observed for transmission of shares. In the absence of such provision in the articles of the company, Regulations 23 to 27 of Table F of Schedule I to

the Act will govern the procedure for transmission. According to these regulations, the legal representatives are entitled to the shares held by deceased member and the company must accept the evidence of succession e.g., a succession certificate or letter of administrations or probate or any other evidence properly required by the Board of directors. He is, however, not a member of the company by reason only of being the legal owner of the shares. But he may apply to be registered as a member. On the contrary, instead of being registered himself as a member, he may make such transfer of the shares as the deceased or insolvent member could have made. The Board of directors also have the same right to decline registration as they would have had in the case of transfer of shares before death. But if the company unduly refuses to accept a transmission, the same remedies are available to the legal representative as in the case of a transfer namely, an appeal to the Tribunal under Section 58.

#### **DISTINCTION BETWEEN TRANSFER AND TRANSMISSION**

<b>S. No.</b>	<b>Transfer of Securities</b>	<b>Transmission of securities</b>
1.	Transfer takes place by a voluntary or deliberate act of the parties by way of a contract.	Transmission is the result of the operation of law. For example, due to death, insolvency or lunacy of a member.
2.	An instrument of transfer is required in case of transfer.	No instrument of transfer is required in case of transmission.
3.	Transfer is a normal course of transferring property.	Transmission takes place on death or insolvency of a holder of securities.
4.	Transfer of securities is generally made for some consideration.	Transmission of securities is generally made without any consideration.
5.	Stamp duty is payable on transfer of securities by a holder of securities.	No stamp duty is payable on transmission of securities.
6.	As soon as transfer is complete, the liability of the transferor ceases.	Shares continue to be subject to the original liabilities.

The Board of Directors of a company or the concerned depository has no discretion to refuse or withhold transfer of any security.

#### **Rejected Documents**

Documents which are not duly stamped or where stamps are not cancelled should be returned to the person lodging them pointing out the errors so as to enable them to rectify the error. In *Federal Bank Ltd. v. Smt. Sarla Devi Rathi* (1997) CLA 183 (Raj.), the company had not registered 100 shares that Smt. Sarla Devi Rathi, the respondent, had purchased and neither they returned the share certificates to her. The company urged that since the respondent had not become a shareholder of the company, no cognizance of the complaint could be taken. The High Court held that there was a *prima-facie* case against the company.

The CLB had pointed out that the company on not registering the transfer should have returned the documents to the party who lodged them (the transferee in this case) and not the transferor as the transferor loses his right in the shares as soon as he executes the transfer in blank.

#### **Time for pointing out insufficiency of stamps**

Where a company by mistake or otherwise registers a transfer which should have been refused because of

insufficient or uncanceled stamps, or because of the instrument being unstamped, it should point out the error to the transferee within such time (within one year from the date of execution) that the transferee can have the matters rectified through the orders of the Collector. Afterwards it would be too late. [*Kothari Industrial Corpn. Ltd. v. Lazor Detergents P. Ltd.* (1994) 1 Comp LJ 178 (CLB – Mad)].

### Impounding of Documents Relating to Share Transfer

The Board of directors are not persons to impound or regularise an instrument of transfer which is not duly stamped, *Mathrubhumi Co. Ltd. v. Vardhaman Publishers Ltd.*, (1992) 73 Com Cases 80 93 (Ker) as they have no authority under Sections 33 and 42 of the Stamp Act.

### JUDICIAL PRONOUNCEMENT ABOUT TRANSFER OF SHARES

**(A) *In Dove Investments P. Ltd. v. Gujarat Industrial Investment Corpn. Ltd.* [(2005) 60 SCL 604 (MAD)]**, the respondent company lodged with the appellant company shares pledged with it for effecting transfer of the same in its name. The appellant registered some of the shares and refused to register the balance on the ground that the respondent had failed to comply with the provisions of Section 108(1A) and 108(1C) [Corresponds to section 56 of the Companies Act, 2013]. The respondent was successful before the CLB which held that provisions of Section 108(1C) [Corresponds to section 56 of the Companies Act, 2013] are directory and directed the appellant to register the shares. The appellant challenged the order of the CLB (Now Tribunal) before the High Court. The Appeal was dismissed. According to the High Court, insofar as Sub-section (1C) is concerned, if the transfer of shares falls within any one of the exempted cases mentioned in that Sub-section, the requirements as to presentation of the instrument of transfer in favour of the prescribed authority and delivery thereof to the company within the prescribed time limit, as contemplated in Sub-section (1A) are not applicable, provided the conditions stipulated in Sub-section (1C) are satisfied. In view of the same, if any bank or financial institution or the Central Government or a State Government or any corporation owned or controlled by the Central Government or a State Government, or a corporation granting a loan against the security of shares, intends to get such shares registered in its own name, in the event of failure on the part of the borrower to repay the amount of loan, it shall complete the instrument of transfer and lodge it with the company for registration of the transfer in its own name. In such a circumstance, they will have to stamp or otherwise endorse on the instrument of transfer the date on which the bank or financial institution decides to get such share registered in its own name and the instrument so stamped or endorsed will have to be delivered to the company, together with the share certificate, for registration of the transfer within two months from the date so stamped or endorsed. It was not in dispute that the instruments of transfer were neither stamped nor endorsed by the petitioner, as required under Sub-section (1C) however, stamped by the prescribed authority contemplated under Sub-section (1A).

**(B) *Mukundlal Manchanda v. Prakash Raodlines Ltd.* (1971) Com Cases 575**, it was held that the requirement of Sub-section 1A(b)(ii) has to be read reasonably, so as to enable its smooth functioning; a delivery of instrument of transfer within a reasonable time should be held as a proper delivery. Further, where the company opines that the instrument of transfer has become stale and that it is improper to act upon it, the instrument of transfer has to be held as liable to be ignored. Further, even the belated delivery can be acted upon under certain circumstances while moving the Central Government under Sub-section (1) of Section 108(1A) [Corresponds to section 56 of the Companies Act, 2013]. In the light of the said provision, even though the discretion lies in the company either to recognize the transfer or not to recognize it depending upon the staleness of the instrument, the affected person can very well move the Central Government under Sub-section (1D) by explaining the circumstances under which the delay occurred and the hardship that resulted by the non-recognition

of the transfer. It was rightly concluded that in the light of the scheme of Section 108 [Corresponds to section 56 of the Companies Act, 2013], particularly after the insertion of Sub-section (1A), (1B), (1C) and (1D), the Court have to bear in mind that the trivialities would not render an act futile and technical formalities required to be complied with for a valid transaction cannot outweigh the importance to be given to the substance of the transaction. Though the matter was taken up by way of appeal before the Divisional Bench of the Karnataka High Court, the Division Bench had not gone into the said aspect, namely, whether mandatory or directory, however, confirmed the judgment of the Single Judge in Mukundlal Manchanda's case was to be upheld and accordingly it was held that except Section 108(1) [Corresponds to section 56 of the Companies Act, 2013] other provisions namely Sub-sections (1A) and (1C) are directory and not mandatory in nature.

- (C) ***Life Insurance Corporation of India v. Escorts Ltd., (1986) 59 AIR 1986 SC 1370***, the Supreme Court held that "a transfer effective between transferor and the transferee is not effective as against the company and any person without notice of the transfer being registered in the company's register.
- (D) ***Vickers System International Ltd. v. Mahesh P. Keshwani (1992) 73 Com Cases 317: (1991) 2 Comp LJ 444 (CLB)***. Transfer of shares by HUF Section 108 [Corresponds to section 56 of the Companies Act, 2013] enables the execution of a transfer deed by or on behalf of the transferor or the transferee. In the case of a joint family, the transfer form would be executed by the holding member or, in his absence, by the manager (Karta) of the family who represents the family. The same would be true when the family is transferee. The CLB directed the company to register shares in the name of the Hindu undivided family showing Mahesh P. Keshwani as its Karta.
- (E) ***Castrol India Ltd. v. S.S. Transfer of Mehta (1993) 78 Com Cases 146 (1993) 2 Comp LJ 8 (CLB)***. Where special permission is necessary, the transfer in question could be effected only with the permission of Special Court, (Trial of Offences Relating to Transactions in Securities Ordinance, 1992), it was held that the refusal by the company to accept the transfer without such permission was justified.
- (F) ***Vallur Mohammad Saheb v. Golden Agro-Tech Industries Ltd. (2008) 83 SCL 391 (CLB-CHENNAI)***, the transferee purchased 2700 shares of the company and lodged the transfer deed along with the original share certificates to the Registrar and Share Transfer Agent (RSTA) of the company. The company did not register the shares in the name of the transferee inspite of the transferor taking up the matter with the company. The transferee, therefore, filed petition under section 111/111A [Corresponds to section 58 & 59 of the Companies Act, 2013] to direct the company as well as its RSTA to pay damages with future interest from the date of filing the petition till the date of realization, or to issue duplicate share certificates to the petitioner. Allowing the petition, it was held that the bar embodied in section 22 of the SICA does not extend to any direction which may be issued by the CLB (Tribunal) under section 111/111A [Corresponds to section 58 & 59 of the Companies Act, 2013] for rectification of the register of members of the company. In view of this legal position, the resistance of the company for not registering the transfer of shares constituting miniscule 2700 shares only in favour of the transferee was not tenable.
- (G) ***Hindustan Mercantile Bank Ltd. v. D.N. Choudhury Cotton Mills Ltd. (2008) 83 SCL 399 (CLB-KOL.)***, the legal opinion on which the transferor company had relied upon was on the basis that the transferee company along with a few other companies was acting in concert to acquire shares in violation of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 [Replaced by SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011]. To come to the conclusion that the transferee along with others was acting in concert, reliance had been placed on

commonality of directors both in the transferee-company and other companies. Since the company was not a listed company, the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997, were not applicable. Further, it was found that neither the transferee company nor other companies had acquired shares of the transferor company. Accordingly, the company was to be directed to register the transfer of shares in favour of the transferee.

- (H) ***Sham Sunder Kukreja v. Hindustan Lever Ltd. (2001) 44 CLA 38 (CLB)***. If, by virtue of Section 111A(3) of the Companies Act, 1956 [Corresponds to section 59(1) of the Companies Act, 2013], the petition should have been filed within 2 months of the registration of the securities submitted for transfer, and where on the basis of facts and circumstances of the case, the transfer was effected in a fraudulent manner, the period of limitation (2 months) shall not apply.
- (I) ***Dr. Rajiv Das v. The United Press Ltd. (2001) (CLB)***. In the case, where the shares of a company were held in joint names and one of these joint holders requested the company to split the shares equally between the joint holders by issuing fresh certificates, the company shall not be legally bound to do so unless the share transfer deeds executed by both the joint holders duly completed and stamped were lodged with the company together with the relevant share certificates, in terms of the provisions of Section 108 of the Companies Act, 1956 [Corresponds to section 56 of the Companies Act, 2013].
- (J) ***T.S. Premkumar v. Tamil Nadu Mercantile Bank Ltd. 2001 (CLB)***. There shall be no justification, if a company/bank asks for information on Income Tax Returns (including that of the nominees of the transferee), the sources of the consideration paid for the purchase of shares, the details of the group to which the transferee is attached, for the purposes of registration of transfer of shares, if the number of the shares which are subject matter of transfer, is insignificant, and after the registration of which the controlling of interest in the company/bank is not changing.
- (K) **Transferor Holds Bonus Shares Only as a Trustee for the Transferee. *Charanjiv Lal v. ITC Ltd. and Another (2005) 5 COMP LJ 138 (CLB)***, the petitioner-transferee purchased 100 equity shares of ITC limited of bearing and lodged the same through post, which were received by the company on 10<sup>th</sup> December, 1991. However, the company did not take any action to register the shares in the name of the petitioner and informed him that it had not received the share certificates and the transfer instrument. To prevent any unauthorized transfer of the shares, he obtained a *status quo* order from Senior Civil Judge, Delhi. In the meanwhile, the company declared 60 bonus shares on two occasions against the impugned 100 shares of which the certificate relating to first 60 bonus shares had been sent to the transferor. The suit filed by the transferee-petitioner was dismissed for want of jurisdiction and hence the petitioner-transferee approached the Company Law Board. The Petition was allowed. The view expressed by the Judge was that the bonus shares always go with the original shares and the transferor holds bonus shares only as a trustee for the transferee. Considering that the original shares have been sold before the record date, in the absence of denial by the transferor nearly a month before the record date, it is the petitioner transferee who is entitled to the bonus shares and not the transferor.

### ***Transfer of Shares in Depository Mode***

Depository system maintains the ownership records of securities in the book entry form while in physical mode every share transfer is required to be accomplished by physical movement of share certificates to, and registration with the company concerned. The process of physical movement of share certificates often involves long delays and a significant portion of transactions end up as bad deliveries due to the faulty completion of paperwork, or signature differences with the specimens on record with the companies, or for other procedural lapses. Investors also face problems on account of loss of share certificates, forgery and

mutilation. The significant time involved in effecting ownership changes also impounds a substantial volume of shares at any given time leading to lower trading volumes.

## FORGED TRANSFER

It may happen that a forged instrument of transfer is presented to the company for registration. In order to avoid the consequences which will follow a forged transfer, companies normally write to the transferor about the lodgement of the transfer instrument so that he can object if he wishes. The company informs him that if no objection is made by him before a day specified in the notice, it would register the transfer. The consequences of a forged transfer are detailed hereunder:

- (a) A forged transfer is a nullity and, therefore, the original owner of the shares continues to be the shareholder and the company is bound to restore his name on the register of members [*People's Ins. Co. v. Wood and Co.*, 1961 (31) Com Cases 61]. A forged document never has any legal effect. It can never move ownership from one person to another, however, genuine it may appear. Thus, a forged instrument of transfer leaves the ownership of the shares exactly where it always was in the so-called transferor. It follows that if a company registers a forged transfer, the true owner can apply so as to be replaced on the register and his name will be restored. But the company does not incur any liability in damages by putting the name on the register.
- (b) However, if the company issues a share certificate to the transferee and he sells the shares to an innocent purchaser, the company is liable to compensate such a purchaser, if it refuses to register him as a member, or if his name has to be removed on the application of the true owner.
- (c) If the company is put to loss by reason of the forged transfer, as it may have paid damages to an innocent purchaser, it may recover the same independently from the person who lodged the forged transfer.

## EXAMPLE

Let us take an example to illustrate the consequences of forged transfer. Suppose, 'A' is a registered shareholder and his name is entered on the register of members in respect of certain number of shares. By fraud or theft, B obtains possession of 'A' share certificate and having forged a document purporting to be a transfer of shares to himself from A, succeeds in getting himself registered as a member and obtains from the company a new share certificate made out in his name. In spite of this, A does not cease to be the owner of the shares and a member of the company, as a forged document, being a nullity, does not move ownership from him to B or any other person. Producing the new certificate as evidence of his title, B purports to sell the shares to C, an innocent purchaser, who in reliance upon B's certificate, buys the shares in good faith and without notice of B's fraud. The company then registers C as a member and issues the share certificate to him in respect of the shares purchased by him. When A discovers the fraud, he being entitled for the rectification of register, has C's name struck off the register of members and has his own name restored as the registered holder of the shares. A never ceased to be the owner of the shares, although the company issued successive certificates to B and C. The company will be liable in damages to C and for other incidental loss. But it would be entitled to indemnity as against B, and if the forged transfer were lodged by a broker acting for B, against the broker also, even though the broker was innocent to the fraud for a person who brings a transfer to the registering authority and requests him to register it, impliedly warrants that it is a genuine document.

The fact that the transferee was a *bona fide* purchaser for value did not make any difference and the transferee was bound to return the scrips to the person to whom the same rightfully belong. [*Kaushalya Devi v. National Insulated Cable Company of India* 1977 Tax LR 1928 (Del)]

In case of joint shareholdings, a transfer to be effective must be executed by all and if the signature of any

one be forged, the transfer will be void.

A person acting in good faith, sends in and procures registration of the transfer and the issue of a fresh certificate on the basis of a forged deed is bound to indemnify the company against the untoward consequences. This happens when a stock broker, trusting his clients innocently forwards forged document to the company. [*Yeung v. Hongkong and Shanghai Banking Corpn.*, (1980) 2 All ER 599].

Further Section 57 states that if any person deceitfully personates as an owner of any security or interest in a company, or of any share warrant or coupon issued in pursuance of this Act, and thereby obtains or attempts to obtain any such security or interest or any such share warrant or coupon, or receives or attempts to receive any money due to any such owner, he shall be punishable with imprisonment for a term which shall not be less than one year but which may extend to three years and with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

A forged transfer cannot pass any title and is a nullity.

### DEATH OF A JOINT SHAREHOLDER

Where shares are held in joint names, and one of the joint shareholder dies the survivor alone will be recognized as the holder of the said shares. It would be sufficient for the company to delete the name of the deceased shareholder after obtaining satisfactory evidence of his death. This of course does not prevent a third person from calling on the company to register his name as holder of the shares after obtaining evidence such as probate of a will for the purpose of proving his title to the shares as against the surviving joint holders.

### TRANSPOSITION OF NAME

In the case of joint-shareholders, one or more of them may require the company to alter or rearrange the serial order of their names in the register of members of the company. In this process, there will be need for effecting consequential changes in the share certificates issued to them. If the company provides in its articles that the senior-most among the joint-holders will be recognised for all purposes like service of notice, a copy of balance sheet, profit and loss account, voting at a meeting etc., the request of transposition may be duly considered and approved by the Board or other authorised officer of the company. Since no transfer of any interest in the shares take place on such transposition, the question of insisting on filling transfer deed with the company, may not arise. Transposition does not also require stamp duty.

The Stock Exchange Division of the Department of Economic Affairs has clarified that there is no need of execution of transfer deed for transposition of names if the request for change in the order of names was made in writing, by all the joint-holders. If transposition is required in respect of a part of the holding, execution of transfer deed will be required.

### DEATH OF TRANSFEROR OR TRANSFEREE BEFORE REGISTRATION OF TRANSFER

Where the transferor dies and the company has no notice of his death the company would obviously register the transfer. But if the company has notice of his death, the proper course is not to register until the legal representative of the transferor has been referred to.

Where the transferee dies and company has notice of his death, a transfer of shares cannot be registered in the name of the deceased. With the consent of the transferor and the legal representatives of the transferee, the transfer may be registered in the names of the later. But if there is a dispute, an order of Court will have to be insisted upon.

In *Killick Nixon Ltd. v. Dhanraj Mills Ltd.*, it was held that the company is not bound to enquire into the

capability of the transferee to enter into a contract. The company has to act on the basis of what is presented in the transfer deed.

### **Proof in a transfer by representative**

Where a transfer is executed by a person in a representative capacity such as an officer of a body corporate or by an attorney, proof of the authority, must be produced, before the transfer can be registered.

### **Relationship between Transferor and Transferee**

Pending registration, the transferee has only an equitable right to the shares transferred to him. He does not become the legal owner until his name is entered on the Register of Members in respect of the shares. But as between the transferor and the transferee, immediately after the transfer is made, the contract of transfer will subsist and the transferee becomes the beneficial owner of the shares so transferred to him. A relation of trustee (transferor) and beneficiary (transferee) is thereby established between them. The transferor is under obligation to comply with all reasonable directions of the transferee. The transferee should, however, take prompt steps to get himself registered as a member.

Section 126 of the Companies Act, 2013 provides that where the transferor gives a mandate to pay the dividend to the transferee pending registration of transfer, the same should be paid to the transferee, otherwise the dividend in relation to such shares should be transferred to the Unpaid Dividend Account mentioned in Section 124. It is further provided that in the case of offer of rights shares or fully paid bonus shares, the same should be kept in abeyance till the title to the shares is decided.

### **RIGHTS OF TRANSFEROR**

In *JRRT (Investments) Ltd. v. Haycraft*, (1993) BCLC 401 (Ch.D) it was held that, the transferor is not deprived off his valuable rights, the right to dividend and the right to vote even where the purchaser has failed to make payment. An unpaid vendor has the right to exercise voting rights in respect of shares registered in his name. He is not obliged to comply with the directions of the purchaser in respect of the shares taken by him.

But on the other hand, the company refuses to register the transfer for no fault or default of the transferee, the transferor, by reason of the shares continuing to stand in his name, will, in cases where he has received consideration for the transfer, be treated as trustee for the transferee and bound to act in accordance with his directions and for his benefit in respect of the shares, unless the transferee rescinds the contract and seeks to recover his money on a consideration which has failed. However, after the transfer form has been executed the transferor cannot be compelled to undertake any additional financial burden in respect of the shares at the instance of the transferee where, after the transfer of shares, but before the company had registered the transfer, the company offered rights shares to its members, the Supreme Court held that the transferor could not be compelled by the transferee to take up on his behalf the rights shares offered to the transferor. [*Mathalone (R) v. Bombay Life Assurance Co. Ltd.* AIR 1953 SC 385 : (1954) 24 Com Cases 1 See also *Life Insurance Corporation of India v. Escorts Ltd.* (1986) 59 Com Cases 548 : AIR 1986 SC 1370]. But where, due to the transferee's own default, the transfer of shares is not registered the transferor cannot be held to be a trustee for the defaulting transferee simply because the share continues to remain in the transferor's name in the books of the company.

The seller's duty is complete when he hands over to the transferee a duly executed transfer form. [*Skinner v. City of London Marine Insurance Corpn.*, (1885) 14 QBD 882].

Where a transferor transfers his share for consideration and delivers along with the share certificate the

transfer form duly signed by him, but the transferee, instead of completing the transfer by signing his own name as transferee and presenting it for registration to the company, chooses to keep the transfer in blank and passes it on to others along with the share certificate, it cannot be said that the transferor, simply because the share continues to stand in his name, should be treated as a trustee for a series of unknown holders of the blank transfer.

When he sold his share to the original transferee he could not be deemed to have represented to the transferee anything more than that the share was transferable nor to have agreed to the transferee keeping or passing on the transfer in blank from hand to hand for an indefinite duration, without its being presented to the company for registration.

Where a shareholder executes a blank transfer to enable another to deal with the shares, he is bound not to do anything to obstruct registration of the transfer and if he improperly intervenes he is liable in damages, *Hooper v. Herts*, (1906) 1 Ch 549: (1904-7) ALL ER Rep 849 (CA).

**Transferor's right to indemnity for calls** - Where a transferor has paid for calls to the company after the shares are transferred, there arises an implied promise by the transferee to indemnify the transferor. Such a promise to indemnify can be implied even in the case of blank transfers [*Ashworth Partington & Co.*, (1925) 1 K].

**Transferee's right to Dividends, Bonus and Rights Shares** - Where the transferor, by reason of the shares standing in his name, has received after the transfer, any dividend on shares, bonus or other benefit accruing in respect thereof, the transferee being the person lawfully entitled thereto, can recover the same from the transferor, provided that he has not allowed his claim to become time barred under the provisions of the Limitation Act. [*Chunnihal Khushaldas Patel v. H.K. Adhyaru*, (1956) 26 Com Cases 168 : AIR 1956 SC 655].

**Dividend to transferee after transfer** - In one case the transfer was registered and dividends paid to the transferee. Later, the register was rectified by removing the transferee's name from the register on the ground of a technical nature, like inadequacy of stamps, it was held that the transferee was not bound to handover the dividend amount to the transferor. [*Kothari Industrial Corpn. Ltd. v. Lazor Detergents P. Ltd.*, (1994) 1 Comp LJ 178 (CLB-Mad)]. However the Madras High Court held that the company should not be allowed to rectify the register on a technical ground after transferring the shares.

**Position under the Securities Contracts (Regulation) Act, 1956** - As regards the position of a transferor after transfer, Section 27 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956) may also be noted. It provides as follows:

**Title to dividends** - (1) It shall be lawful for the holder of any security whose name appears on the books of the company issuing the said security to receive and retain any dividend declared by the company in respect thereof for any year, notwithstanding that the said security has already been transferred by him for consideration, unless the transferee, who claims the dividend from the transferor has lodged the security and all other documents relating to the transfer which may be required by the company with the company for being registered in his name within fifteen days of the date on which the dividend became due.

*Explanation:* The period specified in this section shall be extended -

- (i) in case of death of the transferee, by the actual period taken by his legal representative to establish his claim to the dividend;
- (ii) in case of loss of transfer deed by theft or any other cause beyond the control of the transferee, by the actual period taken for the replacement thereof; and

- (iii) in case of delay in the lodging of any security and other documents relating to the transfer due to causes connected with the post, by the actual period of the delay.

(2) Nothing contained in Sub-section (1) shall affect -

- (a) the right of a company to pay any dividend which has become due to any person whose name is for the time being registered in the books of the company as the holder of the security in respect of which the dividend has become due; or
- (b) the right of the transferee of any security to enforce against the transferor or any other person his rights, if any, in relation to the transfer in any case where the company has refused to register the transfer of the security in the name of the transferee.

## EFFECTS OF TRANSFER

Once a transfer form has been executed, the transfer is complete as between the transferor and the transferee and the transferee acquires the right to have his name entered in the register of members. No further application is necessary for having the name of the transferee entered in the register of members and the transferee perfects his title to the share after the entry in the Register of Members. Once the transferee becomes a member of the company, a contractual relationship arises with the company, [*Killick Nixon Ltd. v. Dhanraj Mills Pvt. Ltd.*, (1983) 54 Com Cases 432 (DB) (Bom)].

A company cannot refuse to register a transfer on the ground that the transfer was without consideration or that there was a collusion and connivance between the transferor and transferee. Any objection about inadequate consideration can be raised only by the transferor himself and not by the company particularly where the shares are fully paid. Where the transfer is in a spot delivery contract, Section 108 [Corresponds to section 56 of the Companies Act, 2013] is not applicable. [*Sanatan Investment Co. Pvt. Ltd. v. Prem Chand Jute Mills Ltd.* (1983) 54 Com Cases 186 (Cal)].

## Priority among Transferees

It was held in *Society General De Paris v. Jonet Walker and other* (1886) 11 Ac 20 that where a shareholder has fraudulently sold his shares to two different transferees, the first purchaser will, on the ground of time alone, be entitled to the shares in priority to the second.

For example, a person assigned his property, including some shares, for the benefit of his creditor. The assignee failed to get the share certificates registered in his name, but gave notice of assignment to the company. The assignor sold the shares to another who applied for registration. It was held that the assignee's claim was prior in time and therefore, entitled to registration. [*Peat v. Clayton*, (1906) 1 Ch. 659].

## Pledging of Shares

Shares of a company can be a subject matter of a valid pledge. Section 2(7) of the Sale of Goods Act, 1930, defines the term 'goods' as meaning every kind of moveable property other than actionable claim and money and includes stocks and shares. Shares are goods under the Sale of Goods Act, 1930 and therefore can be a subject matter of pledge under the Indian Contract Act, 1872. In *Kanhaiyalal Jhanwar vs Pandit Shirali And Co. And Ors* [AIR 1953 Cal 526], the Calcutta High Court held that the deposit of share certificates themselves is sufficient to create a pledge thereon.

On the death of a sole owner of shares, the rights and liabilities goes in favour of the legal heirs. They are entitled to be registered as the holder of the shares. But the company can register them as members with

only their consent and when they apply for it. *Re Cheshire Banking Co., Duff's Executor's case* (1886) 32 Ch D 301.

## LEGAL FRAMEWORK FOR DEPOSITORY SYSTEMS

The legal framework for depository system in the Depositories Act provides for the establishment of single or multiple depositories.

In the depository system, share certificates belonging to the investors are dematerialised and their names are entered in the records of depository as beneficial owners. Consequent to these changes, the investors' names in the companies register are replaced by the name of depository as the registered owner of the securities. The depository however, does not have any voting rights or other economic rights in respect of the shares as a registered owner. The beneficial owner continues to enjoy all the rights and benefits and be subject to all the liabilities in respect of the securities held by a depository. Shares in the depository mode are fungible and do not have distinctive numbers. The ownership changes in the depository are done automatically on the basis of *delivery payment*.

The companies which enter into an agreement with the depository will give an option to the holders of eligible securities to avail the services of the depository through participants. The investors desiring to join the depository are required to surrender the certificates of securities to the issuer company in the specified manner and on receipt of information about dematerialisation of securities by the issuer company, the depository enters in its records the names of the investors as beneficial owners. Similarly, the beneficial owner has right to opt out of a depository in respect of any security and claim the share certificates and get his name substituted in the register of members as the registered owner in place of the depository.

There has to be regular, mandatory flow of information about the details of ownership in the depository record to the company concerned. In case of any reservation about the acquisition of securities on the ground that the transfer of securities is in contravention of any of the provisions of the Securities Contracts (Regulation) Act, 1956, SEBI Act, 1992 or Companies Act, 2013 or any other law for the time being in force, the depository, company, depository participants, the holder of securities or SEBI shall have a right to make an application to the Tribunal for rectification of register or records concerned. Pending decision of the Tribunal, the holder of securities can transfer such securities and the transferee concerned shall be entitled to voting rights unless the voting rights have been suspended by an order of the Tribunal.

The Act provides for detailed regulations to be framed by SEBI and detailed bye-laws to be framed by depositories with the approval of SEBI.

### How does an investor avail services of a depository?

#### (a) In the case of existing securities:

An investor before availing the services of a depository, shall enter into an agreement with the depository through a participant and then shall surrender security certificates to the issuer. The issuer on receipt of security certificate shall cancel them and substitute in its records the name of the depository as the registered owner in respect of that security and inform the depository accordingly. The depository shall thereafter enter the name of the investor in its records as beneficial owner.

#### (b) In the case of fresh issue:

At the time of initial offer the investor would indicate his choice in the application form. If the investor opts to hold a security in the depository mode, the issuer shall intimate the concerned depository about the details of allotment of a security made in the favour of investors and records the depository as registered owner of the

securities. On receipt of such information, the depository shall enter in its records the names of allottees as the beneficial owners. In such case a prior agreement by the investor with the depository as well as an agreement between the issuer company and depository may be necessary.

**(c) In the case of exit from the depository:**

If a beneficial owner or a transferee of a security desires to take away a security from depository, he shall inform the depository of his intention. The depository in turn shall make appropriate entries in its records and inform the issuer. The issuer shall make arrangements for the issue of certificate of securities to the investor within 30 days of the receipt of intimation from the depository.

**(d) In the case of transfer within the depository:**

The depository shall record all transfers of securities made among the beneficial owners on receipt of suitable intimation to the effect that a genuine purchase transaction has been settled.

**(e) In the case of pledge:**

Before creation of any pledge or hypothecation in respect of a security, the beneficial owner is required to obtain prior approval of the depository and on creation of pledge or hypothecation; the beneficial owner shall give intimation of such pledge or hypothecation to the depository. The depository shall make appropriate entries in its records which will be admissible as evidence.

## DEMATERIALIZATION AND REMATERIALIZATION OF SHARES

### Dematerialisation of Shares

Dematerialisation of securities means holding of securities in electronic form in lieu of physical certificates. Dematerialisation is comparable to keeping your money in a bank account. In demat form, physical share certificates are replaced by electronic book entries; purchase of shares are reflected as credits in demat account and sales are reflected as debits. The risk associated with physical share certificates such as loss, replacement, theft, damage, etc. are overcome in the share certificates held in Dematerialisation form which are totally risk free.

- Dematerialisation of shares of a company is regulated by the Depositories Act, 1996.
- According to the Depositories Act, 1996, an investor has the option to hold securities either in physical or electronic form. Part of holding can be in physical form and part in demat form. However, SEBI has notified that settlement of market trades in listed securities should take place only in the demat mode.
- Section 29 of the Companies Act, 2013 provides that every company making public offer; and such other prescribed companies shall issue the securities only in dematerialised form by complying with the provisions of the Depositories Act, 1996 and the regulations made there under. Any company, other than a company mentioned above, may convert its securities into dematerialised form or issue its securities in physical form in accordance with the provisions of this Act or in dematerialised form in accordance with the provisions of the Depositories Act, 1996 and the regulations made thereunder.
- Further, SEBI (Issue of Capital and Disclosure Requirements), 2009 has made it mandatory for a company to make a public or rights issue or an offer for sale of securities in a dematerialized form but allows an option to be given to shareholders to receive the security certificates or hold securities in dematerialized form with a depository.

- Section 8 of the Depositories Act, 1996 provides that every person subscribing to shares offered by a company shall have the option either to receive the share certificates or hold shares with a depository in electronic form. Where a person opts to hold his shares with a depository, the company shall intimate such depository the details of allotment of the shares and on receipt of such information the depository shall enter in its records the name of the allottee as the beneficial owner of the shares [Sub-section (2) of Section 8].
- Section 9 of the Depositories Act, 1996 clarifies that all the securities held by a depository shall be dematerialised and shall be in a fungible form that is, they do not bear any notable feature like distinctive number, folio number or certificate number. Once shares get dematerialized, they lose their identity in terms of share certificate, distinctive numbers and folio numbers.
- According to Section 10 of the Depositories Act, 1996, a depository shall be deemed to be the registered owner of the shares for the purposes of effecting transfer of ownership of the shares on behalf of a beneficial owner and the depository as a registered owner shall not have any voting rights or any other rights in respect of the shares held by it. It is only the beneficial owner of the shares who shall be entitled to all the rights and benefits and be subject to all the liabilities in respect of his shares held by a depository.
- Every depository shall maintain a register and an index of beneficial owners in the manner provided in Section 88 of the Companies Act, 2013. **[Section 11]**

#### **PROCEDURE FOR DEMATERIALISATION OF SHARES BY THE SHAREHOLDER**

- (1) For the purpose of Dematerialisation of the shares of a registered shareholder of a company, the shareholder has to enter into an agreement with a depository through a participant in the manner specified by the bye-laws, for availing of its services [Refer Section 5 of the Depositories Act.]
- (2) Section 6(1) of the Act lays down that a person who has entered into an agreement under Section 5 shall surrender the certificate of the shares, for which he seeks to avail the services of a depository, to the company in the manner specified in the SEBI (Depositories and Participants) Regulations, 1996.
- (3) According to Sub-section (2) of Section 6 of the Act, the company, on receipt of the share certificate under Sub-section (1) from such a shareholder, shall cancel the certificate, (which action is referred to as Dematerialisation of shares) and substitute in its records, the name of the depository as the registered owner in respect of those shares and accordingly inform the depository.
- (4) On receipt of the information from the company under Sub-section (2), the depository shall enter the name of the shareholder in its records as the beneficial owner of the shares and inform the company, who shall in turn inform the shareholder that his shares have been dematerialized and his name has been entered in the depository's electronic records [Refer Sub-section (3) of Section 6 of Depositories Act, 1996.
- (5) A Dematerialisation Request Form (DRF) issued by the Depository Participant is to be filled and deposited with the concerned DP together with certificates after writing "Surrendered for Dematerialisation" on the face of each certificate.
- (6) The DP will send DRF along with the certificates to the concerned company for confirmation of its genuineness simultaneously to Share Transfer Agents electronically through the Depository (NSDL or CDSL as the case may be).
- (7) After checking the genuineness of the certificates and DRF the company/ Share Transfer Agents

destroy the certificates and send a confirmation to the NSDL or CDSL which, in turns, confirm the dematerialisation of securities to DPs.

- (8) DPs on receipt of such confirmation should inform the investor accordingly.

### **PROCEDURE FOR DEMATERIALISATION OF SHARES BY THE COMPANY**

A company proposing to have its shares dematerialized is required to take the following procedural steps:

- (1) It should ensure that its articles of association do contain an article which authorizes the company to have its securities dematerialized. If the articles of the company do not contain such a provision, it shall be required to alter its articles by passing a special resolution in general meeting in accordance with the provisions of Section 14 of the Companies Act, 2013 so as to include such a provision and thereafter comply with the provisions of the Depositories Act, 1996 and the SEBI (Depositories and Participants) Regulations, 1996 for dematerialisation of its securities.
- (2) The said company, which is desirous of dematerialising any of its above-detailed securities, after having altered its articles of association to incorporate an article to authorize the company to dematerialize its securities, will have to approach a depository for the purpose. The depository shall enter into an agreement with the company in respect of securities that are to be declared as eligible to be held in dematerialized form. Further, no such agreements shall be required to be entered into where the State or the Central Government is the issuer of such securities. [Refer Regulation 29(1) of the said regulations].
- (3) If the company has appointed a Registrar to the issue, in case of a new issue, or a share transfer agent for transfer/transmission of its existing shares, who has been granted certificate of registration by SEBI under Sub-section (1) of Section 12 of the Depositories Act, 1996, the depository shall enter into a tripartite agreement with the company and the registrar to the issue or share transfer agent, as the case may be, in respect of the securities to be declared by the depository as eligible to be held in dematerialised form. [Sub-regulation (2) of Regulation 29 of the said regulations].
- (4) Thereafter, the shareholders may surrender their share certificates to the company and the company shall inform the depository accordingly. According to Sub-section (2) of Section 6 of the Act, the company, on receipt of the share certificates under Sub-section (1) from its shareholders, shall cancel the certificates, (which action is referred to as dematerialisation of shares) and substitute in its records, the name of the depository as the registered owner in respect of all those shares and accordingly inform the depository.
- (5) On receipt of the information from the company under Sub-section (2), the depository shall enter the names of the shareholders in its records as the beneficial owners of the shares and inform the company, who shall in turn inform the shareholders that their shares have been dematerialised and their names have been entered in the depository's electronic records as beneficial owners of the shares [Sub-section (3) of Section 6 of Depositories Act, 1996].
- (6) According to Regulation 30 of the said regulations, every depository shall have systems and procedures which will enable it to coordinate with the company or its agent, and the participants, to reconcile the records of ownership of securities with the company or its agent, as the case may be, and with participants, on a daily basis.
- (7) Every depository shall maintain continuous electronic means of communication with all its participants, issuer companies or companies' agents, as the case may be, clearing houses and clearing corporations of the stock exchanges and with other depositories [Regulation 31].
- (8) The depository shall satisfy the Board that it has a mechanism in place to ensure that the interests

of the persons buying and selling securities held in the depository are adequately protected. [Regulation 32]

- (9) Where records are kept electronically by the depository, it shall ensure that the integrity of the automatic data processing systems is maintained at all times and take all precautions necessary to ensure that the records are not lost, destroyed or tampered with and in the event of loss or destruction, ensure that sufficient back up of records is available at all times at a different place. [Regulation 37]

## TRANSFER OF DEMATERIALISED SHARES

Section 7 of the Depositories Act, 1996 lays down that every depository shall, on receipt of intimation from a participant, register the transfer of shares in the name of the transferee and where the beneficial owner or a transferee of any shares seeks to have custody of such shares, the depository shall inform the issuer accordingly.

The transfer deed and all other provisions stipulated in Section 56 of the Companies Act, 2013 shall not apply to the transfers affected within the depository mode.

No stamp duty is levied on transfer of securities held in demat form. Any number of securities can be transferred/ delivered with one delivery instruction. Therefore, the paperwork and signing of multiple transfer forms is done away with.

The procedure for sale of shares held in demat form is as under:-

- Sale shall be made through a broker who is a member of National Stock Exchange;
- Shareholder, *i.e.*, the beneficial owner (BO) will give delivery instruction through Delivery Instruction Slip (DIS) to depository participant (DP) to debit his account and credit the broker's account. Such instruction should reach the DP's office at least 24 hours before the pay-in, failing which, DP will accept the instruction only at the BO's risk;
- The broker shall give instructions to his DP for delivery to clearing corporation of the concerned stock;
- exchange and receive payment from clearing corporation.

The broker shall make payment to the investor in physical form. The procedure for purchases of securities held in demat form is as under –

- (i) broker will receive the securities in his account on the payout day;
- (ii) broker will give instruction to its depository participant to debit his account and credit beneficial owner's account;
- (iii) BO will give 'Receipt Instruction' to DP for receiving credit by filling appropriate form. However, BO can give standing instruction for credit to his account that will obviate the need of giving Receipt Instruction every time.

## PLEDGE OR HYPOTHECATION OF DEMATERIALISED SHARES

A beneficial owner may, with the prior approval of the depository, pledge or hypothecate his shares held in a depository. Upon receipt of intimation from the beneficial owner about the pledge or hypothecation of his shares, the depository shall accordingly make entries in its records. Such an entry in the records of a depository shall be evidence of a pledge or hypothecation [Section 12]. Both the pledger and pledgee must

have a depository account. The procedure for pledge or hypothecation of shares held in demat form is as under:-

- (i) Investor shall submit the details of shares to be pledged to the DP in the prescribed format.
- (ii) DP shall verify the records and on being satisfied that the shares are available for pledge, make a note in the records and forward the application to the Depository for approval.
- (iii) Depository shall obtain confirmation from pledger and record the pledge within 15 days of application.
- (iv) Depository shall send intimation to the DP of both the pledger and pledgee who will inform the pledger and pledgee respectively.
- (v) The pledgee may invoke the pledge in accordance with the terms of pledge and on such invocation the name of pledgee is entered in the Register of Beneficial Owners by the Depository.
- (vi) During the period the pledge is in force, the DP shall not give effect to transfer of any security without the concurrence of the pledgee.
- (vii) On closure of the loan, the pledger shall request the DP to close the pledge. The pledgee, on getting payment, shall make a request for closure of pledge to his DP.
- (viii) For making hypothecation of shares held in demat form the above procedure is to be followed. However, before registering the hypothecatee as a beneficial owner, the Depository should obtain the consent from the hypothecator.

## **REMATERIALISATION OF SECURITIES**

Rematerialisation is conversion of electronic securities into physical certificates of such securities. This can be done in the following manner:

- (1) Beneficial owner sends request to DP.
- (2) DP intimates Depository (NSDL or CDSL) of such request electronically.
- (3) Depository confirms rematerialisation request to the company's Share Transfer Agents.
- (4) Share Transfer Agent updates accounts, prints certificates and confirms the Depository.
- (5) Depository updates accounts and downloads the details to the DP.
- (6) Share Transfer Agent dispatches certificates to holder thereof.
- (7) The DP also sends intimation about rematerialisation to its client.

**ANNEXURE I****SPECIMEN OF THE BOARD RESOLUTION APPROVING THE REGISTRATION OF TRANSFER OF SHARES**

“RESOLVED THAT Registration of transfer of.....fully paid equity shares of the company as per details in the register of share transfers of the company entered on page....to....., entries Nos.....to.....(both inclusive), which was placed before the meeting and each page was initialed by the chairman of the meeting as a mark of identification, be and is hereby approved; and

RESOLVED FURTHER THAT Shri.....,Company Secretary be and is hereby authorized to endorse the relevant share certificates under his signature, arrange for their dispatch to the transferees of the shares and make appropriate entries in the register of members and other records of the company.”

**ANNEXURE II****SPECIMEN OF BOARD RESOLUTION APPROVING REGISTRATION OF TRANSMISSION OF SHARES**

“RESOLVED THAT Transmission of.....no.s of fully paid equity shares of the company bearing distinctive numbers.....to.....(both numbers inclusive) presently registered in the name of Shri

.....who has been reported as deceased on.....in the district of.....which is situated

in the state of....., in the name of Shri .....son of Shri .....resident of

.....be and is hereby approved.

RESOLVED FURTHER THAT since the company has received a letter from the said Shri....., intimating to the company that he has decided to have the said shares registered in his name, the said shares be registered in his name; and

RESOLVED FURTHER THAT Shri.....,Company Secretary, be and is hereby authorized to enter the name of the said Shri.....in the register of members of the company and send the relevant share certificates to him after appropriately endorsing them in his name.

**ANNEXURE III****SPECIMEN OF SPECIAL RESOLUTION FOR ALTERATION OF ARTICLES OF ASSOCIATION OF THE COMPANY TO INCLUDE AN ARTICLE AUTHORISING THE COMPANY TO HAVE ITS SECURITIES DEMATERIALIZED**

“RESOLVED THAT pursuant to Section 14 of the Companies Act, 2013, the articles of association of the company be and are hereby altered in the following manner:

After article No..., the following be inserted as article... :

**Article...Dematerialization of Securities****A. Definitions:**

For the purpose of this article:-

‘Beneficial Owner’ means a person or persons whose name is recorded as such with a depository. ‘SEBI’ means the Securities and Exchange Board of India.

‘Depository’ means a company formed and registered under the Companies Act, 2013, and which has been

granted a certificate of registration to act as a depository under the Securities and Exchange Board of India Act, 1992; and

'Security' means such security as may be specified by SEBI from time to time.

### ***B. Dematerialisation of Securities***

Notwithstanding anything contained in these articles, the company shall be entitled to dematerialize its securities and to offer securities in a dematerialized form pursuant to the Depositories Act, 1996.

### ***C. Options for investors***

Every person subscribing to securities offered by the company shall have the option to receive security certificates or to hold the securities with a depository. Such a person who is the beneficial owner of the securities can at any time opt out of a depository, if permitted by the applicable law in respect of any security in the manner provided by the Depositories Act, 1996 and the company shall, in the manner and within the time prescribed, issue to the beneficial owner the required certificates of securities.

If a person opts to hold his security with a depository, the company shall intimate such depository the details of allotment of the security and/or transfer of securities in his name and on receipt of the information, the depository shall enter in its record the name of the allottee and/or transferee as the beneficial owner of the security.

### ***D. Securities in Depositories to be in Fungible Form***

All securities held by a depository shall be dematerialized and be infungible form. Nothing contained in Sections

89 and 186 of the Act shall apply to a depository in respect of the securities held by it on behalf of the beneficial owners.

### ***E. Distinctive Numbers of Securities held in a Depository***

Nothing contained in the Act or these articles regarding the necessity of having distinctive numbers for securities issued by the company shall apply to securities held with a depository.

### ***F. Rights of Depositories and Beneficial Owners***

- (i) Notwithstanding anything to the contrary contained in the Act or these articles, a depository shall be deemed to be the registered owner for the purposes of effecting transfer of ownership of security on behalf of the beneficial owner.
- (ii) Save as otherwise provided in (a) above, the depository as the registered owner of the securities shall not have any voting rights or any other rights in respect of the securities held by it.
- (iii) Every person holding securities of the company and whose name is entered as the beneficial owner in the records of the depository shall be deemed to be a member of the company. The beneficial owner of securities shall be entitled to all the rights and benefits and be subject to all the liabilities in respect of his securities which are held by a depository.

### ***G. Service of Documents***

Notwithstanding anything to the contrary contained in the Act or these articles, where securities are held in a depository, the records of the beneficial ownership may be served by such depository on the company by means of electronic mode or by delivery of floppies or discs.

**H. Transfer of Securities**

Nothing contained in Section 108 of the Act or these articles shall apply to a transfer of securities effected by a transferor and transferee both of whom are entered as beneficial owners in the records of a depository.

**I. Allotment of Securities Dealt In a Depository**

Notwithstanding anything contained in the Act or these articles, where securities are dealt in a depository, the company shall intimate the details thereof to the depository immediately on allotment and/or registration of transfer of such securities.

**J. Register and Index of Beneficial Owners**

The register and index of beneficial owners maintained by a depository under the Depositories Act, 1996, shall be deemed to be the register and index of members and security holders for the purposes of these articles.”

**Explanatory Statement**

With the enactment of the Depositories Act, 1996, and coming into operation of the depository system, some of the provisions of the Companies Act, 2013, relating to the issue, holding, transfer, transmission of equity shares and other securities of companies have been amended to facilitate the implementation of the depository system.

The depository system of holding securities in an electronic mode is a far safer and more convenient method of securing, holding and trading in the securities of company.

Under the depository system, the securities can be dematerialised. The company intends joining a depository. It is, therefore, proposed that the company's articles of association be suitably altered, as set out in the proposed resolution to enable it to dematerialize its securities. The resolution contains (i) definitions of some of the important terms used in the system; (ii) dematerialization of securities; (iii) options for investors; (iv) securities in depositories to be in fungible form; (v) distinctive numbers of securities held in a depository; (vi) rights of depositories and beneficial owners; (vii) service of documents; (viii) transfer of securities; (ix) allotment of securities dealt in a depository; and (x) register and index of beneficial owners.

None of the directors of the company is concerned or interested in the proposed resolution except to the extent of the share holdings of the directors.

**LESSON ROUND UP**

- Share capital of a company can be classified as:
  - nominal, authorized or registered capital;
  - issued and subscribed capital;
  - called up and uncalled capital;
- A share is defined as a share in the share capital of a company, including stock except where a distinction between stock and shares is expressed or implied.
- The Companies Act, 2013 permits a company limited by shares to issue two classes of shares, namely equity share capital and preference share capital.
- A preference share or preference share capital is that part of share capital which carries a preferential right with respect to both dividend and capital.
- Preference shares may be of various types, namely participating and non-participating, cumulative and

non-cumulative shares, redeemable and irredeemable preference shares.

- Equity share capital means all share capital which is not preference share capital.
- Sweat equity shares means equity shares issued by a company to its employees or directors at a discount or for consideration, other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.
- In general parlance, “transfer” takes place when title to the property is transferred from one person to another whereas “transmission” refers to devaluation of title by operation of law.
- Transmission may takes place either by succession or by testamentary transfer.
- According to Section 44 of Companies Act, 2013, shares, debentures or other interest of a company are moveable property, transferable in the manner provided by the articles of association of the company.
- At present, stamp duty applicable for transfer of shares is 25 paise for every one hundred rupees or part thereof of the value of share. Section 56 of the Companies Act requires that where share transfer form is delivered to the company should be adequately stamped.
- Shares of a private company are not marketable securities due to restriction on right to transfer. Such shares by their very nature are not freely transferable in the market.
- The securities of a public company are freely transferable, subject to the provisions that any contract or arrangement between two or more persons in respect of transfer of securities shall be enforceable as contract.

## GLOSSARY

<b><i>Explanatory Statement</i></b>	To enable shareholders to take apt and a well informed decision, it is necessary to provide them with requisite information. It covers all the information and facts that may enable members to understand the meaning, scope and implication of the proposed resolution.( see section 102 of Companies Act, 2013)
<b><i>Special Resolution</i></b>	A resolution is a Special Resolution when it is intended to be passed as a special resolution. The votes cast in favour of such resolution by members who, are required to be not less than three times the number of the votes, if any, cast against the resolution by members so entitled and voting.( See section 114 of Companies Act, 2013)
<b><i>General Meeting</i></b>	Meeting of the members of the company with the board of directors. This may be Extra ordinary General Meeting or Annual General Meeting.
<b><i>Share Capital</i></b>	Funds raised by issuing shares in return for cash or other considerations. The amount of share capital a company can change over time because each time a business sells new shares to the public in exchange for cash, the amount of share capital will increase. Share capital can be composed of both common and preferred shares.
<b><i>Redemption of shares</i></b>	Where a company issues shares on terms stating that they can be bought back by the company. Not all shares can be redeemed, only those stated to be redeemable when they were issued. The payment for the shares

	must generally come from reserves of profit so that the capital of the company is preserved.
<b>Sweat Equity Shares</b>	Sweat equity shares mean equity shares issued by a company to its employees or directors at a discount or for consideration, other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.
<b>Rights Issue</b>	Rights issue is an issue of capital to be offered to the existing shareholders of the company through a letter of offer.
<b>Bonus Shares</b>	When a company is prosperous and accumulates large distributable profits, it converts these accumulated profits into capital and divides the capital among the existing members in proportion to their entitlements. Members do not have to pay any amount for such shares. A company may, if its Articles provide, capitalize its profits by issuing fully-paid bonus shares

### SELF TEST QUESTIONS

*(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).*

1. Discuss the various kinds of share capital. How is preference share capital distinguished from equity share capital?
2. Define and explain the term “share”. What are the different classes of shares which a company may issue?
3. State the provisions of the Companies Act, 2013 relating to issue of shares at premium and at discount.
4. Discuss the procedure for issue of further shares to existing shareholders under Section 62(1) of the Companies Act, 2013.
5. ABC Limited wishes to issue 1:1 bonus to its members. As a company secretary detail the procedure to the board of directors of your company.
6. Enumerate the steps for transfer of dematerialized shares.
7. Write short notes on the following:-
  - (a) Dematerialisation of securities
  - (b) Transmission of shares
  - (c) Employee Stock Option Scheme
  - (d) Transfer and Transmission.
  - (e) Preferential Allotment of shares



# Lesson 3

## Members and Shareholders

### LESSON OUTLINE

- Members
- Modes of Acquiring Membership
- Who may become a member
- Cessation of Membership
- Register of Members
- Significant Beneficial Owner
- Rights of Members
- Shareholder Democracy
- Shareholder Agreement
- Veto Power
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

In the ordinary usage, the term 'Member' denotes a person who holds shares in a company. The members or the shareholders are the real owners of a company. The member or shareholder of the company is the person who collectively constitutes the company as a corporate entity.

The subscribers to the Memorandum are deemed to be the members of the company, as regards the second category of members, the membership in a company can be obtained through transfer/transmission. The term member, shareholder and holder of share are used interchangeably.

The company law does not prescribe any disqualification, which would depart a person from becoming a member of a company. Any person who is competent to enter into valid contract can become a member of a company.

This chapter covers all the legal and secretarial aspects of obtaining membership and maintaining the register of members. As a company secretary it is important to have knowledge of the subject as this is a good area of secretarial practice.

## INTRODUCTION- WHO ARE MEMBERS?

A company is composed of members, though it has its own separate legal entity. The members of a company are the persons who, for the time being, constitute the company, as a corporate entity.

In the case of a company limited by shares, the shareholders are the members. The terms “members” and “shareholders” are usually used interchangeably, being synonymous, as there can be no membership except through the medium of shareholding. Thus, generally speaking every shareholder is a member and every member is a shareholder. However, there may be exceptions to this statement, e.g., a person may be a holder of share(s) by transfer but will not become its member until the transfer is registered in the books of the company in his favour and his name is entered in the register of members. Similarly, a member who has transferred his shares, though he does not hold any shares yet he continues to be member of the company until the transfer is registered and his name is removed from the register of members maintained by the company under Section 88 of the Companies Act, 2013.

In *Herdilia Unimers Ltd. v. Renu Jain* [1995] 4 Comp. LJ. 45 (Raj.), it was held that the moment the shares were allotted and share certificate signed and the name entered in the register of members, the allottee became the shareholder, irrespective of whether the allottee received the shares or not.

In a company limited by guarantee, the persons who are liable under the guarantee clause in its Memorandum of Association are members of the company.

In an unlimited company, the members are the persons who are liable to the company, each in proportion to the extent of their interests in the company, to contribute the sums necessary to discharge in full, the debts and liabilities of the company, in the event of its being wound-up.

### Definition of ‘Member’

According to Section 2(55) of the Companies Act, 2013, member, in relation to a company, means,

- (1) The subscribers to the memorandum of a company who shall be deemed to have agreed to become members of the company, and on its registration, shall be entered as members in its register of members;
- (2) Every other person who agrees in writing to become a member of a company and whose name is entered in its register of members shall, be a member of the company;
- (3) Every person holding shares of a company and whose name is entered as a beneficial owner in the records of a depository shall be deemed to be a member of the concerned company.

Accordingly, there are two important elements which must be present before a person can acquire membership of a company viz., (i) agreement to become a member; and (ii) entry of the name of the person so agreeing, in the register of members of the company. Both these conditions are cumulative. [*Balkrishan Gupta v. Swadeshi Polytex Ltd.* (1985) 58 Com Cases 563].

The person desirous of becoming a member of a company must have the legal capacity of entering into an agreement in accordance with the provisions of the Indian Contract Act, 1972. Section 11 of the Indian Contract Act lays down that

Every person is competent to contract who:-

- (i) is of the age of majority according to the law to which he is subject.
- (ii) is of sound mind.
- (iii) is not disqualified from contracting by any law to which he is subject.

## MODES OF ACQUIRING MEMBERSHIP

As per Section 2(55) of the Companies Act, 2013, a person may acquire the membership of a company:

- (a) by subscribing to the Memorandum of Association (deemed agreement); or
- (b) by agreeing in writing to become a member:
  - (i) by making an application to the company for allotment of shares; or
  - (ii) by executing an instrument of transfer of shares as transferee; or
  - (iii) by consenting to the transfer of share of a deceased member in his name; or
  - (iv) by acquiescence or estoppel.
- (c) by holding shares of a company and whose name is entered as beneficial owner in the records of a depository (Under the Depositories Act, 1996)

and on his name being entered in the register of members of company. Also every such person holding shares of the company and whose name is entered as beneficial owner in the records of the depository shall be deemed to be the member of the concerned company.

### (a) *Subscribers to the Memorandum*

In the case of a subscriber, no application or allotment is necessary to become a member. By virtue of his subscribing to the memorandum, he is deemed to have agreed to become a member and he becomes *ipso facto* member on the incorporation of the company and is liable for the shares he has subscribed.

A subscriber to the memorandum cannot rescind the contract for the purchase of shares even on the ground of fraud by the promoters. (*In Re. Metal Constituents Co., (1902) 1.Ch. 707.*)

In accordance with the provisions of Section 10(2) of the Act, all monies payable by any member to the company under the memorandum or articles shall be debt due from him to the company. Further, a subscriber to the memorandum must pay for his shares in cash even if the promoters have promised him the shares for services rendered in connection with the promotion of the company. Again, he must take the shares directly from the company, and not through transfer from other member(s). When a person signs a memorandum for any number of shares he becomes absolutely bound to take those shares and no delay will relieve him from that liability unless he fulfills the obligation. His liability remains right up to the time when the company goes into liquidation and he is bound to bring the money for which he is liable to pay to the creditors of the company.

### (b) *Agreement in Writing*

#### (i) *By an application and allotment*

A person who applies for shares becomes a member when shares are allotted to him, a notice of allotment is issued to him and his name is entered on the register of members. The general law of contract applies to this transaction. There is an offer to take shares and acceptance of this offer when the shares are allotted. An application for shares may be absolute or conditional. If it is absolute, an allotment and its notice to the applicant will be sufficient acceptance. On the other hand, if the offer is conditional, the allotment must be made according to be condition as contained in the application. If there is conditional application and unconditional allotment, there is no contract.

**(ii) By transfer of shares**

Shares in a company are movable property as provided in Section 44 of the Act and are transferable in the manner as provided in the articles of the company and as provided in Section 56 of the Companies Act, 2013. A person can become a member by acquiring shares from an existing member and by having the transfer of shares registered in the books of the company, i.e. by getting his name entered in the register of members of the company.

**(iii) By transmission of shares**

A person may become a member of a company by operation of law i.e. if he succeeds to the estate of a deceased member. Membership by this method is a legal consequence. On the death of a member, his executor or the person who is entitled under the law to succeed to his estate, gets the right to have the shares transmitted and registered in his name in the company's register of members. No instrument of transfer is necessary in this case. If the legal representative of deceased member desires to be registered as a member in place of the deceased member, the company shall do so or in the alternative he may request the company to transfer the shares in the name of another person of his choice. The Official Assignee or Official Receiver is likewise entitled to be a member in place of the shareholder, who has been adjudged insolvent.

**(iv) By acquiescence or estoppels**

A person is deemed to be a member of a company if he allows his name, without sufficient cause, to be on the register of members of the company or otherwise holds himself out or allows himself to be held out as a member. In such a case, he is estopped from denying his membership. He can, however, escape his liability by taking prompt action for having his name removed from the register of members on permissible grounds.

**(c) Holding Shares as Beneficial Owner in the Records of Depository.**

Every person holding shares of the company and whose name is entered as a beneficial owner in the records of the depository shall be deemed to be a member of the concerned company.

**WHO MAY BECOME A MEMBER**

Subject to the Memorandum and Articles, any *sui juris* (a person who is competent to contract) except the company itself, can become a member of a company. However, it is important to note the following points in relation to certain organizations and persons:

(a) **Company as a member of another company:** A company is a legal person and so is competent to contract. Therefore, it can become a member of any other company. However, it must be authorised by its Memorandum of Association to invest in the shares of that company or any other company. Also a company cannot become a member of itself. As per section 19 of the Companies Act, 2013, a subsidiary company cannot become a member of its holding company. However, a subsidiary can hold shares in its holding company only under the following exceptional circumstances—

- (i) where the subsidiary company holds such shares as the legal representative of a deceased member of the holding company; or
- (ii) where the subsidiary company holds such shares as a trustee; or
- (iii) where the subsidiary company is a shareholder even before it became a subsidiary company of the holding company.

(b) **Partnership firm as a member:** A partnership firm is not a legal person and as such it cannot, in its own name, become a member of a company except in company registered u/s 8 of Act.

(c) **Limited Liability Partnership,** being an incorporated body under the statute, can become a member of a company.

(d) **Section 8 company:** A non-profit making company licensed under Section 8 of the Act, can become a member of another company if it is authorised by its Memorandum of Association to invest into shares of the other company.

(e) **Foreigners as members:** A foreigner may take shares in an Indian company and become a member subject to the provisions of the Foreign Exchange Management Act, 1999, but in the event of war with his country, he becomes an alien enemy and his power of voting and his rights to receive notices are suspended.

(f) **Minor as member:** A member who is not a *sui juris* e.g., a minor, is wholly incompetent to enter into a contract and as such cannot become a member of a company. Consequently, an agreement by a minor to take shares is void *ab-initio*.

It has been held by the Company Law Board (replaced by the Tribunal under the Companies Act, 2013) that an agreement in writing for a minor to become a member may be signed on behalf of the minor by his lawful guardian and the registration of transfer of shares in the name of the minor, acting through his or her guardian, especially where the shares are fully paid cannot be refused on the ground of the transferee being a minor [*Miss Nandita Jain v. Benett Coleman and Co. Ltd.*, Appeal No. 27 of 1972 dated 17.2.78].

After attaining majority, the minor, if he does not want to be a member, must repudiate his liability on the shares on ground of minority, and if he does so, the company can not plead estoppel on the ground of his having received dividends during his minority or that he had fraudulently misrepresented his age in his application for shares [*Sadiq Ali v. Jai Kishori*, (1928) 30 Bom. L.R. 1346].

If shares are transferred to a minor, the transferor will remain liable for all future calls on such shares so long as they are held by the minor even if the transferor was ignorant of his minority. If the company knows of his minority it may refuse to register the transfer, unless the transfer was made through the guardian.

(g) **Insolvent as member:** An insolvent may be a member of a company as long as he is on the register of members. He is entitled to vote, but he loses all beneficial interest in the shares and company will pay dividend on his shares to the Official Assignee or Receiver [*Morgan v. Gray*, (1953) All E.R. 213].

(h) **Pawnee:** A pawnee has no right of foreclosure since he never had the absolute ownership at law and his equitable title cannot exceed what is specifically granted by law. In this sense, a pledge differs from a mortgage. In view of the above, a pawnee cannot be treated as the holder of the shares pledged in his favour, and the pawner continues to be a member and can exercise the rights of a member [*Balakrishna Gupta v. Swadeshi Polytex Ltd.*, (1985) 58 Com Cases 563 (S.C.)].

(i) **Receiver:** A receiver whose name is not entered in the register of members cannot exercise any of the membership rights attached to a share unless in a proceeding to which company is a party and an order is made therein. Mere appointment of a receiver in respect of certain shares of a company without more rights cannot, deprive the holder of the shares whose name is entered in the register of members of the company, the right to vote at the meeting of the company [*Balakrishna Gupta v. Swadeshi Polytex Ltd.*, (1985) 58 Com Cases 563 (S.C.)].

(j) **Persons taking shares in fictitious names:** A person who takes shares in the name of a fictitious person, becomes liable as a member besides incurring criminal liability under Section 38 of the Act, wherein

punishment is provided for commission of fraud. As per section 447, any person who is found guilty of fraud, is punishable with imprisonment which shall not be less than six months but which may extend to ten years and also liable to pay fine which shall not be less than the amount involved in the fraud, but which may extend to three 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 three years.

(k) **Trade Union as member:** A trade union registered under the Trade Union Act, can be registered as a member and can hold shares in a company in its own corporate name [*All India Bank Officers Confederation v. Dhanlakshmi Bank Ltd.*, (1997) 90 Com Cases 225].

### Clarification regarding status of a holder of Global Depository Receipts (GDRs):

It is clarified by the Ministry of Corporate Affairs, vide Circular No.1/2009 No.17/67/2009 CL-V dated 16/6/2009 that:

- (a) As per section 41(1) and (2) of the Companies Act, 1956, [Corresponds to section 2(55) (i) & (ii) of the Companies Act, 2013] a person is a member of the company, (i) who is a subscriber to the Memorandum or (ii) whose name has been entered in the register of members. Since, holder of Global Depository Receipts is neither the subscriber to the Memorandum nor a holder of the shares, his name cannot be entered in the Register of Members. Therefore, a holder of Global Depository Receipts cannot be called a member of the company.
- (b) As per Section 41(3) of the Companies Act, 1956, [Corresponds to section 2(55) (i) & (ii) of the Companies Act, 2013] a person holding a share capital of the company and whose name is entered as beneficial owner in the records of the depository, is deemed to be a member of the company. Since the Overseas Depository Bank as referred in the 'Scheme' is neither the Depository as defined in the Companies Act, 1956 and the Depository Act, 1996 nor holding the share capital, therefore, it cannot be deemed to be a member of the company.
- (c) A holder of Global Depository Receipts may become a member of the company only on transfer/redemption of the GDR into underlying equity shares after following the procedure provided in the "Scheme"/ provisions of the Companies Act.
- (d) Since the underlying shares are allotted in the name of Overseas Depository Bank, the name of such Overseas Depository Bank is to be entered in the Register of Members of the issuing company. However, until transfer/redemption of such GDR's into underlying shares, Overseas Depository Bank cannot be considered a nominee of the holder of GDR for the purpose of Section 42 read with Section 41 of the Companies Act, 1956 [Corresponds to section 19 read with section 2(55) of the Companies Act, 2013].

### Joint Members

If more than one person apply for shares in a company and shares are allotted to them, each one of such applicant becomes a member (*Narandas v. India Mfg. Co.*, A.I.R. 1953 Bom. 433]. Unless the Articles of the company otherwise provide, joint members can insist on having their names registered in any order they may require. They may also have their holding split into several joint holdings with their names in different orders so that all of them may have a right to vote as first named holding in one or the other joint holdings. *Burns v. Siemens Brothers Dynamo Works Ltd.* (1919) 1 Ch. 225.

### Minimum Number of Members

Section 3(1) of the Companies Act, 2013 provides that a company may be formed for any lawful purpose by seven or more persons, where the company to be formed is to be a public company; or two or more persons,

where the company to be formed is to be a private company; or one person, where the company to be formed is to be One Person Company that is to say, a private company, by subscribing their names or his name to a memorandum and complying with the requirements of this Act in respect of registration.

### Restriction on Membership

By virtue of Section 2(68)(ii) of the Companies Act, 2013, the maximum number of members of a private company except in the case of One Person Company is limited to two hundred excluding the present and past employees of the company who continue to be members of the company. There is no restriction with regard to the maximum number of members of a public company.

### CESSATION OF MEMBERSHIP

A person ceases to be a member of a company when his name is removed from its register of members, which may occur in any of the following situations:

- (a) He transfers his shares to another person, the transfer is registered by the company and his name is removed from the register of members;
- (b) His shares are forfeited;
- (c) His shares are sold by the company to enforce a lien;
- (d) He dies; (his estate, however, remains liable for calls);
- (e) He is adjudged insolvent and the Official Assignee disclaims his shares;
- (f) His redeemable preference shares are redeemed;
- (g) He rescinds the contract of membership on the ground of fraud or misrepresentation or a genuine mistake;
- (h) His shares are purchased either by another member or by the company itself under an order of the Tribunal under Section 242 of the Companies Act, 2013;
- (i) The member is a company which is being wound-up in India, and the liquidator disclaims the shares;
- (j) The company is wound up; or

Though one ceases to be a member, he remains liable as a contributory and is also entitled to share in the surplus, if any.

### Expulsion of a Member

A controversy had arisen as to whether a public limited company had powers to insert an article in its Articles of Association relating to expulsion of a member by the Board of Directors of the company where the directors were of the view that the activities or conduct of such a member was detrimental to the interests of the company.

The Department of Company Affairs (now, Ministry of Corporate Affairs) clarified that an article for expulsion of a member is opposed to the fundamental principles of the Company Jurisprudence and is *ultra vires* the company, the reason being that such a provision against the provisions of the Companies Act relating to the rights of a member in a company, the powers of the Central Government as an appellate authority under Section 111 of the Act and the powers of the Court under Sections 107, 395 and 397 of the Companies Act, 1956. [These sections correspond to sections 58, 48, 235 and 241 of the Companies Act, 2013 respectively.]

According to Section 6 of the Companies Act, 2013, the Act overrides the Memorandum and Articles of

Association and any provision contained in these documents repugnant to the provisions of the Companies Act, is void.

The Department of Company Affairs (now MCA) has, therefore, clarified that any assumption of the powers by the Board of Directors to expel a member by alteration of Articles of Association shall be illegal and void.

The Supreme Court in the case of *Bajaj Auto Ltd. v. N.K. Firodia* [1971] 41 Com Cases 1 has laid down the law as to the conditions on the basis of which directors could refuse a person to be admitted as a member of the company. The principles laid down by the Supreme Court in this case, even though pertain to the refusal by a company to the admission of a person as a member of the company, are applicable even with greater force to a case of expulsion of an existing member. As, under Article 141 of the Constitution, the law declared by the Supreme Court is binding on all courts within the territory of India, any provision pertaining to the expulsion of a member by the management of a company which is against the law as laid down by the Supreme Court will be illegal and *ultra vires*. In the light of the aforesaid position, it is clarified that assumption by the Board of directors of a company of any power to expel a member by amending its articles of association is illegal and void [Circular: Letter No. 32/75, dated 1.11.1975].

### **REGISTER OF MEMBERS ETC.**

Section 88 of the Companies Act, 2013 lays down:

(1) Every company shall keep and maintain the following registers namely:—

- (a) register of members indicating separately for each class of equity and preference shares held by each member residing in or outside India;
- (b) register of debenture-holders; and
- (c) register of any other security holders.

(2) Every register maintained under sub-section (1) shall include an index of the names included therein.

(3) The register and index of beneficial owners maintained by a depository under section 11 of the Depositories Act, 1996, shall be deemed to be the corresponding register and index for the purposes of this Act.

(4) Foreign register.

(5) If a company does not maintain a register of members or debenture-holders or other security holders or fails to maintain them in accordance with the provisions of sub-section (1) or sub-section (2), the company and every officer of the company who is in default shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees and where the failure is a continuing one, with a further fine which may extend to one thousand rupees for every day, after the first during which the failure continues.

### **Modalities of Maintaining the Register**

Rule 3 & 5 of the Companies (Management and Administration) Rules, 2014 deal with maintenance of Register under section 88. It is provided that every company limited by shares shall from the date of its registration maintain a register of its members in Form No. MGT.1.

In the case of a company not having share capital, the register of members shall contain the following particulars, in respect of each member, namely:-

- (a) name of the member; address (registered office address in case the member is a body corporate);

e-mail address; Permanent Account Number or CIN; Unique Identification Number, if any; Father's/Mother's/Spouse's name; Occupation; Status; Nationality; in case member is a minor, name of the guardian and the date of birth of the member; name and address of nominee;

- (b) date of becoming member;
- (c) date of cessation;
- (d) amount of guarantee, if any;
- (e) any other interest if any; and
- (f) instructions, if any, given by the member with regard to sending of notices etc:

#### IMPORTANT POINTS

- The entries in the registers maintained under section 88 shall be made within seven days after the Board of Directors or its duly constituted committee approves the allotment or transfer of shares, debentures or any other securities, as the case may be.
- The registers shall be maintained at the registered office of the company unless a special resolution is passed in a general meeting authorising the keeping of the register at any other place within the city, town or village in which the registered office is situated or any other place in India in which more than one-tenth of the total members entered in the register of members reside.
- Consequent upon any forfeiture, buy-back, reduction, sub-division, consolidation or cancellation of shares, issue of sweat equity shares, transmission of shares, shares issued under any scheme of arrangements, mergers, reconstitution or employees stock option scheme or any of such scheme provided under this Act or by issue of duplicate or new share certificates or new debenture or other security certificates, entry shall be made within seven days after approval by the Board or committee, in the register of members or in the respective registers, as the case may be.
- If any change occurs in the status of a member or debenture holder or any other security holder whether due to death or insolvency or change of name or due to transfer to Investor Education Protection Fund or due to any other reason, entries thereof explaining the change shall be made in the respective register.
- If any rectification is made in the register by the company pursuant to any order passed by the competent authority under the Act, the necessary reference of such order shall be indicated in the respective register.
- If any order is passed by any judicial or revenue authority or by Security and Exchange Board of India (SEBI) or Tribunal attaching the shares, debentures or other securities and giving directions for remittance of dividend or interest, the necessary reference of such order shall be indicated in the respective register.
- In case of companies whose securities are listed on a stock exchange in or outside India, the particulars of any pledge, charge, lien or hypothecation created by the promoters in respect of any securities of the company held by the promoter including the names of pledgee/pawnee and any revocation therein shall be entered in the register within fifteen days from such an event.
- If promoters of any listed company, which has formed a joint venture company with another company have pledged or hypothecated or created charge or lien in respect of any security of the listed company in connection with such joint venture company, the particulars of such pledge, hypothecation, charge and lien shall be entered in the register members of the listed company within fifteen days from such an event.

### Authentication of the Register

The entries in the registers maintained under section 88 and index included therein shall be authenticated by the company secretary of the company or by any other person authorised by the Board for the purpose, and the date of the board resolution authorising the same shall be mentioned.

The entries in the foreign register shall be authenticated by the company secretary of the company or person authorised by the Board by appending his signature to each entry.

### CASE LAW

#### Judicial Pronouncement relating to register of members

1. A person who claims to have purchased the shares of a member will be entitled to have his name entered in the register by satisfying the requirement of either Section 108 or 109 [Corresponds to section 56 of the Companies Act, 2013]. [*Lalithamba Bai v. Harrisons Malayalam Ltd.*, (1988) 2 Comp LJ 41 (Ker)].
2. No company should enter in the register a statement that it has a lien on the shares of a member, [*W. Key & Son Ltd.*, (1902) 1 Ch 467].
3. A company cannot insist upon putting in the register anything except that which is required by the section to be inserted in it. [*T.H. Saunders & Co. Ltd. Re*, (1908) 1 Ch 415].
4. In a voluntary winding up, the liquidator may accept share transfers and alter the register accordingly. [*Taylor, Phillips and Richard's Case*, (1897) 1 Ch 298].
5. A firm in its own name cannot be registered as a member, as a firm is not a legal person like a company incorporated under the Act. Only the partners can be recognised and registered as joint holders. [See *Re Vagliano & Anthracite Collieries Ltd.*, (1910) 79 LJ Ch 769].

### Index of Members

Section 88(2) of the Companies Act, 2013 read with Rule 6 of Companies (Management and Administration) Rules, 2014 requires that every register maintained under section 88(1) shall include an index of the names included therein.

Every register maintained under sub-section (1) of section 88 shall include an index of the names entered in the respective registers and the index shall, in respect of each folio, contain sufficient indication to enable the entries relating to that folio in the register to be readily found:

The maintenance of index is not necessary, in case, the number of members is less than fifty.

The company shall make the necessary entries in the index simultaneously with the entry for allotment or transfer of any security in such Register.

Inspection must be allowed of the Index in the same manner as applicable to the register of members.

### Place of keeping and inspection of the Registers

Section 94 of the Companies Act, 2013 fixes the place for maintaining a company's registers, returns etc. and for allowing their inspection.

According to Section 94(1), the registers required to be kept and maintained by a company under section 88 and copies of the annual return filed under section 92 shall be kept at the registered office of the company:

Such registers or copies of return may also be kept at any other place in India in which more than one-tenth

of the total number of members entered in the register of members reside, if approved by a special resolution passed at a general meeting of the company

### **Filing of Special Resolution in Advance**

A copy of the proposed special resolution in advance to be filed with the registrar as required in accordance with first proviso of sub-section (1) of section 94, shall be filed with the Registrar, at least one day before the date of general meeting of the company in Form No.MGT.14.(Also refer to Rule 5(2) which was already discussed).

### **Inspection of Registers**

According to section 94(2) read with Rule 14 of Companies (Management & Administration) Rules, 2014 the registers and their indices, except when they are closed under the provisions of this Act, 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 and by any other person on payment of such fees as may be specified in the articles of association of the company but not exceeding Rs. 50 for each inspection.

As per Section 94(3) 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 specified in the Articles of Association of the company but not exceeding Rs 10 for each page.

Rule 14 of the Companies (Management and Administration) Rules, 2014 provides that the registers and indices maintained pursuant to section 88 shall be open for inspection during business hours, at such reasonable time on every working day as the board may decide, by any member, debenture holder, other security holder or beneficial owner without payment of fee and by any other person on payment of such fee as may be specified in the articles of association of the company but not exceeding fifty rupees for each inspection.

Explanation.- For the purposes of this sub-rule, reasonable time of not less than two hours on every working day shall be considered by the company.

Further it is provided that any such member, debenture holder, security holder or beneficial owner or any other person may require a copy of any such register or entries therein or return on payment of such fee as may be specified in the articles of association of the company but not exceeding ten rupees for each page. Such copy or entries or return shall be supplied within seven days of deposit of such fee.

### ***Copies of the registers and annual return.-***

Rule 16 of the Companies (Management and Administration) Rule, 2014 provides copies of the registers maintained under section 88 or entries therein and annual return filed under section 92 shall be furnished to any member, debenture-holder, other security holder or beneficial owner of the company or any other person on payment of such fee as may be specified in the Articles of Association of the company but not exceeding rupees ten for each page and such copy shall be supplied by the company within a period of seven days from the date of deposit of fee to the company.

### ***Consequences if inspection is refused***

According to Section 94(4), if any inspection or the making of any extract or copy required under this section 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 one thousand rupees for every day subject to a maximum of one lakh rupees during which the refusal or default continues.

Further section 94(5) provides that “the Central Government may also, by order, direct an immediate inspection of the document, or direct that the extract required shall forthwith be allowed to be taken by the person requiring it.”

### Register -An evidence

Section 95 of the Companies Act, 2013 provides that the registers, their indices and copies of annual returns maintained under sections 88 and 94 shall be prima facie evidence of any matter directed or authorised to be inserted therein by or under this Act.

A register of members is *prima facie* evidence of the truth of its contents. Accordingly, if a person's name, to his knowledge, is there in the register of members of a company, he shall be deemed to be a member and onus lies on him to prove that he is not a member. He must promptly appeal to the Tribunal or a competent court outside India specified by the Central Government by notification, in respect of foreign members or debenture holder residing outside India for rectification of the register under Section 59 of the Act to take his name off the register, failing which the doctrine of holding out will apply.

### CASE LAW

In Re. *M.F.R.D. Cruz*, A.I.R. 1939 Madras 803, the plaintiff applied for 4,000 shares in a company but no allotment was made to him. Subsequently 4,000 shares were transferred to him without his request and his name was entered in the register of members. The plaintiff knew it but took no steps for rectification of the register of members. The company went into liquidation and he was held liable as a contributory. The Court held “when a person knows that his name is included in the register of shareholders and he stands by and allows his name to remain, he is holding out to the public that he is a shareholder and thereby he loses his right to have his name removed”.

### Foreign Register

Section 88(4) of the Companies Act, 2013 empowers companies to keep foreign registers of members or debenture-holders, other security holders or beneficial owners residing outside India. It states:

“A company may, if so authorised by its articles, keep in any country outside India, in such manner as may be prescribed, a part of the register referred to in sub-section (1), called “foreign register” containing the names and particulars of the members, debentureholders, other security holders or beneficial owners residing outside India.”

If a company does not maintain foreign register of members or debenture-holders or other security holders or fails to maintain them in accordance with the provisions of section 88(1) or section 88(2), the company and every officer of the company who is in default shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees and where the failure is a continuing one, with a further fine which may extend to one thousand rupees for every day, after the first during which the failure continues. [Section 88(5)]

A foreign register is deemed to be a part of the company's principal register and it should be kept in the same manner as the principal register and be likewise open to inspection.

A duplicate of such register should be maintained at the registered office in India and all entries made in the foreign register should be made in the duplicate register at the registered office as soon as possible.

A company may discontinue a foreign register at any time but all the entries made in it must be transferred to the principal register.

The decision of a competent Court in the State or Country in which a foreign register is kept, with regard to its rectification, shall be as effective as if it were a decision of a competent Court in India, if the Central Government, by notification in the *Official Gazette*, so directs.

### **Maintenance of Foreign Register**

Rule 7 of Companies(Management and Administration) deals with maintenance of foreign register, it is provided that a company which has share capital or which has issued debentures or any other security may, if so authorised by its articles, keep in any country outside India, a part of the register of members or as the case may be, of debenture holders or of any other security holders or of beneficial owners, resident in that country (hereafter in this rule referred to as the "foreign register"). The company shall, within thirty days from the date of the opening of any foreign register, file with the Registrar notice of the situation of the office in Form No.MGT.3 along with the fee where such register is kept; and in the event of any change in the situation of such office or of its discontinuance, shall, within thirty days from the date of such change or discontinuance, as the case may be, file notice in Form No.MGT.3 with the Registrar of such change or discontinuance.

A foreign register shall be deemed to be part of the company's register (hereafter in this rule referred to as the "principal register") of members or of debenture holders or of any other security holders or beneficial owners, as the case may be.

The foreign register shall be maintained in the same format as the principal register.

A foreign register shall be open to inspection and may be closed, and extracts may be taken there from and copies thereof may be required, in the same manner, *mutatis mutandis*, as is applicable to the principal register, except that the advertisement before closing the register shall be inserted in at least two newspapers circulating in the place wherein the foreign register is kept.

If a foreign register is kept by a company in any country outside India, the decision of the appropriate competent authority in regard to the rectification of the register shall be binding.

Entries in the foreign register maintained under sub-section (4) of section 88 shall be made simultaneously after the Board of Directors or its duly constituted committee approves the allotment or transfer of shares, debentures or any other securities, as the case may be.

The company shall—

- (a) transmit to its registered office in India a copy of every entry in any foreign register within fifteen days after the entry is made; and
- (b) keep at such office a duplicate register of every foreign register duly entered up from time to time.

Every such duplicate register shall, for all the purposes of this Act, be deemed to be part of the principal register.

Subject to the provisions of section 88 and the rules made thereunder, with respect to duplicate registers, the shares or as the case may be, debentures or any other security, registered in any foreign register shall be distinguished from the shares or as the case may be, debentures or any other security, registered in the principal register and in every other foreign register; and no transaction with respect to any shares or as the case may be, debentures or any other security, registered in a foreign register shall, during the continuance

of that registration, be registered in any other register.

The company may discontinue the keeping of any foreign register; and thereupon all entries in that register shall be transferred to some other foreign register kept by the company outside India or to the principal register.

### **Closing of Register of Members**

Section 91 of the Companies Act, 2013 contains guidelines for closing the register of members. It lays down:

- (1) A company may close the register of members or the register of debenture-holders or the register of other security holders for any period or periods not exceeding in the aggregate forty-five days in each year, but not exceeding thirty days at any one time, subject to giving of previous notice of at least 7 days or such lesser period as may be specified by Securities and Exchange Board for listed companies or the companies which intend to get their securities listed, in the prescribed manner.
- (2) If the register of members or of debenture-holders or of other security holders is closed without giving the notice as provided above, or after giving shorter notice than that so provided, or for a continuous or an aggregate period in excess of the limits specified in that sub-section, the company and every officer of the company who is in default shall be liable to a penalty of 5000 rupees for every day subject to a maximum of one lakh rupees during which the register is kept closed.

In a decided case law it was held that the provisions contained in Section 154 of Companies Act, 1956 (Corresponds to section 91 of the Companies Act, 2013) are permissive and not mandatory. The section has application only when a company desires to close its register of members and in such a situation, the requirements of the section are to be complied with. *Talyar Tea Co. v. Union of India*, (1991) 71 Com Cases 95.

The power in this section is intended for the convenience of the company in order to enable the register of members to be brought up to date for the purpose of calculating dividend and bonus, etc. However, even if the register of members is closed, the company is obliged to make certain entries during the period of closure, such as entries relating to registration and probates and letters of administration, notices of change of name and address and court orders, such as changing orders, etc. [*Killick Nixon Ltd. v. Dhanraj Mill Pvt. Ltd.*, (1983) 54 Com Cases 432 (DB) (Bom)].

The closure of the register is cloaked with the right to refuse the transfer of shares/debentures. Record date is an alternate for closing the registers. The purpose of closing the registers is to get the registers updated and to fix a cut-off date for the purpose of payment of dividend or issue of rights and bonus shares. This purpose can also be achieved by fixing a record date for a day.

Further the Rule 10 of the Companies (Management and Administration) Rules, 2014 in relation to Closure of register of members or debenture holders or other security holders provides that a company closing the register of members or the register of debenture holders or the register of other security holders shall give at least seven days previous notice and in such manner, as may be specified by Securities and Exchange Board of India (SEBI), if such company is a listed company or intends to get its securities listed, by advertisement at least once in a vernacular newspaper in the principal vernacular language of the district and having a wide circulation in the place where the registered office of the company is situated, and at least once in English language in an English newspaper circulating in that district and having wide circulation in the place where the registered office of the company is situated and publish the notice on the website as may be notified by the Central Government and on the website, if any, of the Company.

The above mentioned provisions shall not be applicable to a private company provided that the notice has

been served on all members of the private company not less than seven days prior to closure of the register of members or debenture holders or other security holders.

### **Preservation of Registers**

Rule 15 of Companies (Management and Administration) Rules, 2014 provides that the register of members along with the index shall be preserved permanently and shall be kept in the custody of the company secretary of the company or any other person authorized by the Board for such purpose and the register of debenture holders or any other security holders along with the index shall be preserved for a period of eight years from the date of redemption of debentures or securities, as the case may be, and shall be kept in the custody of the company secretary of the company or any other person authorized by the Board for such purpose.

The foreign register of members shall be preserved permanently, unless it is discontinued and all the entries are transferred to any other foreign register or to the principal register. Foreign register of debenture holders or any other security holders shall be preserved for a period of eight years from the date of redemption of such debentures or securities. The foreign register shall be kept in the custody of the company secretary or person authorised by the Board.

### **Power of the Central Government to Investigate into the Ownership of Company**

Sometimes, the registered holder of shares in a company may be a nominee for some other person, who really owns the shares. This enables persons, who in fact control a company, to conceal their real status from the shareholders and from the public and practice fraud with regard to the management of the company. To check such a practice, Sections 216 empowers the Central Government to appoint an inspector to investigate into and report on the ownership of a company.

### **DECLARATION BY PERSONS NOT HOLDING BENEFICIAL INTEREST IN ANY SHARE**

Beneficial interest in a shares, for the purpose of section 89 and 90, includes, directly or indirectly, through any contract, arrangement or otherwise, the right or entitlement of a person alone or together with any other person to—

- (i) exercise or cause to be exercised any or all of the rights attached to such share; or
- (ii) receive or participate in any dividend or other distribution in respect of such share.

Section 89 of the Companies Act, 2013 read with Companies(Management and Administration) Rules, 2014 makes it obligatory on the part of a person, whose name is entered in the register of members of a company as the holder of a shares in that company but who does not hold beneficial interest in such shares to make a declaration to the company specifying the name and other particulars of the person who holds the beneficial interest in such shares [Sub-section (1)].

Sub-section (2) of the Section 89 makes it obligatory for any person who, holds or acquires beneficial interest in a share of a company to make a declaration to the company specifying the nature of his interest, the particulars of the person in whose name the shares stand registered in the books of the company and such other particulars as may be prescribed.

Where any change occurs in the beneficial interest in such shares, the person referred in sub-section (1), and the beneficial owner specified under sub-section (2) shall make a declaration within thirty days, from the date of such change to the company in the prescribed Form containing the prescribed particulars. [Sub-section (3)]

The Central Government may make rules to provide for the manner of holding and disclosing beneficial interest and beneficial ownership under this section. [Sub-section (4)]

Sub-section (5) provides that if any person fails, to make a declaration as required under sub-section (1) or sub-section (2) or sub-section (3), without any reasonable cause, he shall be punishable with fine which may extend to fifty thousand rupees and where the failure is a continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the failure continues.

Sub-section (6) makes it obligatory on the part of the company to make a note of such a declaration in the register concerned and to file within thirty days from the date of receipt of declaration by it, with the Registrar of Companies, a return in the prescribed form with regard to such a declaration.

In a recent notification by MCA, in case of an unlisted public company or a private company which is licensed to operate by the Reserve Bank of India or the Securities and Exchange Board of India or the Insurance Regulatory and Development Authority of India from the International Financial Services Centre located in an approved multi services Special Economic Zone set-up under the Special Economic Zones Act, in sub section (6) of section 89 for the words "thirty days" read as "sixty days". (G.S.R. 08(E) & G.S.R. 09(E), Dated 4-01-2017)

If a company, required to file a return under sub-section (6), fails to do so before the expiry of the time specified therein i.e. thirty days from the date of receipt of declaration by the company, then the company and every officer of the company who is in default shall be punishable with fine which shall not be less than five hundred rupees but which may extend to one thousand rupees and where the failure is a continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the failure continues. [Sub-section (7)]

No right in relation to any share in respect of which a declaration is required to be made under this section but not made by the beneficial owner, shall be enforceable by him or by any person claiming through him. [Sub-section (8)]

Nothing in this section shall be deemed to prejudice the obligation of a company to pay dividend to its members under this Act and the said obligation shall, on such payment, stand discharged. [Sub-section (9)]

### **Step for declaration of beneficial interest in any shares Rule 9 of Companies (Management and Administration) Rules, 2014**

(1) A person whose name is entered in the register of members of a company as the holder of shares in that company but who does not hold the beneficial interest in such shares (hereinafter referred to as "the registered owner"), shall file with the company, a declaration to that effect in Form No.MGT.4, within a period of thirty days from the date on which his name is entered in the register of members of such company:

When any change occurs in the beneficial interest in such shares, the registered owner shall, within a period of thirty days from the date of such change, make a declaration of such change to the company in Form No.MGT.4.

(2) Every person holding and exempted from furnishing declaration or acquiring a beneficial interest in shares of a company not registered in his name (hereinafter referred to as "the beneficial owner") shall file with the company, a declaration disclosing such interest in Form No. MGT.5, within thirty days after acquiring such beneficial interest in the shares of the company:

Provided that where any change occurs in the beneficial interest in such shares, the beneficial owner shall, within a period of thirty days from the date of such change, make a declaration of such change to the company in Form No.MGT.5.

(3) Where any declaration under section 89 is received by the company, the company shall make a note of such declaration in the register of members and shall file, within a period of thirty days from the date of receipt of declaration by it, a return in Form No. MGT. 6 with the Registrar in respect of such declaration with fee.

Provided that nothing contained in this rule shall apply in relation to a trust which is created, to set up a Mutual Fund or Venture Capital Fund or such other fund as may be approved by SEBI.

### **SIGNIFICANT BENEFICIAL OWNER**

Section 90 of the Act provides that every individual, who acting alone or together, or through one or more persons or trust, including a trust and persons resident outside India, holds beneficial interests, of not less than twenty-five per cent. or such other percentage as may be prescribed, in shares of a company or the right to exercise, or the actual exercising of significant influence or control as defined in clause (27) of section 2, over the company (herein referred to as "significant beneficial owner"), shall make a declaration to the company, specifying the nature of his interest and other particulars, in such manner and within such period of acquisition of the beneficial interest or rights and any change thereof, as may be prescribed.

Central Government may prescribe a class or classes of persons who shall not be required to make declaration as stated above.

Further every company shall maintain a register of the interest declared by individuals stated above and changes therein which shall include the name of individual, his date of birth, address, details of ownership in the company and such other details as may be prescribed. The register so maintained shall be open to inspection by any member of the company on payment of such fees as may be prescribed.

Every company shall file a return of significant beneficial owners of the company and changes therein with the Registrar containing names, addresses and other details as may be prescribed within such time, in such form and manner as may be prescribed.

A company shall give notice, in the prescribed manner, to any person (whether or not a member of the company) whom the company knows or has reasonable cause to believe—

- (a) to be a significant beneficial owner of the company;
- (b) to be having knowledge of the identity of a significant beneficial owner or another person likely to have such knowledge; or
- (c) to have been a significant beneficial owner of the company at any time during the three years immediately preceding the date on which the notice is issued, and who is not registered as a significant beneficial owner with the company as required under this section.

The information required by the notice shall be given by the concerned person within a period not exceeding thirty days of the date of the notice.

The company shall,—

- (a) where that person fails to give the company the information required by the notice within the time specified therein; or
- (b) where the information given is not satisfactory,

apply to the Tribunal within a period of fifteen days of the expiry of the period specified in the notice, for an order directing that the shares in question be subject to restrictions with regard to transfer of interest, suspension of all rights attached to the shares and such other matters as may be prescribed.

On any application made to the Tribunal, it may, after giving an opportunity of being heard to the parties concerned, make such order restricting the rights attached with the shares within a period of sixty days of receipt of application or such other period as may be prescribed. The company or the person aggrieved by the order of the Tribunal may make an application to the Tribunal for relaxation or lifting of the restrictions.

If any person fails to make a declaration as required, he shall be punishable with fine which shall not be less than one lakh rupees but which may extend to ten lakh rupees and where the failure is a continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the failure continues.

Where a company, required to maintain register and file the information, with respect to significant beneficial owner, fails to do so or denies inspection as provided therein, the company and every officer of the company who is in default shall be punishable with fine which shall not be less than ten lakh rupees but which may extend to fifty lakh rupees and where the failure is a continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the failure continues.

### **Rectification of a Register of Members**

The register of members of a company contains names, addresses, occupations, if any etc. only of members of the company. Any person, whose name is entered in the register of members of a company, considered to be its member, although he may not own the shares which are shown in his name in the register of members. On the contrary, a person, whose name is not entered in the register of members is not considered as member of the company even though he may have done everything to entitle him to be put on the register of members. Injustice may, therefore, result from such omission or commission.

Section 59 of the Companies Act, 2013 confers powers on the Tribunal or a competent court outside India specified by the Central Government by notification in respect of foreign members or debenture-holders residing outside India to order rectification of register of members of a company if an appeal is made by the aggrieved person or by any member of the company or the company on any of the following grounds:

- (a) where the name of a person is without sufficient cause, entered in the register of members of a company;
- (b) where his name, after having been entered in the register, is omitted without sufficient cause; or
- (c) where default is made or unnecessary delay takes place in entering in the register of members the fact of any person having become, or ceased to be, a member of company.

This may happen where a person has transferred his shares according to law and the company either refuses or delays registration of transfer in the transferee's name.

The Tribunal may, after hearing the parties to the appeal for rectification of register of members either dismiss the appeal or direct that the transfer or transmission shall be registered by the company within ten days or direct for rectification of records of the depository or the register and in the latter case also direct the company to pay damages if any, sustained by the party aggrieved.

It is pertinent to note that though the time limit for filing an application for rectification of register of members has not been specified in the Act, the provisions of Article 137 of the Limitation Act would apply and in consequence, the application for rectification must be made within three years from the date on which the right occurs [Ref. *Anil Gupta v. Delhi Cloth & General Mills Co. Ltd.*, (1983) 54 Com Cases 301 (Delhi)].

The provisions of this section shall not restrict the right of a holder of securities, to transfer such securities and any person acquiring such securities shall be entitled to voting rights unless the voting rights have been

suspended by an order of the Tribunal. [Section 59(3)]

Where the transfer of securities is in contravention of any of the provisions of the Securities Contracts (Regulation) Act, 1956, the Securities and Exchange Board of India Act, 1992 or this Act or any other law for the time being in force, the Tribunal may, on an application made by the depository, company, depository participant, the holder of the securities or the Securities and Exchange Board, direct any company or a depository to set right the contravention and rectify its register or records concerned. [Section 59(4)]

If any default is made in complying with the order of the Tribunal under this section, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees, or with both. [Section 59(5)]

(Note: Students may also read Chapter 2 in this context.)

## RIGHTS OF MEMBERS

When once a person becomes a member he is entitled to exercise all the rights of a member until he ceases to be a member in accordance with the provisions of the Act. The appointment of a receiver, the attachment of the shares, the pledge of the shares or taking over of the management of a company which is holding shares in another company will not alter the position. So long a person's name stands registered in the books as a member, even if he has sold the share and has given the share certificates and the blank transfer deed duly signed, he alone is entitled to exercise the rights of membership [*Balakrishna Gupta & Others v. Swadeshi Polytex Ltd. and Others* (1985) 58 Com Cases 563 (S.C.); and *Life Insurance Corporation of India v. Escorts Ltd. & Others* (1986) 59 Com Cases 548 (S.C.)]. These rights are derived by virtue of the membership contract between the company and the member and the general law. Some of these rights can be exercised by him individually and others alongwith other members unless member himself holds shares equivalent to the minimum holding prescribed under the various provisions of the Companies Act, 2013.

### Individual Rights

Members of a company enjoy certain rights in their individual capacity, which they can enforce individually. These rights are contractual rights and cannot be taken away except with the written consent of the member concerned. These rights can be categorised as under:

- (1) Right to receive copies of the following documents from the company:
  - (i) Abridged financial statement and auditor's report in the case of a listed company (Section 136).
  - (ii) Report of the Cost Auditor, if so directed by the Government.
  - (iii) Notices of the general meetings of the company (Sections 101-102).
- (2) Right to inspect statutory registers/returns and get copies thereof without payment on any fee or on payment of prescribed fee.

The members have been given right to inspect the following registers etc.:

- (i) Debenture trust deed (Section 71);
- (ii) Register of Charges and instrument of charges (Section 85 & 87);
- (iii) Copies of contract of employment with Managing or Whole-time directors);
- (iv) Shareholders' Minutes Book (Section 119);

- (v) Register of Contracts, Companies and Firms in which directors are interested (Section 189);
- (vi) Register of directors and key managerial personnel and their shareholding (Section 170);
- (3) Right to attend meetings of the shareholders and exercise voting rights at these meetings either personally or through proxy (Sections 96, 100, 105 and 107).

(4) Other rights.

Over and above the rights enumerated at Item Nos. 1 to 3 above, the members have the following rights:

- (i) To transfer shares (Sections 44 and 56 and Articles of Association of the company).
- (iii) To resist and safeguard against increase in his liability without his written consent.
- (iv) To receive dividend when declared.
- (v) To have rights shares (Section 62).
- (vi) To appoint directors (Section 152).
- (vii) To share the surplus assets on winding up (Section 320).
- (viii) Right of dissentient shareholders to apply to Tribunal (Section 48).
- (ix) Right to be exercised collectively by passing a special resolution and intimating the same to the Central Government for investigation of the affairs of the company (Section 210).
- (x) Right to make application collectively to the Tribunal for relief in cases of oppression and mismanagement (Sections 241).
- (xi) Right to file class action suits before the Tribunal (Section 245)
- (xi) Right of Nomination. (Section 72)
- (xii) Right to file a suit or take any other action in case of any misleading statement or the inclusion or omission of any matter in the prospectus. (Section 37)

### **Collective Membership Rights**

Members of a company have certain rights which can be exercised by members collectively by means of democratic process, i.e. by majority of members usually unless otherwise prescribed. This involves the principle of submission by all members to the will of the majority, provided that the will is exercised in accordance with the law and the Memorandum and Articles of Association of the company. Thus, the shareholders in majority determine the policy of the company and exercise control over the management of the company.

However, if and when the majority becomes oppressive or is accused of mismanagement of the affairs of the company, Section 241 read with section 244 confers right, to not less than one hundred members of a company or not less than one-tenth of the total number of its members whichever is less or any member or members holding not less than one-tenth of the issued share capital of the company (but they must have paid all calls and others sums due on their shares) and in the case of a company not having a share capital, not less than one-fifth of the total number of its members, to apply to Board under Section 241 for relief in cases of oppression or for relief in cases of mismanagement respectively.

Section 100 of the Companies Act, 2013 confers on members, holding not less than one-tenth of the paid-up share capital of a company, right to make a requisition to the Board of directors to call an extraordinary

general meeting of the company. The section also confers on members having not less than one-tenth of the total voting power in a company not having a share capital, to make a requisition to the Board to call an extraordinary general meeting of the company. If the Board of directors of the company does not, within twenty-one days from the date of the deposit of a valid requisition in regard to any matter, proceed to call a meeting for the consideration of those matters on a day not later than forty-five days from the date of deposit of the requisition, the meeting may be called and held by the requisitionists themselves within a period of 3 months from the date of the requisition.

### **Voting Rights of Members**

The right of attending shareholders' meetings and voting thereat is the most important right of a member of a company, as shareholders' meetings play a very important role in the company's life. Directors are appointed by the shareholders, who direct the affairs of the company, formulate short-term plans and long-term policies of the company, appoint management personnel to constitute organisation to implement their plans and policies in order to achieve the objects of the company.

In view of the importance of the general meetings of a company, the Companies Act has not left the members to the will of the directors to call general meetings. If the members feel that the affairs of the company are not being properly managed by the directors and the directors are avoiding to call a general meeting of the company, Section 100 of the Companies Act confers right on members specified therein to deposit a requisition setting out the matters for the consideration of which the meeting is to be called and if the Board of directors does not proceed within twenty-one days of the requisition to call a meeting within forty-five days of the requisition, the requisitionists may themselves call the meeting.

Section 47 provides that every member of a company limited by shares and holding equity share capital therein, shall have right to vote on every resolution placed before the company and his voting right on a poll shall be in proportion to his share in the paid up equity share capital of the company.

Section 43 of the Companies Act, 2013 provides that a company limited by shares shall be entitled to issue (i) equity share capital with voting rights or (ii) with differential rights as to dividend, voting or otherwise in accordance with such rules as may be prescribed by the Central Government.

Preference shareholders ordinarily vote only on matters directly affecting the rights attached to preference share capital and on any resolution for winding up of the company or for the repayment or reduction of the equity or preference share capital. The voting right of a preference shareholder on poll shall be in proportion to his share in the paid-up preference share capital of the company. In respect of a resolution on a matter affecting both equity shareholders and preference shareholders, the proportion of the voting rights of equity shareholders to the voting rights of the preference shareholders shall be in the same proportion as the paid-up capital in respect of the equity shares bears to the paid-up capital in respect of the preference shares. However, where the dividend in respect of a class of preference shares has not been paid for a period of two years or more, such class of preference shareholders shall have a right to vote on all the resolutions placed before the company (Section 47).

Section 50 of the Act lays down that a company may, if authorised by its articles, accept from any member the whole or a part of the amount remaining unpaid on any shares held by him although no part of that amount has been called up. Such advance payment, however, shall not confer on the member concerned any voting rights.

### **Shareholders' Pre-emptive Rights with regard to further issue of share capital (Right Shares)**

To preserve the shareholders' proportionate dividend, liquidation and voting rights, pre-emptive rights are

often recognised, but their existence and scope can be effected by provisions in the articles. However, Section 62 of the Companies Act, 2013 secures shareholders' pre-emptive rights with regard to the further issue of share capital by the company. The Section lays down:

“(1) Where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered to persons who, at the date of the offer, are holders of equity shares of the company in proportion, as nearly as circumstances admit, to the paid-up share capital on those shares by sending a letter of offer subject to the condition that unless the articles of the company otherwise provide, the offer aforesaid shall be deemed to include a right exercisable by the person concerned to renounce the shares offered to him or any of them in favour of any other person and the notice of offer shall contain a statement of this right [Sub-clause (a)].

### **Rights of Dissenting Shareholders**

Section 48(2) of the Companies Act, 2013 confers certain rights upon the dissenting shareholders. According to section 48(2), where the rights of any class of shares are varied, the holders of not less than ten per cent of the issued shares of that class, being persons who did not consent to such variation or vote in favour of the special resolution for the variation, can apply to the Tribunal to have the variation cancelled. Where any such application is made to the Tribunal, the variation will not be effective unless and until it is confirmed by the Tribunal.

The above application shall be made within twenty-one days after the date on which the consent was given or the resolution was passed, as the case may be, and may be made on behalf of the shareholders entitled to make the application by such one or more of their number as they may appoint in writing for the purpose.

### **Nomination by Security holders (including members) (Section 72)**

Section 72(1) states that every holder of securities of a company may, at any time, nominate, in the prescribed manner, any person to whom his securities shall vest in the event of his death.

Section 72(2) states that when the securities of a company are held by more than one person jointly, the joint holders may together nominate, in the prescribed manner, any person to whom all the rights in the securities shall vest in the event of death of all the joint holders.

Section 72(3) states that notwithstanding anything contained in any other law for the time being in force or in any disposition, whether testamentary or otherwise, in respect of the securities of a company, where a nomination made in the prescribed manner purports to confer on any person the right to vest the securities of the company, the nominee shall, on the death of the holder of securities or, as the case may be, on the death of the joint holders, become entitled to all the rights in the securities, of the holder or, as the case may be, of all the joint holders, in relation to such securities, to the exclusion of all other persons, unless the nomination is varied or cancelled in the prescribed manner.

Section 72 (4) states that when the nominee is a minor, it shall be lawful for the holder of the securities, making the nomination to appoint, in the prescribed manner, any person to become entitled to the securities of the company, in the event of the death of the nominee during his minority.

Rule 19 of Companies (Share Capital and debentures) Rules, 2014 deals with Nomination by securities holders. It provides that:-

(1) Any holder of securities of a company may, at any time, nominate, in Form No. SH.13, any person as his nominee in whom the securities shall vest in the event of his death.

(2) On the receipt of the nomination form, a corresponding entry shall forthwith be made in the relevant register of securities holders, maintained under section 88.

(3) Where the nomination is made in respect of the securities held by more than one person jointly, all joint holders shall together nominate in Form No.SH.13 any person as nominee.

(4) The request for nomination should be recorded by the Company within a period of two months from the date of receipt of the duly filled and signed nomination form.

(5) In the event of death of the holder of securities or where the securities are held by more than one person jointly, in the event of death of all the joint holders, the person nominated as the nominee may upon the production of such evidence as may be required by the Board, elect, either-

- (a) to register himself as holder of the securities ; or
- (b) to transfer the securities, as the deceased holder could have done.

(6) If the person being a nominee, so becoming entitled, elects to be registered as holder of the securities himself, he shall deliver or send to the company a notice in writing signed by him stating that he so elects and such notice shall be accompanied with the death certificate of the deceased share or debenture holder(s).

(7) All the limitations, restrictions and provisions of the Act relating to the right to transfer and the registration of transfers of securities shall be applicable to any such notice or transfer as aforesaid as if the death of the share or debenture holder had not occurred and the notice or transfer were a transfer signed by that shareholder or debenture holder, as the case may be.

(8) A person, being a nominee, becoming entitled to any securities by reason of the death of the holder shall be entitled to the same dividends or interests and other advantages to which he would have been entitled to if he were the registered holder of the securities except that he shall not, before being registered as a holder in respect of such securities, be entitled in respect of these securities to exercise any right conferred by the membership in relation to meetings of the company.

The Board may, at any time, give notice requiring any such person to elect either to be registered himself or to transfer the securities, and if the notice is not complied with within ninety days, the Board may thereafter withhold payment of all dividends or interests, bonuses or other moneys payable in respect of the securities, as the case may be, until the requirements of the notice have been complied with.

(9) A nomination may be cancelled, or varied by nominating any other person in place of the present nominee, by the holder of securities who has made the nomination, by giving a notice of such cancellation or variation, to the company in Form No. SH.14.

(10) The cancellation or variation shall take effect from the date on which the notice of such variation or cancellation is received by the company.

(11) When the nominee is a minor, the holder of the securities, making the nomination, may appoint a person in Form No. SH.13 specified under sub-rule (1), who shall become entitled to the securities of the company, in the event of death of the nominee during his minority.

## **LIABILITY OF MEMBERS**

The liability of a member depends on the nature of the company. If the company is registered with unlimited liability, every member is liable in full for all the debts of the company contracted during the period of his membership. Where the company is limited by guarantee, each member will be bound to contribute in the

event of winding up a sum specified in the liability clause of the memorandum of association. In case of company limited by shares, each member is bound to contribute the full nominal value of shares and his liability ends there. If before the full nominal value of the shares is paid, the company goes into liquidation, the member becomes liable as contributory to pay the balance when called upon to pay, by the liquidator of the company.

Where a company has been incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants, direct that liability of the members shall be unlimited. [Section 7(7)]

If a member ceased to be member of a company within one year prior to the commencement of the winding up of the company he is liable to pay on the shares which he held to the extent of the amount unpaid thereon, if:

- (i) on the winding up, debts exist which were incurred while he was a member, and
- (ii) it appears to the Tribunal that the present members are not able to satisfy the contribution required from them in respect of their shares.

A person is liable as member in spite of a valid transfer of shares by him, if the name of the transferee is not placed on the register of members, in place of the transferors' name. If a person applies for shares in the name of a fictitious person or a person not in existence or uses another person's name for himself, or uses an alias, and shares are allotted in that name or alias, he will be liable as a member.

### **Variation of Shareholder's Rights**

Shareholder's rights are determined by the Companies Act, Memorandum of association, Articles of association of the company and the terms of issue of shares. Rights attached to a class of shares are known as "class rights".

Shareholder's rights relate to dividend, voting at members' meetings and return of capital. Preference shareholders may have rights to a fixed amount or a fixed rate of dividend or to cumulative dividend. Where the ordinary shareholders are conferred the right to participate in the surplus assets on winding up of a company, it is not deemed to be a class right as it is implied even in the absence of any express provision in the articles.

Section 48 (1) of the Companies Act, 2013 lays down that where a share capital of the company is divided into different classes of shares, the rights attached to the shares of any class can be varied with the consent in writing of the holders of not less than three-fourths 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. Further, the variation of rights of shareholders can be effected only:

- (i) if provision with respect to such variation is contained in the Memorandum or Articles of association of the company; or
- (ii) in the absence of any such provision in a Memorandum or Articles of association of the company, if such a variation is not prohibited by the terms of issue of the shares of that class.

However, if variation by one class of shareholders affects the rights of any other class of shareholders, the consent of three-fourths of such other class of shareholders shall also be obtained and the provisions of this section shall apply to such variation.

## SHAREHOLDERS' DEMOCRACY

The concept of shareholders' democracy in the present day corporate world denotes the shareholders' supremacy in the governance of the business and affairs of corporate sector either directly or through their elected representatives.

Democracy means the rule of people, by people and for people. In that context the shareholders democracy means the rule of shareholders, by the shareholders, and for the shareholders in the corporate enterprise, to which the shareholders belong. Precisely it is a right to speak, congregate, communicate with co-shareholders and to learn about what is going on in the company.

Under the Companies Act the powers have been divided between two segments: one is the Board of Directors and the other is of shareholders. The directors exercise their powers through meetings of Board of directors and shareholders exercise their powers through General Meetings. Although constitutionally all the acts relating to the company can be performed in General Meetings but most of the powers in regard thereto are delegated to the Board of directors by virtue of the constitutional documents of the company viz. the Memorandum of Association and Articles of Association.

Under Section 179 of the Companies Act 2013 a general power has been conferred on the Board of directors. The section provides that "Subject to the provisions of this Act, the Board of directors of a company shall be entitled to exercise all such powers and to do all such acts and things, as the company is authorised to exercise and do."

Proviso to this section restricts the power of the Board of directors to do things which are specifically required to be done by shareholders in the General Meetings under the provisions of Companies Act or Memorandum of Association or the Articles of Association.

Thus the Companies Act has tried to demarcate the area of control of directors as well as that of shareholders. Basically all the business to be transacted at the meetings of shareholders is by means of an ordinary resolution or a special resolution or by postal ballot.

### Few businesses which are required to be transacted by shareholders

1. Alteration of Memorandum of Association and Articles of Association.
2. Further issue of share capital.
3. To transfer some portions of uncalled capital to reserve capital to be called up only in the event of winding up of the company.
4. To reduce the share capital of the company.
5. To shift the registered office of the company outside the local limits of any city, town or village where the registered office is situated.
6. To decide a place other than the registered office of the company where the statutory books, required to be maintained.
7. Payment of interest on paid-up amount of share capital for defraying the expenses on construction when plant cannot be commissioned for a longer period of time.
8. To approach Central Government for investigation into the affairs of the company.
9. Any contract or arrangement with related party, above the threshold limits.
10. Payment of commission of more than statutory requirement to a managing or a whole-time director

or a manager.

11. To make loans, to extend guarantee or provide security to other companies or make investment beyond the limit specified.
12. To borrow money and to charge out the assets of the company to secure the borrowed money where the sums to be borrowed along with money already borrowed exceeds the paid-up capital of the company and its free reserves i.e. reserves not set apart for any specific purpose.
13. To appoint directors.
14. To increase or reduce the number of directors within the limits laid down in Articles of Association.
15. To cancel, redeem debentures etc.
16. To make contribution to funds not related to the business of the company.

In view of the rights conferred on shareholders to be exercised at General Meetings, the Act casts an obligation on the directors to send notices for convening general meetings or else the meetings shall be declared to be void as also all proceedings transacted thereat.

Apart from the rights which are vested in the shareholders to be exercised in relation to the conduct of the business of the company, the directors of the company have certain obligations towards the shareholders.

The courts have determined two broad duties to be performed by a director:

1. Duty of utmost care and skill in managing the affairs of the company or else be liable for damages.
2. Fiduciary duty to act *bona fide* in the interest of the company, not to exercise powers for collateral benefit and not to earn profit from the position as a director.

## **SHAREHOLDER'S AGREEMENT**

Shareholders' agreements (SHA) are quite common in business. In India shareholder's agreement have gained popularity and currency only lately with bloom in newer forms of businesses. There are numerous situations where such agreements are entered into – family companies, JV companies, venture capital investments, private equity investments, strategic alliances, and so on. Shareholders' agreement is a contractual arrangement between the shareholders of a company describing how the company should be operated and the defining inter-se shareholders' rights and obligations. shareholders' agreement. SHAs are the result of mutual understanding among the shareholders of a company to which, the company generally becomes a consenting party. Such agreements are specifically drafted to provide specific rights, impose definite restrictions over and above those provided by the Companies Act. SHA creates personal obligation between the members signing such agreement however, such agreements do not become a regulation of the company in the way the provisions of Articles are.

### **Enforceability of the Shareholder's Agreement**

Though the international view is split but to a large extent courts are inclined towards favouring SHA as long as they are not found to be detrimental to the minority stakeholder's rights. In the leading case of *Russell v. Northern Bank Development Corporation Ltd* [1992] BCC 578; [1992] 1 WLR 588, the House of Lords found that though a company cannot deprive itself of its power to alter its constitution, the members of the company could agree in a shareholders' agreement as to how they will exercise their voting rights on a resolution to alter the articles/constitution. The US Courts have largely accepted shareholder agreements. [*Blount v. Taft* [246 S.E.2d 763 at 769 (1978)]]

While shareholders' agreements are enforceable in England regardless of whether they have been incorporated in the articles of association of the company, in India courts have either refused to recognize clauses in shareholders agreements or, even when consistent with company legislation, enforced such clauses only if they have been incorporated in the articles of association of the company. There is a series of rulings where the courts have upheld that in case of any conflict between the Articles and the SHA, the former will always prevail. Some of these are:

- V.B. Rangaraj v. V.B. Gopalakrishnan (AIR 1992 SC 453)
- Shanti Prasad Jain v. Kalinga Tubes Ltd., (35 Com. Cas. 351 SC)
- Mafatlal Industries Ltd., v. Gujarat Gas Co. Ltd (97 Comp Cas 301 Guj),
- Pushpa Katoch v. Manu Maharani Hotels Limited ([2006] 131 Comp Cas 42 (Delhi))

The Supreme Court in *V.B. Rangaraj v. V.B. Gopalakrishnan*, AIR 1992 SC 453 held that a restriction which is not specified in the articles of association is not binding either on the company or on the shareholders. This decision was reiterated by the Bombay High Court in *IL & FS Trust Co. Ltd. v. Birla Perucchini Ltd* [2004] 121 Comp Cas 335 (Bom).

However, the Supreme Court in 2003 in its decision in *M.S. Madhusoodhanan v. Kerala Kaumudi Pvt. Ltd.* (2003 117 CompCas 19 SC ) not disagreeing with the decision in V.B Rangaraj case mentioned above, but distinguishing itself from the facts in that judgment, held that a restriction in relation to identified members on identified shares of a private company did not amount to restriction of transferability of shares per se.

In *Western Maharashtra Development Corporation Ltd. v. Bajaj Auto Ltd* [(2010) 154 Company Cases 593 (Bom)], it was held that such clauses are to hamper the free transferability of shares and in violation of the Companies Act, and hence, are not enforceable. Subsequently in the case of *Messer Holdings Limited v. Shyam Madanmohan Ruia and Ors* [(2010) 98 CLA 325] the Division Bench of Bombay High Court overruled its judgement in *Western Maharashtra Development Corporation Ltd* and provided a more liberal interpretation and recognised the rights inter se among shareholders in case of restrictions on transfer of shares.

In Indian context, while the landmark decision of the Supreme Court in *V.B. Rangaraj* case mentioned above is often cited in the context of shareholders' agreements, most other decisions have been rendered by the High Courts in various states especially the Bombay High Court. The decisions on shareholders' agreements are not uniformly inclined in a direction. The High Court decisions are limited in their applicability as they are susceptible to disagreements by other High Courts, thereby conferring limited precedential value. It is difficult to come to clear and crisp answers as to enforceability of shareholders' agreements.

## VETO POWER

### *Meaning of the term – “veto”*

A veto – Latin for "*I forbid*" – is the power to unilaterally stop an official action, especially the enactment of legislation. A veto may give power only to stop changes, thus allowing its holder to protect the status quo.

The Companies Act, 2013 introduced various provisions to essentially bridge the gap towards protection and welfare of the minority shareholders under Companies Act, 1956. As per the Companies Act, 1956, shareholders who hold the majority of shares, rule the company. This majority principle is recognised in a land mark case *Foss vs. Harbottle* (1843). The decision taken by the majority shareholders was binding on the minority. Now this principal has been replaced and minority shareholders have been given greater power under Companies Act, 2013.

### **Veto Power or Rights**

A right is inherent. Shareholders rights refer to rights enshrined in the constitutional document of the company or as provided by the law. A power has its genesis under the provisions of law.

As per the provisions of the Companies Act, 2013 there are some resemblance where the management can take decisions own their own, by virtue of law. However, there are some instances where the consent of the shareholders is mandatory to approve any decision or transaction which is said to be as the veto power or veto right of shareholders of the company.

For instance in case of related-party transactions, promoters, who are majority shareholders, cannot vote in special resolutions in cases of related-party transactions.

As stated under the provisions of Section 188 any related-party transaction that is not done in the ordinary course of business and is not at an arm's length will need approval of minority shareholders by way of a special resolution.

The other instance where the law provides veto power to shareholders is in case of class action suits. Section 245 of Companies Act, 2013 provides for class action to be instituted against the company as well as the auditors of the company.

Under the provisions of sub-section (3) of Section 245, in the case of a company having a share capital, not less than one hundred members of the company or not less than such percentage of the total number of its members as may be prescribed, whichever is less, or any member or members holding not less than such percentage of the issued share capital of the company as may be prescribed, subject to the condition that the applicant or applicants has or have paid all calls and other sums due on his or their shares;

### **Veto Power and Casting Vote**

Veto power is different than casting vote of Chairman. Casting vote is applicable on in case of equality of votes in favour and against. In case of equality the Chairman may give vote either in favour or against the resolution and it can be carried accordingly. Veto power has not been defined in Companies Act. However, dictionary meaning of veto power is: "to refuse to admit or approve; specifically: to refuse assent to (a legislative bill) so as to prevent enactment or cause reconsideration."

Shareholders Agreement and Articles of Association of a company may provide for certain rights to the minority shareholder who has invested funds in the company. Such powers may include power to refuse capital expenditure over certain specified limit. In case the representative of the minority group is not in favour of the capital expenditure proposed by the company, he can exercise his right under the Articles which in common terminology is referred to as "veto powers".

### **Veto Rights and 'Control'**

The introduction of the concept of 'control' in the 2013 Act has implications for investors in Indian companies. Under the 2013 Act, 'control' is understood to include the right to:

- (i) appoint a majority of directors; or
- (ii) control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholding agreements or voting agreements, or in any other manner.

The definition is similar to the definition of 'control' under the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ("Takeover Code").

The definition of 'control' and the jurisprudence surrounding the same under the Takeover Code has been developed with the objective of protecting minority shareholders and providing an exit to them in the event of change in its control.

The definition of 'control' is linked closely with the definition of 'promoter'. The 2013 Act provides that a person having control over the affairs of the company would be regarded as its 'promoter'.

Given the similarity in the definition of 'control' under the Takeover Code and the 2013 Act and its linkage to the definition of 'promoter' it is likely that the jurisprudence of control under the Takeover Code would be applied under the 2013 Act, as well.

But, the scope of the term 'control' under the Takeover Code itself is not clear. The uncertainty around the interpretation of control would impact negotiation of shareholder agreements. Affirmative vote rights in favour of investors under a shareholders agreement are meant to be an effective tool for safeguarding investment or the interest of the investors. These rights are negotiated and decided in the shareholders' agreement, which are subsequently incorporated into the articles of association of a target company.

Accordingly, an investor or shareholder who has secured for itself certain rights which enable a degree of control over 'management or policy decisions', whether by way of board representation or veto rights, may be regarded as having 'control' of the company and therefore be classified as a 'promoter'. Investors would need to carefully consider the obligations and liabilities associated with the position of a promoter under the 2013 Act when negotiating rights and powers in a company under the shareholders agreement.

### **ASSIGNMENT OF SHARES IN A COMPANY**

Section 44 of the Companies Act, 2013 defines the nature of property in the shares of a company. It lays down: "The shares or debentures or other interest of any member in a company shall be movable property, transferable in the manner provided by the articles of the company."

The definition of "goods" in the Sale of Goods Act, 1930, specifically includes stocks and shares. Hence, it is necessary to provide by the articles the manner in which transfer of shares are to be affected.

A "share" in a company is a right to a specified amount of the share capital of the company, carrying with it certain rights and liabilities, while the company is a going concern and in the winding up. It represents the interest of the holder measured for purposes of liability and dividend by a sum of a money.

A company cannot refuse to transfer shares except as provided by its articles\*. It is well settled that unless the articles otherwise provide, a shareholder has a free right to transfer his shares to whom he chooses. It is not necessary to look to the articles for a power to transfer, since that power is given by the Act. It is only necessary to look to the articles of association to ascertain the mode of transfer and the restrictions upon it.

As between buyer (transferee) and seller (transferor) of shares, the buyer is entitled to all dividends declared after the contract of sale, unless otherwise agreed. Whatever may be the agreement, a transfer of shares after declaration of dividend, does not, as against the company, carry the dividend, even though the transfer may be cum-dividend.

### Specimen Shareholders Agreement

THIS AGREEMENT made the \_\_\_ day of \_\_, 2013 BETWEEN MR. A residing at \_\_\_\_\_ (hereinafter referred to as "A") (which expression shall, unless repugnant to the context or meaning hereof, mean and include his heirs, executors, administrators and assigns) of the First Part.

And

MR. B residing at \_\_\_\_\_ (hereinafter referred to as "B") (which expression shall, unless repugnant to the context or meaning hereof, mean and include his heirs executors, administrators and assigns) of the Second Part.

And

\_\_\_\_\_ (P) LTD., a Company incorporated under the Companies Act, 2013 and having its registered office at \_\_\_\_\_ herein represented by its \_\_\_\_\_ (hereinafter referred to as "XYZ") which expression shall, unless repugnant to the context or meaning hereof, include its successors and assigns) of the Third Part;

WHEREAS:

- (A) A and B hereto have agreed to jointly manage a company in India named "XYZ Pvt Ltd.";
- (B) A and B have agreed to become Equity Partners by investing in the shares of the Company subject to the condition that they shall enter into a Shareholders Agreement in terms of these presents;
- (C) The Company "XYZ PVT. LTD. " has been requested to, and has agreed to, join in the execution of these presents and to take this Agreement on record so that it is aware of the rights and obligations of A AND B, the parties hereto and ensure that they comply with the same;
- (D) The parties hereto are desirous of recording the terms and conditions of their Agreement in writing;

NOW IT IS HEREBY AGREED BY AND BETWEEN THE PARTIES HERETO AS FOLLOWS:-

1. (a) A and B shall jointly invest in the Company which is an existing company limited by shares under the Companies Act, 2013 and known as "XYZ PVT LTD".

(b) The registered office of the Company shall be situate at, or at such other places as may be mutually agreed upon between the parties in writing.

(c) The Company shall carry on the business of running and managing restaurants and (Description of the business and complete address), either by itself or through other agencies or company industries and may carry on any other business as may be decided by B hereto and shall ensure that no other business activity is undertaken by the Company at any time without the consent of A hereto.

2. The authorised share capital of the Company is Rs. \_\_\_\_\_ /- (Rupees \_\_\_\_\_ only) consisting of ( ) equity shares of Rs.10/- (Rupees ten) each.

3. The subscription by A hereto to the aforesaid authorised share capital of the Company shall be 1,00,000 (One lakh) equity shares of Rs.10/- (Rupees ten only) and the subscription by B to the aforesaid authorised share capital of the Company shall be 1,00,000 (One lakh) equity shares of Rs.10/- (Rupees ten only).

4. There shall be no further issue of capital without the consent of both the parties hereto, and unless otherwise agreed upon in writing further investment shall be as mutually decided by both parties.

5 (a) The Board of Directors of the Company shall consist of A and B

(b) A shall have the right to nominate two (2) Additional Directors onto the Board and B shall have the right to nominate three or more Additional Directors on the Board. Both parties shall be entitled at any time to remove any of the representatives on the Board by written notice to the other party and to appoint another or other/s in their place.

(c) The day to day management of the Company shall be looked after by a Managing Director to be appointed with the consent of B hereto. Any major acquisition of property, substantial expansion of business activities or diversification or matters of policy shall be with the prior consent of B.

(d) It is agreed as between the parties hereto that the position of Chairperson of the Company shall be held by B or a nominee of B. The Chairman of the Board shall also be the Chairman of all general meetings of the Company.

6. A and B hereto jointly and severally shall vote and act as members of the Company and with respect to the shares of the Company held by them, so as to ensure that Directors of the Company are at all times appointed and maintained in office in conformity with the provisions of this Agreement. If at any time the provisions of this Agreement are not fully complied with, A and B jointly and severally agree to promptly take all necessary steps to ensure that the provisions of this Agreement hereof are fully implemented in letter and spirit.

7 (a) The Auditors of the Company shall be M/s. .

(b) The Auditors of the Company shall not be changed without the prior written consent of both A and B.

8. Any sale or transfer of shares in the Company by either party shall be as provided in Clause

9. If at any time during the continuance of this Agreement either A or B, desire to sell or transfer all or any of their respective shares held by them in the Company, they shall do so strictly in accordance with the provisions hereinafter written.

10. If either A or B desires at any time to sell the whole or part of their shares in the Company, he shall first offer such shares in writing to the other. If the other does not accept in writing the offer within 15 days of receipt of the offer, the first party shall then be at liberty within 30 days thereafter to sell the shares so offered to any other persons of its choice at the same price and on the same terms and conditions as contained in its written offer to the other party hereto in the first instance, failing which the procedure contained in this sub-clause will have to be repeated by a party desiring to sell his shares.

11. B will bring in further working capital to run an F & B Unit(s) at (Address of registered office). Bank had advanced loans of about Rs. 1,10,00,000/- (Rupees One Crore Ten Lakhs Only) to XYZ which loans have to be repaid by them. B will be bringing further moneys upto Rs. (Rupees Only) to repay the loan. The Balance Rs. /- has been secured with the collateral security provided B. XYZ have entered into a Management and Royalty Agreement with \_\_\_\_\_ (P) Ltd., for the operation and management of the F & B unit(s) of XYZ and are entitled to receive their share of profit. A and B are equally entitled to this share of profit being equal shareholders of XYZ. It is hereby agreed that A shall not be entitled to a percentage of the profit which shall not exceed Rs. \_\_\_\_\_/-(Rupees Only) per month from XYZ out of his share of profit subject to the terms contained herein and/or in any other document executed by him on behalf of XYZ. The balance money attributable to A shall be utilized to repay the loans and interest outstanding to \_\_\_\_\_ Bank, and the amount of Rs. /- brought in by B and interest thereon, and towards the working capital brought in by B and interest thereon and any other loans of the XYZ. This arrangement will continue till the entire sums (liabilities) together with the interest thereon have been repaid. However B will be entitled to withdraw the profit attributable to his share.

12. B will be entitled to interest at the rate of 12% per annum on the sums brought in by him or his

Associates / concerns / businesses.

13. A and B agree and undertake not to disclose or divulge directly or indirectly to any third party any trade or business secret or other secret or confidential information pertaining to the business, affairs or transactions of each other or of the Company or of their clients or customers, that may have been disclosed, imparted to or acquired by either of them from the other or from the Company.

14. A and B jointly and severally undertake:-

- (a) that they shall ensure that they, their representatives, proxies and agents representing them at general meetings of the shareholders of the Company shall at all times exercise their votes in such manner so as to comply with, and to fully and effectually implement, the provisions of this Agreement.
- (b) that if any resolution is proposed contrary to the terms of this Agreement, the parties, their representatives, proxies and agents representing them shall vote against it. If for any reason such a resolution is passed, the parties will, if necessary, join together and convene an extraordinary, general meeting of the Company in pursuance of section 100 of the Companies Act, 2013 for implementing the terms of this Agreement.

15. A and B shall jointly and severally procure and/or ensure that the Director or Directors of its choice on the board of the Company shall at all times fully and effectually implement and comply with (including by exercise of voting rights at meetings of the Board or resolutions by circulation and on resolutions passed at a meeting of any Committee of the Directors) the provisions of this Agreement.

16. If either A or B shall commit a breach of any of the terms or provisions of this Agreement and shall fail to rectify such breach within Sixty (60) days from the receipt of written notice from the party complaining of the breach, then the latter shall be entitled, without prejudice to its other rights and remedies under this Agreement or at law, to terminate the Agreement recorded herein by written notice.

17. No modification or alteration of this Agreement or any of its terms or provisions shall be valid or binding on A and/or B unless made in writing duly signed by both.

18. This Agreement is personal to A and B and shall not be transferred or assigned in whole or in part by either party without the prior written consent of the other.

19. If any dispute or difference shall at any time arise between A and B as to any terms, provisions or matters contained herein on as to their respective rights, claims, duties or liabilities hereunder or otherwise, howsoever in relation to or arising out of or concerning this Agreement, such dispute or difference shall be referred to the arbitration. The venue of such arbitration shall be in Bangalore unless otherwise agreed in writing. Such arbitration shall be held under and in accordance with the provisions of the Arbitration and Conciliation Act, 1996.

20. This Agreement represents the entire agreement between the parties hereto on the subject matter hereof and cancels and supersedes all prior agreements, arrangements or understandings, if any, whether oral or in writing, between the parties hereto on the subject matter hereof.

IN WITNESS WHEREOF the parties hereto have executed these presents the day and year first hereinabove written.

SIGNED AND DELIVERD

for and on behalf of XYZ

SIGNED AND DELIVERD

in the presence of

By its SHAREHOLDERS AND AUTHORISED DIRECTORS

Mr. A

Mr. B

In presence of .....

..... Signed and delivered by Mr B

In presence of .....

**ANNEXURE II**

**A Specimen of Deed of Assignment of Shares in a Company**

THIS ASSIGNMENT is made this ..... day of ..... between AB, son of ..... resident of..... (hereinafter called "the Assignor") of the one part, and CD, son of..... resident of ..... (hereinafter called "the Assignee") of the other part.

THE DEED WITNESSES:

That in consideration of the sum of Rs..... (Rupees.....) paid by the assignee to the assignor, the receipt whereof the assignor hereby acknowledges, the said AB hereby assigns, sells and transfers to the said CD..... Equity Shares of Rs..... each, fully paid up, bearing consecutive Nos..... to..... (inclusive), which stand in the name of the assignor in the Register of Members of..... Co. Ltd. TO HOLD the same to the assignee absolutely, subject nevertheless to the conditions on which the assignor held the same up to date.

AND the assignee hereby agrees to take the said Equity Shares subject to such conditions.

IN WITNESS WHEREOF the assignor and the assignee do hereto affix their respective signatures on the day, month and the year stated above.

Witness:

Assignor

Witness:

Assignee

## LESSON ROUND-UP

- A Company is composed of members, though it has its own entity distinct from members.
- Every shareholder is a member and every member is a shareholder, however, there may be exceptions to this statement.
- Section 2(55) of the Companies Act, 2013 provides the modes by which a person may acquire membership of a Company.
  - by subscribing to the Memorandum,
  - by agreeing in writing to become a member,
  - by holding equity share capital of a Company as beneficial owner in the records of a depository.
- A non-profit making Company licensed under Section 8 of the Companies Act can become member of any other company.
- Foreigners, trade unions can hold shares in a company, and consequently become its members.
- Person ceases to be a member when his name is removed from register of members of a company.
- In accordance with Section 88, every Company shall keep register of its members. This register shall be kept at the registered office of the Company subject to the provisions of Section 94 of the Companies Act, 2013.
- Every member of a public company limited by shares, holding equity shares, shall have votes in proportion to his share of the paid-up equity share capital of the company. On the other hand, preference shareholders ordinarily vote only on matters directly relating to rights attached to preference share capital and on any resolution for winding up of the company or for the repayment or reduction of the equity or preference share capital.

## GLOSSARY

<b><i>Ipsa facto</i></b>	By that very fact or act.
<b>Minor</b>	Person below the age of majority.
<b>Estoppel</b>	The principle that precludes a person from asserting something contrary to what is implied by a previous action or statement of that.
<b>Cessation of membership</b>	A person ceases to be a member of a company when his name is removed from its register of members.
<b>Joint Members</b>	If more than one person apply for shares in a company and shares are allotted to them, each one of such applicant becomes a member.
<b>Insolvent</b>	Insolvency is the inability of a debtor to pay their debt. If a person is unable to pay his debt, he is said to be insolvent.

## SELF-TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.)*

1. Every shareholder of a company is known as a member while every member may not be known as a shareholder. Comment.
2. Who can become a member of the company? Can the following persons or institutions become member of a company:  
(a) Minor; (b) Company; (c) Partnership firm; (d) Foreigner; (e) Insolvent.





# Lesson 4

## Debt Capital

### LESSON OUTLINE

- Borrowing Powers of company
- Debentures
- Debenture Redemption Reserve Account
- Overview of Company Deposits
- Lesson Round Up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

The provisions to issue debentures are covered under Section 71 of the Companies Act, 2013 and Rule 18 of Companies (Share Capital and Debentures) Rules, 2014. The listed companies are additionally governed by Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 and SEBI (Issue and Listing of Debt Securities) Regulations, 2008. Further, the borrowing powers of the board are regulated by Section 179 which mandates that power to borrow has to be through properly convened board meeting. Deposits are also one of the sources available to a company to raise funds to meet the short term or long term requirements of the company. In order to protect the interest of the depositors and to stop them all practices adopted by companies accepting deposits, the Companies Act, 2013 read with rules made under Chapter V has introduced various conditions for acceptance of deposits by companies.

Debt capital is an important source of funding for the corporates. As a prospecting company this chapter will give you the overview of legal and technical issues involved in securing debt capital. As a guide to Board, a company secretary is expected to be in know of the subject.

## PART A

### DEBENTURES

#### BORROWING

In order to run a business effectively/successfully, adequate amount of capital is necessary. In some cases capital arranged through internal resources i.e. by way of issuing equity share capital or using accumulated profit is not adequate and the organisation is resorted to external resources of arranging capital i.e. External Commercial borrowing (ECB), Debentures, Bank Loan, Public Fixed Deposits etc. Thus, borrowing is a mechanism used whereby the money is arranged through external resources with an implied or expressed intention of returning money.

#### Power of Company to Borrow

The power of the company to borrow is exercised by its directors, who cannot borrow more than the sum authorized. The powers to borrow money and to issue debentures whether in or outside India can only be exercised by the Directors at a duly convened meeting. Pursuant to Section 179(3) (c) & (d) directors have to pass resolution at a duly convened Board Meeting to borrow money. The power to issue debentures cannot be delegated by the Board of directors. However, the power to borrow monies can, be delegated by a resolution passed at a duly convened meeting of the directors to a committee of directors, managing director, manager or any other principal officer of the company. The resolution must specify the total amount up to which the moneys may be borrowed by the delegates. Often the power of the company to borrow is unrestricted, but the authority of the directors acting as its agents is limited to a certain extent. For example, Section 180(1)(c) of the Act prohibits the Board of directors of a company from borrowing a sum which together with the monies already borrowed exceeds the aggregate of the paid-up share capital of the company and its free reserves apart from temporary loans obtained from the company's bankers in the ordinary course of business unless they have received the prior sanction of the company by a special resolution in general meeting.

Explanation to section 180(1)(c) provides that the expression "temporary loans" means loans repayable on demand or within six months from the date of the loan such as short-term, cash credit arrangements, the discounting of bills and the issue of other short-term loans of a seasonal character, but does not include loans raised for the purpose of financial expenditure of a capital nature.

It is further provided in proviso to Section 180(1)(c) that the acceptance by a banking company, in the ordinary course of its business, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise, shall not be deemed to be borrowing of monies by the banking company within the meaning of clause (c) of Sub-section (1) of Section 180. It is important at this stage to distinguish between, borrowing which is *ultra vires* the company and borrowing which is *intra vires* the company but outside the scope of the director's authority.

The provisions of Sub-section (5) of Section 180 clearly lay down that debts incurred in excess of the limit fixed by clause (c) of Sub-section (1) shall not be valid unless the lender proves that he lent his money in good faith and without knowledge of the limit imposed by Sub-section (1) being exceeded.

With recent exemption notification no 464(E) private companies have been exempted to comply the entire provisions of Section 180 of the Companies Act 2013, resultantly special resolution is not required to exercise powers under section 180 for private companies.

### Unauthorized or *Ultra Vires* Borrowing

Where a company borrows without the authority conferred on it by the articles or beyond the amount set out in the Articles, it is an *ultra vires* borrowing. Any act which is *ultra vires* the company is void. In such a case the contract is void and the lender cannot sue the company for the return of the loan. The securities given for such *ultra-vires* borrowing are also void and inoperative. *Ultra vires* borrowings cannot even be ratified by a resolution passed by the company in general meeting. However, equity assists the lender where the common law fails to do so. If the lender has parted with his money to the company under an *ultra vires* borrowing, and is, therefore, unable to sue for its return, or enforce any security granted to him, he nevertheless has, in equity, the following remedies:

- (A) **Injunction and Recovery:** Under the equitable doctrine of restitution he can obtain an injunction provided he can trace and identify the money lent, and any property which the company has bought with it. Even if the monies advanced by the lender cannot be traced, the lender can claim repayment if it can be proved that the company has been benefited thereby.
- (B) **Subrogation:** Where the money of an *ultra vires* borrowing has been used to pay off lawful debts of the company, he would be subrogated to the position of the creditor paid off and to that extent would have the right to recover his loan from the company. Subrogation is allowed for the simple reason that when a lawful debt has been paid off with an *ultra vires* loan, the total indebtedness of the company remains the same. By subrogating the *ultra vires* lender, the Court is able to protect him from loss, while debt burden of the company is in no way increased.
- (C) **Suit against Directors:** In case of *ultra vires* borrowing, the lender may be able to sue the directors for breach of warranty of authority, especially if the directors deliberately misrepresented their authority.

### *Intra vires* Borrowing but outside the Scope of Agents' Authority

A distinction should always be made between a company's borrowing powers and the authority of the directors to borrow. Where the directors borrowed money beyond their authority and the borrowing is not *ultra vires* the company, such borrowing is called *Intra vires* borrowing but outside the Scope of Agents' Authority. The company will be liable to such borrowing if the borrowing is within the directors' ostensible authority and the lender acted in good faith or if the transaction was ratified by the company.

Where the borrowing is *intra vires* the company but outside the authority of the directors e.g. where the articles provide that the directors shall have the power only up to Rs. 100 lacs and prior approval of the shareholders would be required to borrow beyond Rs. 100 lacs; any borrowing beyond Rs.100 lacs without shareholders approval i.e. *intra vires* borrowing by the company but outside the authority of directors can be ratified by the company and become binding on the company. The company would be liable, particularly if the money has been used for the benefit of the company. Here the legal position is quite clear. The company has power or capacity to borrow, but the authority of the directors is restricted either by the articles of the company or by the statute, and they have exceeded it. The company may, if it wishes, ratify the agent's act in which case the loan binds the company and the lender as if it had been made with company's authority in the first place.

On the other hand, the company may refuse to ratify the agent's act. Here the normal principles of agency apply. The doctrine of *Indoor Management* (also known as rule in *Royal British Bank v. Turquand* (1856) 11 Q.B. 327) shall protect the lender, provided he can establish that he advanced the money in good faith. A

third-party who deals with an agent knowing that the agent is exceeding his authority has no right of action against the principal. Bearing in mind that the memorandum and articles are public documents, the contents of which the third-party is deemed to know, he will obviously have no right of action against the company if the agent's lack of authority is obvious from reading them. But a third-party is not effected by secret restrictions on the agent's authority, as the lack of authority is not clear from the public documents and the lender can not be aware of it from some other source. Therefore, the company will be liable.

## CASE LAWS

Judicial Pronouncement relating to borrowing power of a company

- (A) The behaviour of the directors, as the company's agents, can have no effect whatsoever on the validity of the loan for no agent can have more capacity than his principal. No agent can have a power which is not with the principal. If, therefore, the borrowing is *ultra vires* the company so that the company has no capacity to undertake it, the lender can have no rights at common law. No debt is created and any security which may have been created in respect of the borrowing is also void. The lender cannot sue the company for the repayment of the loan. [*Sinclair v. Brougham*(1914) 88 LJ Ch 465].
- (D) If the borrowing by the directors is *ultra vires* their powers, the directors may, in certain circumstances, be personally liable for damages to the lender, on the ground of the implied warranty given by them, that they had power to borrow [*Firbank's Executors v. Humphreys*, (1886) 18 QBD 54; *Garrard v. James*, 1925 Ch. 616].
- (G) Sometimes it happens that a power to borrow exists but is restricted to a stated amount, in such a case if by a single transaction an amount in excess is borrowed, only the excess would be *ultra vires* and not the whole transaction [*Deonarayan Prasad Bhadani v. Bank of Baroda*, (1957) 27 Com Cases 223 (Bom)].
- (H) The acquiescence of all shareholders in excess loans contracted by directors beyond their powers but not *ultra vires* the powers of the company would be sufficient to validate such excess debts. [*Sri Balasar aswathi Ltd. v. Parameswara Aiyar*, (1956) 26 Com Cases 298, 308: AIR 1957 Mad 122].
- (I) If the borrowing is unauthorized, the company will be liable to repay, if it is shown that the money had gone into the company's coffers [*Lakshmi Ratan Cotton Mills Co. Ltd. v. J.K. Jute Mills Co. Ltd.*, (1957) 27 Com Cases 660: AIR 1957 All 311].
- (J) In *V.K.R.S.T Firm v. Oriental Investment Trust Ltd.*, AIR 1944 Mad 532 under the authority of the company, its managing director borrowed large sums of money and misappropriated it. The company was held liable stating that where the borrowing is within the powers of the company, the lender will not be prejudiced simply because its officer have applied the loan to unauthorised activities provided the lender had no knowledge of the intended misuse.
- (K) In *T.R. Pratt. (Bom) Ltd. v. E.D. Sassoon and Co. Ltd.*, (1936) 6 Com Cases 90, there was no limit on the borrowing for business in the memorandum of the company. But the directors could not borrow beyond the limit of the issued share capital of the company without the sanction of the general meeting. The directors borrowed money from the plaintiff beyond their powers. It was held that the money having been borrowed and used for the benefit of the principal either in paying its debts, or for its debts, or for its legitimate business, the company cannot repudiate its liability on the ground that the agent had no authority from the company to borrow. When these facts are established a claim on the footing of money had been received would be maintainable. It was also held that under the general principle of law when an agent borrows money for a principal without the

authority of the principal, but if the principal takes benefit of the money so borrowed or when the money so borrowed have gone into the coffers of the principal, the law implies a promise to repay. In that connection it was observed that there appears to be nothing in law which makes this principle inapplicable to the case of a joint stock company and even in cases where the directors or the managing agent had borrowed money without there being authorization for the company, if it has been used for the benefit of the company, the company cannot repudiate its liability to pay.

- (L) In *Equity Insurance Co. Ltd. v. Dinshaw & Co.*, AIR 1940 Oudh 202, it was held that “where the managing agent of a company who is not authorised to borrow, has borrowed money which is not necessary, neither bona fide, nor for the benefit of the company, the company is not liable for the amount borrowed”.
- (M) In *SurajBabu v. Jaitly & Co.* AIR 1946 All 372, P & Co., were the managing agents of L & Co., which was in liquidation. P the manager borrowed a sum of money from J in his own name. In one letter to J he indicated that the loan was for a requirement of L & Co. and that company had actually benefited. It was held that there was no intention to bind the company. “The mere fact that the company had benefited was not in itself sufficient to bind the company”.
- (N) In *Krishnan Kumar Rohatgi and Others v. State Bank of India and Others*, (1980) 50 Com Cases 722, the company borrowed an amount of Rs. 5 lakhs from the Bank under a Promissory Note. The repayment was guaranteed by a person by executing a guarantee in favour of the company. The company used to make payments towards loan and the promissory note used to be renewed from time to time. In the suit for recovery, the company contended that the pro-note was executed by the Chairman without there being a resolution of the Board of directors authorizing the Chairman to execute the pro-note as required under Section 292(1)(c) of the Act, 1956 [Corresponds to section 179(1)(d) of the Companies Act, 2013]. Rejecting these contentions the Patna High Court held that in cases where the directors borrow funds without their having authorization from the company and if the money has been used for the benefit of the company, the company cannot repudiate its liability to repay. Under the general principles of law, when an agent borrows money for a principal without the authority of the principal but the principal takes the benefit of the money so borrowed or when the money so borrowed has gone into the coffers of the principal, the law implies a promise to be paid by the principal.

*Ultra vires* borrowings cannot even be ratified by a resolution passed by the company in a general meeting.

## TYPES OF BORROWINGS

A company uses various kinds of borrowing to finance its operations. The various types of borrowings can generally be categorized into: 1) Long term/short term borrowing, 2) Secured/unsecured borrowing, 3) Syndicated/ Bilateral borrowing, 4) Private/Public borrowing.

- 1A. **Long Terms Borrowings** - Funds borrowed for a period ranging for five years or more are termed as long-term borrowings. A long term borrowing is made for getting a new project financed or for making big capital investment etc. Generally Long term borrowing is made against charge on fixed Assets of the company.
- 1B. **Short Term Borrowings** - Funds needed to be borrowed for a short period say for a period up to one year or so are termed as short term borrowings. This is made to meet the working capital need of the company. Short term borrowing is generally made on hypothecation of stock and debtors.
- 1C. **Medium Term Borrowings** - Where the funds to be borrowed are for a period ranging from two to five years, such borrowings are termed as medium term borrowings. The commercial banks

normally finance purchase of land, machinery, vehicles etc.

- 2A **Secured/unsecured borrowing** – A debt obligation is considered secured, if creditors have recourse to the assets of the company on a proprietary basis or otherwise ahead of general claims against the company.
- 2B **Unsecured debts** comprise financial obligations, where creditors do not have recourse to the assets of the company to satisfy their claims.
- 3A **Syndicated borrowing** – if a borrower requires a large or sophisticated borrowing facility this is commonly provided by a group of lenders known as a syndicate under a syndicated loan agreement. The borrower uses one agreement covering the whole group of banks and different types of facility rather than entering into a series of separate loans, each with different terms and conditions.
- 3B **Bilateral borrowing** refers to a borrowing made by a company from a particular bank/financial institution. In this type of borrowing, there is a single contract between the company and the borrower.
- 4A **Private borrowing** comprises bank-loan type obligations whereby the company takes loan from a bank/financial Institution.
- 4B **Public borrowing** is a general definition covering all financial instruments that are freely tradable on a public exchange or over the counter, with few if any restrictions i.e. Debentures, Bonds etc.

## Debentures

According to Section 2(30) of Companies Act, 2013, “debenture” includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not.

Further it is provided that—

- (a) the instruments referred to in Chapter III-D of the Reserve Bank of India Act, 1934; and
- (b) such other instrument, as may be prescribed by the Central Government in consultation with the Reserve Bank of India, issued by a company,

shall not be treated as debenture.

## Kinds of Debentures

**Convertibility of  
Instrument**

**Security of  
Instrument**

**Redemption  
ability**

**Registration of  
Instrument**

Debentures are generally classified into different categories on the basis of:

***On the basis of Convertibility of Instrument***

- (A) **Non Convertible Debentures (NCD):** These instruments retain the debt character and cannot be converted into equity shares.
- (B) **Partly Convertible Debentures (PCD):** A part of these instruments are converted into Equity shares in the future at notice of the issuer. The issuer decides the ratio for conversion. This is normally decided at the time of subscription.
- (C) **Fully convertible Debentures (FCD):** These are fully convertible into Equity shares at the issuer's notice. The ratio of conversion is decided by the issuer. Upon conversion the investors enjoy the same status as ordinary shareholders of the company.
- (D) **Optionally Convertible Debentures (OCD):** The investor has the option to either convert these debentures into shares at price decided by the issuer/agreed upon at the time of issue.

***On the basis of Security of Instrument***

- (A) **Secured Debentures:** These instruments are secured by a charge on the fixed assets of the issuer company. So if the issuer fails on payment of the principal or interest amount, his assets can be sold to repay the liability to the investors. Section 71(3) of the Companies Act, 2013 provides that secured debentures may be issued by a company subject to such terms and conditions as may be prescribed by the Central Government through rules.
- (B) **Unsecured Debentures:** These instrument are unsecured in the sense that if the issuer defaults on payment of the interest or principal amount, the investor has to be along with other unsecured creditors of the company, they are also said to be naked debentures.

***On the basis of Redemption ability***

- (A) **Redeemable Debentures:** It refers to the debentures which are issued with a condition that the debentures will be redeemed at a fixed date or upon demand, or after notice, or under a system of periodical drawings. Debentures are generally redeemable and on redemption these can be reissued or cancelled. The person who has been re-issued the debentures shall have the same rights and priorities as if the debentures had never been redeemed.
- (B) **Perpetual or Irredeemable Debentures:** A Debenture, in which no time is fixed for the company to pay back the money, is an irredeemable debenture. The debenture holder cannot demand payment as long as the company is a going concern and does not make default in making payment of the interest. But all debentures, whether redeemable or irredeemable become payable on the company going into liquidation. However, after the commencement of the Companies Act, 2013, now a company cannot issue perpetual or irredeemable debentures.

***On the basis of Registration of Instrument***

- (A) **Registered Debentures:** Registered debentures are made out in the name of a particular person, whose name appears on the debenture certificate and who is registered by the company as holder on the Register of debenture holders. Such debentures are transferable in the same manner as shares by means of a proper instrument of transfer duly stamped and executed and satisfying the

other requirements specified in Section 56 of the Companies Act, 2013.

- (B) Bearer debentures:** Bearer debentures on the other hand, are made out to bearer, and are negotiable instruments, and so transferable by mere delivery like share warrants. The person to whom a bearer debenture is transferred become a “holder in due course” and unless contrary is shown, is entitled to receive and recover the principal and the interest accrued thereon. [*Calcutta Safe Deposit Co. Ltd. v. Ranjit Mathuradas Sampat* (1971) 41 Com Cases 1063].

### **Nature of Debentures and transferability**

As per Section 44 of the Act, the debentures of the Company are movable property which will be transferable as per the provisions given in the Articles of Association of the company.’

As per the provisions Section 56, securities will be transferable vide Form SH-4. Transferability is governed by the provisions of the Articles of Association.

### **Pari Passu Clause in case of Debentures**

Debentures are usually issued in a series with a *pari passu* clause and it follows that they would be on an equal footing as to security and should the security be enforced, the amount realised shall be divided pro-rata, i.e., they are to be discharged rateably. In the event of deficiency of assets, they will abate proportionately. The expression '*pari passu*' implies with equal step, equally treated, at the same rate, or at par with. When it is said that existing debentures shall be issued *pari passu* clause, it implies that no difference will be made between the old and new debentures.

If the words *pari passu* are not used, the debentures will be payable according to the date of issue, and if they are all issued on the same day, they will be payable accordingly to their numerical order. However, a company cannot issue a new series of debentures so as to rank *pari passu* with prior series, unless the power to do so is expressly reserved and contained in the debentures of the previous series.

### **Debenture Stock**

A company, instead of issuing debentures, each in respect of separate and distinct debt, may raise one aggregate loan fund or composite stock known as 'debenture stock'. Accordingly, a debenture stock is a borrowed capital consolidated into one mass for the sake of convenience. Instead of each lender having a separate bond or mortgage, he has a certificate entitling him to a certain sum being a portion of one large loan. It is generally secured by a trust deed. As in the case of shares, a person may subscribe for, or transfer any amount even a fraction amount. Debenture stock is the indebtedness itself, and the debenture stock certificate furnishes evidence of the title or interest of the holder in the indebtedness. Debenture is the document which furnishes evidence of the debt. Debenture stock must be fully paid, while debenture may or may not be fully paid.

### **Difference between Debenture and Debenture Stock**

Debenture is the description of an instrument, while 'debenture stock' is the description of a debt or sum secured by an instrument. In the words of Lord Lindley, it is “borrowed capital consolidated into one mass for the sake of convenience”.

### **Distinction between Debenture and Loan**

A debenture means a document which creates or acknowledges a debt. A loan creates a right in the creditor to demand repayment, and the substance of a debt is a liability upon the debtor to repay the money [Ram Ratan Karmarkar v. Amulya Charan Karmarkar, 56 CWN 728 at p. 729].

**Distinction between Debenture and Shares**

S. No.	Debentures	Shares
1	Debentures constitute a loan.	Shares are part of the capital of a company.
2	Debenture holders are creditors.	Shareholders are members/owners of the company.
3	Debenture holder gets fixed interest which carries a priority over dividend.	Shareholder gets dividends with a varying rate.
4	Debentures generally have a charge on the assets of the company.	Shares do not carry any such charge.
5	Debentures can be issued at a discount without restrictions.	Shares cannot be issued at a discount.
6	The rate of interest is fixed in the case of debentures.	Whereas on equity shares the dividend varies from year to year depending upon the profit of the company and the Board of directors decides to declare dividends or not.
7	Debenture holders do not have any voting rights.	Shareholders enjoy voting rights.
8	Interest on debenture is payable even if there are no profits i.e. even out of capital.	Dividend can be paid to shareholders only out of the profits of the company and not otherwise.
9	Interest paid on debenture is a business expenditure and allowable deduction from profits.	Dividend is not allowable deduction as business expenditure.

**BROAD REGULATORY FRAMEWORK FOR DEBT SECURITIES**

**SEBI (Issue of Capital and Disclosure Requirement) Regulations, 2009**

**SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015**

**SEBI (Issue and Listing of Debt Securities) Regulations, 2008**

**SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008**

**The Companies Act, 2013**

**Companies (Share Capital and Debentures) Rules, 2014**

- Issue of debt securities that are convertible, either partially or fully or optionally into listed or unlisted

equity shall be guided by the disclosure norms applicable to equity or other instruments offered on conversion in terms of **SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009**.

- **SEBI issued (Issue and Listing of Debt Securities) Regulations, 2008** pertaining to issue and listing of debt securities which are not convertible, either in whole or part into equity instruments. They provide for a rationalized disclosure requirements and a reduction of certain onerous obligations attached to an issue of debt securities.
  - These Regulations are applicable to –
  - public issue of debt securities and
  - listing of debt securities issued through public issue or on private placement basis on a recognized stock exchange.
- Securitised debt instruments are regulated by the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008 for listing on stock exchanges and the Securitization Companies and Reconstruction Companies (Reserve Bank) Guidelines and Directions, 2003.
- The Provisions of Chapter V of **SEBI (LODR) Regulations, 2015** shall apply only to a listed entity which has listed its 'Non-Convertible Debt Securities' and/or 'Non-Convertible Redeemable Preference Shares' on a recognised stock exchange in accordance with SEBI (Issue and Listing of Debt Securities) Regulations, 2008 or SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013 respectively. The provisions of this chapter shall also be applicable to "perpetual debt instrument" and "perpetual non-cumulative preference share" listed by banks.

### **CREATION OF SECURITY – Role of Debenture Trustee**

Creation of security means mortgaging the property in favour of Debenture Trustee for the benefit of debenture holders. This is an incidence of ownership of property and creation of security has to be done by the owner of the property. However, the debenture holders are beneficiaries and they have no access to mortgaged property. The Debenture Trustee holds the secured property on behalf of issuer of security and for benefit of debenture holders. In the event of default by the issuer of security, the Debenture Trustee will have the power and authority to bring the secured property to sale following the procedure in the Transfer of Property Act and the proceeds of sale will have to be applied to redeem the debentures

### **Provisions of Companies Act, 2013 – Issue of Debentures**

Section 71(1) states that a company may issue debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption. The issue of debentures with an option to convert such debentures into shares, wholly or partly, shall be approved by a special resolution passed at a general meeting.

Section 71(2) states that no company shall issue any debentures carrying any voting rights.

Section 71(3) read with Rule 18(1) of Companies (Share Capital and Debentures) Rules, 2014 provides that the secured debentures may be issued only when the following conditions are complied with: -

- (A) An issue of secured debentures may be made, provided the date of its redemption shall not exceed ten years from the date of issue. A company engaged in the setting up of infrastructure projects may issue secured debentures for a period exceeding ten years but not exceeding thirty years;

Provided that the following classes of companies may issue secured debentures for a period

exceeding ten years but not exceeding thirty years,

- (i) Companies engaged in setting up of infrastructure projects;
  - (ii) 'Infrastructure Finance Companies' as defined in clause (viiia) of sub direction(1) of direction 2 of Non-Banking Financial (Non-deposit accepting or holding) Companies Prudential Norms (ReserveBank) Directions,2007;
  - (iii) Infrastructure Debt Fund Non-Banking Financial Companies' as defined in clause (b) of direction 3 of Infrastructure Debt Fund Non-Banking Financial Companies (Reserve Bank) Directions, 2011;
  - (iv) Companies permitted by a Ministry or Department of the Central Government or by Reserve Bank of India or by the National Housing Bank or by any other statutory authority to issue debentures for a period exceeding ten years.
- (B) Such an issue of debentures shall be secured by the creation of a charge on the properties or assets of the company or its subsidiaries or its holding company or its associates companies, having a value which is sufficient for the due repayment of the amount of debentures and interest thereon.
- (C) the company shall appoint a debenture trustee before the issue of prospectus or letter of offer for subscription of its debentures and not later than sixty days after the allotment of the debentures, execute a debenture trust deed to protect the interest of the debenture holders; and
- (D) the security for the debentures by way of a charge or mortgage shall be treated in favour of the debenture trustee on —
- (i) any specific movable property of the company (not being in the nature of pledge); or
  - (ii) any specific immovable property wherever situate, or any interest therein.

In case of a non-banking financial company, the charge or mortgage may be created on any movable property.

Further in case of any issue of debentures by a Government company which is fully secured by the guarantee given by the Central Government or one or more State Government or by both, there is no requirement for creation of charge under this sub-rule.

In case of any loan taken by a subsidiary company from any bank or financial institution the charge or mortgage may also be created on the properties or assets of the holding company.

#### **Let us remember!**

The date of Redemption of debenture shall not exceed 10 years from the date of issue. A company engaged in the setting up of infrastructure projects may issue secured debentures upto redemption period of thirty years.

#### **Creation of debenture redemption reserve account**

Section 71(4) read Rule 18(7) of aforesaid rules provides that when debentures are issued by a company, the company shall create a debenture redemption reserve account(DRR) out of the profits of the company available for payment of dividend. The amount credited to such account shall not be utilised by the company except for the redemption of debentures.

### Quantum of Debenture Redemption Reserve

DRR is not required to be created for the convertible part of partly convertible debentures. The provisions for creation of DRR for various classes of companies are as follows:

S.no.	Class of Company	Condition
1	All India Financial Institutions (AIFIs) regulated by Reserve Bank of India and Banking Companies	No DRR for debentures issued by for both public as well as privately placed debentures
2	Financial Institutions (FIs) within the meaning of clause (72) of section 2 of the Companies Act, 2013	As applicable to NBFCs registered with RBI.
3	For NBFCs registered with the RBI under Section 45-IA of the RBI (Amendment) Act, 1997	25% of the value of outstanding debentures issued through public issue as per present SEBI (Issue and Listing of Debt Securities) Regulations, 2008,  No DRR is required in the case of privately placed debentures.
4	Housing finance companies registered with the National Housing Bank	25% of the value of outstanding debentures issued through public issue as per present SEBI (Issue and Listing of Debt Securities) Regulations, 2008  No DRR is required in the case of privately placed debentures.
5	For other companies including manufacturing and infrastructure companies	25% of the value of outstanding debentures issued through public issue as per present SEBI (Issue and Listing of Debt Securities) Regulations, 2008
6	Listed Companies	25% DRR is required in the case of privately placed debentures
7	Unlisted companies	25% of the value of outstanding debentures for issue of debentures on private placement basis

### Investment in DRR

For Every company required to create DRR is required to invest or deposit at least 15 % of the debentures maturing during the current financial year ending 31st March of next year. The company may choose any of the below given methods:

- (i) in deposits with any scheduled bank, free from any charge or lien;
- (ii) in unencumbered securities of the Central Government or of any State Government;
- (iii) in unencumbered securities mentioned in sub-clauses (a) to (d) and (ee) of section 20 of the Indian Trusts Act, 1882;
- (iv) in unencumbered bonds issued by any other company which is notified under sub-clause (f) of section 20 of the Indian Trusts Act, 1882;
- (v) the amount invested or deposited as above shall not be used for any purpose other than for redemption of debentures maturing during the year referred above: The amount remaining invested or deposited, as the case may be, shall not at any time fall below fifteen percent of the amount of the debentures maturing during the year ending on the 31st day of March of that year;

In case of partly convertible debentures, Debenture Redemption Reserve shall be created in respect of non-convertible portion of debenture issue in accordance with this sub-rule.

### **Appointment of Debenture Trustees**

Section 71(5) read with Rule 18(2) of aforesaid rules, provide that a company before making issue of prospectus or an offer or inviting public or members to more than 500 persons, shall appoint one or more debenture trustees. The names of the debenture trustees shall be stated in letter of offer inviting subscription for debentures and also in all the subsequent notices or other communications sent to the debenture holders. Before the appointment of debenture trustee or trustees, a written consent shall be obtained from such debenture trustee or trustees proposed to be appointed and a statement to that effect shall appear in the letter of offer issued for inviting the subscription of the debentures.

The disqualifications for debenture trustees are as under:

- (a) beneficially holds shares in the company;
- (b) is a promoter, director or key managerial personnel or any other officer or an employee of the company or its holding, subsidiary or associate company;
- (c) is beneficially entitled to moneys which are to be paid by the company otherwise than as remuneration payable to the debenture trustee;
- (d) is indebted to the company, or its subsidiary or its holding or associate company or a subsidiary of such holding company;
- (e) has furnished any guarantee in respect of the principal debts secured by the debentures or interest thereon;
- (f) has any pecuniary relationship with the company amounting to 2% or more of its gross turnover or total income or fifty lakh rupees or such higher amount as may be prescribed, whichever is lower, during the two immediately preceding financial years or during the current financial year;
- (g) is relative of any promoter or any person who is in the employment of the company as a director or key managerial personnel.

### **Duties of Debenture Trustees**

Section 71(6) read with Rule 18(3) of aforesaid rules provide that a debenture trustee shall take steps to protect the interests of the debenture holders and redress their grievances.

It shall be the duty of every debenture trustee to—

- (a) satisfy himself that the letter of offer does not contain any matter which is inconsistent with the terms of the issue of debentures or with the trust deed;
- (b) satisfy himself that the covenants in the trust deed are not prejudicial to the interest of the debenture holders;
- (c) call for periodical status or performance reports from the company;
- (d) communicate promptly to the debenture holders defaults, if any, with regard to payment of interest or redemption of debentures and action taken by the trustee therefor;
- (e) appoint a nominee director on the Board of the company in the event of-
  - (i) two consecutive defaults in payment of interest to the debenture holders; or
  - (ii) default in creation of security for debentures; or
  - (iii) default in redemption of debentures.
- (f) ensure that the company does not commit any breach of the terms of issue of debentures or covenants of the trust deed and take such reasonable steps as may be necessary to remedy any such breach;
- (g) inform the debenture holders immediately of any breach of the terms of issue of debentures or covenants of the trust deed;
- (h) ensure the implementation of the conditions regarding creation of security for the debentures, if any, and debenture redemption reserve;
- (i) ensure that the assets of the company issuing debentures and of the guarantors, if any, are sufficient to discharge the interest and principal amount at all times and that such assets are free from any other encumbrances except those which are specifically agreed to by the debenture holders;
- (j) do such acts as are necessary in the event the security becomes enforceable;
- (k) call for reports on the utilization of funds raised by the issue of debentures;
- (l) take steps to convene a meeting of the holders of debentures as and when such meeting is required to be held;
- (m) ensure that the debentures have been converted or redeemed in accordance with the terms of the issue of debentures;
- (n) perform such acts as are necessary for the protection of the interest of the debenture holders and do all other acts as are necessary in order to resolve the grievances of the debenture holders.

Section 71 sub-section (8) puts obligation on the company to pay interest and redeem the debentures in accordance with the terms and conditions of their issue.

Where at any time the debenture trustee comes to a conclusion that the assets of the company are insufficient or are likely to become insufficient to discharge the principal amount as and when it becomes due, the debenture trustee may file a petition before the Tribunal and the Tribunal may, after hearing the company and any other person interested in the matter, by order, impose such restrictions on the incurring of any further liabilities by the company as the Tribunal may consider necessary in the interests of the debenture-holders.

Some of the obligations of Debenture Trustees provided in the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 are—

- (i) The debenture trustee shall be vested with the requisite powers for protecting the interest of holders of debt securities including a right to appoint a nominee director on the Board of the issuer in consultation with institutional holders of such securities.
- (ii) The debenture trustee shall carry out its duties and perform its functions under these regulations, the Securities and Exchange Board of India (Debenture Trustees) Regulations, 1993, the trust deed and offer document, with due care, diligence and loyalty.
- (iii) The debenture trustee shall ensure disclosure of all material events on an ongoing basis.
- (iv) The debenture trustees shall supervise the implementation of the conditions regarding creation of security for the debt securities and debenture redemption reserve.

## CASE LAWS

### ***Judicial Pronouncement about Debentures***

The following kinds of documents have been held to be treated as debentures:

- a) A series of income-bonds by which a loan to the company was repayable only out of its profits [Lemon v. Austin Friars Investment Trust Ltd. 1926 Ch 1 (CA)];
- b) A receipt or a certificate for a deposit made with a company (other than a bank) when the deposit was repayable after a fixed period after it was made, [United Dominions Trust Ltd. v. Kirkwood, (1966) 2 QB 43].
- c) The definition of debenture is so wide as to include any security of a company whether constituting a charge on the company's assets or not [Cf. Pearl Assurance Co. Ltd. v. West Midlands Gas Board, (1950) 2 All ER 844 (ChD)].

### **Debenture Trust deed**

Debenture Trust deed is a written instrument legally conveying property to a trustee often for the purpose of securing a loan or mortgage. It is the document creating and setting out the terms of a trust. It will usually contain the names of the trustees, the identity of the beneficiaries and the nature of the trust property, as well as the powers and duties of the trustees. It constitutes trustees charged with the duty of looking after the rights and interests of the debenture holders. As per section 71(7), any provision contained in a trust deed for securing the issue of debentures, or in any contract with the debenture-holders secured by a trust deed, shall be void in so far as it would have the effect of exempting a trustee there of from, or indemnifying him against, any liability for breach of trust, where he fails to show the degree of care and due diligence required of him as a trustee, having regard to the provisions of the trust deed conferring on him any power, authority or discretion:

Provided that the liability of the debenture trustee shall be subject to such exemptions as may be agreed upon by a majority of debenture-holders holding not less than three-fourths in value of the total debentures at a meeting held for the purpose.

A trust deed for securing any issue of debentures shall be open for inspection to any member or debenture holder of the company, in the same manner, to the same extent and on the payment of the same fees, as if it were the register of members of the company; and a copy of the trust deed shall be forwarded to any

member or debenture holder of the company, at his request, within seven days of the making thereof, on payment of fee.

As per section 71 and sub-rule (1) of Rule 18 of the Companies (Share Capital and Debentures) Rules, 2014 a trust deed in Form No. SH. 12 or as near there to as possible shall be executed by the company issuing debentures in favour of the debenture trustees within three months of closure of the issue or offer. [Rule18(5)]

Rule 18(8) states that a trust deed for securing any issue of debentures shall be open for inspection to any member or debenture holder of the company, in the same manner, to the same extent and on the payment of the same fees, as if it were the register of members of the company. Further, a copy of the trust deed shall be forwarded to any member or debenture holder of the company, at his request, within seven days of the making thereof, on payment of fee.

### **Exemptions clauses in the trust deed**

Section 71(7) states that any provision contained in a trust deed for securing the issue of debentures, or in any contract with the debenture-holders secured by a trust deed, shall be void in so far as it would have the effect of exempting a trustee thereof from, or indemnifying him against, any liability for breach of trust, where he fails to show the degree of care and due diligence required of him as a trustee, having regard to the provisions of the trust deed conferring on him any power, authority or discretion. The liability of the debenture trustee shall be subject to such exemptions as may be agreed upon by a majority of debenture-holders holding not less than three-fourths in value of the total debentures at a meeting held for the purpose.

Section 71(12) states that a contract with the company to take up and pay for any debentures of the company may be enforced by a decree for specific performance.

### **Penal Provisions**

Section 71 sub-section 9, provides that where at any time the debenture trustee comes to a conclusion that the assets of the company are insufficient or are likely to become insufficient to discharge the principal amount as and when it becomes due, the debenture trustee may file a petition before the Tribunal (NCLT). Tribunal may, after hearing the company and any other person interested in the matter, by order, impose such restrictions on the incurring of any further liabilities by the company as the Tribunal may consider necessary in the interests of the debenture-holders.

Further the sub-section 10 provides that where a company fails to redeem the debentures on the date of their maturity or fails to pay interest on the debentures when it is due, the Tribunal may, on the application of any or all of the debenture-holders, or debenture trustee and, after hearing the parties concerned, direct, by order, the company to redeem the debentures forthwith on payment of principal and interest due thereon.

If any default is made in complying with the order of the Tribunal under this section, every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than two lakh rupees but which may extend to five lakh rupees, or with both.

## **PART B**

### **OVERVIEW OF COMPANY DEPOSITS**

Companies aim to secure finance by different cost-effective methods to suit their financial requirements. Companies have always been attracted towards financing through deposits and, at times, problems have

arisen in the context of such deposits. In order to control the malpractices, the Companies Act, 2013 has introduced strict provisions under the deposit regime.

Sections 73 to 76 of the Companies Act 2013 read with the Companies (Acceptance of Deposits) Rules, 2014 regulate the invitation, acceptance and repayment of deposits by Companies.

### Applicability

The provisions under Sections 73 to 76 of the Companies Act 2013 and the Companies (Acceptance of Deposits) Rules, 2014 shall apply to all companies except -

- a banking company and
- a non- banking financial company as defined in the Reserve Bank of India Act, 1934 and
- a housing finance company registered with the National Housing Bank established under the National Housing Bank Act, 2013; and
- such other company as the Central Government may, after consultation with the Reserve Bank of India, specify in this behalf.

[Section 73(1) read with Rule 1(3)]

### What is Deposit?

According to the Section 2(31) of the Act read with Rule 2(c) of Companies (Acceptance of Deposits) Rules, 2014, '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 Government or a State Government, or any amount received from any other source whose repayment is guaranteed by the Central Government or a State Government or any amount received from a local authority, or any amount received from a statutory authority;
- (ii) any amount received from foreign Governments, foreign/international banks, multilateral financial institutions, 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 Foreign Exchange Management Act, 1999;
- (iii) any amount received as a loan or facility from any banking company or from the State Bank of India 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, regional financial institutions, Insurance Companies or Scheduled Banks;
- (v) any amount received against issue of commercial paper or any other instrument issued in accordance with the guidelines or notification issued by the Reserve Bank of India;
- (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:

- (a) 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;
- (b) Any adjustment of the amount for any other purpose shall 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 a relative of the director of the Private company:
- Provided that the director of the company or relative of the director of the private company, as the case may be, 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 and the company shall disclose the details of money so accepted in the Board's report.
- (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 excluding intangible assets of the company or bonds/ debentures compulsorily convertible into shares of the company within five 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;
- (ixa) any amount raised by issue of non-convertible debenture not constituting a charge on the assets of the company and listed on a recognised stock exchange as per applicable regulations made by Securities and Exchange Board of India.
- (x) Interest free security deposit from an employee not exceeding his annual salary
- (xi) any non-interest bearing amount received and 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 three hundred and sixty five 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 three hundred and sixty five days shall not apply.
- (b) as advance, accounted for in any manner whatsoever, received in connection with consideration for an immovable property under an agreement or arrangement, provided that such advance is adjusted against such 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.
- (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 five 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;

If the amount received under (a) (b) and (d) 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.

*Explanation:* For the purpose of 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 fulfillment of the following conditions:-

- (a) the loan is brought in pursuance of the stipulation imposed by the lending institutions on the promoters to contribute such finance; and
- (b) the loan is provided by the promoters themselves or by their relatives or by both and
- (c) 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

For the purposes of this clause, any amount-

- (a) 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
- (b) 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 treated as a deposit.

- (xv) any amount received by way of subscription in respect of a chit under the Chit Fund Act, 1982

- (xvi) any amount received by the company under any collective investment scheme in compliance with regulations framed by the Securities and Exchange Board of India;

- (xvii) an amount of twenty five lakh rupees 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 five years from the date of issue) in a single tranche, from a person.

*Explanation.-* For the purposes of this sub-clause,-

- I. "start-up company" means a private company incorporated under the Companies Act, 2013 or Companies Act, 1956 and recognised as such in accordance with notification number G.S.R. 180(E) dated 17th February, 2016 issued by the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry;
- II. "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.

- (xviii) any amount received by a company from Alternate Investment Funds, Domestic Venture Capital Funds, "Infrastructure Investment Trusts" and Mutual Funds registered with the Securities and Exchange Board of India in accordance with regulations made by it."

## TEST YOUR KNOWLEDGE

### Illustration

Please check which of the following source of funds are coming under the definition of deposits in case of a company.

- (a) ₹5 Crore from Government Agency, Financial institutions, Banks or by way of Commercial Paper.
- (b) ₹50 Lakhs by way of Share Application money
- (c) ₹50 Lakhs from one of its director by way of loan (d) ₹50 Lakhs from issue of bonds and debentures
- (e) Rs.50 Lakhs by means of inter corporate deposit
- (f) ₹25 Lakhs from its employees.
- (g) ₹50 Lakhs as business advance from customers
- (h) ₹50 Lakhs as advance against consideration for an immovable property.
- (i) ₹25 Lakhs as security deposit for performance of provision of services
- (j) ₹50 Lakhs from its promoter.
- (k) ₹25 Lakhs raised by issue of non convertible debentures. These are not constituting charge on assets of the company.

### Solution

- (a) The said amount is to be received or borrowed from any government agency or Financial Institution or Bank or by way of Commercial paper is not covered under deposits.
- (b) Company must allot share within 60 days of receipt of share application money or it must refund the share application money to the subscribers within 15 days from the date of completion of sixty days, otherwise, such amount shall be treated as a deposit.
- (c) Company can receive loan from its director (or relative of director of the private company) provided they give a declaration to the company that the loan given is from own funds and not from borrowed money.
- (d) Company can raise money by way of bonds and debentures provided amount is secured by a first charge against property; or such bonds or debentures should be compulsorily convertible into shares within 10 years; otherwise it would come under the definition of deposits.
- (e) Inter corporate deposits are not covered in the definition of deposits
- (f) If amount received from employee doesn't exceed their total annual salary; and such deposits should be non-interest bearing security deposit it would not come under the definition of deposit.

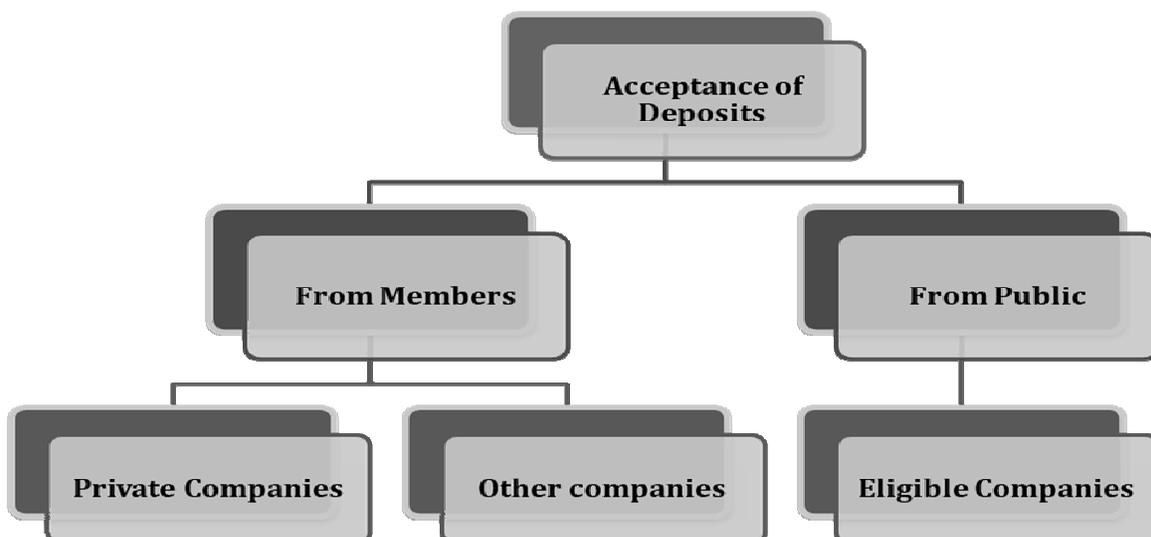
- (g) Advance can be raised from customers however; such advance should be adjusted within 365 days from the date of receipt of advance. Otherwise it would be termed as deposits.
- (h) Such amount should be adjusted against such property only; otherwise it would be termed as deposits.
- (i) Security deposits are out of the ambit of definition of deposits. It is suggested to accept security deposits Under specific agreement.
- (j) 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 is not deposits subject to fulfillment of the following conditions, namely:-
  - (i) the loan is brought in pursuance of the stipulation imposed by the lending institutions on the promoters to contribute such finance;
  - (ii) the loan is provided by the promoters themselves or by their relatives or by both; and
  - (iii) the exemption under this sub-clause shall be available only till the loans of financial institution or bank are repaid and not thereafter;
- (k) This amount is not a deposit in term of rule 2(1)(c) (ixa) provided these non-convertible debenture are listed on recognized stock exchange

### Who is Depositor?

‘Depositor’ means —

- (i) any member of the company who has made a deposit with the company in accordance with sub-section (2) of section 73 of the Act, or
- (ii) any person who has made a deposit with a public company in accordance with section 76 of the Act. [Rule 2(1)(d)]

### Acceptance of Deposits



## Acceptance of Deposits from members

### Quantum of Deposits that can be accepted

Chapter V divides the companies accepting deposits in to two categories–

I. Companies accepting deposits from members [Section 73 (2)]: Any company subject to compliance of provisions of this section may accept deposits.

II. Companies accepting deposits from public i.e. eligible companies only public and specified companies may accept deposits from public subject to compliance of provisions of this section from members. In case of private companies, the fulfillment of conditions given in section 73 (2) (a) to (e) is exempted, in case it accepts from its members monies not exceeding one hundred per cent of aggregate of the paid-up share capital, free reserves and securities premium account and also such company needs to file details of monies accepted to Registrar. [Section 76].

- (1) No eligible company shall accept or renew any deposit from its members, if the amount of such deposits together with the amount of deposits outstanding as on the date of acceptance or renewal of such deposits from members exceeds 10% of the aggregate of the paid-up share capital, free reserves and securities premium account of the company and; [Rule 3(4)(a)]
- (2) No eligible company shall accept or renew any deposit from public, if the amount of such deposit other than the deposit received from members, together with the amount of deposits outstanding on the date of acceptance or renewal exceeds 25% of aggregate of the paid-up share capital, free reserves and securities premium account of the company. [Rule 3(4)(b)]
- (3) No company referred in section 73(2) shall accept or renew any deposits from its members if the amount of such 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. [Rule 3]

Provided that a private company may accept from its members monies not exceeding one hundred percent 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.

- (4) No Government company eligible to accept deposits under section 76 shall accept or renew any deposit, if the amount of such deposits together with the amount of other deposits outstanding as on the date of acceptance or renewal exceeds 35% of the paid-up share capital, free reserves and securities premium account of the company. [Rule 3(5)]

The Quantum of deposits:

Type of company	Members	Public
Eligible Company	Upto 10% of aggregate of the paid up share capital, free reserves and securities premium account	Upto 25% of aggregate of the paid up share capital, free reserves and securities premium account
Company referred in section 73(2)	Upto 35% of aggregate of the paid up share capital, free reserves and securities premium account	Prohibited

Government Company (eligible under section 76)	–	Upto 35% of aggregate of the paid up share capital, free reserves and securities premium account
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The maximum limit in respect of deposits to be accepted from members shall not apply to following classes of private companies, namely:-

- (i) a private company which is a start-up, for five years from the date of its incorporation;
- (ii) a private company which fulfils all of the following conditions, namely:-
  - (a) which is not an associate or a subsidiary company of any other company;
  - (b) the borrowings of such a company from banks or financial institutions or any body corporate is less than twice of its paid up share capital or fifty crore rupees, whichever is less ; and
  - (c) such a company has not defaulted in the repayment of such borrowings subsisting at the time of accepting deposits under section 73:

All the companies accepting deposits shall file the details of monies so accepted to the Registrar in Form DPT – 3.

It may be noted that private companies and public companies (other than eligible companies) are not allowed to accept deposits from public.

## PROCEDURE OF ACCEPTANCE OF DEPOSITS

Section 73(2) states that a company may accept deposits from its members on such terms and conditions, including the provision of security, if any, or for the repayment of such deposits with interest, as may be agreed upon between the company and its members,

- subject to the passing of a resolution in general meeting,
- subject to such rules as may be prescribed in consultation with the Reserve Bank of India and subject to the fulfillment of following conditions under Section 73(2)
  - (a) issuance of a circular to its members including therein a statement showing the financial position of the company, the credit rating obtained, the total number of depositors and the amount due towards deposits in respect of any previous deposits accepted by the company and such other particulars in such form and in such manner as prescribed under Rule 4 of Companies (Acceptance of deposits) Rules, 2014.
  - (b) filing a copy of the circular along with such statement with the Registrar within thirty days before the date of issue of the circular;
  - (c) depositing, on or before the thirtieth day of April each year, such sum which shall not be less than 20% of the amount of its deposits maturing during the following financial year and kept in a scheduled bank in a separate bank account to be called deposit repayment reserve account:
  - (e) certifying that the company has not committed any default in the repayment of deposits accepted either before or after the commencement of this Act or payment of interest on such deposits and where a default had occurred, the company made good the default and a period of five years had lapsed since the date of making good the default; and
  - (f) providing security, if any for the due repayment of the amount of deposit or the interest thereon including the creation of such charge on the property or assets of the company.

Provided that in case when a company does not secure the deposits or secures such deposits partially, then,

the deposits shall be termed as “unsecured deposits” and shall be so quoted in every circular, form, advertisement or in any document related to invitation or acceptance of deposits.

Keeping the procedures or steps of acceptance of deposits in view, companies can be segregated into three types viz. Private Company, Public company (other than eligible company) and eligible company. There are several procedural differences among these companies, which are discussed below.

### POINTS OF DIFFERENCE

Category of Company	Private Company as per [Section73 (2)]	Public Company (other as per than eligible company [Section73 (2)]	Public company (eligible company under section 76 of the Act)
Source of deposits	From directors and members	From directors and members	From directors, members and General public
Conditions for deposits to be taken from directors	It is allowed to be taken without any limit. However, director of the company Or relative of the director of the private company has to furnish declaration at the time of money being given to the company that the amount is not being given out of funds acquired by him by borrowing or accepting loans or deposits from others.	It is allowed to be taken without any limit. However, director has to furnish declaration at the time of money being given to the company that the amount is not being given out of funds acquired by him by borrowing or accepting loans or deposits from others.	It is allowed to be taken without any limit. However, director has to furnish declaration at the time of money being given to the company that the amount is not being given out of funds acquired by him by borrowing or accepting loans or deposits from others.
Conditions for deposits to be taken from shareholders	It is allowed to be taken subject to the limit of 35% of the paid up share and capital, free reserves and securities premium account. The compliance of condition as specified under (a) to (e) of section 73(2) of the Act are exempted in case it accepts from members monies not exceeding 100% of aggregate of the paid up share capital, free reserve and securities premium account. This is subject to compliance of Point (f) of 73(2) and Rules specified.	It is allowed to be taken subject to the limit of 35% of the paid up share capital, free reserves and securities premium account subject to the compliance of provisions of section 73(2) of the Act.	It is allowed to be taken subject to the limit of 10% of the paid up share capital, free reserves securities premium account subject to the compliance of provisions of section73(2)of the Act. Provided that at any point of time, deposits shall not exceed 25% of the paid up share capital, free reserves and securities premium account.

Conditions for deposits to be taken from Public	Prohibited	Prohibited	It is allowed to be taken subject to the limit of 25% of the paid up share capital, free reserves and securities premium account. However, in case of Government company, who is eligible to accept deposits from public under section 76, it is allowed to be taken subject to the limit of 35% of the paid up share capital, free reserves and securities premium account.
Resolution	The company should pass a resolution in a general meeting.	The company should pass a resolution in a general meeting.	The company should pass a resolution in a general meeting.
Advertisement	Not necessary	Not necessary	Necessary
Circular	Circular shall be issued to its members by registered post with acknowledgement due or by speed post or by electronic mode in Form DPT-1 and in addition to such issue of circular to publish the same in one English newspaper and one vernacular language in vernacular newspaper having wide circulation in the state of registered office of the company. [Rule4]	Circular shall be issued to its members by registered post with Acknowledgement due Or by speed post or by electronic mode in Form DPT-1 and in addition to such Issue of circular to publish the same in one English newspaper and one vernacular language in vernacular newspaper having wide circulation in the state of registered office of the company. [Rule4]	Every eligible company intending to invite deposits shall issue a circular in the form of an advertisement in Form DPT 1 for the purpose in English language in an English newspaper having countrywide circulation and in vernacular language in a vernacular newspaper having wide circulation in the State in which the register office of the company is situated, and shall also place such Circular on the website of the company, if any.
Display of circular on website	Optional	Optional	Mandatory, if any

<p>Credit Rating</p>	<p>*Required to be taken before the submission of the circular to the registrar as is an essential disclosure of the said circular</p>	<p>Required to be taken before the submission of the circular to the registrar as is an essential disclosure of the said circular</p>	<p>Required to be taken (including the rating of its net worth, liquidity and ability to pay its deposits on due date) before the submission of the circular to the registrar as is an essential disclosure of the said circular. 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,</p>
			<p>The credit rating referred to above 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 Non-Banking Financial Companies in the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998, issued by the Reserve Bank of India, as amended from time to time. [Rule3(8)]</p>

\*Exempted in case private company accepts from its members monies not exceeding 100 percent of aggregate of paid-up share capital and free reserves.

So far procedure of acceptance of deposits is concerned, there are some procedural similarities exist among Private Company, Public company (other than eligible company) and eligible company, which are discussed below.

**POINTS OF SIMILARITY**

Category of Company	Private Company	Public Company (other than eligible Company)	Public company (eligible company under section 76 of the Act)
Tenure of deposits	The deposit shall not be repayable on demand or upon receiving a notice within a period of less than 6 months and more than 36 months. However, to meet the short requirements of fund, such companies can accept or renew deposits for a period of less than six months but not less than three months and such deposits should not exceed ten percent of aggregate of paid up capital and free reserves of the company.		
Statement	*Along with the circular a statement shall be circulated which shall contain the financial position of the company, the credit rating, the number of depositors and the amount due.		
Registration of circular	*The circular signed by majority of directors or their agents duly authorized along with the statement shall be submitted to registrar 30 days before the date of such issue.		
Validity of circular	*6(six) months from the end of the financial year in which it was issued or the date on which the AGM is held whichever is earlier.		
Security	If secured deposits are invited then the company shall create a charge on its assets referred to in Schedule III excluding intangible assets.		
Quoting of “Unsecured Deposit”	Where the proposed deposits is unsecured or is partly secured, the deposits shall be termed as “unsecured deposits” and shall be quoted in every circular, form, advertisement or in any other document relating to invitation or acceptance of deposits.		
Deposit repayment reserve account	*On or before 30th April of each year, such sum which shall not be less than twenty per cent. of the amount of its deposits maturing during the following financial year and kept in a scheduled bank in a separate bank account to be called deposit repayment reserve account.		
Register	One or more separate registers for deposits accepted or renewed shall be maintained at the registered office and entries shall be made within 7 days from the date of issuance of deposit receipt.		

Return of deposits	A return shall be filed on or before 30th June of every year with the Registrar in Form DPT-3 alongwith fee giving the status as on 31st March of that year duly audited by the auditor of the company.
Penal rate of interest	A penal Rate of 18% p.a. shall be payable for the over due period in case of whether secured or unsecured, matured and claimed but remaining unpaid.
Premature payment	In case of premature payment of deposits,1% shall be reduced from the interest agreed to be paid.

\*Exempted for private companies if it accepts from its members monies not exceeding 100 percent of aggregate of paid-up share capital and free reserves.

Procedure of acceptance of deposits can be discussed under two broad headings i.e. procedure of acceptance of deposits from members and procedure of acceptance of deposits from public (other than members) because non- eligible companies are allowed to accept deposits from its directors, members and their relatives where as eligible companies are allowed to accept deposits from members as well as public.

### **PROCEDURE OF ACCEPTANCE OF DEPOSITS FROM MEMBERS**

A company may, subject to the passing of a resolution in general meeting and subject to such rules as maybe prescribed in consultation with the Reserve Bank of India, accept deposits from its members on such terms and conditions, including the provision of security, if any, or for the repayment of such deposits with interest, as may be agreed upon between the company and its members.

The procedure to accept deposits from members can be summarized as under:-

1. The companies intending to invite deposits from its members shall convene a Board meeting to consider and Approve the business to propose and accept deposits from members and decide the day, date, time and place of the general meeting.
2. Issue notice of general meeting to the members of the company.
3. Hold the general meeting and pass resolution for acceptance of deposits.
4. Comply with the Rules prescribed in consultation with RBI and terms and conditions mutually agreed by the company and deposit holders either for acceptance or for repayment of deposits.
- \*5. Issue circular to the members of the company including therein a statement showing the financial position of the company, the credit rating obtained, the total number of depositors and the amount due towards depositors in respect of any previous deposits and such other particulars as may be prescribed. These details indicate the soundness of the company or a warning about risks involved. The circular shall be published at least once in English language in a leading English newspaper and in vernacular language in a vernacular newspaper having wide circulation in the State in which the registered office of the company is situated.
6. File the copy of aforesaid circular in the Form DPT-1 along with such statement with the Registrar within thirty days before the date of issue of circular.
7. In case, a company does not secure the deposits or secures such deposit partially, then, the deposits shall be termed as “unsecured deposits” and shall be so quoted in every circular, form,

advertisement or in any document related to invitation or acceptance of deposits.

- \*8. A company inviting secured deposits shall provide for security by way of a charge on its assets for the due repayment of the amount of deposit and interest thereon. The company shall submit Form CHG-1 with Registrar for assets other than intangible assets. Secured deposits including interest thereon can in no case exceed the market value of the charged assets assessed by the registered valuer.
9. After the expiry of 30 days of filing Form DPT-1, the circular in Form DPT-1 along with application form is sent to all members by registered post with acknowledgement due/speed post/electronic mail.
10. Collect duly signed application form along with money from the members.
11. Issue receipts of deposits within 21 days of the receipts of money/realization of cheque.
12. Maintain register of deposits at its registered office which shall contain the details as prescribed under rule 14 Companies (Acceptance of Deposits) Rules, 2014 from the date of such acceptance.
13. Pay interest as per the rate proposed on agreed terms.
- \*14. Deposit such sum which shall not be less than twenty percent of the amount of its deposits maturing during the financial year and the financial year next following and keeping it in a separate bank account called deposit repayment reserve account.
15. Certification that the Company has not committed any default in the repayment of deposits accepted either before or after the commencement of this Act or payment of interest on such deposits and where a default had occurred, the company made good the default and a period of five years had lapsed since the date of making good the default
16. Submit return of deposits in Form DPT-3 on or before 30th June each year for information as on 31st March of respective year.

\*Exempted for private companies if it accepts from its members monies not exceeding 100 percent of aggregate of paid-up share capital and free reserves and the company files the details of monies so accepted to Registrar.

#### **CONDITIONS FOR ACCEPTANCE OF DEPOSITS FROM PUBLIC (OTHER THAN MEMBERS)**

A public company having net worth of not less than Rs.100 Crores or turnover of not less than Rs. 500 Crores (Eligible Company) and which has obtained the prior consent of the members in a general meeting by means of special resolution and also filed the special resolution with the Registrar of Companies before making any invitation to the public for acceptance of deposits. Eligible company, which is accepting deposits within the limit specified under clause (c) of sub-section (1) of section 180 (Borrowing Powers) may accept deposits by means of an ordinary resolution.

Further, no Government company eligible to accept deposits under section 76 shall accept or renew any deposits, if the amount of such deposits together with the amount of other deposits out standing as on the date of acceptance or renewal exceeds thirty five percent of the aggregate of its paid up share capital and free reserves.

The procedure to accept deposits from public (other than members) can be summarized as under:-

1. Convene a Board meeting to consider and approve the business to propose and accept deposits from public and to decide the day, date, time and place of the general meeting.
2. Hold the general meeting and pass special resolution, for acceptance of deposits.

3. Submit Form MGT-14 with the Registrar of Companies within 30 days of passing the resolution.
4. Once the proposal is approved, Directors are required to approach to the credit rating agency for the grant of rating, execution of deposit insurance contract, appointment of deposit or trustee and execution of trust deed, if the deposits are secured, appointment of registered valuer, discussion and preparation of circular for the issue of deposits may be given.
5. Circular shall be issued to its members of the company by registered post with acknowledgement due or by speed post or by electronic mode in Form DPT-1 and in addition to such issue of circular to publish the same in one English newspaper and one vernacular language in vernacular newspaper having wide circulation in the state of registered office of the company. The eligible companies have to file a copy of the text of advertisement signed by a majority of directors with the Registrar before 30 days of publication. They shall upload the same on their website, if any.
6. File the copy of aforesaid circular in the Form DPT-1 along with such statement with the Registrar within thirty days before the date of issue of circular.
7. In case, a company does not secure the deposits or secures such deposit partially, then, the deposits shall be termed as "unsecured deposits" and shall be so quoted in every circular, form, advertisement or in any document related to invitation or acceptance of deposits.
8. The company shall execute a deposit trust deed in Form DPT-2 at least seven days before issuing circular or circular in the form of advertisement.
9. Eligible company inviting secured deposits shall provide for security by way of a charge on its assets for the due repayment of the amount of deposit and interest thereon. The company shall submit Form CHG-1 with Registrar for assets other than intangible assets. Secured deposits including interest there on can in no case exceed the market value of the charged assets assessed by the registered valuer.
10. Eligible companies proposed to accept deposits from public is required to issue advertisement one in English newspaper having countrywide circulation and one newspaper in vernacular language having wide circulation in the state in which the registered office of the company is situated. Said circular/advertisement shall be valid till before the expiry of six months from the end of respective financial year in which it was issued or up to the date of Annual General Meeting (or last due date of AGM), if not held) wherein the financial statement is laid before members, whichever is earlier.
11. Upload the circular/advertisement on the company Website, if any.
12. Collect duly signed application form along with money from the members.
13. Issue receipts of deposits within 21 days of the receipts of money/realization of cheque.
14. Maintain register of deposits at its registered office which shall contain the details as prescribed under Rule 14 Companies (Acceptance of Deposits) Rules, 2014, from the date of such acceptance.
15. Pay interest as per the rate proposed on agreed terms.
16. Deposit such sum which shall not be less than twenty percent of the amount of its deposits maturing during the financial year and the financial year next following and keeping it in a separate bank account called deposit repayment reserve account.
17. Submit return of deposits in Form DPT-3 on or before 30th June each year for information as on 31st March of respective year.

## CHECKLIST OF SECRETARIAL COMPLIANCE FOR ACCEPTANCE OF DEPOSITS AS PER COMPANIES ACT, 2013:

Checklist of secretarial compliance for acceptance of deposits under Companies Act, 2013, are discussed below. The Company Secretary should check:

1. Whether proper Board meeting has been held and the matter of acceptance of deposit has been proposed and issue of notice for holding general meeting for obtaining approval of the shareholder has been taken place.
2. Whether general meeting has been held and approval of the shareholders by means of a special or ordinary resolution has been passed.
3. Whether the said resolution has been filed with Registrar in Form MGT-14 within 30 days of passing of such resolution.
4. Whether Board meeting has been held to obtain the approval for the draft Circular/Form of Advertisement from the Board and the said draft Circular/Form of Advertisement has been signed by majority of the directors of the Company.
5. Whether copy of Circular/Form of Advertisement approved by the Board has been filed with the Registrar of Companies in Form DPT-1 for registration.
6. Whether one or more deposit trustees for creating security for the secured deposits has been appointed and the company has executed a deposit trust deed in Form DPT-2 at least seven days before issuing circular or circular in the form of advertisement.
7. Whether the company has obtain the rating unless exempted,(including its net worth, liquidity and ability to pay its deposits on due date) from are cognized credit rating agency for informing the public the rating given to the Company.
8. Whether the company has issued circular/form of advertisement after 30 days from the date of filing of a Copy of Circular/Form of Advertisement with the Registrar.
9. Whether the circular has been issued to members by registered post with acknowledgement due or speed post or by electronic mode or publish the circular in the form of an advertisement inform DPT-1 and in addition to such issue of circular the company has published the same in one English newspaper having country wide circulation and one vernacular language in vernacular newspaper having wide circulation in the state of registered office of the company.
10. Whether the company has uploaded the copy of the circular on the Company's website, if any.
11. Whether the company has issued deposit receipt in the prescribed form at and under the signature of officer duly authorized by Board, within a period of two weeks from the date of receipt of money or realization of cheques.
12. Whether the company has made entries in the register as per the instruction provided in the rules within seven days from the date of issuance of the deposit receipt and such entries shall be authenticated by a director or secretary of the Company or by any other officer authorized by the Board.
13. Whether the company has filed deposit return in Form DPT-3 by furnishing in formation contained there in as on 31st day of March duly audited by auditors before 30th June every year.
14. Whether the company has prepared the statement regarding deposits existing as on the date of commencement of the act in Form DPT-4.

These are some of the checklist which are to be taken care of from compliance point of view.

### Exemption for Private companies

In the public interest the Central Government hereby amends the notification no. G.S.R. 464 dated 5th June 2015 has allowed private companies to accept deposits from its members, monies not exceeding 100% of aggregate of the paid up share capital and free reserves, and such company shall file the details of monies so accepted to the Registrar in such manner as may be specified without complying with Section 73(2) (a) to (e). Thus a private company will have to follow only the condition mentioned in Section 73(2) (f).

Shall not apply to a private company —

- (A) which accepts from its members monies not exceeding one hundred per cent. of aggregate of the paid up share capital, free reserves and securities premium account; or
- (B) which is a start-up, for five years from the date of its incorporation; or
- (C) which fulfils all of the following conditions, namely:-
  - (a) which is not an associate or a subsidiary company of any other company;
  - (b) if the borrowings of such a company from banks or financial institutions or any body corporate is less than twice of its paid up share capital or fifty crore rupees, whichever is lower; and
  - (c) such a company has not defaulted in the repayment of such borrowings subsisting at the time of accepting deposits under this section: Provided that the company referred to in clauses (A), (B) or (C) shall file the details of monies accepted to the Registrar in such manner as may be specified.

### ANNEXURES

#### SPECIMEN RESOLUTION FOR ACCEPTANCE OF DEPOSITS FROM MEMBERS AND/OR PUBLIC

“RESOLVED THAT pursuant to the provisions of Section 73 and 76 of the Companies Act, 2013 (the Act) read with the Companies (Acceptance of Deposits) Rules, 2014 (the Rules) and other applicable provisions, if any, and subject to such conditions, approvals, permissions, as may be necessary, consent of the members be and is hereby accorded to the Company to invite/accept/renew/receive money by way of unsecured/secured deposits from its members and public.

RESOLVED FURTHER THAT Mr. C, Chairman & Managing Director, be and is here by authorized to issue the circular or circular in the form of advertisement, which has been approved by the Board of Directors of the company at their meeting held on the (day) of (month), 2014 (year) and which delineates the silent features of the deposit scheme of the company and other relevant particulars as prescribed by the Act and the Rules.

RESOLVED FURTHER THAT Mr. C, Chairman & Managing Director, be and is hereby authorized to have the circular or circular in the form of advertisement, which has been duly signed by the majority of directors, filed with the Registrar of Companies, NCT of Delhi & Haryana, New Delhi, pursuant to the Rules, and to publish the same in English language in Times of India (Delhi edition) and in Hindi in Dainik Jagran (Delhi edition).

RESOLVED FURTHER THAT for the purpose of giving effect to this Resolution, the Board of Directors be and is hereby authorized to do such acts, deeds, matters and things as Board of Directors may in its absolute discretion consider necessary, proper, expedient, desirable or appropriate for such invitation/acceptance/renewal/receipts as aforesaid and matters incidental thereto.”

(The aforesaid specimen resolution is drafted on the assumption that the registered office of the company is in the state of Delhi and Times of India (Delhi edition) and Dainik jagran (Delhi edition) are widely circulated newspaper in the state of Delhi.)

## LESSON ROUND UP

- All companies are given power to borrow by their articles which fix the maximum limit of borrowings.
- The power to borrow monies and to issue debentures (whether in or outside India) can only be exercised by the Directors at a duly convened meeting.
- Where the company borrows without the authority conferred on it by the Articles or beyond the amount set out in the Articles, it is an ultra vires borrowing and hence void. Ultra vires borrowings cannot even be ratified by a resolution passed by the company in general meeting. In case of ultra vires borrowings the lender has the following remedies: (a) Injunction and Recovery, (b) Subrogation, (c) Suit against Directors.
- A debenture is a document given by a company under its seal as an evidence of a debt to the holder usually arising out of a loan and most commonly secured by a charge.
- Debentures may be of different kinds, viz. redeemable debentures, registered and bearer debentures, secured and unsecured or naked debentures, convertible debentures.
- A debenture stock is a borrowed capital consolidated into one mass for the sake of convenience.
- A loan creates a right in the creditor to demand repayment, and the substance of a debt is a liability upon the debtor to repay the money.
- A debenture trust deed is one of the several instruments required to be executed to secure redemption of debentures and payment of interest on due dates.
- Section 71(4) of the Act required every company to create a debenture redemption reserve account to which adequate amount shall be credited out of its profits available for payment of dividend until such debentures are redeemed and shall utilize the same exclusively for redemption of a particular set or series of debentures only.
- Certificate of deposit is a document of title to a time deposit.
- Commercial paper refers to unsecured promissory notes issued by credit worthy companies to borrow funds on a short term basis.
- The convertible debentures are regulated by SEBI (ICDR) Regulations, 2009.
- The non-convertible debentures are regulated by SEBI (Issue and Listing of Debt Securities) Regulations, 2008.
- Section 73 prohibits a company to invite, accept or renew deposits from public. This prohibition however shall not apply in case of banking company and non-banking financial company and such other company as the Central Government may specify.
  - A company can invite deposits from its members subject to the passing of a resolution in general meeting subject to some conditions.
  - The company inviting deposits shall issue a circular to its members in Form DPT-1
  - The company inviting deposits shall enter into a contract for providing deposit insurance at least 30 days before the issue of circular or advertisement or before the date of renewal. (Exempted till 31st March, 2017)
  - For appointing deposit trustees the company shall execute deposit trust deed in Form DPT-2.
  - The company accepting deposits shall maintain at its registered office one or more registers for deposits accepted or renewed.
  - The Return of Deposits shall be filed in Form DPT-3 with the Registrar.

## GLOSSARY

<b>Ultra Vires</b>	Beyond the powers
<b>Intra vires</b>	Within the powers
<b>Paripassu</b>	On equal footing or proportionately
<b>Bonds</b>	A bond is an instrument of indebtedness of the bond issuer to the holders. It is a debt security, under which the issuer owes the holders a debt and, depending on the terms of the bond, is obliged to pay them interest (the coupon) and/or to repay the principal at a later date, termed the maturity. Interest is usually payable at fixed intervals (semiannual, annual, sometimes monthly). Very often the bond is negotiable, i.e. the ownership of the instrument can be transferred in the secondary market.

## SELF-TEST QUESTIONS

*(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation).*

1. What are the restrictions imposed on the borrowing powers of the Board of directors? If a company borrows beyond its powers, examine the remedies open to such creditor:
  - (i) When the money has not been spent;
  - (ii) When the money has been spent to pay the debts of the company.
2. What is the difference between debenture and a loan? Is fixed deposit a Debenture or Loan?
3. What is debenture? What are the kinds of debentures?
4. What is a convertible debenture? What are the provisions of the Companies Act, 2013 regarding convertible debentures or loans?
5. Is it compulsory to maintain a Debenture Redemption Reserve Account? If yes, how?
6. Write short notes on the following:
  - (i) Ultra vires borrowings
  - (ii) Intra vires borrowings
  - (iii) Security for borrowings
  - (iv) Types of borrowings
  - (v) Raising loans from financial institutions.
7. Who is a debenture trustee? Why is it compulsory to appoint a trustee in connection with the issuance of debentures? What are the duties of a trustee?
8. Prepare a checklist of secretarial compliance to be made by a company secretary for acceptance of deposits.
9. What is the procedure for accepting deposits from members?

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# Lesson 5

## Charges

### LESSON OUTLINE

- Definition of charge
- kinds of a charge viz. fixed charge, floating charge
- Judicial pronouncements on different types of charges
- Crystallization of floating charge
- Registration of charges
- Condonation of delay
- Register of charges
- Satisfaction of charges
- Modification of charges
- Purchase or Acquisition of a Property Subject to Charge
- Consequences on non-registration of charge
- Procedure for registration of creation/modification/satisfaction of charge
- Lesson Round-up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

Borrowings by companies are often backed by securities on the strength of which loans are given by the banks or FIs. A charge is created when security is given for securing loans or debentures by way of a mortgage on the assets of the company. The charge may be fixed or floating. The Companies Act covers the provisions relating to registration, modification, satisfaction of charges, consequences of failure in Registration, delay, if any, in this regard etc.

The purpose of registration of a charge is to give notice to the Registrar of Companies ("RoC") and to people who intend to advance money to the company about the encumbrance created on the assets of the company. The lender may inspect the Index of Charges and Forms in the MCA Portal. Non-registration of charges does not make the transaction invalid, but such charge shall not be taken into account by the liquidators and any other creditors of the company. Section 77-87 read with Companies (Registration of Charges) Rules, 2014 deals with Regulatory and Procedural aspects covering registration of charges, condonation of delay by Central Government/ Registrar, etc., maintenance of Register of Charges, etc.

After reading this lesson you will be able to understand the procedure of creation of charges, their registration, modification, satisfaction, etc. and their registration aspects.

## WHAT IS A CHARGE?

A charge is a security given for securing loans or debentures by way of a mortgage on the assets of the company. A company, like a natural person, can offer security for its borrowings. Normally, the debentures and other borrowings of the company are secured by a charge on the assets of the company. Where property, both existing and future, is agreed to be made available as a security for the repayment of debt and creditors have a present right to have it made available, a charge is created. The legal right of the creditor can only be enforced at some future date if certain conditions governing the loan are not met. The creditor gets no legal right either absolute or special to the property charged. He only gets the right to have the security made available/enforced by an order of the Court.

In simple terms a charge is a right created by a company i.e. “Borrower” on its assets or properties or any of its undertakings present or future, in favor of a financial institution or a bank or any other lender, i.e. “creditor” who has agreed to extend financial assistance.

**According to Section 2(16) of the Act, “charge” means an interest or lien created on the property or assets of a company or any of its undertakings or both as security and includes a mortgage.**

The Charge here has the following essential features:

- There are minimum two parties to the transaction, the creator of the charge and the charge- holder.
- The subject- matter of charge may be on current or future assets and properties of the borrower.
- The intention of the borrower to offer one or more of its specific asset or properties as security for repayment of the borrowed money together with payment of interest at the agreed rate etc should manifest from an agreement entered by him in favour of the lender, written or otherwise.

The key words mentioned in the definition are “interest” and “lien”. The meaning of “interest” as per Black’s law dictionary is *‘legal share in something; all or part of a legal or equitable claim to a right in property <right, title, and interest>. Collectively, the word includes any aggregation of rights, privileges, powers and immunities; distributively, it refers to anyone right, privilege, power, or immunity.’*

*The meaning of “lien” as per the Black’s Law dictionary is á legal right or interest that a creditor has in another’s property lasting usually until a debt or duty it secures is satisfied. ‘Lien’ strictly, is simply a right to possess and retain property until some claim attaching to it is satisfied or discharged.’*

*In both the cases whether “interest” and “lien” a charge is to be created.*

## NEED FOR CREATING A CHARGE ON COMPANY’S ASSETS

Almost all the large and small companies depend upon share capital and borrowed capital for financing their projects. Borrowed capital may consist of funds raised by issuing debentures, which may be secured or unsecured, or by obtaining financial assistance from financial institution or banks.

The financial institutions/banks do not lend their monies unless they are sure that their funds are safe and they would be repaid as per agreed repayment schedule along with payment of interest. In order to secure their loans they resort to creating right in the assets and properties of the borrowing companies, which is known as a charge on assets. This is done by executing loan agreements, hypothecation agreements, mortgage deeds and other similar documents, which the borrowing company is required to execute in favour of the lending institutions/ banks, etc.

As a matter of convenience and practice, as and when more funds are required by companies, they approach the same institutions/banks or certain new institutions/ banks and offer same assets as security for fresh loans.

However, when the same assets are charged for second and subsequent times, a very important question arises as to priority in respect of the charges in favour of different institutions. This situation is managed by securing consent of the earlier lending institutions to the creation of second and subsequent charges on the same assets. With their consents, the charges of all the lending institutions ranks *pari passu*, i.e., on the same footing.

However, the earlier lending institution may not give its consent to the creation of second charge on the ground that the realisable value of the asset charged in its favour is not adequate to cover its loan and as such it cannot share its right of charge with the lending institutions which seek second and subsequent charges.

The real question which alerts the lending institutions is how to ensure that the assets being offered as security for their proposed loans are not already encumbered.

### **Kinds of Charges**

A. On the basis of the nature of charge:

A charge on the property of the company as security for debts may be of the following kinds, namely:

- (i) Fixed or specific charge;
- (ii) Floating charge.

### **Fixed or Specific Charge**

A charge is called fixed or specific when it is created to cover assets which are ascertained and definite or are capable of being ascertained and defined, at the time of creating the charge e.g., land, building, or plant and machinery. A fixed charge, therefore, is a security in terms of certain specific property and the company gives up its right to dispose off that property until the charge is satisfied. In other words, the company can deal with such property, subject to the charge so that the charge holder's interest in the property is not affected and the charge holder gets priority over all subsequent transferees except a bona fide transferee for consideration without notice of the earlier charge. In the winding-up/Liquidation of the company, a debenture holder secured by a specific charge will be placed in the highest ranking class of creditors.

### **Floating Charge**

A floating charge, as a type of security, is peculiar to companies as borrowers. A floating charge is not attached to any definite property but covers property of a fluctuating type e.g., stock-in-trade and is thus necessarily equitable. A floating charge is a charge on a class of assets present and future which in the ordinary course of business is changing from time to time and leaves the company free to deal with the property as it sees fit until the holders of charge take steps to enforce their security. "The essence of a floating charge is that the security remains dormant until it is fixed or crystallised". But a floating security is not a future security. It is a present security, which presently affects all the assets of the company expressed to be included in it. On the other hand, it is not a specific security; the holder of such charge cannot affirm that the assets are specifically mortgaged to him. The assets are mortgaged in such a way that the mortgagor i.e. the company can deal with them without the concurrence of the mortgagee.

The advantage of a floating charge is that the company may continue to deal in any way with the property

which has been charged. The company may sell, mortgage or lease such property in the ordinary course of its business if it is authorised by its memorandum of association.

B. On the basis on the conditions of the charge

- *pari-passu* charge- Under, this the charge is shared by more than one lender in the ratio of their outstanding amount. The prior consent of the existing charge holder is required by the company.
- Exclusive charge- The security under the exclusive charge is provided to a particular lender only.
- Further charge- With the consent on the first charge holder, the particular assets on which charge is already created may be provided to other lenders as second charge. In case of liquidation of assets, the first charge holder has the right to recover his dues and the balance is recovered by the second charge holder followed by others.

## CASE LAWS

Some Judicial pronouncements about different types of charges

1. ***Official Liquidator v. Sri Krishna Deo, (1959) 29 Com Cases 476: AIR 1959 All 247 and Roy & Bros. v. Ramnath Das, (1945) 15 Com Cases 69, 75 (Cal)***. The plant and machinery of a company embedded in the earth or permanently fastened to things attached to the earth became a part of the company's immovable property and therefore apart from the registration under the Companies Act, registration under the Indian Registration Act would also be necessary to make the charge valid and effective.
3. ***Cosslett (Contractors) Ltd., Re, (1996) 1 BCLC 407 (Ch D)*** A construction company's washing machine which was in use at the site was declared under the terms of the contract to be the employer's property during the period of construction. This was held to have created a fixed charge and not a floating charge on the machine because the machine was only one fixed item and was not likely to change.
4. A "floating security", observed ***Lord Macnaghten in Government Stock Investment Company Ltd. v. Manila Rly. Company Ltd., (1897) A.C. 81***, "is an equitable charge on the assets for the time being of a going concern. It attaches to the subject charged in the varying condition in which it happens to be from time to time. It is the essence of such a charge that it remains dormant until the undertaking charged ceases to be a going concern, or until the person in whose favour the charge is created intervenes".
5. ***Illingworth & Another v. Holdsworth & Another, (ibid)***. "A floating charge is ambulatory and shifting in its nature hovering over and so to speak floating with the property which it is intended to affect until some event occurs or act is done which causes it to settle and fasten on the subject of the charge within its reach and grasp.
6. ***Maturi U. Rao v. Pendyala A.I.R. 1970 A.P. 225*** When the floating charge crystallizes it becomes fixed and the assets comprised therein are subject to the same restrictions as the fixed charge.
7. ***In Smith v. Bridgend County Borough Council (2002) 1 BCLC 77 (HC)***, the agreement was held to constitute a floating charge, in so far as it allowed the employer, in various situations of default by the contractor, to sell the contractor's plant and equipment and apply the proceeds in discharge of its obligations. A right to sell an asset belonging to a debtor and appropriate the proceeds to payment of the debt could not be anything other than a charge. It was a floating charge because the property in question was a fluctuating body of assets which could be consumed or removed from the site in the ordinary course of the contractor's business.

### Crystallisation of Floating Charge

A floating charge attaches to the company's property generally and remains dormant till it crystallizes or becomes fixed. The company has a right to carry on its business with the help of assets over which a floating charge has been created till the happening of some event which determines this right. A floating charge crystallises and the security becomes fixed in the following cases:

- (a) when the company goes into liquidation;
- (b) when the company ceases to carry on its business;
- (c) when the creditors or the debenture holders take steps to enforce their security e.g. by appointing receiver to take possession of the property charged;
- (d) on the happening of the event specified in the deed.

In the aforesaid circumstances, the floating charge is said to become fixed or to have crystallised. Until the charge crystallises or attaches or becomes fixed, the company can deal with the property so charged in any manner it likes.

Although a floating charge is a present security, yet it leaves the company free to create a specific mortgage on its property having priority over the floating charge. In *Government Stock Investment Co. Ltd. v. Manila Railway Co. Ltd.*, (1897) A.C. 81, the debentures were secured by a floating charge. Three months' interest became due but the debenture holders took no steps and so the charge did not crystallize but remained floating. The company then made a mortgage of a specific part of its property. Held, the mortgagee had priority. The security for the debentures remained merely a floating security as the debenture holders had taken no steps to enforce their security.

In *Parmanent Houses (Holdings) Ltd.* 1988 BCLC 563(CH D) where a company issued debenture creating a charge in favor of a lending bank mentioning that the charge shall crystallize on happening of an event or default in payment. When the payment was not made on demand by bank, it was held that the charge was no longer a floating charge at the time when receiver was appointed.

### Effect of Crystallisation of a Floating Charge

On crystallization, the floating charge converts into a fixed charge on the property of the company. It has priority over any subsequent equitable charge and other unsecured creditors. But preferential creditors who have priority for payment over secured creditors in the winding-up get priority over the claims of the debenture holders having floating charge.

### Postponement of a Floating Charge

The creation of a floating charge leaves the company free to create a legal and equitable mortgage on the same property until the floating charge crystallises. Where such a mortgage is created it has priority over the floating charge which gets postponed. The floating charge is postponed in favour of the following persons if they act before the crystallization of the security:

- (a) a landlord who distrains for rent;
- (b) a creditor who obtains a garnishee order absolute;
- (c) a judgement creditor who attaches goods of the company and gets them sold (But if the goods are not sold and the debenture holders take action in the meantime, the floating charge has priority);

- (d) the employees of the company, as well as other preferential creditors in the event of winding-up of the company;
- (e) the supplier of goods to the company under a hire-purchase agreement on terms that goods are to remain the property of the seller until they are paid for in full, has priority over the floating charge, whether such hire-purchase agreement is made before or after the issue of the debentures with a floating charge.

Debenture-holders with a floating charge do not, therefore, enjoy the same rights as the secured creditors, for claims against the company. The deed creating the floating charge may, however, contain a clause restricting the power of the company to create charges in priority to or *pari passu* with it. But even in such a case a person who takes mortgage without notice of floating charge gets priority. But such a contingency can be safeguarded by registering the charge. In terms of Section 80 of the Act, where a mortgage or charge on any property or assets of a company or any of its undertakings required to be registered under Section 77 of the Act has been so registered, any person acquiring such property, assets, undertakings or any part thereof or any interest or share therein shall be deemed to have notice of the charge as from the date of such registration.

### **Restraint on the Power to Create Charges with Priority to a Floating Charge**

As the floating charge allows wide powers to the company to deal with its property subject to the floating charge, it is common to insert a clause restricting the powers of the company to create charge with priority to or *pari passu* with it. Thus, if the company creates a mortgage in favour of any person who has notice of the floating charge and restriction, such person ranks after the floating charge. But a person who obtains a valid mortgage, and can show either (i) that he was not aware of the existence of the floating charge; (ii) that though he was aware of the charge, he was not aware of the restriction, is entitled to priority by virtue of the legal estate. Furthermore, where a specific charge is created expressly subject to a floating charge, the specific charge is postponed as from the date when the floating charge crystallises by the appointment of a receiver.

### **Invalidity of Floating Charge**

A floating charge remains afloat until a winding up commences, unless it has already crystallised through the intervention of the debenture holders or the creditors. Also, a floating charge is valid only against the unsecured creditors, whether in a winding-up/liquidation or otherwise. But the Act prevents an unsecured creditor to get priority over the other creditors by obtaining a liquidation/floating charge when he learns that the company's liquidation is imminent.

Accordingly, Section 332 of the Companies Act, 2013 provides that a floating charge on the undertakings or property of the company, which is created within 12 months immediately preceding the commencement of the winding up proceedings of a company shall be invalid, unless it is proved that the company was solvent immediately after the creation of the charge. But the charge will be valid to the extent of the amount of any cash paid to the company at the time of or after the creation of, and in consideration for the charge, together with interest on that amount at 5 per cent per annum or such other rate as may be notified by the Central Government.

### **WHAT IS A MORTGAGE?**

A mortgage is the transfer of an interest in specific immoveable property for the purpose of securing the payment of money advanced or to be advanced by way of loan, an existing or future debt or the performance of an agreement which may give rise to pecuniary liability.

**Difference between Mortgage and Charge**

S. No.	Mortgage	Charge
1	A mortgage is created by the act of the parties.	A charge may be created either through the act of parties or by operation of law.
2	A mortgage requires registration under the Transfer of Property Act, 1882.	A charge created by operation of law does not require registration. But a charge created by act of parties requires registration.
3	A mortgage is for a fixed term.	The charge may be in perpetuity.
4	A mortgage is a transfer of an interest in specific immovable property.	A charge only gives a right to receive payment out of a particular property.
5	A mortgage is good against subsequent transferees mortgage is good against subsequent transferees.	A charge is good against subsequent transferees with notice.
6	A simple mortgage carries personal liability unless excluded by express contract.	In case of charge, no personal liability is created. However, where a charge is the result of a contract, there may be a personal remedy.
7	A mortgage is a transfer of an interest in a specific immovable property.	There is no such transfer of interest in the case of a charge. Charge does not operate as transfer of an interest in the property and a transferee of the property gets the property free from the charge provided he purchases it for value without notice of the charge.

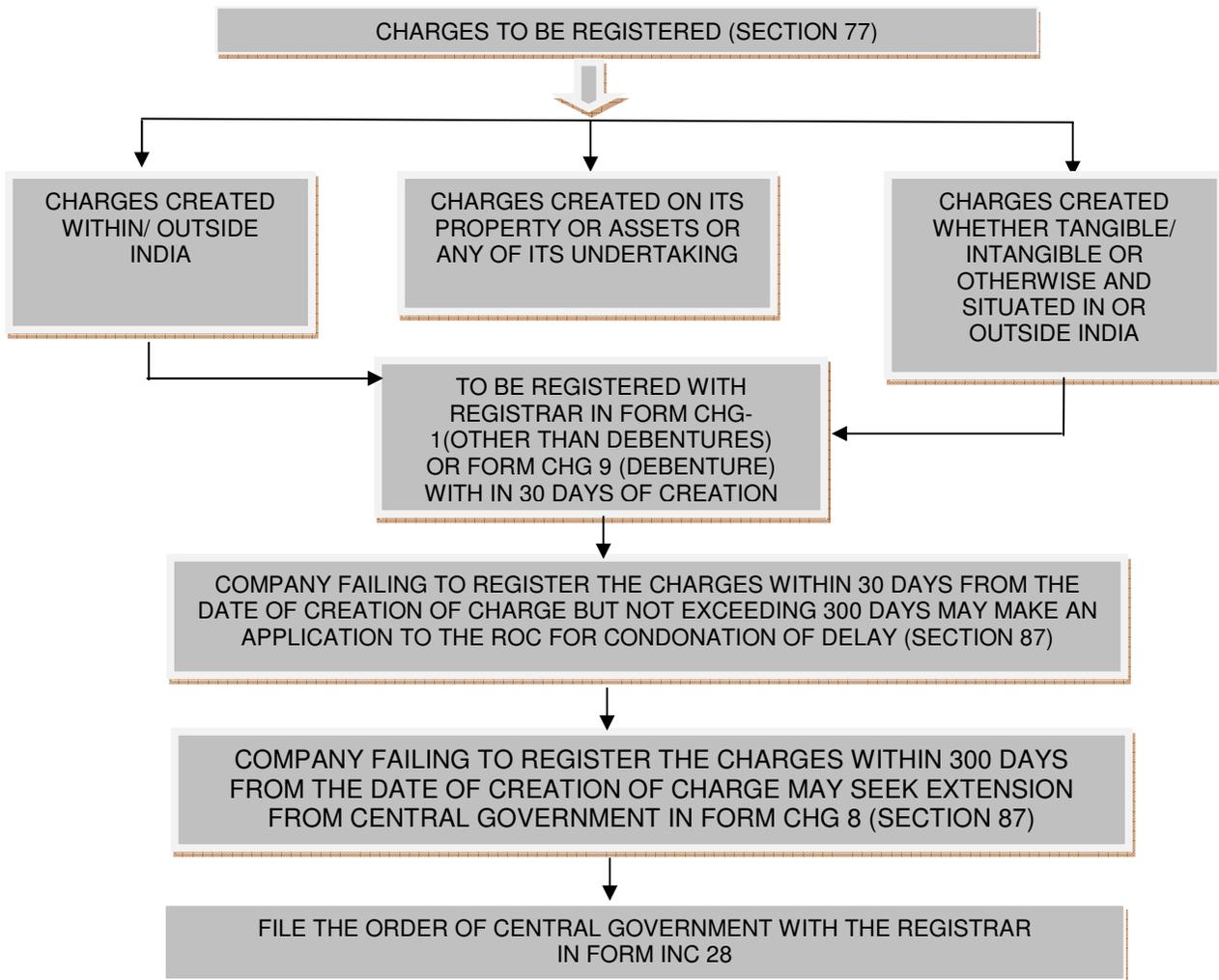
**CHARGE AND PLEDGE DISTINGUISHED**

According to the generally accepted definition, a 'pledge' is a bailment of personal property as security for some debt or engagement, redeemable on certain terms, and with an implied power of sale on default. It consists of a delivery of goods by a debtor to his creditor as security for a debt or other obligation, to be held until the debt is repaid along with interest or other obligation of the debtor is discharged, and then to be delivered back to the pledger, the title not being changed during the continuance of the pledge.

Unlike a pledge, a 'charge' is not a transfer of property of one to another. It is a right created in favour of one, referred to as "the lender" in the immovable property of another, referred to as "the borrower", as security for repayment of the loan and payment of interest on the terms and conditions contained in the loan documents evidencing charge.

Both a pledge and a charge are the result of voluntary act of parties. Both create security but the nature of the security is different.

## REGISTRATION OF CHARGES- PROVISIONS OF COMPANIES ACT, 2013



### Registration of charges- Section 77(1)

Any charge created

- (a) within or outside India,
- (b) on its property or assets or any of its undertakings,
- (c) whether tangible or otherwise, and situated in or outside India

Shall be registered.

- (i) Particulars of charges that is being filed with Registrar of Companies is to be signed by the company creating the charge and the charge holder in Form No. CHG-1 (for other than Debentures) or Form CHG-9 (for debentures) as the case may be.
- (ii) The Charge has to be registered within 30 days of its creation. It may be registered on an application by the company to the registrar beyond 30 days but before 300 days on payment of additional fees.

Fourth Proviso to Section 77(1) states that the section w.r.t. registration of charges, shall not apply to such charges as may be prescribed in consultation with the Reserve Bank of India.

### **Condonation of delay by Registrar- within 300 days from the date of creation of charge/its modification**

Proviso to Section 77(1) states that the Registrar may on an application by the company allow registration of charge within three hundred days of creation or modification of charge on payment of additional fee. The Registrar may, on being satisfied that the company had sufficient cause for not filing the particulars and instrument of charge, if any, within a period of thirty days of the date of creation of the charge, allow the registration of the same after thirty days but within a period of three hundred days of the date of such creation of charge or modification of charge on payment of additional fee.

The application for delay shall be made and supported by a declaration from the company signed by its secretary or director that such belated filing shall not adversely affect rights of any other intervening creditors of the company.

### **Condonation of delay by the Central Government beyond 300 days from the date of creation**

If company fails to register the charge even within this period of three hundred days, it may seek extension of time in accordance with Section 87 from the Central Government.

Section 87 (1) states that the Central Government on being satisfied that—

- (i) (a) the omission to file with the Registrar the particulars of any charge created by a company or any charge subject to which any property has been acquired by a company or any modification of such charge; or
- (b) the omission to register any charge within the time required under this Chapter or the omission to give intimation to the Registrar of the payment or the satisfaction of a charge, within the time required under this Chapter; or
- (c) the omission or mis-statement of any particular with respect to any such charge or modification or with respect to any memorandum of satisfaction or other entry made, was accidental or due to inadvertence or some other sufficient cause or it is not of a nature to prejudice the position of creditors or shareholders of the company; or
- (ii) on any other grounds, it is just and equitable to grant relief,

it may on the application of the company or any person interested and on such terms and conditions as it may seem to the Central Government just and expedient, direct that the time for the filing of the particulars or for the registration of the charge or for the giving of intimation of payment or satisfaction shall be extended or, as the case may require, that the omission or mis-statement shall be rectified.

Section 87 (2) states that when the Central Government extends the time for the registration of a charge, the order shall not prejudice any rights acquired in respect of the property concerned before the charge is actually registered.

### ***Rule 12 of Companies (Registration of Charges) Rules, 2014***

When the instrument creating or modifying a charge is not filed within a period of three hundred days from the date of its creation (including acquisition of a property subject to a charge) or modification and where the satisfaction of the charge is not filed within thirty days from the date on which such payment of satisfaction, the Registrar shall not register the same unless the delay is condoned by the Central Government.

The application for condonation of delay and for such other matters covered in sub-clause (a), (b) and (c) of clause (i) of sub-section (1) of section 87 of the Act shall be filed with the Central Government in Form No.CHG-8 along with the fee.

The order passed by the Central Government under sub-section (1) of section 87 of the Act shall be required to be filed with the Registrar in Form No.INC.28 along with the fee as per the conditions stipulated in the said order.

### **SUBSEQUENT REGISTRATION SHALL NOT PREJUDICE ANY RIGHT**

Third Proviso to Section 77(1) states that any subsequent registration of a charge shall not prejudice any right acquired in respect of any property before the charge is actually registered.

### **Application for registration of charge by the charge-holder, when company fails to register a charge**

According to Section 78 where a company fails to register the charge within the period of 30 days referred to in sub-section (i) of Section 77, the person in whose favour the charge is created may apply to the Registrar for registration of the charge alongwith the instrument created for the charge in Form No.CHG-1 or Form No.CHG-9, as the case may be, duly signed along with fee.

The registrar may, on such application, give notice to the company about such application. The company may either itself register the charge or shows sufficient cause why such charge should not be registered.

On failure on part of the company, the Registrar may allow registration of such charge within fourteen days after giving notice to the company shall allow such registration.

Where registration is affected on application of the person in whose favour the charge is created, that person shall be entitled to recover from the company, the amount of any fee or additional fees paid by him to the Registrar for the purpose of registration of charge.

### **Certificate of Registration of Charge/ Modification of charge**

According to Section 77(2) read with Rule 6 of Companies (Registration of Charges) Rules, 2014, when a charge is registered with the Registrar, Registrar shall issue a certificate of registration of charge in Form No.CHG-2 and for registration of modification of charge in Form No.CHG-3 to the company and to the person in whose favour the charge is created.

The certificate issued by the Registrar whether in case of registration of charge or registration of modification, as the case may be shall be conclusive evidence that the requirements of Chapter VI of the Act (Registration of Charges) and the rules made thereunder as to registration of creation or modification of charge, as the case may be, have been complied with.

Further, Section 77(3) provides that no charge created by the company shall be taken into account by the liquidator appointed under this Act or the Insolvency and Bankruptcy Code, 2016, as the case may be, or any other creditor unless it is duly registered and a certificate of registration is given by the Registrar. However, this does not prejudice any contract or obligation for the repayment of the money secured by a charge.

### **Acquiring Property under Charge and Modification of Charge**

Section 79 of the Act makes it clear that the requirement of registering the charge shall also apply to a company acquiring any property subject to charge or any modification in terms and conditions of any charge already registered.

The provisions relating to condonation of delay shall apply, *mutatis mutandis*, to the registration of charge on any property acquired subject to such charge and modification of charge under section 79 of the Act.

### Verification of Instruments

According to Rule 3(4) of the Companies (Registration of Charges) Rules, 2014, a copy of every instrument evidencing any creation or modification of charge and required to be filed with the Registrar in pursuance of section 77, 78 or 79 shall be verified as follows:

- (a) where the instrument or deed relates solely to the property situated outside India, the copy shall be verified by a certificate issued either under the seal of the company, or under the hand of any Director or Company Secretary of the company or an authorised officer of the charge holder or under the hand of some person other than the company who is interested in the mortgage or charge;
- (b) where the instrument or deed relates, whether wholly or partly, to the property situated in India, the copy shall be verified by a certificate issued under the hand of any Director or Company Secretary of the company or an authorised officer of the charge holder.

### Satisfaction of Charges

According to section 82 read with the rules, the company shall give intimation to the Registrar of the payment or satisfaction in full of any charge within a period of thirty days from the date of such payment or satisfaction in Form No.CHG-4 along with the fee. The Registrar may, on an application by the company or the charge holder, allow such intimation of payment or satisfaction to be made within a period of three hundred days of such payment or satisfaction on payment of such additional fees as may be prescribed.

On receipt of such intimation, the Registrar shall issue a notice to the holder of the charge calling a show cause within such time not exceeding fourteen days, as to why payment or satisfaction in full should not be recorded as intimated to the Registrar. If no cause is shown, by such holder of the charge, the Registrar shall order that a memorandum of satisfaction shall be entered in the register of charges maintained by the Registrar under section 81 and shall inform the company. If the cause is shown to the Registrar shall record a note to that effect in the register of charges and shall inform the company accordingly.

However the aforesaid notice shall not be sent, in case intimation to the registrar is in specified form and is signed by the holder of charge. [Proviso to Section 82(2)]

### Power of registrar to make entries of satisfaction in absence of intimation from the company:

There may be times where a company may fail to send intimation of satisfaction of charge to the Registrar but according to section 83 of the Act, registrar may on receipt of satisfactory evidence of satisfaction register memorandum of satisfaction. The evidences may be –

- (a) The debt for which the charge was given has been paid or satisfied in whole or in part; or
- (b) Part of the property or undertaking charged has been released from the charge;
- (c) Part of the property or undertaking ceased to form part of the company's property or undertaking.

The Registrar may enter in the register of charges a memorandum of satisfaction.

Section 83(2) states that the Registrar shall inform affected parties within thirty days of making the entry in the register of charges.

Certificate of registration of satisfaction of charge: Where the Registrar enters a memorandum of satisfaction

of charge in full in pursuance of section 82 or 83, he shall issue a certificate of registration of satisfaction of charge in Form No.CHG-5.

### **Notice of Charge**

According to section 80, where any charge on any property or assets of a company or any of its undertakings is registered under section 77, any person acquiring such property, assets, undertakings or part thereof or any share or interest therein shall be deemed to have notice of the charge from the date of such registration. The section clarifies that if any person acquires a property, assets or undertaking for which a charge is already registered, it would be deemed that he has complete knowledge of charge from the date the charge is registered.

### **Register of Charges Maintained in ROC's Office**

In accordance with section 81 and the rules the Registrar of Companies shall maintain a register containing particulars of the charges registered in respect of every company. The particulars of charges maintained on the Ministry of Corporate Affairs portal ([www.mca.gov.in/MCA21](http://www.mca.gov.in/MCA21)) shall be deemed to be the register of charges for the purposes of section 81 of the Act.

This charge register shall be open to inspection by any person on payment of fee for each inspection.

### **Intimation of appointment of receiver or manager**

Section 84 provides that if any person obtains an order for the appointment of a receiver of, or of a person to manage, the property, subject to a charge, of a company or if any person appoints such receiver or person under any power contained in any instrument, he shall, within a period of thirty days from the date of the passing of the order or of the making of the appointment, give notice of such appointment to the company and the Registrar along with a copy of the order or instrument and the Registrar shall, on payment of the prescribed fees, register particulars of the receiver, person or instrument in the register of charges.

Section 84(2) states that any person so appointed shall, on ceasing to hold such appointment, give to the company and the Registrar a notice to that effect and the Registrar shall register such notice.

As per Rule 9 the notice of appointment or cessation of a receiver of, or of a person to manage, the property, subject to charge, of a company shall be filed with the Registrar in Form No. CHG.6 along with fee.

### **Company's Register of Charges**

Section 85 read with rule 10 provides that every company shall keep at its registered office a register of charges in Form No. CHG.7 which shall include therein all charges and floating charges affecting any property or assets of the company or any of its undertakings, indicating in each case such particulars as may be prescribed.

The entries in the register of charges maintained by the company shall be made forthwith after the creation, modification or satisfaction of charge, as the case may be.

Such register of charges shall contain the particulars of all the charges registered with the Registrar on any of the property, assets or undertaking of the company and the particulars of any property acquired subject to a charge as well as particulars of any modification of a charge and satisfaction of charge.

All the entries in the register shall be authenticated by a director or the secretary of the company or any other person authorised by the Board for the purpose.

The register of charges shall be preserved permanently and the instrument creating a charge or modification thereon shall be preserved for a period of eight years from the date of satisfaction of charge by the company.

A copy of the instrument creating the charge shall also be kept at the registered office of the company along with the register of charges.

### Inspection of Charges – Section 85(2)

The register of charges and the instrument of charges kept by the company shall be open for inspection –

- (a) by any member or creditor of the company without fees;
- (b) by any other person on payment of fee subject to reasonable restriction as the company by its articles impose.

Liquidator or any other creditor take into account the unregistered charges.

### GIST OF E-FILING UNDER CHARGE MANAGEMENT

S.No.	E-Form	Purpose
1	CHG-1	Application for registration of creating or modifying the charge (for other than Debentures)
2	CHG-2	Certificate of registration
3	CHG-3	Certificate of modification of charge
4	CHG-4	intimation of the satisfaction to the Registrar
5	CHG-5	Memorandum of satisfaction of charge
6	CHG-6	Notice of appointment or cessation of receiver or manager
7	CHG-7	Register of charges
8	CHG-8	Application for condonation of delay shall be filed with the Central Government
9	CHG-9	Creating or modifying the charge in (for debentures including rectification)

### CONSEQUENCES OF NON-REGISTRATION OF CHARGE

According to Section 77 of the Companies Act, 2013, all types of charges created by a company are to be registered by the ROC, where they are non-compliant and are not filed with the Registrar of Companies for registration, it shall be void as against the liquidator and any other creditor of the company. In the case of *ONGC Ltd v. Official Liquidators of Ambica Mills Co Ltd* (2006) 132 Comp Cas 606 (Guj), the ONGC had not been able to point out whether the so called charge, on the basis of which it was claiming preference as a secured creditor, was registered or not. It was held that in the light of this failure, ONGC could not be treated as a secured creditor in view of specific provisions of section 125 and the statutory requirement under the said section. This does not, however, mean that the charge is altogether void and the debt is not recoverable. So long as the company does not go into liquidation, the charge is good and may be enforced.

**Void against the liquidator** means that the liquidator on winding up of the company can ignore the charge

and can treat the concerned creditor as unsecured creditor. The property will be treated as free of charge i.e. the creditor cannot sell the property to recover its dues.

**Void against any creditor** of the company means that if any subsequent charge is created on the same property and the earlier charge is not registered, the earlier charge would have no consequence and the latter charge if registered would enjoy priority. In other words, the latter charge holder can have the property sold in order to recover its money.

Thus, non-filing of particulars of a charge does not invalidate the charge against the company as a going concern. It is void only against the liquidator and the creditors at the time of liquidation. The company itself cannot have a cause of action arising out of non-registration [Independent Automatic Sales Ltd. vs. Knowles & Foster (1962) 32 Comp Cas].

## **PARTICULARS OF CHARGES**

The following particulars in respect of each charge are required to be filed with the Registrar:

- (a) date and description of instrument creating charge;
- (b) total amount secured by the charge;
- (c) date of the resolution authorising the creation of the charge; (in case of issue of secured debentures only);
- (d) general description of the property charged;
- (e) a copy of the deed/instrument containing the charge duly certified or if there is no such deed, any other document evidencing the creation of the charge to be enclosed;
- (f) list of the terms and conditions of the loan; and
- (g) name and address of the charge holder.

## **PROCEDURE FOR REGISTRATION OF CREATION/MODIFICATION SATISFACTION OF CHARGE**

If a company has passed special resolutions under Section 180(2) authorising its Board of directors to borrow funds for the requirements of the company and under Section 180(1)(a), authorising its Board of directors to create charge on the assets and properties of the company to provide security for repayment of the borrowings in favour of the financial institutions/banks or lenders and in exercise of that authority has signed the loan documents and now proposes to have the charge, created it should follow the procedure detailed below:

1. Where the special resolution as required under section 180 is passed, Form MGT-14 of the Companies (Management and Administration) Rules, 2014 is to be filed with the Registrar.
2. According to section 77, every company creating any charge created within or outside India on property or assets or any of the company's undertakings whether tangible or otherwise, situated in or outside India shall have to be registered. For the purpose of creating/ modifying a charge file particulars of the charge with the concerned Registrar of Companies within thirty days of creating the Form No.CHG-1 (for other than Debentures) or Form No.CHG-9 (for debentures including rectification), as the case may be.

3. Attach the following documents with e-Form No. CHG-9 / CHG-1:
  - (a) A certified true copy of every instrument evidencing any creation or modification of charge;
  - (b) In case of joint charge and consortium finance, particulars of other charge holders;
  - (c) Instrument(s) evidencing creation or modification of charge in case of acquisition of property which is already subject to charge together with the instrument evidencing such acquisitions.
4. Payment of fees can be made online in accordance with Annexure 'B' of Companies (Registration offices and fees) Rules, 2014. Electronic payments through internet can be made either by credit card or by internet banking facility.
5. If the particulars of charge cannot be filed within thirty days due to unavoidable reasons, then it may be filed within three hundred days of such creation after payment of such additional fee as prescribed under Annexure 'B' of Companies (Registration offices and fees) Rules, 2014.
6. Such application for delay to the Registrar shall be made in Form No. CHG-1 and supported by a declaration from the company signed by its secretary or director that such belated filing shall not adversely affect rights of any other intervening creditors of the company.
7. Where a charge is registered Registrar will issue a certificate of registration of such charge in Form No. CHG-2. Where the particulars of modification of charge are registered the Registrar shall issue a certificate of modification of charge in Form No. CHG-3.
8. A company shall within a period of thirty days from the date of the payment or satisfaction in full of any charge registered, give intimation of the same to the Registrar in Form No. CHG-4 along with the fee as prescribed under Annexure 'B' of Companies (Registration Offices and Fees) Rules, 2014.
9. Where the Registrar enters a memorandum of satisfaction of charge in full, obtain a certificate of registration of satisfaction of charge in Form No. CHG-5.
10. Incorporate changes in relation to creation, modification and satisfaction of charge in the register of charges maintained by the company in Form No. CHG.7 and enter therein particulars of all the charges registered with the Registrar on any of the property, assets or undertaking of the company and the particulars of any property acquired subject to a charge as well as particulars of any modification of a charge and satisfaction of charge. Such register is to be kept at the registered office of the company.
11. All the entries in the register shall be authenticated by a director or the secretary of the company or any other person authorised by the Board for the purpose.
12. The register of charges shall be preserved permanently and the instrument creating a charge or modification thereon shall be preserved for a period of eight years from the date of satisfaction of charge by the company.
13. Where the satisfaction of the charge is not filed with the Registrar within thirty days from the date on such payment of satisfaction, an application for condonation of delay shall be filed with the Central Government in Form No. CHG-8 along with the fee as prescribed under Annexure 'B' of Companies (Registration Offices and Fees) Rules, 2014.
14. Where the instrument creating or modifying a charge is not filed with the Registrar within a period of three hundred days from the date of its creation (including acquisition of a property subject to a

charge) or modification an application for condonation of delay shall be filed with the Central Government in Form No.CHG-8 along with the fee as prescribed under Annexure 'B' of Companies (Registration Offices and Fees) Rules, 2014.

15. The order passed by the Central Government shall be required to be filed with the Registrar in Form No.INC.28 along with the fee as per the conditions stipulated in the said order.
16. For all other matters other than condonation of delay, application shall be made to the Central Government in Form No.CHG-8 along with the fee.

**ANNEXURES**

**(1) Specimen of special resolution under Section 180 (3) (c) authorising the Board to borrow for company's business upto a limit beyond paid up capital and free reserves**

Special resolution

**To consider and, if thought fit, to pass with or without modification(s), the following resolution as Special Resolution:**

“RESOLVED THAT pursuant to the provisions of Section 180(3)(c) and other applicable provisions, if any, of the Companies Act, 2013, and subject to such approval as may be necessary, consent of the company be and is hereby accorded to the Board of directors of the company for borrowing, from time to time, such sum of money as may not exceed Rs. .... (Rupees ..... ), for the purpose of the business of the company, notwithstanding that the moneys to be borrowed together with the monies already borrowed (apart from temporary loans obtained from the company's bankers in the ordinary course of business) will exceed the aggregate of the paid-up capital of the company and its free reserves, that is to say, the reserves not set apart for any specific purpose, provided that the total amount upto which the monies may be borrowed by the Board of directors of the company shall not exceed the aggregate of the paid-up capital and free reserves of the company by more than the sum of '..... (Rupees ..... ) at any one time.

Resolved further that the Board be and is hereby authorized to do all the acts, deed and things as it may in its absolute discretion deem necessary and appropriate to give effect to the above resolution”

**Explanatory Statement**

The shareholders of the company had, at the extraordinary general meeting of the company held on ....., passed a special resolution under Section 180 (3) (c) for borrowing the maximum amount of Rupees ....., upto which the Board of directors of the company could borrow funds from financial institutions and banks in excess of the company's paid-up capital and free reserves. However, in view of the increased business activities of the company, the said ceiling of Rupees (.....) has been found to be inadequate. Your directors are of the opinion that the ceiling of borrowings by the Board be raised to rupees one hundred crore.

Hence the proposed resolution for consideration and approval by the members of the company. None of the directors is concerned or interested in the proposed resolution.

**(2) Specimen of resolution under Section 180(1)(a) for creating charge on company's assets and properties**

1. To consider and, if thought fit, to pass with or without modification(s), the following as Special Resolution;

“RESOLVED THAT consent of the Company be and is hereby accorded in terms of Section 180(1) (a) and other applicable provisions, if any, of the Companies Act, 2013 or any modification or re-enactment thereof, to mortgaging and/or charging by the Board of directors of the Company by way of equitable and/or legal mortgage on such immovable and movable properties of the Company, both present and future, together with power to takeover the assets of the Company in certain events, to or in favour of Industrial Development Bank of India (IDBI) and The Industrial Finance Corporation of India Ltd. (IFCI) by way of first pari passu Charge to secure the Rupee Term Loans of ₹1000.00 lacs and ` 880.00 lacs respectively granted to the Company together with interest at the agreed rate(s), liquidated damages, front end fees, premia on pre payment, costs, charges, expenses and all other moneys payable by the Company under the Loan Agreements, Deeds of Hypothecation and other documents executed/to be executed by the Company in respect of the Term Loans of IDBI and IFCI.

RESOLVED FURTHER THAT the Board of directors be and is hereby authorised and shall always be deemed to have been authorised to finalise with IDBI and IFCI the documents for creating the aforesaid mortgage and/ or charge and to do all acts, deeds and things as may be necessary for giving effect to the above resolution.”

2. To consider and, if thought fit, to pass with or without modification(s), the following as Special Resolution;

“RESOLVED THAT consent of the Company be and is hereby accorded in terms of Section 180(1)(a) and other applicable provisions, if any, of the Companies Act, 2013 or any modification or re-enactment thereof, to mortgaging and/or charging by the Board of directors of the Company by way of equitable and/or legal mortgage on such immovable and movable properties of the Company, both present and future, in favour of State Bank of India, New Delhi the Company's Bankers by way of Second Charge to secure the various fund based/non-fund based credit facilities granted/to be granted to the Company and the interest at the agreed rate, costs, charges, expenses and all other moneys payable by the Company under the Deed(s) of Hypothecation and other documents executed/to be executed by the Company in respect of credit facilities of State Bank of India, in such form and manner as may be acceptable to State Bank of India.

RESOLVED FURTHER THAT the Board of directors be and is hereby authorised and shall always be deemed to have been authorised to finalise with State Bank of India the documents for creating the aforesaid mortgage and/or charge and to do all acts, deeds and things as may be necessary for giving effect to the above resolution.”

**Explanatory Statement Item No. 1 & 2**

Industrial Development Bank of India (IDBI) and The Industrial Finance Corporation of India Ltd. (IFC) have sanctioned Term Loans of ₹1000.00 lacs and ₹880.00 lacs respectively to the company. These loans are to be secured by First Charge on immovable and movable properties of the Company, both present and future, in the manner, as may be required by IDBI and IFCI. Such mortgage/charge shall rank first pari passu Charge with the Charges already created/to be created in favour of the participating Institutions/Banks for their assistances.

State Bank of India, New Delhi has also agreed to grant, in principle, various fund based/non-fund based Cash Credit facilities to the Company. According to the conditions of granting such facilities to the Company, these facilities are required to be secured by a second charge by way of equitable and/or legal mortgage on all the immovable and movable properties of the Company, both present and future on such terms as may be agreed to between the Company, State Bank of India and other existing lenders.

Section 180(1)(a) of the Companies Act, 2013 provides, inter alia, that the Board of directors of a public company shall not, without the consent of a public company in general meeting, sell, lease or otherwise dispose of the whole, or substantially the whole, of the undertaking(s) of the Company or where the Company owns more than one undertaking, of the whole or substantially the whole of any such undertaking. Mortgaging/charging of the immovable and movable properties of the Company as aforesaid to secure Rupee Term Loans and the various Cash Credit facilities may be regarded as disposal of the whole or substantially the whole of the said undertaking(s) of the Company and therefore requires consent of the Company pursuant to Section 180(1)(a) of the Companies Act, 2013.

The Directors recommend the resolutions for approval of the shareholders as ordinary resolutions under Section 180(1)(a) of the Companies Act, 2013.

None of the Directors are concerned or interested in the proposed resolutions.

**(3) Specimen of the Board Resolution under Section 179(3)(d) to borrow Moneys within the authority of the Board.**

The Chairman informed the Board that The Industrial Finance Corporation of India Ltd. (IFCI), New Delhi, has at the request of the company, sanctioned Rupee Term Loan of '..... to meet a part of the cost of Modernisation-cum-Expansion scheme comprising replacement of the existing old stainless steel Distillation plant by copper Distillation Plant, installation of an additional MS Digester and construction of storage lagoons as stipulated by the Pollution Control Board at the Company's existing factory at .....

A copy of the letter of sanction no..... dated ..... received from IFCI (a copy whereof duly signed by the Chairman for the purpose of identification was placed on the table of the meeting).

After some discussions, the following resolution was passed unanimously:-

**(I) RESOLVED**

1. That the Company do accept the offer of The Industrial Finance Corporation of India Ltd. (IFCI) vide their letter no..... dated ..... to grant to the company rupee term loan of '..... (Rupees..... only) (hereinafter referred to as 'the said Term Loan') on the terms and conditions contained in the Letter of Intent no ..... dated ..... received from IFCI (copy whereof was placed on the table at the meeting).
2. That Shri..... and Shri ..... be and are hereby authorised severally to convey to IFCI acceptance on behalf of the Company of the said offer for financial assistance on the terms and conditions contained in their Letter of Intent referred to above and agree to such changes and modifications in the said terms and conditions as may be suggested and acceptable to IFCI from time to time and to execute such deeds, documents and other writings as may be necessary or required for this purpose.
3. That the company do borrow from IFCI the said term loan of '..... (Rupees..... only) on the terms and conditions set out in the General Conditions No. GC-1-99 applicable to

assistance provided by IFCI (hereinafter referred to as 'The General Conditions') and in the Standard Form of Loan Agreement for rupee term loan in addition to the special terms and conditions mentioned in the Letter of Intent no..... dated ..... received from IFCI (Copies whereof were placed on the table at the meeting) and also avail of interim disbursement(s) from time to time as may be allowed by IFCI.

4. That the IFCI will be at liberty to appoint and remove, at its sole discretion, Nominee Director(s) on the Board of directors of the Company from the date of the passing of this resolution and that the appointment of the Nominee director(s) shall not be construed as any commitment on the part of IFCI to grant/ disburse and sanctioned assistance.
5. That the aforesaid Standard Forms of Loan Agreement(s) be and are hereby approved and Shri..... and Shri..... be and are hereby severally authorised to accept on behalf of the Company such modifications therein as may be acceptable to IFCI and finalise the same.
6. That the Common Seal of the Company be affixed to the stamped engrossment(s) in duplicate of the loan agreement(s) (as per the standard form(s) with such modifications as may be agreed to between IFCI and the company) in the presence of one of the officers i.e. Shri ..... and Shri ..... who shall sign the same in token thereof.
7. That the Company shall execute the Loan Agreement(s) relating to the above facilities within the period stipulated by IFCI, the condition being that till such agreement being executed there is no binding obligation or commitment on the part of IFCI to advance any money or incur any obligation thereunder.
8. That the standard forms of the following documents namely:
  - (i) Deed of Hypothecation
  - (ii) Undertaking for meeting shortfall/overrun
  - (iii) Undertaking regarding non-disposal of shareholdings
  - (iv) General Declaration and Undertaking(s) placed before the meeting be and are hereby approved and that Shri..... of the Company be and are hereby severally authorised to finalise, on behalf of the company, the said documents and also to approve and finalise such other deeds, documents and writings as may be required by IFCI in connection with the above facilities.
9. That the Common Seal of the Company be affixed to the stamped engrossment(s) of the Deed of Hypothecation and to such other documents as may be required to be executed under the Common Seal of the company in favour of IFCI to secure the aforesaid facilities in the presence of one of the officers i.e. Shri ..... and Shri..... who shall sign the same in token thereof.
10. That Shri..... and Shri..... of the Company be and are hereby severally authorised to accept amendments to such executed loan agreement/deed of hypothecation and other documents as and when become necessary and to sign letter(s) of undertakings, declarations, agreements and other papers which the company may be required to sign for availing of the required facilities and, if so required, the Common Seal of the Company be affixed thereto in the presence of any one of the said officers, who shall sign the same in token thereof as required by the Articles of Association of the Company.

11. That the company do file the particulars of the charge(s) to be created in favour of the IFCI with the concerned Registrar of Companies within the time prescribed by law therefor.
12. That the copies of foregoing resolutions certified to be true copy by the Company Secretary be furnished to the IFCI and they be requested to act thereon.

### LESSON ROUND UP

- A charge is a right created by any person including a company referred to as “the borrower” on its assets and properties, present and future, in favour of a financial institution or a bank, referred to as “the lender”, which has agreed to extend financial assistance. The power of the company to borrow includes the power to give security also.
- Mortgage is created by the act of parties whereas a charge may be created either through the act of parties or by operation of law.
- A company is required to file e-form CHG-1 or CHG-2 through MCA portal giving complete particulars together with the instrument creating charge within 30 days of creation of charge under Section 77 of the Companies Act, 2013.
- For intimating modification of charge, e-form CHG-1 or CHG-2 is required to be filed within 30 days of modification. A variation in the rate of interest payable on the loan amount by the borrowing company to the lending institution or the bank will constitute a modification of charge, unless the terms of variation are covered in the original charge.
- A registration of charge constitutes a notice to whosoever acquires a future interest in the charged assets.
- In e-governance era, there is a facility for inspection of charge through electronic means using internet.
- The certificate issued by the Registrar whether in case of registration of charge or registration of modification, shall be conclusive evidence that the requirements of Chapter VI of the Act (Registration of Charges) and the rules made thereunder as to registration of creation or modification of charge, as the case may be, have been complied with.
- Every company is required to keep at its registered office a register of all charges as well as a copy of every instrument creating any charge.
- Company may apply to Central Government for extension of time for filing particulars to ROC for creation, modification or satisfaction of charge in form CHG-8.
- Company or any person interested in the charge can make an application to the Central Government for rectification of Register of charges in form CHG-8.
- For intimating memorandum of satisfaction of charge to ROC, e-form CHG-5 is required to be filed within 30 days from the date of such satisfaction.

### GLOSSARY

Garnishee Charge	<p>An individual who holds money or property that belongs to a debtor subject to an attachment proceeding by a creditor.</p> <p>A charge is a security given for securing loans or debentures by way of a mortgage on the assets of the company. As mentioned earlier, the power of the company to borrow includes the power to give security also.</p>
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# Lesson 6

## Distribution of Profits

### LESSON OUTLINE

- Meaning and Definition of Dividend
- Declaration of Dividend
- Unpaid Dividend
- Procedure of declaration of Dividend
- Declaration of dividend out of reserves
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

Declaration and Payment of Dividend is dealt in Chapter VIII of Companies Act 2013 read with Companies (Declaration and Payment of Dividend) Rules, 2014, it broadly covers transfer of profits to reserves, maximum dividend that can be declared, declaration of dividend in case of inadequacy of profits, maintenance of separate bank account for distribution of dividend, transfer of Unpaid Dividend to Unpaid Dividend Account and Investor Protection and enhanced penalty etc. The chapter also covers fundamental aspects from Secretarial Standard on Dividend (SS-3), adherence to which is recommendatory in nature.

Company Secretary is the bridge between the shareholders and the company. Many a times he is the investor relation officer of the company. He is expected to be well versed with the provisions and on the other hand he should be capable enough to guide the management on any practical issue relating to dividend. After reading this lesson you will be able to understand the legal and procedural aspects relating to distribution of dividend, transfer of unpaid or unclaimed dividend to Unpaid Dividend Account and transfer of unpaid dividend to Investor Education and Protection Fund (IEPF), utilization of IEPF etc.

## INTRODUCTION

Profit or a portion of profit that can be legally distributed as a dividend to the shareholders is known as Divisible Profit. All profit of the company is not divisible and number of factors should be considered while determining divisible profit of the company. Hence, profits available for dividend to shareholders are known as divisible profits. On the other hand dividend refers to a reward that a company gives to its shareholders. A company's dividend is decided by its board of directors and it requires the shareholders' approval. Dividend is usually a part of the profit that the company shares with its shareholders.

Dividends cannot be declared except out of profits. If a company declares and pays a dividend in the absence of profits, the directors will have to make good the amount to the company from their own pockets.

## MEANING AND DEFINITION OF DIVIDEND

A dividend is a distribution of a portion of a company's earnings, decided by the board of directors, to a class of its shareholders. A share of the after-tax profit of a company, distributed to its shareholders according to the number and class of shares held by them is called dividend. The amount and timing of the dividend is decided by the board of directors, who also determine whether it is paid out of current earnings or the past earnings kept as reserve.

Holders of preference shares receive dividend at a predetermined fixed rate and are paid first. However, 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. [*Ewing v. Israel & Oppenheimer Ltd.* (1918) 1 Ch. 101].

Holders of equity shares are entitled to receive any amount of dividend, based on the level of profit and the company's need for cash for expansion or other purposes.

Dividend defined under section 2(35) of the Companies Act, 2013, includes any interim dividend.

SS-3 defines dividend so as to mean a distribution of any sums to Members out of profits and wherever permitted out of free reserves available for the purpose.

The power to pay dividend is inherent in a company and is not derived from the Companies Act, 2013 or the Memorandum or Articles of Association although the Act and the Articles regulate the manner in which dividends are to be declared.

Right to claim dividend will only arise after a dividend is declared by the company in general meeting and until and unless it is so declared, the shareholder has no claim against the company in respect of it. The observation of the Bombay High Court in *Bacha F Guzdar v. CIT* (1952) 22 Com Cases 198 (Bom) was improved upon by the Supreme Court saying that the right to participation in the profits exists independent of any declaration by the company with only difference that the enjoyment of profits is postponed until dividends are declared [*Bacha F Guzdar (Mrs.) v. CIT* (1955) 25 Com Cases 1 at p. 6]

SS-3 clarifies that distribution of discount coupons to all the Shareholders shall not be treated as deemed Dividend.

## Final dividend

Dividend is said to be a final dividend if it is declared at the annual general meeting of the company. Final dividend once declared becomes a debt enforceable against the company. Final Dividend can be declared only if it is recommended by the Board of Directors of the Company. In accordance with Section 134(3)(k), Board of

directors must state in the Directors' Report the amount of dividend, if any, which it recommends to be paid.

SS-3 defines final dividend so as to mean the dividend recommended by the Board of Directors and declared by the Members at an Annual General Meeting.

### Interim dividend

Dividend is said to be an interim dividend, if it is declared by the Board of Directors between two annual general meetings of the company. All the provisions relating to the payment of dividend shall be applicable on the interim dividend also.

SS-3 defines interim dividend so as to mean the Dividend declared by the Board of Directors.

### Declaration of Dividend (Section 123)

Section 51 of the Act, states that a company may, if so authorized by its articles, pay dividend in proportion to the amount paid up on each share.

According to SS-3 a dividend shall be declared only on the recommendation of the Board, made at a meeting of the Board. As per Regulation 43 of SEBI(LODR) Regulations, 2015 the listed companies are mandated to declare and disclose the dividend on per share basis only.

A. Sources of declaration of dividend: Section 123(1) of Companies Act 2013 provides that the dividend shall be declared or paid by a company for any financial year only out of —

- (a) (i) the profits of the company for that year arrived at after providing for depreciation in accordance with the provisions of sub-section (2), or
- (ii) out of the profits of the company for any previous financial year or years arrived at after providing for depreciation in accordance with the provisions of that sub-section and remaining undistributed, or
- (iii) out of both;

In computing profits any amount representing unrealised gains, notional gains or revaluation of assets and any changes in carrying amount of an asset or of a liability on measurement of the asset or the liability at fair values shall be excluded; and"

- (b) out of money provided by the Central Government or a State Government for the payment of dividend by the company in pursuance of a guarantee given by that Government.

In accordance with SS-3, a company shall not declare Dividend on its equity shares in case of non-compliance of provisions relating to the acceptance of deposits under the Act, till such time the deposits accepted have been repaid with interest in accordance with the terms and conditions of the agreement entered with the depositors.

A company shall also not declare any Dividend, if it has defaulted in —

- (a) Redemption of debentures or payment of interest thereon or creation of debenture redemption reserve,
- (b) Redemption of preference shares or creation of capital redemption reserve,
- (c) Payment of Dividend declared in the current or previous financial year(s), or
- (d) Repayment of any term loan to a bank or financial institution or interest thereon.

Till such time the default is subsisting.

No Dividend shall be declared by the company during the extended time, if any, granted by the Tribunal/Court for repayment of above liabilities.

**B. Transfer of profits to reserves:** 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.

**C. Dividend in case of absence or inadequacy of profits:-** According to Second proviso to Section 123(1) read with rule 3 of Companies (Declaration and Payment of Dividend) Rules, 2014, in case of 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 reserves, such declaration of dividend shall be made in accordance with such the following conditions, namely:-

- (1) The rate of dividend declared shall not exceed the average of the rates at which dividend was declared by it in the three years immediately preceding that year: This shall not apply to a company which has not declared any dividend in each of preceding 3 financial years.
- (2) The total amount to be drawn from such accumulated profits shall not exceed one-tenth 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. The balance of reserves after such withdrawal shall not fall below fifteen per cent of its paid up share capital as appearing in the latest audited financial statement.

**D. Dividend to be declared from free reserves only:** No dividend shall be declared or paid by a company from its reserves other than free reserves.

Free reserves as defined under section 2(43) means such reserves which, as per the latest audited balance sheet of a company, are available for distribution as dividend: Provided that the following shall not be treated as free reserves;—

- (1) any amount representing unrealised gains, notional gains or revaluation of assets, whether shown as a reserve or otherwise, or
- (2) any change in carrying amount of an asset or of a liability recognised in equity, including surplus in profit and loss account on measurement of the asset or the liability at fair value.

**E. Manner of providing depreciation:** According to Section 123(2) for the purpose of declaration of dividend by a company as per Section 123(1)(a), it shall provide depreciation in accordance with Schedule II.

**F. Declaration of interim dividend:** Section 123(3) of the Companies Act, 2013 provides that 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 the annual general meeting 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.

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 immediately preceding three financial years.

SS-3 while clarifying the interim dividend provides that while declaring the Interim Dividend, the Board shall consider the financial results for the period for which Interim Dividend is to be declared and should be satisfied that the financial position of the company justifies and supports the declaration of such Dividend. The financial results shall take into account –

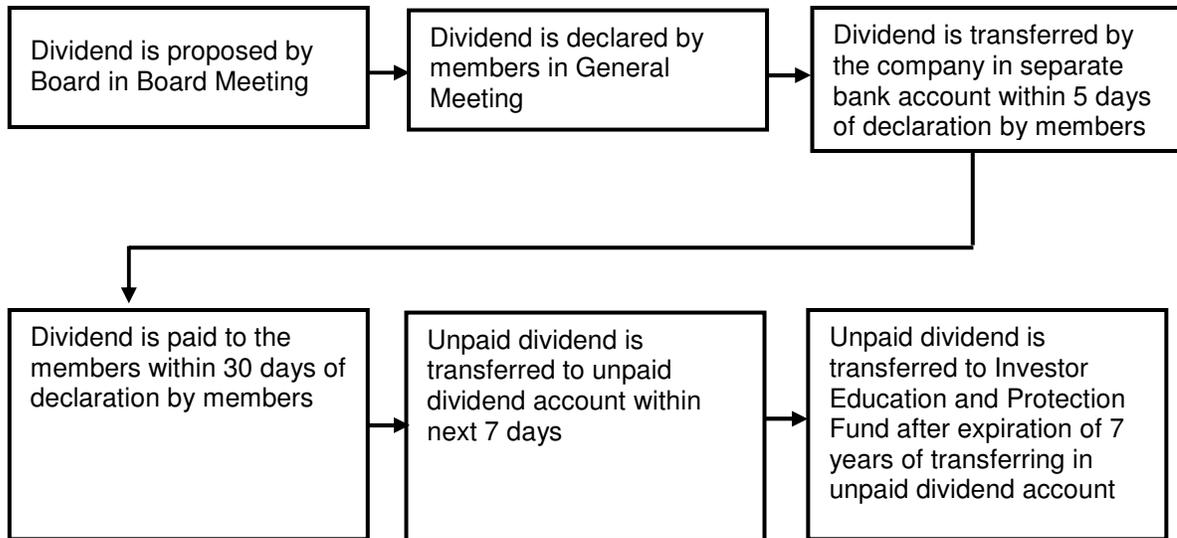
- (a) depreciation for the full year,
- (b) tax on profits of the company including deferred tax for full year,
- (c) other anticipated losses for the financial year,
- (d) Dividend that would be required to be paid at the fixed rate on preference shares.
- (e) the losses incurred, if any, during the current financial year upto the end of the quarter, immediately preceding the date of declaration of Interim Dividend.

Further, in case of clause (e) above, Interim Dividend shall not be declared at a rate higher than average Dividend declared during the immediately preceding three financial years.

Further SS-3 provides that Interim Dividend shall be declared at a meeting of the Board. In the event of a loss or inadequacy of profits during a financial year, no Interim Dividend shall be declared/ paid out of Free Reserves.

- G. Amount of Dividend to be deposited in Special Account of a Schedule Bank:** Section 123(4) provides that the amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate account within five days from the date of declaration of such dividend.
- H. Dividend only to registered shareholder:** Section 123(5) explains that no dividend shall be paid by a company in respect of any share therein except to the registered shareholder of such share or to his order or to his banker and shall not be payable except in cash.
- I. Payment of Dividend:** Inferring from section 124(1) dividend must be paid within 30 days from the date of declaration of dividend. SS-3 hereby clarifies that the Dividend shall be deposited in a separate bank account within five days from the date of declaration and shall be paid within thirty days of declaration. The intervening holidays, if any, falling during such period shall be included.
- J. Capitalization of Profits:** Nothing in this sub-section shall be deemed to prohibit 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.
- K. Mode of payment:** If 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.
- L. No dividend to be declared/paid in case of failure of repayment of deposits:** Section 123(6) provides that a company which fails to comply with the provisions of sections 73(prohibition of acceptance of deposits except in the manner provided) and 74 (Repayment of deposits etc accepted before commencement of Companies Act 2013) shall not, so long as such failure continues, declare any dividend on its equity shares.

*SS-3 provides that a company shall not declare dividend on its equity shares in case of non-compliance of provisions relating to the acceptance of deposits under the Act, till such time the deposits accepted have been repaid with interest in accordance with the terms and conditions of the agreement entered with the depositors.*



### UNPAID DIVIDEND ACCOUNT (Section 124)

Section 124(1) states that when a dividend has been declared by a company but has not been paid or claimed within thirty days from the date of the declaration to any shareholder entitled to the payment of the dividend, the company shall, within seven days from the date of expiry of the said period of thirty days, transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by the company in that behalf in any scheduled bank to be called the Unpaid Dividend Account.

Section 124(4) states that any person claiming to be entitled to any money transferred under sub-section (1) to the Unpaid Dividend Account of the company may apply to the company for payment of the money claimed.

**(a) Details of unpaid dividend to be placed at the website:** Section 124 (2) provides that the company shall, within a period of ninety days of making any transfer of an amount under Section 124(1) 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, if any, and also on any other website approved by the Central Government for this purpose in prescribed form. Rule 5(8) prescribe form IEFF-2 for this purpose.

**(b) Effect of Non-Transfer of the Dividend:** Section 124(3) provides that if any default is made in transferring the total amount referred to in sub-section (1) or any part thereof to the Unpaid Dividend Account of the company, it shall pay, from the date of such default, interest on so much of the amount as has not been transferred to the said account, at the rate of twelve per cent per annum and the interest accruing on such amount shall ensure to the benefit of the members of the company in proportion to the amount remaining unpaid to them.

**(c) Transfer to Investor Education and Protection Fund (IEPF):** Section 124 (5) states that any money transferred to the Unpaid Dividend Account of a company in pursuance of this section which remains unpaid or unclaimed for a period of seven years from the date of such transfer shall be transferred by the company along with interest accrued, if any, thereon to the Fund established under sub-section (1) of section 125 (Investor Education and Protection Fund) and 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.

**(d) Shares in respect of unpaid dividend also to be transferred to IEPF:** Section 124(6) provides that all shares in respect of which dividend has not been paid or claimed for seven consecutive years or more shall be transferred by the company in the name of IEPF along with a statement containing such details as may be prescribed. Rule 6(5) prescribes Form IEPF-4 for this purpose.

Provided that any claimant of shares transferred above shall be entitled to claim the transfer of shares from Investor Education and Protection Fund in accordance with such procedure and on submission of such documents as may be prescribed. Rule 7 of the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Rules, 2016, details the procedure which may be adopted by any claimant. The procedure is explained as under:

*STEP 1:-*Apply for refund to the Authority by submitting an online application in Form IEPF-5.

*STEP 2:-*Simultaneous application to the company- send IEPF Form duly signed by him along with, requisite documents as enumerated in Form IEPF-5 to the nodal officers of the concerned company at its registered office for verification of his claim.

*STEP 3:-* The company shall, within 15 days from the date of receipt of claim, send a verification report to the Authority, along with all the documents submitted by the claimant. In case of non receipt of documents by the Authority after the expiry of ninety days from the date of filing of Form IEPF-5, the Authority may reject Form IEPF-5, after giving an opportunity to the claimant to furnish response within a period of thirty days.

*STEP 4:-*After verification of the entitlement of the claimant-

(a) to the amount claimed, the Authority and then Drawing and Disbursement Officer of the Authority shall present a bill to the Pay and Accounts Office for e- payment as per the guidelines,

(b) to the shares claimed, the Authority shall issue a refund sanction order with the approval of the Competent Authority and shall credit the shares to the DEMAT account of the claimant to the extent of the claimant's entitlement.

*STEP 5:-*An application received for refund of any claim under this rule duly verified by the concerned company shall be disposed off by the Authority within sixty days from the date of receipt of the verification report from the company, complete in all respects and any delay beyond sixty days shall be recorded in writing specifying the reasons for the delay and the same shall be communicated to the claimant in writing or by electronic means.

*STEP 6:-*In case, claimant is a legal heir or successor or administrator or nominee of the registered share holder, he has to ensure that the transmission process is completed by the company before filing any claim with the Authority.

*STEP 7:-* In case, claimant is a legal heir or successor or administrator or nominee of any other registered security or in cases where request of transfer or transmission of shares is received after the transfer of shares by company to the Authority, the company shall verify all requisite documents required for registering transfer or transmission and shall issue letter to the claimant indicating his entitlement to the said security and furnish a copy of the same to the Authority while verifying the claim of such claimant.

*STEP 8:* The claimant shall file only one consolidated claim in respect of a company in a financial year.

In case any dividend is paid or claimed for any year during the said period of seven consecutive years, the share shall not be transferred to Investor Education and Protection Fund.

**(e) Offence & penalty:** Section 124(7) provides that if a company fails to comply with any of the requirements of this section, the company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

### **Investor Education and Protection Fund (Section 125)**

The Central Government shall establish a Fund to be called the Investor Education and Protection Fund. Section 125(2) prescribes that the following shall be credited to the Fund—

- (a) the amount given by the Central Government by way of grants after due appropriation made by Parliament by law in this behalf for being utilised for the purposes of the Fund;
- (b) donations given to the Fund by the Central Government, State Governments, companies or any other institution for the purposes of the Fund;
- (c) the amount in the Unpaid Dividend Account of companies transferred to the Fund under sub section (5) of section 124;
- (d) the amount in the general revenue account of the Central Government which had been transferred to that account under sub-section (5) of section 205A of the Companies Act, 1956, as it stood immediately before the commencement of the Companies (Amendment) Act, 1999, and remaining unpaid or unclaimed on the commencement of this Act;
- (e) the amount lying in the Investor Education and Protection Fund under section 205C of the Companies Act, 1956;
- (f) the interest or other income received out of investments made from the Fund;
- (g) the amount received under sub-section (4) of section 38;
- (h) the 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 seven or more years;
- (m) redemption amount of preference shares remaining unpaid or unclaimed for seven or more years; and
- (n) such other amount as may be prescribed.

Provided that no such 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 seven years from the date it became due for payment.

### **UTILISATION OF INVESTOR EDUCATION AND PROTECTION FUND**

Section 125 (3) provides the Fund shall be utilised for—

- (a) the refund in respect of unclaimed dividends, matured deposits, matured debentures, the application money due for refund and interest thereon;
- (b) promotion of investors' 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 and 245 by members, debenture-holders or depositors as may be sanctioned by the Tribunal; and
- (e) any other purpose incidental thereto, in accordance with such rules as may be prescribed:

Provided that the person whose amounts referred to in clauses (a) to (d) of sub-section (2) of section 205C transferred to Investor Education and Protection Fund, after the expiry of the period of seven years as per provisions of the Companies Act, 1956, shall be entitled to get refund out of the Fund in respect of such claims in accordance with rules made under this section.

### **RIGHT TO DIVIDEND, RIGHTS SHARES AND BONUS SHARES TO BE HELD IN ABEYANCE PENDING REGISTRATION OF TRANSFER OF SHARES**

Section 126 provides that when 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, notwithstanding anything contained in any other provision of this Act,—

- (a) transfer the dividend in relation to such shares to the Unpaid Dividend Account referred to in section 124 unless the company is authorised 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 under clause (a) of sub-section (1) of section 62 and any issue of fully paid-up bonus shares in pursuance of first proviso to sub-section (5) of section 123.

### **PUNISHMENT FOR FAILURE TO DISTRIBUTE DIVIDENDS**

Section 127 of Companies Act 2013 provides that when a dividend has been declared by a company but has not been paid or the warrant in respect thereof has not been posted within thirty 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 two years and with fine which shall not be less than one thousand rupees for every day during which such default continues and the company shall be liable to pay simple interest at the rate of eighteen per cent. per annum during the period for which such default continues.

*Exceptions:* Proviso to section 127 has provided a list where no offence under this section shall be deemed to have been committed:—

- (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; or
- (e) where, for any other reason, the failure to pay the dividend or to post the warrant within the period under this section was not due to any default on the part of the company.

## PROCEDURE FOR DECLARATION AND PAYMENT OF INTERIM DIVIDEND

1. Verify from company's Articles of Association that they authorize the directors to declare interim dividend; if not then alter the Articles of Association accordingly.
2. Issue notice for holding a meeting of the Board of directors of the company to consider the matter. The notice must be in accordance. It must state time, date and venue of the meeting and details of the business to be transacted there at and be sent to all the directors for the time being in India and to all other directors, at their usual address in India.
3. In case of listed companies, notify Stock exchange(s) where the securities of the company are listed, at least 2 working days in advance of the date of the meeting of its Board of Directors at which the recommendation of interim dividend is to be considered. [Regulation 29 of SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015].
4. At the Board meeting, the Board of Directors considers in detail all the matters with regard to the declaration and payment of an interim dividend including:
  - (a) Before declaring an interim dividend, the directors must satisfy themselves that the financial position of the company allows the payment of such a dividend out of profits available for distribution. The company must have earned adequate profits to pay interim dividend after providing for depreciation for the full year. The directors of a company may be held personally liable in the event of wrong declaration of an interim dividend. Therefore, it is prudent on the part of the directors to have a proforma profit and loss account and balance sheet of the company prepared up to the latest possible date of the financial year in respect of which interim dividend is proposed to be declared and provision must be made for all the working expenses and depreciation for the whole year. In case, a company is incurring loss as per financials of latest quarter, interim dividend shall not be higher than average dividend declared by the company during last three financial years.
  - (b) quantum of dividend,
  - (c) entitlement,
  - (d) closure of register of members for the purpose of payment of interim dividend or fixation of record date,
  - (e) publication of notice in newspapers for closure of share transfer register and the register of members of the company at least 7 days before the proposed closure (applicable for listed companies)
  - (f) opening of a separate bank account,
  - (g) printing of dividend warrants,
  - (h) authority for signing the dividend warrants and pass appropriate resolutions covering all these aspects of the matter,
  - (i) posting of the dividend warrants, and
  - (j) pass a suitable resolution for declaration and payment of interim dividend on equity shares of the company.
  - (k) Interim dividend on preference shares: Generally, dividend on preference shares is paid annually.

However, the dividend at a fixed rate on the preference shares can be paid more than once during a year, in proportion to the period of completion of current financial period over the whole financial year, by declaring it as interim dividend, in the Board meeting by the Board of directors. A suitable resolution should be passed to the effect that the dividend will be paid to the registered preference shareholders whose names appear in the register of preference shareholders as on the date of commencement of closure of share transfer books.

5. In case of a listed company, immediately within 30 minutes of the conclusion of the Board meeting, but only after the close of the market hours, intimate the stock exchanges with regard to the Board's decision about declaration and payment of interim dividend with the prescribed financial information is also required to be given to the concerned stock exchange(s) by a letter or telegram/telex. [Regulation 30 of SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015].

6. In case of listed company, publish notice of book closure in a newspaper circulating in the district in which the registered office of the company is situated at least seven days before the date of commencement of book closure.

Further:

- (i) To give notice of book closure to the stock exchange at least 7 working days or as many days as the stock exchange may prescribe, before the closure of transfer books or record date, stating the dates of closure of its transfer books/record date.
- (ii) To send the copies of notice stating the date of closure of the register of transfers or record date, and specifying the purpose for which the register is closed or the record date is fixed, to other recognized stock exchanges.
- (iii) Time gap between two book closures and record date would be at least 30 days.
- (iv) To declare and disclose the dividend on per share basis only.

7. Close the register of members and the share transfer register of the company.

8. Hold a Board/committee meeting for approving registration of transfer/transmission of the shares of the company, which have been lodged with the company prior to the commencement of book closure. In compliance with the Board resolution, register transfer/transmission of shares lodged with the company prior to the date of commencement of the closure of the register of members and mail the share certificates to the transferees after endorsing the shares in their names.

9. Round off the amount of interim dividend to the nearest rupee and where such amount contains part of a rupee consisting of paise then if such part is fifty paise or more, it should be increased to one rupee and if such part is less than fifty paise, it should be ignored.

10. Open the "Interim Dividend Account of.....Ltd." with the bank as resolved by the Board and deposit the amount of dividend payable in the account within five days of declaration and give a copy of the Board resolution containing instructions regarding opening of the account and give the authority to Bank to honour the dividend warrants when presented.

11. If the company is listed, then for payment of dividend it has to mandatorily use, either directly or through its Registrars to an Issue and Share Transfer Agent (RTI & STA), any RBI (Reserve Bank of India) approved electronic mode of payment such as Electronic Clearing Services (ECS) [LECS (Local ECS)/RECS (Regional ECS)/NECS (National ECS)], National Electronic Fund Transfer (NEFT), etc. In order to enable usage of electronic payment instruments, the company (or its RTI & STA) shall maintain requisite bank

details of its investors as under-

- (a) For investors that hold securities in demat mode, company or its RTI & STA shall seek relevant bank details from the depositories. To this end, vide circular SEBI/MRD/DEP/Cir-3/06 dated February 21, 2006 and letter MRD/DEP/PP/123624/2008 dated April 23, 2008, depositories have been advised to ensure that correct account particulars of investors are available in the database of depositories.
- (b) For investors that hold physical share/debenture certificates, company or its RTI & STA shall take necessary steps to maintain updated bank details of the investors at its end.
- (c) In cases where either the bank details such as MICR (Magnetic Ink Character Recognition), IFSC (Indian Financial System Code), etc. that are required for making electronic payment are not available or the electronic payment instructions have failed or have been rejected by the bank, company or its RTI & STA may use physical payment instruments for making cash payments to the investors. Company shall mandatorily print the bank account details of the investors on such payment instruments.
- (d) Depositories are directed to provide to companies (or to their RTI & STA) updated bank details of their investors. [Refer SEBI Circular No. CIR/MRD/DP/10/2013 dated March 21, 2013]

12. Make arrangements with the bank and in collaboration with other banks if required, for payment of the Dividend Warrants at par at the centers as determined by the Stock Exchanges in case of listed company.

13. Prepare a statement of dividend in respect of each share holder containing the following details

- (a) Name and address of the shareholder with ledger folio No.
- (b) No. of shares held.
- (c) Dividend payable.

14. Ensure that the dividend tax is paid to the tax authorities within the prescribed time.

15. To have sufficient number of dividend warrants printed in consultation with the company's banker appointed for the purpose of dividend. To get approval of RBI for printing the warrants with MICR facility. Get the dividend warrants filled in and signed by the persons authorized by the Board.

16. No RBI approval is required for payment of dividend to shareholders abroad, in case of investment made on repatriation basis.

17. Prepare two copies of the list of members with names and addresses only for mailing purposes—one to cut and paste on envelopes which could even be printed on self sticking labels and the other for securing receipt from the Post Office.

18. Where an instrument of transfer has been received by company prior to book closure but transfer of such shares has not been registered when the dividend warrants were posted, then keep the amount of dividend in special A/c called "Unpaid Dividend Account" opened unless the registered holder of these shares authorizes company in writing to pay dividend to the transferee specified in the said instrument of transfer.

19. Dispatch dividend warrants within thirty days of the declaration of dividend. In case of joint shareholders, dispatch the dividend warrant to the first named shareholder.

20. Send sufficient number of cancelled dividend warrant forms with MICR code allotted by the RBI, to the bank for circulation to the branches where the dividend warrants will be payable at par.

21. Instructions to all the specified branches of the bank that dividend should be paid at par should be sent by the Bank.

22. Publish a Company notice in a newspaper circulating in the district in which the registered office of the company is situated to the effect that dividend warrants have been posted and advising those members of the company who do not receive them within a period of fifteen days, to get in touch with the company for appropriate action (in the case of listed companies, as a good practice).

23. Issue bank drafts and/or cheques to those members who inform that they received the dividend warrants after the expiry of their currency period or their dividend warrants were lost in transit after satisfying that the same have not been encashed.

24. Arrange for transfer of unpaid or unclaimed dividend to a special account named "Unpaid dividend A/c"

Within 7 days after expiry of the period of 30 days of declaration of final dividend. [Section 124]

25. Confirm the interim dividend in the next Annual General Meeting.

### **PROCEDURE FOR DECLARATION AND PAYMENT OF FINAL DIVIDEND**

The following steps are required to be taken by a company in respect of declaration and payment of final dividend:

1. Issue notice for holding a meeting of the Board of directors of the company to consider the matter. It must contain time, date and venue of the meeting and details of the business to be transacted there at and must be sent to all the directors for the time being in India and to all other directors, at their usual address in India.

2. In case of listed companies notify stock exchange(s) where the securities of the company are listed, at least 2 working days in advance of the date of the meeting of its Board of Directors at which the recommendation of final dividend is to be considered. [Regulation 29 of SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015].

3. Hold Board meeting for the purpose of passing the following resolutions:

- (a) approving the annual accounts (balance sheet and profit and loss account of the company for the year ended on 31st March.....);
- (b) recommending the quantum of final dividend to be declared at the next annual general meeting and the source of funds for the payment thereof, i.e.:
  - (i) out of profits of the company after providing for depreciation for the current financial year and also for earlier years, if not already provided and amount to be transferred from the current profits to reserves; or
  - (ii) out of reserves in accordance with the provisions of Rule 3 of the Companies (Declaration and Payment of Dividend), Rules, 2014.
- (c) fixing time, date and venue for holding the next annual general meeting of the company, inter alia, for declaration of dividend recommended by the Board;
- (d) approving notice for the annual general meeting and authorizing the company secretary or any competent person if company does not have a company secretary to issue the notice of the AGM on behalf of the Board of directors of the company to all the members, directors and auditors of the company and other persons entitled to receive the same.

- (e) determining the date of closure of the register of members and the share transfer register of the company as per requirements of Section 91 of the Companies Act and SEBI (LODR) Regulations, 2015 (in the case of listed companies) signed by the company with the stock exchanges where the securities of the company are listed. In the case of listed companies, the date of commencement of closure of the transfer books should not be on a day following a holiday. The dates so fixed should also not clash with the clearance programme in the stock exchanges. It is advisable to consult in advance the regional stock exchange and then fix the dates for closure of books.

5. The company may transfer to reserves such percentage as it consider appropriate of the current profits.

6. In case of a listed company, immediately within 30 minutes of the conclusion of the Board meeting, intimate the stock exchanges with regard to the Board's decision about declaration and payment of dividend and the amounts appropriated from reserves, capital profits, accumulated profits of past years or other special source to provide wholly or partly for the dividend, by way of a letter or telegram/fax [Regulations 29 and 30]

7. Publish notice of book closure in a newspaper circulating in the district in which the registered office of the company is situated at least seven days before the date of commencement of book closure.

In case of listed companies:

- (i) To give notice of book closure to the stock exchange at least 7 working days or as many days as the stock exchange may prescribe, before the closure of transfer books or record date, stating the dates of closure of its transfer books/record date.
- (ii) To send the copies of notice at least 7 working days in advance. Stating the date of closure of the register of transfers or record date, and specifying the purpose for which the register is closed or the record date is fixed, to other recognized stock exchanges. [Regulation 42 of SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015].
- (iii) Time gap between two book closures would be at least 30 days [Regulation 42(4) of SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015].

8. To declare and disclose the dividend on per share basis only. The listed entity shall not forfeit unclaimed dividends before the claim becomes barred by law and such forfeiture of effected, shall be annulled in appropriate cases. (Regulation 43 of Listing Regulations read with section 51 of Companies Act, 2013).

9. "Regulation 43A of SEBI Listing Regulation provided that the top five hundred listed entities based on market capitalization (calculated as on March 31 of every financial year) shall formulate a dividend distribution policy which shall be disclosed in their annual reports and on their websites. The dividend distribution policy shall include the following parameters:

- (a) the circumstances under which the shareholders of the listed entities may or may not expect dividend;
- (b) the financial parameters that shall be considered while declaring dividend;
- (c) internal and external factors that shall be considered for declaration of dividend;
- (d) policy as to how the retained earnings shall be utilized; and
- (e) parameters that shall be adopted with regard to various classes of shares:

Provided that if the listed entity proposes to declare dividend on the basis of parameters in addition to clauses (a) to (e) or proposes to change such additional parameters or the dividend distribution

policy contained in any of the parameters, it shall disclose such changes along with the rationale for the same in its annual report and on its website.

The listed entities other than top five hundred listed entities based on market capitalization may disclose their dividend distribution policies on a voluntary basis in their annual reports and on their websites.”

10. Close the register of members and the share transfer register of the company.

11. The amount of dividend as recommended by the Board of directors shall be shown in the Directors' Report as appropriation of profits for the financial year to which the Report relates. The same amount is shown in the Balance Sheet as at the end of the related financial year as “Proposed Dividend” under the head “Current Liabilities & Provisions”, Sub-head “Provisions”.

12. Hold a Board/committee meeting for approving registration of transfer/transmission of the shares of the company, which have been lodged with the company prior to the commencement of book closure. In compliance with the Board resolution, register transfer/transmission of shares lodged with the company prior to the date of commencement of the closure of the register of members and mail the share certificates to the transferees after endorsing the shares in their names.

13. Hold the annual general meeting and pass an ordinary resolution declaring the payment of dividend to the shareholders of the company as per recommendation of the Board. The shareholders cannot declare the final dividend at a rate higher than the one recommended by the Board. However, they may declare the final dividend at a rate lower than the one recommended by the Board. The following should be noted in this regard:

- (a) Once a company has declared a dividend for a financial year at an annual general meeting, it cannot declare further dividend at an extraordinary general meeting in relation to the same financial year; it is beyond the powers of the company to do so, although the Companies Act does not prohibit the declaration of a dividend at a general meeting other than an annual general meeting.
- (b) Pro-rata means in proportion or proportionately, according to a certain rate. It denotes a method of dividing something between a number of participants in proportion to some factor. The profits of a company are shared, pro rata, among the shareholders, i.e. in proportion to the number of shares each shareholder holds.
- (c) In the case of preference shares, dividend is always paid at a fixed rate. However, in the case of equity shares, a dividend must be declared and paid according to the amounts paid or credited as paid on the shares, i.e., according to the paid-up value of the shares.
- (d) All dividends shall be apportioned and paid proportionately to the amounts paid or credited as paid on the shares during any portion or portions of the period in respect of which the dividend is paid; but if any share is issued on terms providing that it shall rank for dividend as from a particular date such share shall rank for dividend accordingly. [Schedule I, Table F, Article 83(3)].

14. Prepare a statement of dividend in respect of each shareholder containing the following details:

- (a) Name and address of the shareholder with ledger folio no.
- (b) No. of shares held.
- (c) Dividend payable.

15. Ensure that the dividend tax is paid to the tax authorities within the prescribed time.

16. Round off the amount of interim dividend to the nearest rupee and where such amount contains part of a rupee consisting of paise then if such part is fifty paise or more it should be increased to one rupee and if

such part is less than fifty paise it should be ignored.

17. Open a separate bank account for making dividend payment and credit the said bank account with the total amount of dividend payable within five days of declaration of dividend.

18. If the company is listed, then for payment of dividend it has to mandatorily use, either directly or through its Registrars to an Issue and Share Transfer Agent (RTI & STA), any RBI (Reserve Bank of India) approved electronic mode of payment such as Electronic Clearing Services (ECS) [LECS (Local ECS)/ RECS (Regional ECS)/NECS (National ECS)], National Electronic Fund Transfer (NEFT), etc. In order to enable usage of electronic payment instruments, the company (or its RTI & STA) shall maintain requisite bank details of its investors as per SEBI Circular No. CIR/MRD/DP/10/2013 dated March 21, 2013 in the manner as stated aforesaid under the procedure for declaration and payment of interim dividend.

19. To have sufficient number of dividend warrants printed in consultation with the company's banker appointed for the purpose of dividend. To get approval of the RBI for printing the warrants with MICR facility. Get the dividend warrants filled in and signed by the persons authorized by the Board.

20. No RBI approval required for payment of dividend to shareholders abroad, in case of investment made on repatriation basis.

21. Prepare two copies of the list of members with names and addresses only for mailing purposes—one to cut and paste on envelopes which could even be printed on self sticking labels and the other for securing receipt from the Post Office.

22. Where an instrument of transfer has been received by company prior to book closure but transfer of such shares has not been registered when the dividend warrants were posted, then keep the amount of dividend in special A/c called "Unpaid Dividend Account" unless the registered holder of these shares, authorizes company in writing to pay dividend to the transferee specified in the said instrument of transfer. (Section 206A)

23. Dispatch dividend warrants within thirty days of the declaration of dividend. In case of joint shareholders, dispatch the dividend warrant to the first named shareholder.

24. Send sufficient number of cancelled dividend warrant forms with MICR code allotted by the RBI, to the bank or circulation to the branches where the dividend warrants will be payable at par.

25. Instructions to all the specified branches of the bank that dividend should be paid at par should be sent by the Bank.

26. Publish a Company notice in a newspaper circulating in the district in which the registered office of the company is situated to the effect that dividend warrants have been posted and advising those members of the company who do not receive them within a period of fifteen days, to get in touch with the company for appropriate action (in the case of listed companies, as a good practice).

27. Issue bank drafts and/or cheques to those members who inform that they received the dividend warrants after the expiry of their currency period or their dividend warrants were lost in transit after satisfying that the same have not been encashed.

28. Arrange for transfer of unpaid or unclaimed dividend to a special account named "Unpaid dividend A/c"

Within 7 days after expiry of the period of 30 days of declaration of final dividend.

## DECLARATION OF DIVIDEND OUT OF RESERVES

The procedure is as follows:

- (1) Give notice to all the directors of the company for holding a Board meeting. In the meeting, take decision to declare dividend out of company's reserves because of inadequacy or absence of profits and also fix the date, time and place of the Annual General Meeting. Authorise the Company Secretary or any competent person if company does not have a company secretary to issue the notice of the AGM on behalf of the Board of directors of the company to all the members, directors and auditors of the company and other persons entitled to receive the same.
- (2) Ensure that the Companies (Declaration and Payment of Dividend), Rules 2014 are complied with.
- (3) While calculating the profits of the previous years, take only the net profit after tax.
- (4) Ensure that while computing the amount of profits, the amount transferred from the Development Rebate Reserve is included and all items of capital reserves including reserves created by revaluation of assets are excluded.
- (5) In the case of listed companies, inform the Stock Exchange with which the shares of the company are listed within 30 minutes of closure of Board meeting about decision to recommend declaration of dividend out of Company's Reserves. [Regulation 30 of SEBI (LODR) Regulations, 2015].
- (6) Issue notices in writing at least 21 days before the date of the Annual General Meeting and hold the meeting and pass the necessary resolution.
- (7) In the case of listed companies, forward copies of the notice and a copy of the proceeding of the general meeting to the Stock Exchange.
- (8) Open a separate bank account for making dividend payment and credit the said bank account with the total amount of dividend payable within five days of declaration of dividend.
- (9) Issue dividend warrants within 30 days from the date of declaration of dividend. Rest of the procedural steps are same as in case of payment of final dividend.

## CLAIMING OF UNCLAIMED/UNPAID DIVIDEND

In accordance with Section 124, a dividend which has been declared by a company but has not been paid, or claimed, within thirty days from the date of the declaration, to/by any shareholder entitled to the payment of the dividend, the company shall, within seven days from the date of expiry of the said period of thirty days, transfer the total amount of dividend which remains unpaid or unclaimed within the said period of thirty days, to a special account to be opened by the company in that behalf in any scheduled bank, to be called "Unpaid Dividend Account of.....Company Limited/Company (Private) Limited".

Under the explanation, the expression "dividend which remains unpaid" means any dividend the warrant in respect thereof has not been encashed or which has otherwise not been paid or claimed.

Any person claiming to be entitled to any money transferred to the Unpaid Dividend Account of the company may apply to the company for payment of the money claimed. The person can claim this amount from company only within seven years of its transfer to Unpaid Dividend Account. After this period not only his dividend amount but also shares shall be transferred to the Invest or Education and Protection Fund (IEPF).

## PROCEDURE FOR TRANSFER OF UNPAID OR UNCLAIMED DIVIDEND TO THE INVESTOR EDUCATION AND PROTECTION FUND

Any money transferred to the Unpaid Dividend Account of a company in pursuance of Section 124 which remains unpaid or unclaimed for a period of seven years from the date of such transfer shall be transferred by the company along with interest accrued, if any, thereon to the Investor Education and Protection Fund and the company shall send a statement in the prescribed form of the details of such transfer to the Investor Education and Protection Fund Authority and it shall issue a receipt to the company as evidence of such transfer.

(1) Every company shall within a period of ninety days after holding of the Annual General Meeting or the date on which it should have been held as per the provisions of section 96 of the Act and every year thereafter till completion of the seven years period, identify the unclaimed dividend, as on the date of holding of Annual General Meeting or the date on which it should have been held as per the provisions of section 96 of the Act, separately furnish and upload on its own website and also on website of Authority or any other website as may be specified by the Government, a statement or information through Form No. IEPF-2, separately for each year, containing following information, namely:-

- (a) the names and last known addresses of the persons entitled to receive the sum; (b) the nature of amount;
- (c) the amount to which each person is entitled;
- (d) the due date for transfer into the Invest or Education and Protection Fund; and
- (e) such other information as may be considered relevant for the purposes.

(2) The amount of unclaimed or unpaid dividend required to be credited by the companies to the Fund shall be remitted into the specified branches of Punjab National Bank, which is the accredited Bank of the Pay and Accounts Office, Ministry of Corporate Affairs and other authorized banks engaged by the MCA-21 system, within a period of thirty days of such amounts becoming due to be credited to the Fund.

(3) The amount shall be tendered by the companies along with challan (in triplicate) to the specified Bank

Branches of Punjab National Bank and other authorized banks under MCA-21 system who will return two copies of the challan, duly stamped in token of having received the amount, to the Company. The third copy of the challan will be forwarded along with the daily credit scroll by the receiving branch to its Focal Point Branch of the Bank for onward transmission to the Pay and Accounts Office, Ministry of Corporate Affairs.

(4) Every company shall file with the concerned Authority one copy of the challan referred to in point (3) indicating the deposit of the amount to the Fund and shall fill in the full particulars of the amount tendered, including the head of account to which it has been credited.

(5) The company shall, along with the copy of the challan as required under point(4), furnish a Statement in Form No. IEPF 1 containing details of such transfer to the Authority within thirty days of submission of challan.

(6) The amount may also be remitted by Electronic Fund Transfer in such manner, as may be specified by the Central Government.

(7) On receipt of the statement, the Authority shall enter the details of such receipt in a Register maintained physically or electronically by it in respect of each company every year, and reconcile the amount so remitted and collected, with the concerned designated bank on monthly basis.

(8) Each designated bank shall furnish an abstract of such receipts during the month to the Authority within seven days after the close of every month.

(9) The company shall maintain record consisting of name, last known address, amount, folio number or client ID, certificate number, beneficiary details etc. of the persons in respect of whom unpaid or unclaimed amount has remained unpaid or unclaimed for a period of seven years and has been transferred to the Fund and the Authority shall have the powers to inspect such records.

## ANNEXURES

### ANNEXURES-I

#### SPECIMEN OF BOARD RESOLUTION FOR DECLARATION OF INTERIM DIVIDEND ON EQUITY SHARES

RESOLVED THAT an interim dividend of Rs. 2 (Rupees two) only on each fully paid.....no. of equity shares of Rs.10 (Rupees ten) each of the company amounting to Rs.....be paid out of the profits of the company for the half year ended.....2014 to those members of the company whose names would appear on the register of members of the company on the.....day of....., 2014.

RESOLVED FURTHER THAT a bank account to be designated as “Interim Equity Dividend (2015) Account of .....Limited” be opened in the name of the company with.....Bank at its Branch at..... and a sum of Rs.....,being the total interim dividend amount, be deposited in the said account within five days.

RESOLVED FURTHER THAT Shri....., Managing Director and Shri....., the Company Secretary be and are hereby authorized to open the bank account by signing the account opening form and by furnishing to the said bank the required papers, documents, information etc. and completing all other required formalities for the purpose of opening the bank account and to make arrangements with the said bank for the payment at par, of the interim dividend within thirty days from the date of this resolution.

RESOLVED FURTHER THAT Shri....., Managing director and Shri....., Company Secretary of the company for the time being, be and are hereby authorized to jointly sign the dividend warrants to be issued on the said bank and the said bank be and is hereby authorized to honour the interim dividend warrants jointly signed by the said authorised signatories, as and when presented for encashment.

### ANNEXURE-II

#### SPECIMEN OF BOARD RESOLUTION FOR DECLARING INTERIM DIVIDEND ON PREFERENCE SHARES

RESOLVED THAT dividend at the fixed rate of 8 per cent per annum on the (no. of shares) cumulative redeemable preference shares of Rs.100 each of the company, for the six months commencing from July 1,.....2014 and ending on December 31,.....2014.....aggregating Rs....., be paid to the registered holders thereof whose names would appear on the register of holders of the said shares on the.....2014, the date of commencement of the closure of the share transfer books of the company.

RESOLVED FURTHER THAT a bank account to be designated as “Interim Preference Dividend (2015) Account of.....Limited” be opened in the name of the company with.....Bank at its Branch

at.....and a sum of Rs. ....,being the total interim dividend amount, be deposited in the said account.

RESOLVED FURTHER THAT Shri....., Managing Director and the Company Secretary, Shri....., be and is hereby authorized to open the bank account by signing the account opening form and by furnishing to the said bank the required papers, documents, information etc. and completing all other required formalities for the purpose of opening the bank account and to make arrangements with the said bank for the payment at par, of the interim dividend within 30 days from the date of this resolution.

RESOLVED FURTHER THAT Shri....., Managing director and Shri.....,Company Secretary of the company for the time being, be and are hereby authorised to jointly sign the dividend warrants to be issued on the said bank and the said bank be and is hereby authorized to honour the interim dividend warrants jointly signed by the said authorized signatories, as and when presented for encashment.

Name of Company:..... Registered Office:.....

**ANNEXURE-III**

**NOTICE OF BOOK CLOSURE**

**Notice**

Pursuant to Section 91 of the Companies Act, 2013 and the applicable clauses of the SEBI(LODR) Regulations, 2015, notice is hereby given that the register of members and the share transfer register of the company will remain closed, for the purpose of payment of interim dividend/final dividend, from the.....th day of.....(month),

.....2014 to the.....th day of.....2015 (both days inclusive).

Members of the company are requested to intimate to the company at its registered office above, their latest postal addresses, where the interim dividend warrants may be sent by the company.

Place:.....

For.....Limited

Date:.....

(.....)

New Delhi-110 001.

Company Secretary

Messrs..... Advertising Agents,

**Note for publication**

Please arrange for the publication of the above company notice in the earliest editions of....., English daily newspaper and.....,Hindi daily newspaper, not later than the.....th day of.....,

2014. Kindly ensure that the Hindi newspaper must carry the notice in Hindi language after it is appropriately translated into Hindi.

For Limited

Dated.....

(.....)

Company Secretary

**ANNEXURE-IV****SPECIMEN OF BOARD RESOLUTION RECOMMENDING PAYMENT OF DIVIDEND ON EQUITY SHARES OUT OF CURRENT PROFITS**

“RESOLVED THAT in accordance with the provisions of Section 123 and other applicable provisions, if any, of the Companies Act, 2013 and the Companies (Declaration and Payment of Dividend) Rules, 2014, the Board of directors of the company do hereby recommend a dividend at the rate of Rs.....per equity share out of the current profits of the company for the year ended on 31<sup>st</sup> March 2014 on the..... fully paid equity shares of the company absorbing Rs.....out of the profits of the year and that, subject to the declaration by the members of the company at the ensuing annual general meeting, such dividend be paid to the registered holders of the equity shares whose names would appear on the register of members on.....2014.”

**ANNEXURE-V****SPECIMEN EXTRACTS OF MINUTES CONTAINING THE BOARD RESOLUTION FOR RECOMMENDING DECLARATION OF DIVIDEND OUT OF RESERVES**

The Chairman informed the meeting that the profits of the current year, i.e. the financial year ended on the 31<sup>st</sup> March, 2014 are inadequate for payment of a reasonable amount of dividend to the members of the company

He further informed that the free reserves of the company do, however, permit the distribution of dividend not exceed the average of the rates at which dividend was declared by it in the three years immediately preceding that year.

The directors considered the matter and passed the following resolution:

RESOLVED THAT the Board of directors of the company do hereby recommend to the members of the company, the declaration and payment of a dividend at the rate of ten per cent on all the fully paid equity shares of the company out of the free reserves of the company that stood in the books of the company on.....2014 absorbing a total of`.....,with due compliance of the Companies (Declaration and Payment of Dividend) Rules, 2014, and that, subject to the declaration by the members at the forthcoming annual general meeting, to the holders of the equity shares whose names will appear on the register of members on.....2014.

**LESSON ROUND- UP**

- Under Section 2(35) of the Companies Act, 2013, ‘dividend’ includes any interim dividend.
- Dividend is the share of the company’s profit distributed among the members.
- The Board may declare interim dividend during any financial year out of the surplus in the Profit and Loss Account at any time between two AGM of the company.
- Final Dividend means a Dividend which declared at the Annual General Meeting of the company.
- In case of inadequacy of profits the company can declare the dividend with accordance with the Rule 3 of Companies (Declaration and Payment of Dividend) Rules 2014.
- The amount of dividend shall be deposited in a schedule bank in a separate account within 5 days from the date of declaration.
- Dividend may be paid by cheque or warrant or in any electronic mode to the shareholders entitled to the

payment of dividend.

- Where the dividend is not paid or claimed within 30 days, the company shall, within 7 days transfer the amount to Unpaid Dividend Account which shall be opened in a scheduled bank.
- In case of any default in transferring the amount, the company shall be liable to pay interest on the amount as has not been transferred.
- The amount remaining unpaid along with interest accrued thereon for 7 years shall be transferred to Investor Education and Protection Fund.
- In case of non-payment of dividend declared by the company, every party in default be punishable with imprisonment of upto two years and with fine.

## GLOSSARY

Interim dividend	Dividend declared in between two Annual General Meetings
Book Closure	Register of Members or other security holders are closed for the purpose of dividend distribution (See section 91 of the Companies Act, 2013)
DEMAT account	A Demat Account is an account that allows investors to hold their shares in an electronic form. Stocks in Demat account remain in dematerialized form. Dematerialization is the process of converting physical shares into electronic format.
Dividend Warrant	An order of payment (such as a cheque payable to a shareholder) in which a dividend is paid.

## SELF TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

- (1) Define the term 'Dividend'. State briefly the provisions related to declaration of dividend under the Companies Act 2013.
- (3) State the procedure for transfer of unpaid or unclaimed dividend to the Investor Education and Protection Fund.
- (4) Explain the law relating to declaration and payment of final dividend.
- (5) Distinguish between 'Interim Dividend' and 'Final Dividend'.
- (6) Write short notes on the following:-
  - (i) Investor Education and Protection Fund (IEPF).
  - (ii) Punishment of failure to distribute dividend

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# Lesson 7

## Corporate Social Responsibility

### LESSON OUTLINE

- CSR Committee
- CSR activities of Company
- CSR expenditure
- Computation of net profits
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

The concept of Corporate Social Responsibility (CSR) is all about corporates giving back to society. The Companies Act, 2013, mandates companies falling under certain class to contribute CSR Committee and spend at least a fixed expenditure of CSR activities. Non-compliance of the same will have burden on the company.

As a prospected Company Secretary, you are expected to be in know of the legal and technical requirements with respect to CSR, in order to guide the management and Board. This chapter gives you a brief insight of the same.

Corporate Social Responsibility is the concept that mandates corporates to spend towards the social good. The concept of CSR is governed by clause 135 of the Companies Act, 2013.

After reading this lesson, you will able to grasp the technical and legal requirements with respect to CSR under the Act.

## INTRODUCTION

We live a dynamic life in a world that is growing more and more complex. Global scale environmental, social, cultural and economic issues have now become part of our every day life. Boosting profits is no longer the sole business performance indicator for the corporates and they have to play the role of responsible corporate citizens as they owe a duty towards the society, where they operate and draw resources from it and as such they are part of society. Corporate Social Responsibility [CSR] is underpinned by public policy and therefore, it has undeniable links with law. CSR is not something new to India and the concept of trusteeship advocated by Mahatma Gandhi, the Father of the Nation was embraced by many companies, in various forms over the years.

The government perceives CSR as the business contribution to the nation's sustainable development goals. Essentially, it is about how business takes into account the economic, social and environmental impact of the way in which it operates. Perception of the government about CSR gained shape and form in the Companies Act, 2013, which mandates Companies to undertake Corporate Social Responsibility, as one of the Board Agenda.

Corporate Social Responsibility is the way companies manage their businesses to produce an overall positive impact on society through economic, environmental and social actions. Corporate social responsibility (CSR), also called corporate conscience, corporate citizenship, social performance, or sustainable responsible business/ businesses. Business depends for its survival on long term prosperity of the society.

CSR has been defined by different people giving it a varied dimension. According to Michel Hopkins "Corporate Social Responsibility is concerned with treating the stakeholders of a company or institution ethically or in a responsible manner. 'Ethically or in a responsible manner' refers to treating key stakeholders in a manner deemed acceptable according to international norms."

Corporate Social Responsibility is an important business strategy because, to some extent a consumer wants to buy products from companies he trusts, a supplier wants to form business partnership with companies he can rely on, an employee want to work for a company he respects, other concerns want to establish business contacts with companies seeking feasible solutions and innovations in areas of common concern.

Corporate social responsibility is basically a new business strategy to reduce investment risks and maximise profits by taking all the key stakeholders into confidence. The proponents of this perspective often include corporate social responsibility in their advertising and social marketing initiatives. It is a tool to increase the reputation of the company in the eyes of society.

It is certainly a business approach that creates a long term consumer and employee value by not only creating a 'green strategy' on natural environment but also considering every dimension of how a business operates in social, cultural and environment. The company should meet the needs of its all stakeholders (consumer, employees, shareholder, clients and other related persons) without sacrificing the ability to meet the needs of the future stakeholders.

## CORPORATE SOCIAL RESPONSIBILITY

### Applicability

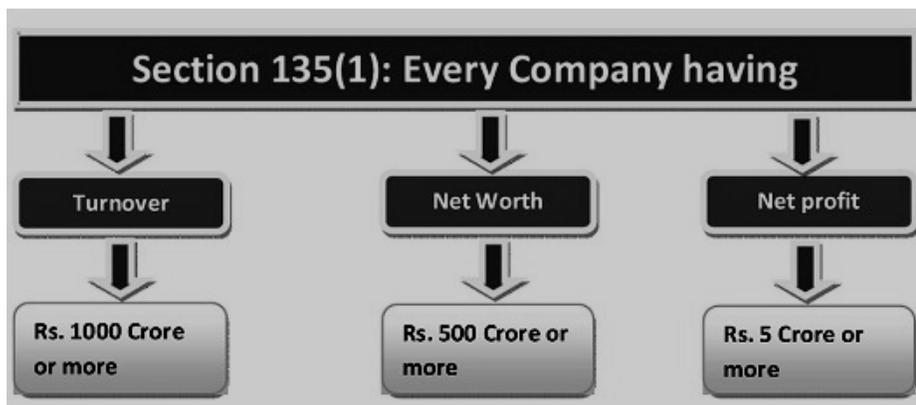
As per section 135 of the Companies Act 2013, the CSR provision is applicable to companies which fulfills

any of the following criteria during the immediately preceding financial year:-

- Companies having net worth of rupees five hundred crore or more, or
- Companies having turnover of rupees one thousand crore or more or
- Companies having a net profit of rupees five crore or more

The CSR Rules have widened the ambit for compliance obligations to include the holding and subsidiary companies as well as foreign companies whose branches or project offices in India which fulfill the criteria specified above.

According to the CSR Rules, the CSR provision will also be applicable to every company including its holding or subsidiary, and a foreign company having its branch office or project office in India having net worth of rupees five hundred crore (500 Crore) or more, or turnover of rupees one thousand crore (1000 crore) or more or a net profit of rupees five crore (5 Crore) or more during any financial year.



### Cessation

Thus, the CSR Rules specify that a company which does not satisfy the specified criteria for a consecutive period of three financial years is not required to comply with the CSR obligations, implying that a company not satisfying any of the specified criteria in a subsequent financial year would still need to undertake CSR activities unless it ceases to satisfy the specified criteria for a continuous period of three years.

### CSR Committee

Companies that trigger any of the aforesaid conditions must constitute a Corporate Social Responsibility Committee of the Board to formulate and monitor the CSR policy of a company. Section 135 of the 2013 Act requires the CSR Committee to consist of at least three directors, including at least one independent director.

Where a company is not required to appoint an independent director under sub-section (4) of section 149, it shall have in its Corporate Social Responsibility Committee two or more directors.

Further, the CSR Rules have relaxed the requirement regarding the presence of three or more directors on the CSR Committee of the Board, in case where a private company has only two directors on the Board, the CSR Committee can be constituted with these two directors.

The CSR Committee of a foreign company shall comprise of at least two persons wherein one or more persons should be resident in India and the other person nominated by the foreign company.

The Board's report shall disclose the composition of the Corporate Social Responsibility Committee.

Rule 3 of the Companies (Corporate Social Responsibility Policy) Rules, 2014 specify that every company which ceases to be a company covered under section 135 as per the limits specified thereunder for three consecutive financial years shall not be required to constitute a CSR Committee and comply with the provision of section 135, till such time that it meets the criteria specified.

### **The functions of CSR Committee**

- To formulate and recommend to the Board, a CSR Policy which would indicate the activities to be undertaken in areas or subject, specified in Schedule VII of the Act.
- To recommend the amount of the expenditure to be incurred on the activities undertaken in pursuance of the CSR policy.
- To institute a transparent monitoring mechanism for implementation of the CSR projects or programs or activities undertaken by the company.
- To monitor the CSR policy of the company time to time.

### **CSR Activities**

- The CSR activities shall be undertaken by the company, as per its stated CSR Policy, as projects or programs or activities (either new or ongoing), excluding activities undertaken in pursuance of its normal course of business.
- The CSR Committee of the company may decide to undertake its CSR activities approved by the Board, through
  - (a) a company established under section 8 of the Act or a registered trust or a registered society, established by the company, either singly or alongwith any other company, or
  - (b) a company established under section 8 of the Act or a registered trust or a registered society, established by the Central Government or State Government or any entity established under an Act of Parliament or a State legislature.
- Further, if the Board of a company decides to undertake its CSR activities through a company established under section 8 of the Act or a registered trust or a registered society, other than those specified above, such company or trust or society shall have an established track record of three years in undertaking similar programs or projects; and the company has specified the projects or programs to be undertaken, the modalities of utilisation of funds of such projects and programs and the monitoring and reporting mechanism.
- A company may also collaborate with other companies for undertaking projects or programs or CSR activities in such a manner that the CSR Committees of respective companies are in a positions to report separately on such projects or programs in accordance with these rules.
- The CSR projects or programs or activities undertaken in India only shall amount to CSR Expenditure.
- The CSR projects or programs or activities that benefit only the employees of the company and their families shall not be considered as CSR activities in accordance with section 135 of the Act.
- Companies may build CSR capacities of their own personnel as well as those of their implementing agencies through institutions with established track records of atleast three financial years but such expenditure, including expenditure on administrative overheads, shall not exceed five percent of total CSR expenditure of the company in one financial year.

- Contribution of any amount directly or indirectly to any political party under section 182 of the Act, shall not be considered as CSR activity.

### List of CSR Activities

Some activities are specified in Schedule VII as the activities which may be included by companies in their Corporate Social Responsibility Policies. 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 the amended Schedule VII of the Act, are broad-based and are intended to cover a wide range of activities as illustratively. These are activities related to:

- (i) eradicating hunger, poverty and malnutrition, promoting health care including preventive health care and sanitation including contribution to the Swachh Bharat Kosh set-up by the Central Government for the promotion of sanitation and making available safe drinking water.
- (ii) promoting education, including special education and employment enhancing vocation skills especially among children, women, elderly and the differently abled and livelihood enhancement projects.
- (iii) promoting gender equality, empowering women, setting up homes and hostels for women and orphans; setting up old age homes, day care centres and such other facilities for senior citizens and measures for reducing inequalities faced by socially and economically backward groups;
- (iv) ensuring environmental sustainability, ecological balance, protection of flora and fauna, animal welfare, agro forestry, conservation of natural resources and maintaining quality of soil, air and water including contribution to the Clean Ganga Fund set-up by the Central Government for rejuvenation of river Ganga;
- (v) protection of national heritage, art and culture including restoration of buildings and sites of historical importance and works of art; setting up public libraries; promotion and development of traditional arts and handicrafts;
- (vi) measures for the benefit of armed forces veteran, war widows and their dependents;
- (vii) training to promote rural sports, nationally recognized sports, para olympic sports and Olympic sports;
- (viii) contribution to the Prime Minister's National Relief Fund or any other fund set up by the Central Government for socio-economic development and relief and welfare of the Scheduled Castes, the Scheduled Tribes, other backward classes, minorities and women;
- (ix) contributions or funds provided to technology incubators located within academic institutions which are approved by the Central Government;
- (x) rural development projects.
- (xi) slum area development where 'slum area' shall mean any area declared as such by the Central Government or any State Government or any other competent authority under any law for the time being in force.

However, in determining CSR activities to be undertaken, preference would need to be given to local areas and the areas around where the company operates.



As per Clarification issued by MCA on 18th June, 2014; following may be noted with regard to provisions mentioned under section 135:

- One-off events such as marathons/ awards/ charitable contribution/ advertisement/sponsorships of TV programmes etc. do not be qualified as part of CSR expenditure.
- Expenses incurred by companies for the fulfillment of any Act/ Statute of regulations (such as Labour Laws, Land Acquisition Act etc.) are not count as CSR expenditure under the Companies Act.

### CSR Policy

CSR Policy relates to the activities to be undertaken by the company as specified in Schedule VII to the Act and the expenditure thereon, excluding activities undertaken in pursuance of normal course of business of a company.

The Rules provide that the CSR Policy of a company shall, *inter alia* include the following, namely:

- A list of CSR projects or programs which a company plans to undertake falling within the purview of the Schedule VII of the Act, specifying modalities of execution of such project or programs and implementation schedule for the same; and
- Monitoring process of such projects or programs.

But the activity should not be undertaken in pursuance of normal course of business of a company. The Board shall ensure that the activities included by the company in its CSR Policy are related to the activities mentioned in Schedule VII of the Act.

The CSR Policy of the company shall specify that the surplus arising out of the CSR projects or programs or activities shall not form part of business profit of a company.

The Board after taking into account the recommendations made by the Corporate Social Responsibility Committee, approve the Corporate Social Responsibility Policy for the company and disclose contents of such Policy in its report and also place it on the company's website. The Board of every company ensures that the activities as are included in Corporate Social Responsibility Policy of the company are undertaken by the company.

### CSR Expenditure

- The Board of every company shall ensure that the company spends, in every financial year, at least two per cent of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy. This amount will be CSR expenditure.
- If the company fails to spend such amount, the Board shall, in its report specify the reasons for not spending the amount.
- The company shall give preference to the local area and areas around it where it operates, for spending the amount earmarked for Corporate Social Responsibility activities.
- Expenditure incurred on specified activities that are carried out in India only will qualify as CSR expenditure. Such expenditure includes contribution to the corpus or on projects or programs relating to CSR activities.
- Expenditure incurred in undertaking normal course of business will not form a part of the CSR expenditure. Companies would need to clearly distinguish those activities which are undertaken specifically in pursuance of normal course of business and those that are done incrementally as part of the CSR initiatives.
- Any surplus arising out of CSR activities will not be considered as business profit for the spending company.
- Expenditure incurred by foreign holding company for CSR activities in India will qualify as CSR spend of the Indian subsidiary if, the CSR expenditures are routed through Indian subsidiaries and if the Indian subsidiary is required to do so as per section 135 of the Act.

### Computation of net profit

"Net profit" as per explanation of Section 135(5) means that net profit shall not include such sums as may be prescribed, and shall be calculated in accordance with the provisions of section 198. The net worth, turnover and net profits are to be computed in terms of Section 198 of the 2013 Act as per the profit and loss statement prepared by the company in terms of Section 381 (1) (a) and Section 198 of the 2013 Act. Every company will have to report its standalone net profit during a financial year for the purpose of determining whether or not it triggers the threshold criteria as prescribed under Section 135(1) of the Companies Act.

- **Indian company:** The CSR Rules have clarified the manner in which a company's net worth will be computed to determine if it fits into the 'spending' norm. In order to determine the 'net profit', dividend income received from another Indian company or profits made by the company from its overseas branches have been excluded. Moreover, the 2% CSR is computed as 2% of the average net profits made by the company during the preceding three financial years.
- **Foreign company:** The CSR Rules prescribe that in case of a foreign company that has its branch or a

project office in India, CSR provision will be applicable to such offices. CSR Rules further prescribe that the balance sheet and profit and loss account of a foreign company will be prepared in accordance with Section 381(1)(a) and net profit to be computed as per Section 198 of the Companies Act. It is not clear as to how the computation of net worth or turnover would be arrived at in case of a branch or project office of a foreign company

Profits from any overseas branch of the company, including those branches that are operated as a separate company would not be included in the computation of net profits of a company. Besides, dividends received from other companies in India which need to comply with the CSR obligations would not be included in the computation of net profits of a company.

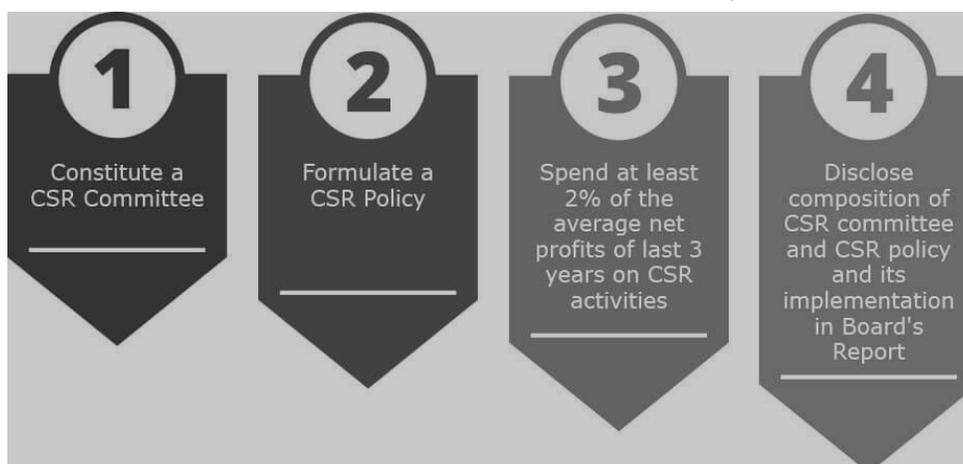
### Disclosure Requirements

It is mandatory for companies to disclose in Board's Report, an annual report on CSR. The report of the Board of Directors attached to the financial statements of the Company would also need to include an annual report on the CSR activities of the company in the format prescribed containing following particulars –

- A brief outline of the company's CSR policy, including overview of projects or programs proposed to be undertaken and a reference to the web-link to the CSR policy and projects or programs.
- The Composition of the CSR Committee.
- Average net profit of the company for last three financial years
- Prescribed CSR Expenditure
- Details of CSR spent during the financial year.
- In case the company has failed to spend the two per cent of the average net profit of the last three financial years or any part thereof, the company shall provide the reasons for not spending the amount in its Board report.
- A responsibility statement of the CSR Committee that the implementation and monitoring of CSR Policy, is in compliance with CSR objectives and Policy of the company.

If the company has been unable to spend the minimum required on its CSR initiatives, the reasons for not doing so are to be specified in the Board Report. If a company has a website, the CSR policy and the report containing details of such activities have to be made available on the company's website for informational purposes.

### GIST OF CSR U/S 135 OF COMPANIES ACT, 2013



**Annexure I**

**FORMAT FOR THE ANNUAL REPORT ON CSR ACTIVITIES TO BE INCLUDED IN THE BOARD REPORT**

1. A brief outline of the company's CSR policy, including overview of projects or programs proposed to be undertaken and a reference to the web-link to the CSR policy and projects or programs.
2. The Composition of the CSR Committee.
3. Average net profit of the company for last three financial years.
4. Prescribed CSR Expenditure (two percent of the amount as in item 3 above)
5. Details of CSR spent during the financial year.
  - (a) Total amount to be spent for the financial year;
  - (b) Amount unspent, if any;
  - (c) Manner in which the amount spent during the financial year is detailed below:

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
S No	CSR project or activity identified	Sector in which the project is covered	Projects or programs (1) Local area or other  (2) Specify the State and district where projects or programs was taken	Amount outlay (budget) project or programs wise	Amount spent on the projects or programs Sub-heads: (1) Direct expenditure on projects or programs  (2) Overheads:	Cumulative expenditure upto the reporting period.	Amount spent: Direct or through implementing agency
1							
2							
3							
	TOTAL						

\* Give details of implementing agency

6. In case the company has failed to spend the two percent of the average net profit of the last three financial years or any part thereof, the company shall provide the reasons for not spending the amount in its Board report.

7. A responsibility statement of the CSR committee that the implementation and monitoring of CSR Policy, is in compliance with CSR objectives and policy of the company.

Sd/- (Chief Executive Officer or Managing Director or Director)	Sd/- (Chairman or Committee)	CSR (Person specified under clause (d) of sub section (1) of section 380 of the Act)  (wherever applicable)
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### Frequently asked Questions

### Annexure II

Sl. No.	FAQs
1.	<b>Whether CSR expenditure of a company can be claimed as business expenditure?</b>
	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.
2.	<b>What tax benefit can be availed under CSR?</b>
	No Specific Tax Exemptions Have Been Extended to CSR Expenditure Per Se. The Finance Act, 2014 Also Clarifies That Expenditure On CSR does not form part of business expenditure. While no specific tax exemption has been extended to expenditure incurred on CSR, spending on several activities like contributions to Prime Minister's Relief Fund, scientific research, rural development projects, skill development projects, agricultural extension projects, etc., which find place in Schedule VII, already enjoy exemptions under different sections of the Income Tax Act, 1961.
3.	<b>Whether a holding or subsidiary of a company which fulfils the criteria under section 135(1) has to comply with section 135, even if the holding and subsidiary itself does not fulfill the criteria.</b>
	Holding or subsidiary of a company does not have to comply with section 135(1) unless the holding or subsidiary itself fulfills the criteria.
4.	<b>Whether provisions of CSR are applicable on Section 8 company, if it fulfills the criteria of section 135(1) of the Act.</b>
	Section 135 of the Act reads "Every company.....", i.e. no specific exemption is given to section 8 companies with regard to applicability of section 135, hence section 8 companies are required to follow CSR provisions.
5.	<b>Whether display of CSR policy of a company on website of the company is mandatory or not?</b>

	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 (refer Rule 8 & 9 of CSR Policy, Rules 2014).
<b>6.</b>	<b>Whether reporting of CSR is mandatory in Board's Report?</b>
	The Board's Report of a company qualifying under section 135(1) pertaining to a financial year commencing on or after the 1st day of April, 2014 shall include an annual report on CSR containing particulars specified in Annexure. (refer Rule 9 of CSR Policy, Rules 2014).
<b>7.</b>	<b>Whether it is mandatory for Foreign Company to give report on CSR activity?</b>
	In case of a foreign company, the balance sheet filed under sub-clause (b) of sub-section (1) of section 381 shall contain an Annexure regarding report on CSR.
<b>8.</b>	<b>Can the unspent amount from out of the minimum required CSR expenditure be carried forward to the next year?</b>
	The Board is free to decide whether any unspent amount from out of the minimum required CSR expenditure is to be carried forward to the next year. However, the carried forward amount should be over and above the next year's CSR allocation equivalent to at least 2% of the average net profit of the company of the immediately preceding three years.
<b>9.</b>	<b>What is the role of Government in monitoring implementation of CSR by companies under the provision of the Companies Act, 2013?</b>
	The main thrust and spirit of the law is not to monitor but to generate conducive environment for enabling the corporates to conduct themselves in a socially responsible manner, while contributing towards human development goals of the country.  The existing legal provisions like mandatory disclosures, accountability of the CSR Committee and the Board, provisions for audit of the accounts of the company etc., provide sufficient safeguards in this regard. Government has no role to play in monitoring implementation of CSR by companies.
<b>10.</b>	<b>Can CSR funds be utilized to fund Government Scheme?</b>
	The objective of this provision is indeed to involve the corporates in discharging their social responsibility with their innovative ideas and management skills and with greater efficiency and better outcomes. Therefore, CSR should not be interpreted as a source of financing the resource gaps in Government Scheme. Use of corporate innovations and management skills in the delivery of 'public goods' is at the core of CSR implementation by the companies. In-principle, CSR fund of companies should not be used as a source of funding Government Schemes. CSR projects should have a larger multiplier effect than that under the Government schemes.  However, under CSR provision of the Act and rules made thereunder, the Board of the eligible company is competent to take decision on supplementing any Government Scheme provided

	the scheme permits corporates participation and all provisions of Section 135 of the Act and rules thereunder are complied by the company.
11.	<b>How can companies with small CSR funds take up CSR activities in a project/programme mode?</b>
	A well designed CSR project or programme can be managed with even small fund. Further, there is a provision in the CSR Policy Rules, 2014 that such companies can combine their CSR programs with other similar companies by way of pooling their CSR resources. (refer Rule 4 in Companies (CSR Policy) Rules, 2014).

### LESSON ROUND UP

- As per section 135 of the Companies Act 2013, the CSR provision will be applicable companies which fulfills any of the following criteria during the immediately preceding financial year:-
  - Companies having net worth of rupees five hundred crore or more, or
  - Companies having turnover of rupees one thousand crore or more or
  - Companies having a net profit of rupees five crore or more
- The Board of every company shall ensure that the company spends, in every financial year, at least two per cent of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy. This amount will be CSR expenditure
- The CSR Committee of the company may decide to undertake its CSR activities approved by the Board, through
  - (a) a company established under section 8 of the Act or a registered trust or a registered society, established by the company, either singly or alongwith any other company, or
  - (b) a company established under section 8 of the Act or a registered trust or a registered society, established by the Central Government or State Government or any entity established under an Act of Parliament or a State legislature.
- It is mandatory for companies to disclose in Board's Report, an annual report on CSR.

### GLOSSARY

#### Registered Trust

As per section 3 of Indian Trust Act 1882 "A Trust is an obligation annexed to the ownership of the property, and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him, for the benefit of another, or of another and the owner".

A trust may either be a private trust or public trust.

As per section 5 of the Indian Trusts Act, a private Trust in relation to an immovable property must be created by a non-testamentary instrument in writing, signed by the author of the trust or the trustee and registered (under Section 17 of Indian Registration Act) . Thus, registration of a trust is necessary when it is declared by a non-testamentary instrument. This registration would still be required, even if the instrument declaring the trust is exempt from registration under the Indian

Registered Society	<p>Registration Act. In case of a Private Trust declared by a will, registration will not be necessary, even if it involves an immovable property. Registration will not be required, of a trust in relation to movable property. In case of Public Trust, whether in relation to movable property or an immovable property and whether created under a will or <i>inter vivos</i>, registration is optional but desirable.</p> <p>A society registration can be done for the development of fine arts, science, or literature or else for diffusion of purposeful knowledge or charitable purposes of political education. According to section 20 of The Society Registration Act, 1860 a society registration can be done for following purposes:</p> <ul style="list-style-type: none"> <li>• Promotion of fine arts</li> <li>• Diffusion of political education</li> <li>• Grant of charitable assistance</li> <li>• Promotion of science and literature</li> <li>• Creation of military orphan funds</li> <li>• Maintenance or foundation of galleries or public museum</li> <li>• Maintenance or foundation of reading rooms or libraries</li> <li>• Promotion or diffusion or instruction of useful knowledge</li> </ul> <p>Un- registered societies have certain disadvantages.</p>
Section 8 Company	<p>A limited company can be incorporated under section 8 of Companies Act, 2013 with the following:</p> <p>(a) It has in its objects the promotion of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment or any such other object;</p> <p>(b) it intends to apply its profits, if any, or other income in promoting its objects; and</p> <p>(c) itintends to prohibit the payment of any dividend to its members.</p> <p>Importantly, these are incorporated with the object of promotion of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment or any such other object.</p>
Net profit	<p>For the purposes of section 135 of Companies Act, 2013 "net profit" shall not include such sums as may be prescribed, and shall be calculated in accordance with the provisions of section 198.</p> <p>Further according to Rule 2(f) of the Companies (Corporate Social Responsibility Policy ) Rules, 2014 "Net profit" means the net profit of a company as per its financial statement prepared in accordance with the applicable provisions of the Act, but shall not include the following, namely :-</p>



# Lesson 8

## Accounts, Audit and Auditors

### LESSON OUTLINE

- Accounts of Companies
- Requirement of keeping books of account.
- Financial statements
- Consolidated financial statements
- National Financial Reporting Authority (NFRA)
- Internal audit
- Appointment, qualification, disqualification, removal of auditors
- Casual vacancy in the office of auditor
- Audit Report
- Branch audit
- Secretarial Audit
- Cost records and audit
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

The health of a business is shown by the books of account of the company. The company is maintaining the records through the books as required by statute or as per the need of the hour. But, the maintenance of the books of account is not enough. The verification and checking is also important.

The checking of books of account is known as auditing. The auditing is also known as post mortem of books. It is helpful in the future planning. The auditing is done by the auditor. In India, the statutory audit is conducted by statutory auditor. It is mandatory in nature. Every company is required to audit its books of account. It is not only statutory audit which is in existence; now a days, the cost audit, Secretarial audit, management audit etc. are also conducted by the companies. It is helpful in the formulation of the company's policies.

After reading this lesson, you will be able to understand the provisions about keeping books of account, inspection of books of account and other provisions for balance sheet and profit and loss account under the Companies Act. It also discusses provisions for audit and auditors, their appointment, qualifications, resignation, removal, duties and liabilities.

## INTRODUCTION

The shareholders provide capital to the company for running the business. They are in a way, the owners of the company. But, all of them cannot take part in managing the affairs of the company as their number is usually much more. But they have every right to know as to how their money has been dealt with by the directors in a particular period. This is why perhaps compulsory disclosure through annual information to the shareholders by the directors about the working and financial position of the company enables them to exercise a more intelligent and purposeful control over the affairs of the company. For preparation of annual accounts the maintenance of proper books of account is a must. Section 128 of the Companies Act, 2013 contains the provisions for books of account etc. to be kept by company.

## IMPORTANT TERMINOLOGIES w.r.t. ACCOUNTS OF COMPANIES

The terms “books of accounts”, “books and papers” “financial statement” and financial year have been defined under the Companies Act, 2013 [“the Act”].

As per section 2(12) of the Act, "book and paper" and "book or paper" include books of account, deeds, vouchers, writings, documents, minutes and registers maintained on paper or in electronic form.

As per section 2(13) of the Act, “books of account” includes records maintained in respect of—

- (i) all sums of money received and expended by a company and matters in relation to which the receipts and expenditure take place;
- (ii) all sales and purchases of goods and services by the company;
- (iii) the assets and liabilities of the company; and
- (iv) the items of cost as may be prescribed under section 148 in the case of a company which belongs to any class of companies specified under that section.

As per section 2(40) of the Act, financial statement in relation to a company, includes

- (i) a balance sheet as at the end of the financial year;
- (ii) a profit and loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year;
- (iii) cash flow statement for the financial year;
- (iv) a statement of changes in equity, if applicable; and
- (v) any explanatory note annexed to, or forming part of, any document referred to in sub-clause (i) to sub-clause (iv).

According to 2(41) "financial year", in relation to any company or body corporate, means the period ending on the 31st day of March every year, and where it has been incorporated on or after the 1st day of January of a year, the period ending on the 31st day of March of the following year, in respect whereof financial statement of the company or body corporate is made up:

An application may be made by a company or body corporate, which is a holding company or a subsidiary or associate company of a company incorporated outside India and is required to follow a different financial year for consolidation of its accounts outside India, the Tribunal may, if it is satisfied, allow any period as its financial year, whether or not that period is a year:

## REQUIREMENT OF KEEPING BOOKS OF ACCOUNT ETC. (SECTION 128)

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.

Section 128 specifies that: –

- i. The company must prepare and keep at its registered office the books of account and other relevant books and papers and financial statement for every financial year.
- ii. The books of account must give a true and fair view of the state of the affairs of the company or its branches.
- iii. The books of account must be kept on accrual basis and according to the double entry system of accounting.

### **Place of Keeping Books of Account**

Section 128(1) of the Act requires every company to prepare and keep the books of account and other relevant books and papers and financial statements at its registered office. However, all or any of the books of accounts may be kept at such other place in India as the Board of directors may decide. When the Board so decides, the company is required within seven days of such decision to file with the Registrar of Companies [“RoC”] a notice in writing giving full address of that other place. Such intimation is to be made in e-form AOC 5 to the RoC.

### **Maintenance of Books of account in electronic form**

- The maintenance of books of account or other relevant papers in electronic mode is permitted. Such books of accounts or other relevant books and papers maintained in electronic mode shall remain accessible in India so as to be usable for subsequent use [“the Companies (Accounts) Rules, 2014 hereinafter referred in this Chapter as “Rule”] (Rule 3(1) of the Rules).
- The information contained in the records shall be retained completely in the format in which they were originally generated, sent or received, or in a format which shall present accurately the information generated, sent or received and the information contained in the electronic records shall remain complete and unaltered (Rule 3(2) of the Rules).
- The information received from branch offices shall not be altered and shall be kept in a manner where it shall depict what was originally received from the branches (Rule 3(3) of the Rules).
- The information in the electronic record of the document shall be capable of being displayed in a legible form (Rule 3(4) of the Rules).
- There shall be a proper system for storage, retrieval, display or printout of the electronic records as the Audit Committee, if any, or the Board may deem appropriate and such records shall not be disposed of or rendered unusable, unless permitted by law:

Provided that the back-up of the books of account and other books and papers of the company maintained in electronic mode, including at a place outside India, if any, shall be kept in servers physically located in India on a periodic basis. (Rule 3(5) of the Rules)

- The company shall intimate to the Registrar on an annual basis at the time of filing of financial statement -
  - (a) the name of the service provider;
  - (b) the internet protocol address of service provider;
  - (c) the location of the service provider (wherever applicable);

- (d) where the books of account and other books and papers are maintained on cloud, such address as provided by the service provider. (Rule 3(6) of the Rules)

### **Books of Account in Respect of Branch Office**

The branches of the company, if any, in India or outside India shall also keep the books of account in the same manner as specified in sub-section (1), for the transaction effected at the branch office. Further the branch offices are required to send the proper summarized return at quarterly intervals to the company at its registered office and kept open to directors for inspection. [Rule 4(1) of the Rules]

### **Preservation of books of accounts**

The books of account of every company relating to a period of not less than eight financial years immediately preceding a financial year, or where the company had been in existence for a period less than eight years, in respect of all the preceding years together with the vouchers relevant to any entry in such books of account shall be kept in good order:

Where an investigation has been ordered in respect of the company under Chapter XIV of the Act i.e. Inspection, Inquiry and Investigation, the Central Government may direct that the books of account may be kept for such longer period as it may deem fit. [Section 128(5)]

### **Persons responsible to maintain books**

According to section 128(6) the following persons are responsible to take all reasonable steps to secure compliance by the company with the requirement of maintenance of books of accounts etc.

- i. Managing Director,
- ii. Whole-Time Director, in charge of finance
- iii. Chief Financial Officer; or
- iv. Any other person of a company charged by the Board with duty of complying with provisions of section 128.

### **Penalty**

In case the aforementioned persons referred to in Section 128(6) of the Act (i.e. MD, WTD, CFO etc.) contravene such provisions, they shall in respect of each offence, be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees or both.

### **SECTION 129: FINANCIAL STATEMENT**

This section provides that the financial statements shall give a true and fair view of the state of affairs of the company or companies in the form as provided for different class or classes in Schedule III and shall comply with accounting standards notified under section 133 of the Act. Insurance companies, banking company, companies engaged in generation/ supply of electricity or any other class of companies shall make financial statements in the form as has been specified in or under the Act governing such companies. [Section 129(1)]

The financial statement shall be laid in the annual general meeting of that financial year. [Section 129(2)]

In addition to financial statements provided under sub-section (2), where a company has one or more subsidiaries or associate companies, it shall prepare a consolidated financial statement of the company and of all the subsidiaries and associate companies in the same form and manner as that of its own and in accordance with applicable accounting standards, which shall also be laid before the annual general meeting of the company along with the laying of its financial statement under sub-section (2), as mentioned above.

The company shall also attach along with its financial statement, a separate statement containing the salient features of the financial statement of its subsidiary or subsidiaries and associate company or companies in such form AOC-1.

The consolidation of accounts of companies is discussed later in this chapter. Further, the Central Government may exempt a class or classes of companies from any of the requirements of this section.

### **True and Fair view**

As per provisions of sub-sections (1) and (2), every financial statement of the company must give true and fair view of the state of affairs of the company at the end of financial year. True and Fair view in respect of financial statement means-

- financial statements and items contained should comply with accounting standards notified under section 133;
- financial statement shall be in form or forms as provided for different class or classes of companies in Schedule III;
- in case of any insurance or banking company or any company engaged in the generation or supply of electricity or to any other class of company for which a form of financial statement has been specified in or under the Act governing such class of company, not treated to be disclosing a true and fair view of the state of affairs of the company, merely by the reason of the fact that they do not disclose -
  - in the case of an insurance company, any matters which are not required to be disclosed by the Insurance Act, 1938, or the Insurance Regulatory and Development Authority Act, 1999;
  - in the case of a banking company, any matters which are not required to be disclosed by the Banking Regulation Act, 1949;
  - in the case of a company engaged in the generation or supply of electricity, any matters which are not required to be disclosed by the Electricity Act, 2003;
  - in the case of a company governed by any other law for the time being in force, any matters which are not required to be disclosed by that law.

### **Persons responsible for compliance**

The persons responsible to take all reasonable steps to secure compliance by the company with the requirement of Section 129 are [(Section 129(7))-

- Managing Director
- Whole-Time Director
- CFO
- Other person of a company charged by the Board with the duty of complying with requirements of section 129.

Where any of the aforementioned officers are absent, all the directors shall be responsible and punishable.

### **Penalty**

In case persons referred to in sub-section (7) fail to take reasonable steps to secure compliance or contravene provisions of Section 129, they shall in respect of each offence be punishable with imprisonment

for a term which may extend to one year or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees or with both.

### **FORM OF FINANCIAL STATEMENTS (SCHEDULE III)**

The financial statements shall be in the form or forms as may be provided for different class or classes of companies. Schedule III contains general instructions for preparation of balance sheet and statement of profit and loss account.

### **CONSOLIDATED FINANCIAL STATEMENTS**

The Companies Act 2013 has made preparation of consolidated accounts mandatory for all companies including unlisted companies and private companies having one or more subsidiaries or associates or joint ventures.

According to sub section 3 of the section 129 of the Companies Act, 2013, where a company has one or more subsidiaries or associates or joint ventures, it shall, in addition to its financial statements for the financial year, prepare a consolidated financial statement of the company and of all the subsidiaries or associates or joint ventures in the same form and manner as that of its own which shall also be laid before the annual general meeting of the company along with the laying of its financial statement.

The company shall also attach along with its financial statement, a separate statement containing the salient features of the financial statement of its subsidiary/ies or associate/s or joint venture/s in Form AOC-1 (Rule 5).

### **MANNER OF CONSOLIDATION OF ACCOUNTS**

The consolidation of financial statements of the company shall be made in accordance with the provisions of Schedule III of the Act and the applicable accounting standards:

Provided that in case of a company covered under sub-section (3) of section 129 which is not required to prepare consolidated financial statements under the Accounting Standards, it shall be sufficient if the company complies with provisions on consolidated financial statements provided in Schedule III of the Act.

Provided further that nothing in this rule shall apply in respect of preparation of consolidated financial statements by a company if it meets the following conditions:-

- (i) it is a wholly-owned subsidiary, or is a partially-owned subsidiary of another company and all its other members, including those not otherwise entitled to vote, having been intimated in writing and for which the proof of delivery of such intimation is available with the company, do not object to the company not presenting consolidated financial statements;
- (ii) it is a company whose securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India; and
- (iii) its ultimate or any intermediate holding company files consolidated financial statements with the Registrar which are in compliance with the applicable Accounting Standards.

### **RE-OPENING OF ACCOUNTS ON COURT'S OR TRIBUNAL'S ORDERS [Section 130]**

Section 130 provides for provisions relating to re-opening or re-casting of books of accounts of the company. Accordingly,

- (i) A company shall not re-open its books of account and shall not recast its financial statements, unless an application to the tribunal, in this regard is made by any one or more of the following -
  - (a) the Central Government, or

- (b) the Income-tax authorities, or
  - (c) the Securities and Exchange Board of India (SEBI), or
  - (d) any other statutory regulatory body or authority or any person concerned, and
  - (e) an order in this regard is made by a court of competent jurisdiction or the Tribunal.
- (ii) The re-opening and recasting of financial statements is permitted only for the following reasons –
- (a) the relevant earlier accounts were prepared in a fraudulent manner; or
  - (b) the affairs of the company were mismanaged during the relevant period, casting a doubt on the reliability of financial statements.
- (iii) The Tribunal shall give the notice to-
- (a) the Central Government,
  - (b) the Income-tax authorities,
  - (c) the Securities and Exchange Board,
  - (d) any other statutory regulatory body or authority concerned and shall take into consideration the representations, if any, made by Central Government or the authorities, Securities and Exchange Board or the body or authority concerned or any other person concerned before passing any order under this section.
- (iv) The accounts so revised or re-cast under this section shall be final.

The Act clearly provides that in respect of re-opening of books of account relating to a period earlier than eight financial years immediately preceding the current financial year, no order shall be made by the tribunal unless the Central Government has directed to for keeping of books of account for a period longer than eight years under section 128(5), the books of account may be ordered to be re-opened within such longer period.

### **VOLUNTARY REVISION OF FINANCIAL STATEMENTS OR BOARD'S REPORT [Section 131]**

Section 131 allows the directors to prepare revised financial statement or a revised Board's report in respect of any of the three preceding financial years after obtaining approval of the Tribunal, if it appears to them that the company's financial statement or the Board's Report do not comply with the requirements of Section 129 or Section 134.

The Tribunal shall give notice to the Central Government and the Income-tax authorities and shall take into consideration the representations, if any, made by that Government or the authorities before passing any order under this section.

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 such 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.

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 section 134; and

- (b) the making of any necessary consequential alternation.

### **SIGNATURE OF FINANCIAL STATEMENT**

The financial statement, including consolidated financial statement, if any, shall be approved by the Board of Directors before they are signed on behalf of the Board by the chairperson of the company where he is authorised by the Board or by two directors out of which one shall be managing director, if any, and the Chief Executive Officer, the Chief Financial Officer and the company secretary of the company, wherever they are appointed, or in the case of One Person Company, only by one director, for submission to the auditor for his report thereon.

The auditors' report shall be attached to every financial statement. A report by its Board of Directors shall also be attached to statements laid before a company in general meeting.

### **RIGHT OF MEMBER TO COPIES OF AUDITED FINANCIAL STATEMENT**

According to section 136 a copy of financial statements including consolidated financial statement, if any, auditor's report along with 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 every member of the Company, every trustee for the debenture holder and all other persons who are so entitled, twenty one days before the date of the meeting.

The copies of the documents are sent less than twenty-one 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 ninety-five per cent. 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 ninety-five per cent. of the total voting power exercisable at the meeting.

### **Obligation of listed company**

In the case of a company whose shares are listed on a recognised stock exchange, provisions of section 136 shall be deemed to have been complied with, if the copies of the documents are made available for inspection at its registered office, during working hours, for a period of twenty-one days before the date of the meeting and a statement containing the salient features of such documents in the prescribed form [i.e. form AOC-3] or copies of the documents, as the company may deem fit, is sent to every member of the company and to every trustee for the holders of any debentures issued by the company not less than twenty-one days before the date of the meeting.

Every listed company is required to supply a copy of the complete financial statements with auditor's report and director's report, to such shareholders who ask for full financial statements.

Further in case of all listed companies and such public companies which have a net worth of more than one crore rupees and turnover of more than ten crore rupees, the financial statements may be sent-

- (a) by electronic mode to such members whose shareholding is in dematerialised format and whose email ids are registered with Depository for communication purposes;
- (b) where shareholding is held otherwise than by dematerialised format, to such members who have positively consented in writing for receiving by electronic mode; and
- (c) by despatch of physical copies through any recognised mode of delivery as specified under section 20 of

the Act, in all other cases.

Every listed company is also required to 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:

A listed company which has a subsidiary incorporated outside India (herein referred to as "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 of this proviso shall 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.

### **Financial statements of subsidiaries**

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.

### **Right to inspect**

Every company shall be under an obligation to allow every member or trustee of the holder of any debentures issued by the company to inspect the financial statements and documents to be attached thereto stated under sub-section (1) at its registered office during business hours.

In case if the listed company has sent the salient features of financial statements to members and debenture trustees in prescribed form then copy of financial statements including consolidated financial statement, if any, auditor's report along with every other document required by law to be annexed or attached to the financial statements shall be available for inspection at its registered office during working hours for a period of 21 days before the date of meeting.

### **Penal provisions**

If any default is made in complying with the provisions of this section, the company shall be liable to a penalty of –

- (i) twenty-five thousand rupees and
- (ii) every officer of the company who is in default shall be liable to a penalty of five thousand rupees.

### **SECTION 137: COPY OF FINANCIAL STATEMENT TO BE FILED WITH REGISTRAR**

Section 137 requires every company to file the financial statements including consolidated financial statement together with Form AOC- 4 and AOC-4(CFS) with the Registrar of Companies (RoC) within 30 days from the day on which the annual general meeting held and adopted the financial statements with such

fees or additional fee as specified in Companies (Registration Offices and Fees) Rules, 2014.

If the financial statements are not adopted at the annual general meeting or adjourned annual general meeting, such unadopted financial statements along with the required documents be filed with the RoC with in thirty days of the date of annual general meeting. The RoC shall take them in his record as provisional, until the adoption at annual general meeting.

The One Person Company shall file the copy of financial statements duly adopted by its members within a period of one hundred and eighty days from the closure of financial year.

The company shall also attach the accounts of subsidiaries incorporated outside India and which have not established their place of business in India with the financial statements.

Provided also that in the case of a subsidiary which has been incorporated outside India (herein referred to as "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 of the fourth proviso (accounts of subsidiaries) shall 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.

The class of companies as may be notified by the Central Government from time to time, shall mandatorily file their financial statement in Extensible Business Reporting Language (XBRL) format and the Central Government may specify the manner of such filing under such notification for such class of companies (Rule 12(2)).

If annual general meeting has not been held, the financial statement duly signed along with the statement of facts and reasons for not holding the annual general meeting shall be filed with the RoC within thirty days of the last days before which the annual general meeting should have been held.

### **Penalty for non-compliance**

If company fails to comply with the requirement of submission of financial statement with RoC, the company shall be punishable with fine of one thousand rupees for every day during which failure continues subject to maximum of rupees ten lakh. The managing director and CFO if any, and, in the absence of such managing director or CFO, any other director who is charged by the Board with the responsibility of complying with the provisions of this section, in the absence of such director, all directors of the company shall be punishable with imprisonment for a term which may extend upto six months or with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees or with both.

### **NATIONAL FINANCIAL REPORTING AUTHORITY (NFRA)**

Through Section 132 of the Companies Act, 2013, the Central Government has introduced a new regulatory authority named as National Authority for Financial Reporting known as National Financial Reporting Authority (NFRA) with wide powers to recommend, enforce and monitor the compliance of accounting and auditing standards. The Companies Act, 1956 empowers the Central Government to form a Committee for recommendations on Accounting Standards which is National Advisory Committee on Accounting Standards (NACAS). This is now being renamed with enhanced independent oversight powers and authority as National Financial Reporting Authority (NFRA).

NFRA shall be responsible for monitoring and enforcing compliance of auditing and accounting standards and for that purpose, oversee the quality of professions associated with ensuring such compliances. The Authority shall investigate professional and other misconducts which may be committed by Chartered

Accountancy members and firms. There is also a provision for appellate authority.

The National Financial Reporting Authority shall be a quasi – judicial body to regulate matters related to accounting and auditing. With increasing demand of non – financial reporting, it may be referred to as a National level business Reporting Authority to regulate standards of all kind of reporting- financial as well as non – financial, by the companies in future.

National Financial Reporting Authority shall give its recommendations on accounting standards and auditing standards. It shall only recommend and it is the Central Government who shall prescribe such standards.

### Objective

The objectives of National Financial Reporting Authority *inter alia* shall be as follows:

- (1) Make recommendations on formulation of accounting and auditing policies and standards for adoption by companies, class of companies or their auditors;
- (2) Monitor and enforce the compliance with accounting standards, monitor and enforce the compliance with auditing standards;
- (3) Oversee the quality of service of professionals associated with ensuring compliance with such standards and suggest measures required for improvement in quality of service, and
- (4) Perform such other functions as may be prescribed in relation to aforementioned objectives.

These objectives simply bring chartered accountants, cost accountants, management accountants, company secretaries as well as independent directors / members audit committees under jurisdiction of NFRA.

### Constitution of NFRA

The constitution of National Financial Reporting Authority, which is supposed to be constituted as an oversight regulatory body to recommend accounting and auditing standards, shall be governed by sub - section (3) and (4) of section 132. Accordingly,

- (i) It shall consist of a chairperson, who shall be a person of eminence & having expertise in accountancy, auditing, finance, business administration, business law, economics or similar disciplines, to be nominated by Central Government, and such other prescribed members not exceeding 15.
- (ii) The chairperson and all members shall make a declaration in prescribed form about no conflict of interest or lack of independence in respect of their appointment. The chairperson and all full – time members shall not be associated with any audit firm or related consultancy firm during course of their appointment and two years after ceasing to hold such appointment.
- (iii) The head office of National Financial Reporting Authority shall be at New Delhi and it may, meet at such other places in India, as it deems fit.
- (iv) Its accounts shall be audited by Comptroller and Auditor General of India (CAG) and such accounts as certified by CAG, together with audit report, shall be forwarded annually to the Central Government.

### Jurisdiction, Powers of and Imposition of Penalties by NFRA

The National Financial Reporting Authority shall have jurisdiction over bodies corporate and persons for matters of professional and other misconduct committed, by any member or firm of Chartered Accountants registered under the Chartered Accountants Act, 1949. No other institute or body (including professional institutes) shall initiate or continue any proceeding in such matters of misconduct where the authority has

initiated an investigation under this section.

The Authority shall have powers as are vested in a civil court under Code of Civil Procedure, 1908 in respect of following matters:

1. Discovery and production of books of accounts and other documents
2. Summoning and enforcing the attendance of persons and examining them on oath
3. Inspection of any books, registers and other documents of any person
4. Issuing commission for examination of witness or documents.

Sub-section (4) provides a bar on any body or any institute, in initiating or continuing the proceedings in such matters of misconduct where the National Financial Reporting Authority has initiated an investigation under this section;

The Authority shall have powers to make an order in relation to:

A. Imposing penalty of

- (i) not less than one lakh rupees which may extend to five times of the fees received in case of individuals and
- (ii) not less than five lakh rupees which may extend to ten times of the fees received in case of firms

- B. Debarring member or the firm from engaging himself or itself from practice as member of the Institute of Chartered Accountant of India for a period of six months to ten years as may be decided by the National Financial Reporting Authority.

### **Appeals and Appellate Authority**

Any person aggrieved by any order of the National Financial Reporting Authority may prefer appeal to Appellate Authority in such manner and on payment of such fee as may be prescribed.

### **SECTION 133: CENTRAL GOVERNMENT TO PRESCRIBE ACCOUNTING STANDARDS**

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 National Financial Reporting Authority. The Ministry has subsequently clarified that till the Standards of Accounting or any addendum thereto is prescribed by Central Government in consultation and recommendation of the National Financial Reporting Authority, the existing Accounting Standards notified under the Companies Act 1956 shall continue to apply.

- On 6th Feb. 2015 the Ministry of Corporate Affairs (MCA), the Central Government, in consultation with the National Advisory Committee on Accounting Standards (NACAS), notified the Companies (Indian Accounting Standards) Rules, 2015 in exercise of the powers conferred by section 133 and section 469 of the Companies Act, 2013 and sub-section (1) of section 210A of the Companies Act, 1956. These rules came into force on 1st April 2015.

As a result of this notification, notifying the Companies (Indian Accounting Standards) Rules, 2015, there shall be two separate sets of Accounting Standards –

1. Indian accounting Standards (Ind AS) as specified in the Annexure to Companies (Indian Accounting Standards) Rules, 2015

2. Accounting standards as specified in Annexure to the Companies (Accounting Standards) Rules, 2006

**Indian accounting Standards (Ind AS)**

Indian Accounting Standards (Ind AS) are the accounting standards prescribed under Section 133 of the Companies Act, 2013. Indian Accounting Standards (Ind AS) are specified in the Annexure to the Companies (Indian Accounting Standards) Rules, 2015. These accounting standards are converged with corresponding International Financial Reporting Standards.

**Applicability under Rule 3 of the Companies (Indian Accounting Standards) Rules, 2015**

<ol style="list-style-type: none"> <li>1. Indian accounting Standards (Ind AS) as specified in the Annexure to Companies (Indian Accounting Standards) Rules, 2015</li> </ol>	<ul style="list-style-type: none"> <li>- Applicable to classes of company specified in Rule 4(1) of the Companies (Indian Accounting Standards) Rules, 2015.</li> </ul>
<ol style="list-style-type: none"> <li>2. Accounting standards as specified in Annexure to the Companies (Accounting Standards) Rules, 2006.</li> </ol>	<ul style="list-style-type: none"> <li>- Applicable to the companies other than the classes of companies specified in Rule 4(1) of the Companies (Indian Accounting Standards) Rules, 2015.</li> </ul>

<b>Applicability</b>	<b>w.e.f.</b>
Voluntary basis	Any company and its holding, subsidiary, joint venture or associate company may comply with the Indian Accounting Standards (Ind AS) for financial statements for accounting periods beginning on or after 1st April, 2015, with the comparatives for the periods ending on 31st March, 2015, or thereafter
Mandatory basis for the accounting periods beginning on or after April 1, 2016 with the comparatives for the periods ending on 31st March, 2016, or thereafter	<p>The following companies shall mandatorily comply with Ind AS namely:-</p> <ul style="list-style-type: none"> <li>➤ Companies whose equity or debt securities are listed or are in the process of being listed on any stock exchange (except SME Exchange) in India or outside India and having net worth of rupees five hundred crore or more;</li> <li>➤ Unlisted companies having net worth of rupees five hundred crore or more;</li> <li>➤ holding, subsidiary, joint venture or associate companies of companies covered above.</li> </ul>

<p>mandatory basis for the accounting periods beginning on or after April 1, 2017, with the comparatives for the periods ending on 31st March, 2017, or thereafter</p>	<p>The following companies shall comply Ind AS namely:-</p> <ul style="list-style-type: none"> <li>➤ Companies whose equity or debt securities are listed or are in the process of being listed on any stock exchange (except SME Exchange) in India or outside India and having net worth of less than rupees five hundred crore;</li> <li>➤ Unlisted companies having net worth of rupees two hundred and fifty crore or more but less than rupees five hundred crore.</li> <li>➤ holding, subsidiary, joint venture or associate companies of companies covered above.</li> </ul>
<p>In case of NBFCs, for accounting periods beginning on or after the 1st April, 2018, with comparatives for the periods ending on 31st March, 2018, or thereafter—</p>	<p>The following NBFCs shall comply with the Ind AS</p> <p>(A) NBFCs having net worth of rupees five hundred crore or more;</p> <p>(B) holding, subsidiary, joint venture or associate companies of companies.</p>
<p>In case of NBFCs, for accounting periods beginning on or after the 1st April, 2019, with comparatives for the periods ending on 31st March, 2019, or thereafter</p>	<p>The following NBFCs shall comply with the Ind ASs</p> <p>(A) NBFCs whose equity or debt securities are listed or in the process of listing on any stock exchange in India or outside India and having net worth less than rupees five hundred crore;</p> <p>(B) NBFCs, that are unlisted companies, having net worth of rupees two-hundred and fifty crore or more but less than rupees five hundred crore; and</p> <p>(C) holding, subsidiary, joint venture or associate companies of companies.</p>

#### **Companies exempted under Rule 5 of the Companies (Indian Accounting Standards) Rules, 2015**

The Companies (Indian Accounting Standards) Rules, 2015 shall not be applicable on Banking Companies and Insurance Companies. The Banking Companies and Insurance Companies shall apply the Ind AS as notified by the Reserve Bank of India (RBI) and Insurance Regulatory Development Authority (IRDA) respectively. An insurer or insurance company shall however, provide Ind AS compliant financial statement data for the purposes of preparation of consolidated financial statements by its parent or investor or venturer, as required by the parent or investor or venturer to comply with the requirements of these rules.

## AUDIT AND AUDITORS

### Appointment of Auditors (Section 139)

The Board of Directors of a company shall appoint an individual or firm as the first auditor of a company, other than a Government company, within thirty days from the date of registration of the company. The appointment of first auditor shall be ratified by members at the first annual general meeting. The auditor so appointed shall hold the office from the conclusion of that meeting till the conclusion of sixth annual general meeting and thereafter till the conclusion of every sixth meeting. In the case of failure of the Board to appoint the first auditor, it shall inform the members of the company, who shall within ninety days at an extraordinary general meeting appoint such auditor and such auditor shall hold office till the conclusion of the first annual general meeting.

Any casual vacancy (except as a result of the resignation of an auditor) in the office of an auditor of a company, other than a Government company, shall be filled by the Board of Directors within thirty days. If casual vacancy is as a result of the resignation of an auditor, the Board of Directors shall fill the vacancy within thirty days but such appointment shall also be approved by the company at a general meeting convened within three months of the recommendation of the Board and he shall hold the office till the conclusion of the next annual general meeting.

A retiring auditor may be re-appointed at an annual general meeting, 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.

If at any annual general meeting, no auditor is appointed or re-appointed, the existing auditor shall continue to be the auditor of the company.

### Manner and procedure of selection and appointment of auditors

In case of a company that is required to constitute an Audit Committee under section 177, such committee, and, in cases where such a committee is not required to be constituted, the Board shall take into consideration the qualifications and experience of the individual or the firm proposed to be considered for appointment as auditor and whether such qualifications and experience are commensurate with the size and requirements of the company.

- Before considering the appointment of auditor, the Audit Committee or the Board, as the case may be, shall consider any pending proceeding relating to professional matters of conduct against the proposed auditor before the ICAI or any competent authority or any Court. Further they may call for such other information from the proposed auditor as it may deem fit.
- Where a company is required to constitute the Audit Committee, the committee shall recommend the name of an individual or a firm as auditor to the Board for consideration and in other cases, the Board shall consider and recommend an individual or a firm as auditor to the members in the AGM for appointment.
- If the Board agrees with the recommendation of the Audit Committee, it shall further recommend the appointment of auditor to the members in the AGM otherwise; it shall refer back the recommendation to the committee for reconsideration citing reasons for such disagreement.

- Thereafter if the Audit Committee decides not to reconsider its original recommendation, then Board shall record reasons for its disagreement with the Audit committee and send its own recommendation for consideration of the members in the AGM and if the Board agrees with the recommendations of the Audit Committee, it shall place the matter for consideration by members in the AGM.
- The auditor appointed in the AGM meeting shall hold office from the conclusion of that meeting till the conclusion of the sixth annual general meeting, with the meeting wherein such appointment has been made being counted as the first meeting.

### **Conditions for Appointment and Notice to Registrar-**

Rule 4 of the Companies (Audit and Auditors) Rules, 2014 hereinafter referred as the Rule.

As per second proviso of section 139(1) read with rule 4 stipulates that written consent of the auditor must be taken before appointment. The auditor appointed shall submit a certificate that:

- (a) the individual/firm is eligible for appointment and is not disqualified for appointment under the Act, the Chartered Accountants Act, 1949 and the rules or regulations made thereunder;
- (b) the proposed appointment is as per the term provided under the Act;
- (c) the proposed appointment is within the limits laid down by or under the authority of the Act;
- (d) the list of proceedings against the auditor or audit firm or any partner of the audit firm pending with respect to professional matters of conduct, as disclosed in the certificate, is true and correct.

The Certificate shall also indicate whether the auditor satisfies the criteria provided in section 141 of the Act.

The Company shall inform the auditor concerned of his or its appointment and also file a notice of such appointment with the Registrar in Form ADT-1 within 15 days of the meeting in which the auditor is appointed.

### **APPOINTMENT OF AUDITOR IN GOVERNMENT COMPANY- Section 139(5), 139(7), 139(8), 139 (11)**

The appointment of auditor in Government Company or government controlled (directly/indirectly) company shall be held in accordance with the following provisions:

The First auditor shall be appointed by the Comptroller and Auditor General within 60 days from the date of incorporation and in case of failure to do so, the Board shall appoint auditor within next 30 days and on failure to do so by Board of Directors, it shall inform the members, who shall appoint the auditor within 60 days at an extraordinary general meeting (EGM), such auditor shall hold office till conclusion of first Annual General Meeting.

In case of subsequent auditor for existing government companies, the Comptroller & Auditor General shall appoint the auditor within a period of 180 days from the commencement of the financial year and the auditor so appointed shall hold his position till the conclusion of the Annual General Meeting.

In the case of a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor-General of India, be filled by the Comptroller and Auditor-General of India within thirty days. In case the Comptroller and Auditor-General of India does not fill the vacancy within the said period, the Board of Directors shall fill the vacancy within next thirty days.

The Act also provides that in case the Company has an Audit Committee, then all appointments of Auditor

including filling of casual vacancy, shall be made after taking into account the recommendations of the Committee.

### ELIGIBILITY & QUALIFICATIONS OF AUDITOR

Section 141 (1) & (2) of the Act prescribed the following eligibility and qualifications of auditor which are as under:-

- (i) Only a Chartered Accountant (individual) or a firm where majority of partners practicing in India are Chartered Accountants can be appointed as auditor.
- (ii) 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.

### DISQUALIFICATIONS OF AUDITOR

Section 141 (3) of the Act read with Rule 10 prescribed the following persons shall not be eligible for appointment as an auditor of a company, namely:

- A body corporate, except LLP;
- An officer or employee of the company;
- Any partner/employee of officer or employee of company;
- A person who himself or his relative/partner is holding any security or interest in the company, or any company which is its holding, subsidiary, associate;
  - A person whose relative 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, may hold security or interest in the company of face value not exceeding one thousand rupees or such sum not exceeding Rs. One Lacs. This shall wherever relevant be also applicable in the case of a company not having share capital or other securities.
  - In the event of acquiring any security or interest by a relative, above the threshold prescribed, the corrective action to maintain the limits as specified above shall be taken by the auditor within sixty days of such acquisition or interest.
  - A 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 rupees five lakh shall not be eligible for appointment;
  - 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 one lakh rupees shall not be eligible for appointment;
- 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;

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.
- A person whose relative is a director or is in the employment of the company as a director or KMP;
  - A person who is in full time employment elsewhere; Person who is auditor of more than 20 companies; In case of private company –a person is ineligible if such person or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies other than one person companies, dormant companies, small companies and private companies having paid-up share capital less than one hundred crore rupee
  - A person who has been convicted by a court of an offence involving fraud and a period of ten years has not elapsed from the date of such conviction;
  - a person who, directly or indirectly, renders any service referred to in section 144 to the company or its holding company or its subsidiary company

Explanation.—For the purposes of this clause, the term "directly or indirectly" shall have the meaning assigned to it in the Explanation to section 144.'

Explanation to Section 144 defines the term 'directly or indirectly' to 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.

According to section 141 (4) where a person appointed as an auditor of a company incurs any of the disqualifications mentioned as above 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.

### **Mandatory Rotation of Auditors**

The Companies Act, 2013 has introduced the system of rotation of auditors under section Section 139 (2) and Rule 5 which is applicable to-

- all listed companies;
- all unlisted public companies having paid up share capital of rupees 10 crore or more;
- all private limited companies having paid up share capital of rupees 20 crore or more;
- all companies having paid up share capital of below threshold limit mentioned in (a) and (b) above, but having public borrowings from financial institutions, banks or public deposits of rupees 50 crore or more.

The concept of rotation of auditors shall not apply to one person companies and small companies.

All the companies mentioned above shall not appoint or re-appoint an individual as an auditor of the company for more than 1 term of 5 consecutive years. An individual auditor, who has completed his term of 5 consecutive years, shall not be eligible for re-appointment as auditor in the same company for 5 years from the date of completion.

All the companies mentioned above shall not appoint or re-appoint an audit firm as an auditor of the company for more than 2 terms of 5 consecutive years. An audit firm which has completed its 2 terms of 5 consecutive years shall not be eligible for re-appointment as auditor in the same company for 5 years from the completion of such terms. If any firm/LLP which has one or more partners who are also partners in the outgoing audit firm/LLP cannot be appointed as auditors during the 5 year period. In other words, if two or more audit firms have common partner(s), and one of these firms has completed its 2 terms of 5 consecutive years, none of such audit firms shall be eligible for re-appointment as auditor in the same company for 5 years.

No audit firm shall be appointed as auditor of the company for a period of five years, if same firm presently having a common partner(s) to the previous audit firm, whose tenure has expired in a company immediately preceding the financial year.

The right of the company to remove the auditor or the right of the auditor to resign from such office of the company is not affected by this sub-section. Thus, an auditor can resign or be removed by the shareholders before completion of his term as discussed above. The firm shall include a limited liability partnership incorporated under the Limited Liability Partnership Act, 2008.

### **ROTATION OF AUDITORS- Section 139(3)**

Members of a company subject to provisions of the Act, can provide for following by passing a resolution:

- (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.

### **ROTATION OF AUDITORS ON EXPIRY OF THEIR TERM -Section 139 (4) and Rule 6**

Rotation of auditors on expiry of auditor's term then same procedure will be followed as required for appointment of auditors. The procedure is as under:-

- (1) The Audit Committee shall recommend to the Board, the name of an individual auditor or of an audit firm who may replace the incumbent auditor on expiry of the term of such incumbent.
- (2) Where a company is required to constitute an Audit Committee, the Board shall consider the recommendation of such committee, and in other cases, the Board shall itself consider the matter of rotation of auditors and make its recommendation for appointment of the next auditor by the members in annual general meeting.

For the purpose of rotation, the period for which the auditor is holding office prior to the commencement of this act will also be counted in calculating the period of 5 years or 10 years as the case may be. The incoming auditor/audit firm shall not be eligible if such auditor/audit firm is associated with the outgoing auditor/audit firm under the same network of audit firms i.e. includes the firms operating/ functioning under the same brand name, trade name or common control, hitherto or in future. If a partner, who is in charge of an audit firm and also certifies the financial statements of the company, retires from the said firm and joins

another firm of chartered accountants, such other firm shall also be ineligible to be appointed for a period of five years.

Where a company has appointed two or more persons as joint auditors, the company may follow the rotation of auditors in such a manner that both or all of the joint auditors, as the case may be, do not complete their term in the same year.

### **RE-APPOINTMENT OF RETIRING AUDITOR- Section 139 (9)**

At any annual general meeting, a retiring auditor shall be reappointed as auditor of the company except under the following circumstances:

- (a) he is not qualified for re-appointment.
- (b) he has given the company a notice in writing of his unwillingness to be re-appointed.
- (c) a special resolution has been passed at that meeting appointing somebody else instead of him or providing expressly that retiring auditor shall not be re-appointed.

Section 139 (10) lays that 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.

### **[Audit and Auditors] [Section 139 to 148]**

#### **APPOINTMENT OF AUDITOR (Section 139)**

<b>Particulars</b>	<b>Non Government Company</b>	<b>Listed/Specified Company</b>	<b>Government Company</b>
Application of 1 <sup>st</sup> Auditor after Incorporation	By BOD (W-30 days from the date of Regn.) Or By Members at EGM (W-90 days of Information)	BY BOD (W-30 days from the date of Regn.) Or By Members at EGM (W-90 days of Information)	BY CAG (W-60 days from the date of Regn.) Or By BOD (w-30 days) Or By Member at EGM (W-60 days of Information)
Auditor at First AGM The written consent and a certificate (appointment shall be in accordance with the conditions) from the auditor.	By Members To hold office till conclusion of 6 <sup>th</sup> AGM.	By Members (for maximum one term of 5/10 consecutive years) Cooling off period of 5 years before next appointment	By CAG (W-180 days from 1 <sup>st</sup> April)
Subsequent Auditor	By Members To hold office till	By Members (for Maximum one term	By CAG (W-180 days from 1 <sup>st</sup>

	conclusion of 6 <sup>th</sup> meeting.	of 5/10 consecutive years)	April
Casual Vacancy due to <ul style="list-style-type: none"> <li>• Resignation</li> <li>• Other Reasons</li> </ul>	By Members within 3 months of recommendation of Board and till next AGM		By CAG within 30 days Or By BOD within next 30 days

**APPOINTMENT OF AUDITOR OTHER THAN RETIRING AUDITOR BY SPECIAL NOTICE- Section 140 (4)**

Special notice shall be required from members proposing to move a resolution at the next annual general meeting to appoint a person other than the retiring auditor or to provide that the retiring auditor shall not be re-appointed.

Such special notice shall not be required in case where the retiring auditor has completed a consecutive tenure of five years or, as the case may be, ten years, as provided under sub-section (2) of section 139.

Following points are relevant for the purpose of special notice:

- (i) Company, on receipt of such special notice for removing auditor, should forthwith send a copy of the same to the retiring auditor.
- (ii) If the auditor makes a representation in writing to the company and requests for its notification to the members, the company shall
  - (a) state the fact of representation in any notice of resolution, and
  - (b) send copy of representation to members to whom notice of meeting is sent, whether before or after the receipt of representation by the company.
  - (c) if the copy of representation is not so sent , copy thereof should be filed with the Registrar.
- (iii) such representation should be of a reasonable length and not too long.
- (iv) For circulation to members, it should not be received by the company too late.
- (v) Auditor may require the company to read out the representation in the meeting if it is not so notified to members because it was too late or because of company's default.

Provided that if the Tribunal is satisfied on an application either of the company or of any other aggrieved person that the rights conferred by this sub- 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.

**POWERS OF TRIBUNAL- Section 140 (5)**

A National Company Law Tribunal (NCLT) can either –

- (i) *suo moto* or
- (ii) on an application from Central Government, or
- (iii) on an application from person concerned,

can direct the company to change the auditor 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.

In the case of application being made by the Central Government and the NCLT being satisfied that change of auditor is required, it shall within 15 days of the receipt of such application, make an order that the Auditor shall not function as an auditor of the company and the Central Government may appoint another auditor in his place. This will happen only when an application is made by the Central Government and not by any other person.

Where the auditor, whether individual or firm, against whom the final order as aforementioned is passed by the NCLT under this section, he 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 such order. Further, the auditor shall also be liable for action under Section 447 which provides for punishments for frauds.

It has been clarified by way of explanation that in case a firm is appointed as auditor of the company, the liability shall be of the firm and every partner or partners who acted in fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its directors or officers shall be liable and not be eligible to be appointed as auditor of any company for a period of 5 years.

#### **CASUAL VACANCY IN THE OFFICE OF AUDITOR - Section 139 (8)**

The provisions for filling of casual vacancy in the office of auditor are as follows:

- (a) The Board of the company shall have power to fill the casual vacancy in the office of auditor within 30 days.
- (b) In case casual vacancy has occurred due to resignation of auditor, such appointment should also be approved by the company in general meeting convened within 3 months of the recommendation of the Board and auditor shall hold the office till the conclusion of the next annual general meeting.
- (c) In case of a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor- General of India, such vacancy should be filled by the Comptroller and Auditor-General of India within 30 days. In case the Comptroller and Auditor-General of India does not fill the vacancy within the said period, the Board of Directors shall fill the vacancy within next 30 days.
- (d) Appointment of auditors to fill casual vacancy shall be made after taking into account the recommendation of the audit committee.

#### **REMOVAL OF AUDITOR-Section 140 (1) and Rule 7**

The auditor appointed under section 139 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 in that behalf in the manner prescribed in Rule 7.

As per Rule 7, the auditor appointed under section 139 may be removed from his office before the expiry of the term only by –

- (i) Obtaining the prior approval of the Central Government by filling an application in form ADT-2 within 30 days of resolution passed by the Board
- (ii) The company shall hold the general meeting within sixty days of receipt of approval of the Central Government for passing the special resolution.

- (iii) The auditor concerned shall be given a reasonable opportunity of being heard.

### **RESIGNATION OF AUDITOR- Section 140 (2), 140 (3) and Rule 8**

The auditor who has resigned from the company shall file a statement in Form ADT-3 indicating the reasons and other facts as may be relevant with regard to his resignation as follows:

- (i) In case of other than Government Company, the auditor shall within 30 days from the date of resignation, file such statement to the company and the registrar.
- (ii) In case of Government Company or government controlled company, auditor shall within 30 days from the resignation, file such statement to the company and the Registrar and also file the statement with the Comptroller and Auditor General of India (CAG).

The onus to file such statement containing relevant facts and reasons for resignation is on the resigning auditor and any contravention of sub clause (2) is punishable with monetary fine which shall not be less than fifty thousand rupees or the remuneration of the auditor, whichever is less, but which may extend to five lakh rupees.

### **REMUNERATION OF AUDITOR – Section 142**

Section 142 of the Act prescribed that the remuneration of the auditor of a company shall be fixed in its general meeting or in such manner as may be determined therein. The Board may fix remuneration of the first auditor appointed by it. The remuneration will be in addition to the out of pocket expenses incurred by the auditor in connection with the audit of the company and any remuneration paid to him for any other service rendered by him at the request of the company.

### **AUDITOR NOT TO RENDER CERTAIN SERVICES (PROHIBITED SERVICES)-Section 144**

An auditor shall provide to the company only such other services as are approved by the Board of Directors/ 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:-

- (a) accounting and book keeping services;
- (b) internal audit;
- (c) design and implementation of any financial information system;
- (d) actuarial services;
- (e) investment advisory services;
- (f) investment banking services;
- (g) rendering of outsourced financial services;
- (h) management services; and
- (i) any other kind of services as may be prescribed.

### **AUDITOR'S RIGHT TO ATTEND GENERAL MEETING**

According to section 146 notice of all the general meetings shall also be forwarded to the auditor of the

company and he must attend any general meeting either by himself or through his authorised representative (qualified to be an auditor) and shall have right to be heard at such meeting on any part of the business which concerns him as the auditor.

## POWERS AND DUTIES OF AUDITORS

Section 143(1) provided that every auditor can access at all times to the books of accounts, vouchers and seek such information and explanation from the company and enquire such matters as he considers necessary, including the matters specified in sub-Clauses (a) to (f). It is the duty of every auditor to make proper enquiry regarding these matters, besides other matters and if he is satisfied, it is not necessary to disclose this fact in his report. However, on enquiry, if he finds some adverse features, it is his duty to report the same. Specific enquiries to be made by the auditor under this sub-Section are as under—

(a) *Loans and Advances made by the Company*

Auditor shall inquire into “whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are not prejudicial to the interest of the company or its members.” It is applicable to all loans and advances made on the basis of security. The auditor should verify that the security held against the loans and advances made by the company are legally enforceable and also ascertain the valuation of securities to see whether the loan is fully secured or partly secured.

(b) *Transactions represented by book entries*

Auditor is required to inquire “whether the transactions of the company which are represented merely by book entries are not prejudicial to the interests of the company”. He should verify the all book entry transactions and determine whether such transactions have actually taken place and are not prejudicial to the interest of the company.

(c) *Sale of investments*

Auditor should inquire, “whether so much of the assets of the company (except an investment company or a banking company) as consists of shares, debentures and other securities, have been sold at a price less than that at which they were purchased by the company”. Auditor must verify the cases where securities are sold at a price less than their cost of acquisition and if he finds that such sale is bona fide and the price realised is considered to be reasonable, having regards to the circumstances of each case, no further reporting is required.

(d) *Loans and Advances shown as deposits*

Auditor must verify “whether loans and advances made by the company have been shown as deposits”. The auditor must inquire in respect of all the deposits shown by the company and satisfy himself that the loans and advances have not been shown as deposits.

(e) *Charging of Personal expenses to revenue account*

Auditor should inquire as to “whether personal expenses have been charged to revenue account”. Auditor must ensure that no personal expenses of directors and officers of the company have been charged to revenue account.

(f) *Allotment of shares for cash*

Auditor should inquire as to “whether cash has actually been received in respect of shares stated to have been allotted for cash and if no cash has actually been so received, whether the position as

stated in the account books and balance sheet is correct, regular and not misleading". In this connection, auditor must ensure in respect of shares allotted in cash by the company that cash has actually been received in respect of such allotment by the company.

He should verify and report the cases where cash was not received and that the position, as stated in books of accounts and balance sheet, is correct, regular and not misleading.

Auditor will have access to books of accounts and vouchers, not only to those kept at registered office of the company but also to those kept at any other place. Such access shall be available at all times. Also, auditor of a holding company shall have access to the books of all of its subsidiary and associate companies for the purpose of consolidation of financial statements of holding company and its subsidiaries and associate companies.

### **POWERS OF COMPTROLLER AND AUDITOR-GENERAL OF INDIA IN CASE GOVERNMENT COMPANY [Section 143 (5) to 143 (7)]**

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 Government, or partly by the Central Government and partly by one or more State Government, the Comptroller and Auditor-General of India shall appoint the auditor under sub-section (5) or sub-section (7) of section 139 and direct such auditor the manner in which the accounts of the company are required to be audited and thereupon the auditor so appointed shall submit a copy of the audit report to the Comptroller and Auditor-General of India which, among other things, include the directions, if any, issued by the Comptroller and Auditor-General of India, the action taken thereon and its impact on the accounts and financial statement of the company.

The CAG shall have a right to the conduct a supplementary audit of financial statement of the company and comment upon or supplement such audit report within 60 days from the date of receipt of the audit report u/s 143 (5).

Any comments given by the CAG upon, or supplement to, the audit report shall be sent by the company to every person entitled to copies of audited financial statements u/s 136 (1) and also be placed before the annual general meeting of the company at the same time and in the same manner as the audit report.

The CAG may, by an order, cause test audit to be conducted of the accounts of company covered u/s 139 (5) or 139 (7) and the provisions of section 19A of the Comptroller and Auditor-General's (Duties, Powers and Conditions of Service) Act, 1971, shall apply to the report of such test audit.

### **AUDIT REPORT**

Section 143 (2) provides that auditor shall make a report to the members of the company on the accounts examined by him and on every financial statement which is required to be laid in the general meeting of the company. The Audit report should take into consideration the provisions of this Act, the Accounting and Auditing standards and matters which are required under this Act or rules made thereunder or under any order made u/s 143(11).

The Audit report should state that to the best of his information and knowledge, the said accounts and financial statements give a true and fair view of the state of the company's affair as at the end of the financial year and the profit or loss and the cash flow for the year and such other matters as may be prescribed.

Section 143 (3) lay down that auditor's report shall also state other details which are as under:

- (a) whether he has sought and obtained all the information and explanations which were necessary 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 and proper returns adequate for the purposes of his audit have been received from branches not visited by him;
  - (c) whether the branch audit report prepared by a person other than the company's auditor has been sent to him;
  - (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 under section 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; This shall not apply to the following:
    - a one person company or a small company; or
    - a turnover of less than Rs. 50 Crores as per the latest audited financial statement; or which has aggregate borrowings of less than Rs. 25 Crores, from banks, financial institutions, or any body corporate, at any point of time during the preceding financial year.
  - (j) Rule 11 prescribed that Auditor's Report shall also include their views and comments on the following matters, namely:-
    - (i) whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;
    - (ii) whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;
    - (iii) whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.
    - (iv) whether the company had provided requisite disclosures in its financial statements as to holdings as well as dealings in Specified Bank Notes during the period from 8th November, 2016 to 30th December, 2016 and if so, whether these are in accordance with the books of accounts maintained by the company

The auditor is required to provide the reasons, where any of the matters required to be included in the Audit Report under this Clause is answered in negative or with a qualification. {Section 143 (4)}

### **BRANCH AUDIT - SECTION 143 (8) AND RULE 12**

Branch Auditor: Accounts of branch office can be audited by –

1. The company's auditor; or

2. Any other person, qualified to be and appointed as an auditor as per the provisions of the Act as branch auditor; or
3. In case of foreign branch, by the company's auditor or by an accountant or a competent person appointed in accordance with the prevailing laws of the foreign country.

The branch auditor shall prepare a report on the accounts of the branch examined by him and the company's auditor shall deal with such report in his audit report in a manner as he considers necessary.

Duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor.-

- (1) 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 sub-sections (1) to (4) of section 143 i.e. right of access to books of accounts, ensure about the mandatory books of accounts maintained, prepare auditors' report and state the reasons of qualification in report, if any etc .
- (2) The branch auditor shall submit his report to the company's auditor.
- (3) The provisions of sub-section (12) of section 143 read 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.

#### **AUDITING STANDARDS - SECTION 143 (9) & (10)**

Every auditor must comply with the auditing standards. While the Central Government prescribes the Auditing Standards or addendums thereto, it shall consult with and take recommendations of the Institute of Chartered Accountants of India (ICAI) and the National Financial Reporting Authority (NFRA). Till such time the Auditing Standards are notified by the Central Government, the auditing standards specified by the ICAI are deemed to be the auditing standards.

#### **REPORTING OF FRAUDS BY AUDITOR- Section 143(12) to 143 (15) & Rule 13**

Section 143(12) and Rule 13 provides that If an auditor of a company, in the course of the performance of his duties as statutory auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of rupees one crore or above, is being or has been committed against the company by its officers or employees, the auditor shall report the matter to Central Government.

- (1) The auditor shall report the matter to the Central Government as under:-
  - (a) the auditor shall report the matter to the Board or the Audit Committee, immediately but not later than two days of his knowledge of the fraud, seeking their reply or observations within forty-five days;
  - (b) on receipt of such reply or observations, the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the Central Government within fifteen days from the date of receipt of such reply or observations;
  - (c) in case the auditor fails to get any reply or observations from the Board or the Audit Committee within forty-five days, he shall forward his report to the Central Government along with a note containing the details of his report that was earlier forwarded to the Board or the Audit Committee for which he has not received any reply or observations;
- (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 telephone number or mobile number and be signed by the auditor with his seal and shall indicate his Membership Number.

(4) The report shall be in the Form ADT-4.

(5) In case of a fraud involving lesser than the amount specified above, the auditor shall report the matter to Audit Committee or to the Board immediately but not later than two days of his knowledge of the fraud and he shall report the matter specifying the following:-

- (a) Nature of Fraud with description;
- (b) Approximate amount involved; and
- (c) Parties involved.

(5) The fraud reported to the Audit Committee or the Board during the year shall be disclosed in the Board's Report specifying the following-

- (a) Nature of Fraud with description;
- (b) Approximate Amount involved;
- (c) Parties involved, if remedial action not taken; and
- (d) Remedial actions taken.

(6) 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 section 148 and section 204 respectively.

## **SECTION 148 : MAINTENANCE OF COSTING AND STOCK RECORDS**

A company engaged in production, processing, manufacturing or mining activity, is also required to maintain particulars relating to utilization of material, labour or other items of cost as the Central Government may prescribe for such class of companies.

### **COST RECORDS & AUDIT– Section 148**

Section 148(1) states that notwithstanding anything contained in Chapter X of Companies Act 2013, 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 utilisation 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.

However 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.

Section 148(2) states that 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 sub-section (1) and which have a net worth of such amount as may be prescribed or a turnover of such amount as may be prescribed, shall be conducted in the manner specified in the order.

Section 148(3) states that the audit under sub-section (2) shall be conducted by a Cost Accountant who shall be appointed by the Board on such remuneration as may be determined by the members in such manner as may be prescribed.

**Further Rule 14 of Companies( Audit & Auditors), Rules, 2014 provides that**

- (a) in the case of companies which are required to constitute an audit committee-
  - (i) the Board shall appoint an individual, who is a cost accountant, or a firm of cost accountants in practice, as cost auditor on the recommendations of the Audit committee, which shall also recommend remuneration for such cost auditor;
  - (ii) the remuneration recommended by the Audit Committee under (i) shall be considered and approved by the Board of Directors and ratified subsequently by the shareholders;
- (b) in the case of other companies which are not required to constitute an audit committee, the Board shall appoint an individual who is a cost accountant or a firm of cost accountants in practice as cost auditor and the remuneration of such cost auditor shall be ratified by shareholders subsequently.

Further that no person appointed under section 139 as an auditor of the company shall be appointed for conducting the audit of cost records and the auditor conducting the cost audit shall comply with the cost auditing standards.

For the purposes of this sub-section, the expression “cost auditing standards” mean such standards as are issued by the Institute of Cost Accountants of India, constituted under the Cost and Works Accountants Act, 1959, with the approval of the Central Government.

Section 148(4) states that an audit conducted under this section shall be in addition to the audit conducted under section 143.

Section 148(5) states the qualifications, disqualifications, rights, duties and obligations applicable to auditors under this Chapter shall, so far as may be applicable, apply to a cost auditor appointed under this section and it shall be the duty of the company to give all assistance and facilities to the cost auditor appointed under this section for auditing the cost records of the company.

Further the report on the audit of cost records shall be submitted by the cost accountant to the Board of Directors of the company.

Section 148(6) states that a company shall within thirty days from the date of receipt of a copy of the cost audit report prepared in pursuance of a direction under sub-section (2) furnish the Central Government with such report along with full information and explanation on every reservation or qualification contained therein.

Section 148(7) states that if, after considering the cost audit report referred to under this section and the information and explanation furnished by the company under sub-section (6), the Central Government is of the opinion that any further information or explanation is necessary, it may call for such further information and explanation and the company shall furnish the same within such time as may be specified by that Government.

Section 148(8) states that if any default is made in complying with the provisions of this section,—

- (a) the company and every officer of the company who is in default shall be punishable in the manner as provided in sub-section (1) of section 147;
- (b) the cost auditor of the company who is in default shall be punishable in the manner as provided in sub-sections (2) to (4) of section 147.

The Companies (Cost Records and Cost Audit) Rules, 2014 as amended has following highlights:

- Applicability for cost audit: Section 148(2) read with Rule 4 of the Companies (Cost Records

and Cost Audit) Rules, 2014 provides the Central government, by order, may direct for the audit of cost records of class of companies, as mentioned in Rule 4 of the Companies (Cost Records and Cost Audit) Rules, 2014.

- Maintenance of records: Every company under these rules including all units and branches thereof, shall, in respect of each of its financial year commencing on or after the 1st day of April, 2014, maintain cost records in form CRA-1.
- Cost audit: The categories of companies specified in Rule 3 and the threshold limits laid down in Rule 4, shall within 180 days of the commencement of every financial year, appoint a cost auditor.
- 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 suggestion, if any in form CRA-3.

The Central Government is empowered to direct, 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 utilisation 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:

#### **Exception to the Cost Records requirements:**

The requirement for cost records under these rules shall not be applicable to a company which is classified as a micro enterprise or a small enterprise including as per the turnover criteria under Section 7(9) of the Micro, Small and Medium Enterprises Development Act, 2006.

#### **Exception to the Cost Audit requirements:**

The requirement for cost audit under these rules shall not be applicable to a company covered under the Rules if revenue from exports, in foreign exchange, exceeds 75% of its total revenue OR if it is operating from a special economic zone.

#### **COST AUDIT :**

In a case 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 sub-section (1) of Section 148 and which have a net worth of such amount as may be prescribed or a turnover of such amount as may be prescribed, shall be conducted in the manner specified in the order.

Provided that the report on the audit of cost records shall be submitted by the cost accountant to the Board of Directors of the company.

- (a) The cost auditor shall forward his report to the Board of Directors of the company within a period of 180 days 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.
- (b) Every company covered under these rules shall, 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.

#### **SECRETARIAL AUDIT**

Secretarial Audit is a compliance audit and it is a part of total compliance management in an organisation.

The Secretarial Audit is an effective tool for corporate compliance management. It helps to detect non-compliance and to take corrective measures.

Secretarial Audit is a process to check compliance with the provisions of various laws and rules/regulations/procedures, maintenance of books, records etc., by an independent professional to ensure that the company has complied with the legal and procedural requirements and also followed the due process. It is essentially a mechanism to monitor compliance with the requirements of stated laws.

Considering the increasing importance of Corporate Governance, Section 204 of the Companies Act, 2013 mandates every listed company and such other class of prescribed companies to annex a Secretarial Audit Report, given by a company secretary in practice with its Board's report.

Secretarial Audit is an independent, objective assurance intended to add value and improve an organisation's operations. It helps to accomplish the organisation's objectives by bringing a systematic, disciplined approach to evaluate and improve effectiveness of risk management, control, and governance processes.

As per rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, the prescribed class of companies is as under:

- (a) every public company having a paid-up share capital of fifty crore rupees or more; or
- (b) every public company having a turnover of two hundred fifty crore rupees or more.

Additionally for listed entities SEBI vide recent notification provides that Every listed entity and its material unlisted subsidiaries incorporated in India shall undertake secretarial audit and shall annex with its annual report, a secretarial audit report, given by a company secretary in practice, in such form as may be specified with effect from the year ended March 31, 2019

It shall be the duty of the company to give all assistance and facilities to the company secretary in practice, 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 in the Secretarial Audit Report. The format of the Secretarial Audit Report shall be in Form No. MR.3.

Secretarial Audit is also applicable to a private company which is a subsidiary of a public company, and which falls under the prescribed class of companies as indicated above.

The companies which are not covered under section 204 may obtain Secretarial Audit Report voluntarily as it provides an independent assurance of the compliances of applicable laws of the company.

## **ROLE OF COMPANY SECRETARY**

Company secretary in practice has been exclusively recognised for conducting secretarial audit. The section 204 further provides that Secretarial Audit Report is to be submitted in a format prescribed under rules. As per sub-rule (2) of Rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, the format of the Secretarial Audit Report shall be in Form MR-3 .

Section 134 and Sub-section (3) of Section 204 provides that the Board of Directors, in its report, shall explain in full any qualification or observation or other remarks made by the company secretary in practice in the secretarial audit report.

## **The Objectives of Secretarial Audit**

The objectives of Secretarial Audit may be summarized as under:-

- To check & report on compliances of applicable laws and Secretarial Standards;
- To point out non-compliances and inadequate compliances;
- To protect the interest of various stakeholders i.e. the customers, employees, society etc;
- To avoid any unwarranted legal actions/penalties by law enforcing agencies and other persons aswell.

### **Scope of Secretarial Audit**

The scope of Secretarial Audit comprises verification of the compliances under the following enactments, rules, regulations, notifications and guidelines:

- (i) The Companies Act, 2013 (the Act) and the Rules made thereunder:

On various matters under Companies Act, 2013, Central Government has been empowered to make rules. A perusal of the scheme of the Act makes it clear that compliances under the Act may be divided into two categories. Compliances of the first type are annual and non-event based such as filing of the annual return, annual report including secretarial audit report, wherever applicable, etc. The compliances of second category are event based i.e. on happening of certain event.

These events require compliance of various provisions of the Act.

While secretarial audit envisages the verification of all secretarial records of a company. For ease of presentation, the following key areas have been highlighted for verification:

Under Companies Act, 2013

1. Maintenance of registers and records
2. Filing of forms, returns and documents
3. Memorandum and/or Articles of Association
4. Meetings of directors/committees thereof, shareholders and other stakeholders
5. Secretarial Standards
6. Directors and Key Managerial Personnel (“KMP”)
7. Disclosures
8. Issue of shares and other securities
9. Transfer and transmission of shares and other securities and related matters
10. Dividend
11. Deposits
12. Borrowings
13. Loans, investments, guaranties and securities
14. Loans to directors etc. and Related party transactions
15. Charges
16. Corporate Social responsibility

- (ii) Other major Acts and Regulations:

- a. The Securities Contracts (Regulation) Act, 1956 and the Rules made under that Act; (where

applicable): With special reference to listing, delisting and continuous listing of any of the securities.

- b. The Depositories Act, 1996 and the Regulations and Bye-laws framed under that Act; (where applicable)
- c. The Foreign Exchange Management Act, 1999 and the Rules and Regulations made thereunder to the extent of Foreign Direct Investment, Overseas Direct Investment and External Commercial Borrowings; (where applicable)
- d. The regulations and guidelines made under the Securities and Exchange Board of India Act, 1992 (where applicable). The various laws/regulations/guidelines which could be considered under this are:
  - (i) The Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011;
  - (ii) The Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015;
  - (iii) The Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009;
  - (iv) The Securities and Exchange Board of India (Share Based Employee Benefit) Regulations, 2014;
  - (v) The Securities and Exchange Board of India (Issue and Listing of Debt Securities) Regulations, 2008;
  - (vi) The Securities and Exchange Board of India (Registrars to an Issue and Share Transfer Agents) Regulations, 1993 regarding the Companies Act and dealing with client;
  - (vii) The Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2009;
  - (viii) The Securities and Exchange Board of India (Buyback of Securities) Regulations, 1998;
  - (ix) SEBI (Listing Obligations and Disclosures Requirements) Regulations, 2015 (where applicable).

3. Other Applicable Laws include:

Reporting on compliance of 'Other laws as may be applicable specifically to the company' shall mean all the laws which are applicable to specific industry for example for Banks- all laws applicable to Banking Industry; for insurance company-all laws applicable to insurance industry; likewise for a company in petroleum sectoral laws applicable to petroleum industry; similarly for companies in pharmaceutical sector, cement industry etc.

The Secretarial Audit or should prepare a list of specific laws as applicable to the company whose secretarial audit is being conducted and verify compliance with the same. SS-1 requires every company to specify list of laws applicable specifically to the company at its Board Meeting.

Examining and reporting whether the adequate systems and processes are in place to monitor and ensure compliance with general laws like labour laws, competition law, and environmental laws.

The provisions relating to audit of accounts and financial statement of a company is dealt in the Statutory Audit, and that relating to taxation is dealt in Tax Audit, the Secretarial Auditor may rely on the reports given by statutory auditors or other designated professionals. However, Secretarial Auditor is expected to report on the Secretarial Compliance of these laws.

- (iv) to examine and report on the compliance with Secretarial Standards issued by ICSI.

## (v) Adherence to board process and compliance mechanism

The scope of Secretarial Audit should include the assessment of the adequacy and quality of board process and compliance mechanism. In preparing the Audit Report, the secretarial auditor shall consider the following matters (illustrative):

1. Instances of non-compliance during the defined audit period, in relation to the statutes, rules, regulations, etc. applicable to the company, continuing non-compliance, if any, and the reasons thereof;
2. Significant litigation(s) initiated by the company or filed against the company with brief details of the cases;
3. (a) Board structure –
  - (i) Composition of the Board
  - (ii) Is there a stated process to ascertain the suitability of directors?
  - (iii) Is there a stated process in place for succession planning?
 (b) Deficiencies in the Board systems and processes –
  - (i) In convening meetings.
  - (ii) In the circulation of agenda (whether the agenda is made available to the Board along with supporting papers/presentations sufficiently in advance of the meetings).
  - (iii) In conducting the meetings (frequency and length).
  - (iv) In the decision making process of the Board.
  - (v) Adequacy and integrity of minutes recorded.
  - (vi) In the functioning of Board constituted Committees.
4. The existence and adequacy of internal control systems, procedures and processes, commensurate with the size of the company and the nature of its business, for ensuring compliance with laws applicable to the company;
5. Any material event(s) that have happened, after the end of the financial year but before the date of the report, having a significant impact on any of the above reported items.
6. Whether any event occurred or action was taken in the audit company which may have bearing on the Compliances under various laws, regulations, guidelines and standards etc.

### **NEED FOR SECRETARIAL AUDIT**

Secretarial Audit is the process of independent verification, examination of level of compliance of applicable Corporate Laws to a company. The audit process if properly devised ensures timely compliance and eliminates any un-intended non compliance of various applicable rules and regulations. An action plan of the Corporate Secretarial Department is to be designed so as to ensure that all event based and time based compliances are considered and acted upon. Secretarial

Audit is to be on the principle of “Prevention is better than cure” rather than post mortem exercise and to find faults. Broadly, the need for Secretarial Audit is:

- Effective mechanism to ensure that the legal and procedural requirements are duly complied with.

- Provides a level of confidence to the directors & Key Managerial Personnel etc.
- Directors can concentrate on important business matters as Secretarial Audit ensures legal and procedural requirements.
- Strengthen the image and goodwill of a company in the minds of regulators and stakeholders.
- Secretarial Audit is an effective governance and compliance risk management tool.
- It helps the investor in analyzing the compliance level of companies, thereby increases the reputation.

### Appointment of Secretarial Auditor

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

### SECTION 138: INTERNAL AUDIT

#### *Classes of companies requiring Internal Audit*

The following class of companies shall be required to appoint an internal auditor or a firm of internal auditors:-

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

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.

The board may appoint any practicing Chartered Accountant or a Cost Accountant or any other person whom it deems fit to be appointed as its internal auditor. For this purpose, company board may consider the nature and volume of business of company; qualifications, experience and capabilities of such person being appointed as auditor and scope of internal audit.

### Who can be an Internal Auditor

- (a) A Chartered Accountant or;
- (b) A Cost Accountant or;

- (c) Such other professional as may be decided by the Board to conduct internal audit of the functions and activities of the Company.

For this sub-section, Chartered Accountant means a Chartered Accountant, who is a member of the Institute of Chartered Accountants of India and has a valid certificate of practice and Cost Accountant means a member of The Institute of Cost Accountants of India. Other professionals, as may be decided by the company's board, may also be appointed as an internal auditor.

Following classes of companies are required to appoint internal auditor-

1. All Listed Company	2. Public Company with				3. Private Company with	
	Paid up capital	Turnover	Outstanding loans and borrowings	Outstanding deposits	Turnover	Outstanding loans and borrowings
	50 Cr or more or	200 Cr or more or	100 Cr or more or	25 Cr or more	200 Cr or more or	100 Cr or more.

### LESSON ROUND-UP

- As per the Act, books of account and other books and papers should be available for inspection by any director on working days during business hours.
- The expression 'annual accounts' embraces both balance sheet and statement of profit and loss.
- The term 'Balance Sheet' means a statement prepared from the books of a concern showing the debit and credit balances after the trading and profit and loss accounts have been prepared – a statement drawn up at the end of each trading or financial period, setting forth the various assets, and liabilities of a concern at a particular date.
- Profit and loss account is a Statement by which the directors disclose to the shareholders of the company the result of the actual working of the company. It serves to give the shareholders an idea of the earning capacity of the company in relation to its capital, and enables them to judge about the administration and management of the affairs of the company.
- The Act provides that every profit and loss account and balance sheet of the company shall comply with the accounting standards.
- The balance sheet and profit and loss account must be approved by the Board of directors and signed by the directors before they are submitted to the auditors for their report. The Act gives other provisions also for authentication of annual accounts. The Act also requires the company to file such annual accounts with the Registrar of Companies.
- The main object of audit is to ensure that the statement of accounts of the relevant financial year truly and fairly reflect the state of affairs of the company. Audit also provides a moral check on those who are entrusted with the task of running business and of keeping and maintaining the books of account of the company. An audit of accounts is conducted with two-fold purpose: (i) detection and prevention of errors; (ii) detection and prevention of fraud.
- The Act provides that the auditor of a Government company shall be appointed or re-appointed by the Comptroller and Auditor General of India within the limits specified.
- The Act provides that the auditors' report shall be signed only by the person appointed as an auditor of the company.
- The Central Government has notified Cost Accounting Records Rules for a number of specified industries with a view to ensuring that the records so maintained highlight the area of inefficiencies or high costs.

## GLOSSARY

XBRL Format

XBRL is a data-rich dialect of XML (Extensible Markup Language), the universally preferred language for transmitting information via the Internet. It was developed specifically to communicate information between businesses and other users of financial information, such as analysts, investors and regulators. XBRL provides a common, electronic format for business reporting. It does not change what is being reported. It only changes how it is reported

Comptroller and Auditor General of India

The Comptroller and Auditor General (CAG) of India is an authority, established by the Constitution under Constitution of India/Part V - Chapter V/Sub-part 7B/Article 148. The Comptroller and Auditor-General performs such duties and exercise such powers in relation to the accounts of the Union and of the States and of any other authority or body as may be prescribed by or under any law made by Parliament and, until provision in that behalf is so made

The reports of the CAG are taken into consideration by the Public Accounts Committees (PACs) and Committees on Public Undertakings (COPUs), which are special committees in the Parliament of India and the state legislatures. The CAG is also the head of the Indian Audit and Accounts Department, the affairs of which are managed by officers of Indian Audit and Accounts Service

## SELF-TEST QUESTIONS

1. Section 128(1) requires every company to prepare and keep the books of accounts and other relevant books and papers and financial statements at its registered office. State the manner of maintenance of books of accounts in electronic form.
2. What is the procedure to report frauds?
3. ABC Ltd. wants to appoint FMC & Associates as its internal auditor. What are the conditions of such appointment?
4. What are the conditions of removal of auditor?



# Lesson 9

## Transparency and Disclosures

### LESSON OUTLINE

- Annual Report
- Board's Report
- Annual Return
- Website Disclosures
- Policies
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

Disclosure and transparency are of utmost importance in a fiduciary relationship between the directors and shareholders. Boards' Report or Directors' Report is an important tool for the stakeholders to judge or analyse the performance and corporate governance measures adopted by the company.

Company Secretary guides the directors in preparation of this report; they are expected to be well versed with the related provisions.

Disclosure requirements are covered under various enactments including Companies Act, 2013, and rules made thereunder, Reserve Bank of India Act, 1934, Securities Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, Sexual Harassment of women at workplace (Prevention, Prohibition and Redressal) Act, 2013.

After reading this lesson you will be able to understand the contents of the directors' report whether mandated by law or adopted as a good corporate practice and various other disclosures required to be made to the shareholders.

## INTRODUCTION

Transparency is a pivotal feature in the market based monitoring of companies and is central to shareholders' ability to exercise their ownership rights on an informed basis, which can help attract capital and maintain confidence in the capital markets.

Adequate disclosure also helps improve public understanding of the structure and activities of enterprises, corporate policies and performance with respect to environmental and ethical standards, and companies' relationships with the communities in which they operate. Disclosures are made both through the print media and the electronic media. Today corporates have to disclose mandatorily under various legislations including the Companies Act, 2013, SEBI (LODR) Regulations, 2015, Sexual Harassment (Prevention, Prohibition and Redressal) Act, 2013 etc. Briefly they have been discussed here under:

### 1. Annual Report

The annual report is a comprehensive report provided by most public companies to disclose their corporate activities over the past year. The report is typically issued to shareholders and other stakeholders who use it to evaluate the firm's performance including both operating and financial highlights.

According to Regulation 34 of SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015 [SEBI (LODR)] a listed entity shall submit the annual report to the stock exchange within twenty one working days of it being approved and adopted in the annual general meeting as per the provisions of the Companies Act, 2013.

As per recent SEBI Notification the listed entity shall submit to the stock exchange and publish on its website-

- (a) a copy of the annual report sent to the shareholders along with the notice of the annual general meeting not later than the day of commencement of dispatch to its shareholders;
- (b) in the event of any changes to the annual report, the revised copy along with the details of and explanation for the changes shall be sent not later than 48 hours after the annual general meeting." (Notified on 9th May, 2018 effective from March 31, 2019)

Such annual report shall contain the following:

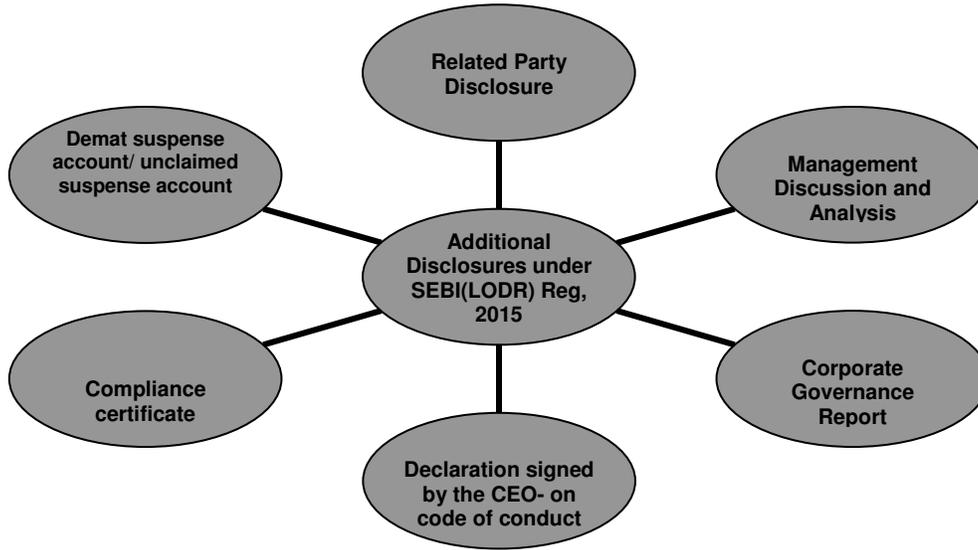
- (a) audited financial statements i.e. balance sheets, profit and loss accounts etc, and Statement on Impact of Audit Qualifications, if applicable;
- (b) consolidated financial statements audited by its statutory auditors;
- (c) cash flow statement presented only under the indirect method as prescribed in Accounting Standard-3 or Indian Accounting Standard 7, as applicable, specified in Section 133 of the Companies Act, 2013 read with relevant rules framed thereunder or as specified by the Institute of Chartered Accountants of India, whichever is applicable;
- (d) directors report;
- (e) management discussion and analysis report - either as a part of directors report or addition thereto;
- (f) for the top five hundred listed entities based on market capitalization (calculated as on March 31 of every financial year), Business Responsibility Report describing the initiatives taken by them from an environmental, social and governance perspective, in the format as specified by the Board from time to time:

Listed entities other than top five hundred listed companies based on market capitalization and

listed entities which have listed their specified securities on SME Exchange, may include the Business Responsibility Reports on a voluntary basis in the format as specified.

Further it is provided that the annual report shall contain any other disclosures specified in Companies Act, 2013 along with other requirements as specified in Schedule V of above mentioned regulations.

As per SEBI(LODR), the annual report shall contain the following additional disclosures:



**A. Related Party Disclosure:**

1. The listed entity shall make disclosures in compliance with the Accounting Standard on “Related Party Disclosures”.
2. The disclosure requirements shall be as follows:

Sr. no.	In the accounts of	Disclosures of amounts at the year end and the maximum amount of loans/ advances/ Investments outstanding during the year.
1	Holding Company	Loans and advances in the nature of loans to subsidiaries by name and amount. Loans and advances in the nature of loans to associates by name and amount. Loans and advances in the nature of loans to firms/companies in which directors are interested by name and amount.
2	Subsidiary	Same disclosures as applicable to the parent company in the accounts of subsidiary company.
3	Holding Company	Investments by the loanee in the shares of parent company and subsidiary company, when the company has made a loan or advance in the nature of loan.

For the purpose of above disclosures directors’ interest shall have the same meaning as given in Section 184 of Companies Act, 2013.

(2A) Disclosures of transactions of the listed entity with any person or entity belonging to the promoter/promoter group which hold(s) 10% or more shareholding in the listed entity, in the format prescribed in the relevant accounting standards for annual results. (Notified on 9<sup>th</sup> May, 2018, applicable in respect of Annual reports filed for the year ended March 31, 2019 and thereafter)

3. The above disclosures shall be applicable to all listed entities except for listed banks.

### **B. Management Discussion and Analysis:**

1. This section shall include discussion on the following matters within the limits set by the listed entity's competitive position:
  - (a) Industry structure and developments.
  - (b) Opportunities and Threats.
  - (c) Segment-wise or product-wise performance.
  - (d) Outlook
  - (e) Risks and concerns.
  - (f) Internal control systems and their adequacy.
  - (g) Discussion on financial performance with respect to operational performance.
  - (h) Material developments in Human Resources / Industrial Relations front, including number of people employed.
- (i) details of significant changes (i.e. change of 25% or more as compared to the immediately previous financial year) in key financial ratios, along with detailed explanations therefor, including:
  - (i) Debtors Turnover
  - (ii) Inventory Turnover
  - (iii) Interest Coverage Ratio
  - (iv) Current Ratio
  - (v) Debt Equity Ratio
  - (vi) Operating Profit Margin (%)
  - (vii) Net Profit Margin (%)or sector-specific equivalent ratios, as applicable.
- (j) details of any change in Return on Net Worth as compared to the immediately previous financial year along with a detailed explanation thereof. (Notified on 9<sup>th</sup> May, 2018, applicable in respect of Annual reports filed for the year ended March 31, 2019 and thereafter)

### **2. Disclosure of Accounting Treatment:**

Where in the preparation of financial statements, a treatment different from that prescribed in an Accounting Standard has been followed, the fact shall be disclosed in the financial statements, together with the management's explanation as to why it believes such alternative treatment is more representative of the true and fair view of the underlying business transaction.

### **C. Corporate Governance Report**

The following disclosures shall be made in the section on the corporate governance of the annual report.

(1) *A brief statement on listed entity's philosophy on code of governance.*

(2) *Board of directors:*

- (a) composition and category of directors (e.g. promoter, executive, non-executive, independent non-executive, nominee director - institution represented and whether as lender or as equity investor);
- (b) attendance of each director at the meeting of the board of directors and the last annual general meeting;
- (c) number of other board of directors or committees in which a directors is a member or chairperson, and with effect from the Annual Report for the year ended 31st March 2019, including separately the names of the listed entities where the person is a director and the category of directorship; (Notified on 9th May, 2018, applicable in respect of Annual reports filed for the year ended March 31, 2019 and thereafter)
- (d) number of meetings of the board of directors held and dates on which held;
- (e) disclosure of relationships between directors inter-se;
- (f) number of shares and convertible instruments held by non- executive directors;
- (g) web link where details of familiarisation programmes imparted to independent directors is disclosed.
- (h) A chart or a matrix setting out the skills/expertise/competence of the board of directors specifying the following: (i) With effect from the financial year ending March 31, 2019, the list of core skills/expertise/competencies identified by the board of directors as required in the context of its business(es) and sector(s) for it to function effectively and those actually available with the board; and (ii) With effect from the financial year ended March 31, 2020, the names of directors who have such skills / expertise / competence
- (i) confirmation that in the opinion of the board, the independent directors fulfill the conditions specified in these regulations and are independent of the management.
- (j) detailed reasons for the resignation of an independent director who resigns before the expiry of his tenure along with a confirmation by such director that there are no other material reasons other than those provided.(Notified on 9th May, 2018, applicable in respect of Annual reports filed for the year ended March 31, 2019 and thereafter)

(3) *Audit committee:*

- (a) brief description of terms of reference;
- (b) composition, name of members and chairperson;
- (c) meetings and attendance during the year.

(4) *Nomination and Remuneration Committee:*

- (a) brief description of terms of reference;
- (b) composition, name of members and chairperson;
- (c) meeting and attendance during the year;
- (d) performance evaluation criteria for independent directors.

(5) *Remuneration of Directors:*

- (a) all pecuniary relationship or transactions of the non-executive directors vis-à-vis the listed entity

shall be disclosed in the annual report;

- (b) criteria of making payments to non-executive directors. alternatively, this may be disseminated on the listed entity's website and reference drawn thereto in the annual report;
- (c) disclosures with respect to remuneration: in addition to disclosures required under the Companies Act, 2013, the following disclosures shall be made:
  - (i) all elements of remuneration package of individual directors summarized under major groups, such as salary, benefits, bonuses, stock options, pension etc;
  - (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 issued at a discount as well as the period over which accrued and over which exercisable.

*(6) Stakeholders' grievance committee:*

- (a) name of non-executive director heading the committee;
- (b) name and designation of compliance officer;
- (c) number of shareholders' complaints received so far;
- (d) number not solved to the satisfaction of shareholders;
- (e) number of pending complaints.

*(7) General body meetings:*

- (a) location and time, where last three annual general meetings held;
- (b) whether any special resolutions passed in the previous three annual general meetings;
- (c) whether any special resolution passed last year through postal ballot – details of voting pattern;
- (d) person who conducted the postal ballot exercise;
- (e) whether any special resolution is proposed to be conducted through postal ballot;
- (f) procedure for postal ballot.

*(8) Means of communication:*

- (a) quarterly results;
- (b) newspapers wherein results normally published;
- (c) any website, where displayed;
- (e) whether it also displays official news releases; and
- (f) presentations made to institutional investors or to the analysts.

*(9) General shareholder information:*

- (a) annual general meeting - date, time and venue;
- (b) financial year;
- (c) dividend payment date;
- (d) the name and address of each stock exchange(s) at which the listed entity's securities are listed and

- a confirmation about payment of annual listing fee to each of such stock exchange(s);
- (e) stock code;
- (f) market price data- high, low during each month in last financial year;
- (g) performance in comparison to broad-based indices such as BSE sensex, CRISIL Index etc;
- (h) in case the securities are suspended from trading, the directors report shall explain the reason thereof;
- (i) registrar to an issue and share transfer agents;
- (j) share transfer system;
- (k) distribution of shareholding;
- (l) dematerialization of shares and liquidity;
- (m) outstanding global depository receipts or american depository receipts or warrants or any convertible instruments, conversion date and likely impact on equity;
- (n) commodity price risk or foreign exchange risk and hedging activities;
- (o) plant locations;
- (p) address for correspondence.

*(10) Other Disclosures:*

- (a) disclosures on materially significant related party transactions that may have potential conflict with the interests of listed entity at large;
- (b) details of non-compliance by the listed entity, penalties, strictures imposed on the listed entity by stock exchange(s) or the board or any statutory authority, on any matter related to capital markets, during the last three years;
- (c) details of establishment of vigil mechanism, whistle blower policy, and affirmation that no personnel has been denied access to the audit committee;
- (d) details of compliance with mandatory requirements and adoption of the non-mandatory requirements;
- (e) web link where policy for determining 'material' subsidiaries is disclosed;
- (f) web link where policy on dealing with related party transactions;
- (g) disclosure of commodity price risks and commodity hedging activities.
- “(h) Details of utilization of funds raised through preferential allotment or qualified institutions placement as specified under Regulation 32 (7A).
- (i) a certificate from a company secretary in practice that none of the directors on the board of the company have been debarred or disqualified from being appointed or continuing as directors of companies by the Board/Ministry of Corporate Affairs or any such statutory authority.
- (j) where the board had not accepted any recommendation of any committee of the board which is mandatorily required, in the relevant financial year, the same to be disclosed along with reasons thereof: Provided that the clause shall only apply where recommendation of / submission by the committee is required for the approval of the Board of Directors and shall not apply where prior approval of the relevant committee is required for undertaking any transaction under these Regulations.

- (k) total fees for all services paid by the listed entity and its subsidiaries, on a consolidated basis, to the statutory auditor and all entities in the network firm/network entity of which the statutory auditor is a part. (Notified on 9<sup>th</sup> May, 2018, applicable in respect of Annual reports filed for the year ended March 31, 2019 and thereafter)

*(11) Non-compliance of any requirement of corporate governance report of sub-paras (2) to (10) above, with reasons thereof shall be disclosed.*

*(12) The corporate governance report shall also disclose the extent to which the discretionary requirements as specified in Part E of Schedule II have been adopted.*

*(13) The disclosures of the compliance with corporate governance requirements specified in regulation 17 to 27 and clauses (b) to (i) of sub-regulation (2) of regulation 46 shall be made in the section on corporate governance of the annual report.*

***D. Declaration signed by the chief executive officer stating that the members of board of directors and senior management personnel have affirmed compliance with the code of conduct of board of directors and senior management.***

***E. Compliance certificate from either the auditors or practicing company secretaries regarding compliance of conditions of corporate governance shall be annexed with the directors' report.***

**F. Disclosures with respect to demat suspense account/ unclaimed suspense account**

(1) The listed entity shall disclose the following details in its annual report, as long as there are shares in the demat suspense account or unclaimed suspense account, as applicable :

- (a) aggregate number of shareholders and the outstanding shares in the suspense account lying at the beginning of the year;
- (b) number of shareholders who approached listed entity for transfer of shares from suspense account during the year;
- (c) number of shareholders to whom shares were transferred from suspense account during the year;
- (d) aggregate number of shareholders and the outstanding shares in the suspense account lying at the end of the year;
- (e) that the voting rights on these shares shall remain frozen till the rightful owner of such shares claims the shares.

**Dissemination to the shareholders.**

According to Reg 36 of SEBI (LODR) the listed entity shall send the annual report in the following manner to the shareholders:

- (a) Soft copies of full annual report to all those shareholder(s) who have registered their email address(es) for the purpose;
- (b) Hard copy of statement containing the salient features of all the documents, as prescribed in Section 136 of Companies Act, 2013 or rules made thereunder to those shareholder(s) who have not so registered;
- (c) Hard copies of full annual reports to those shareholders, who request for the same.

The listed entity shall send annual report to the holders of securities, not less than twenty-one days before

the annual general meeting.

## 2. Board's Report

The Board's Report is the most important means of communication by the Board of Directors of a company with its shareholders. It is a comprehensive document which serves to inform the shareholders about the performance and various other aspects of the company, its major policies, relevant changes in management, future programmes of expansion, modernization and diversification, capitalization or reserves, etc. The Board's Report enables not only the shareholders but also the lenders, bankers, government and the public to make an appraisal of the company's performance and provides an insight into the future growth and profitability of the company.

The Companies Act, 2013 is based on enhanced disclosures and transparency. The Board's Report is a document, preparation of which requires thorough understanding of the subject. The Act requires the Board of Directors to disclose on various parameters including the risk management, board evaluation, implementation of Corporate Social Responsibility, a statement of declaration given by independent directors. The Secretarial Audit Report is also required to be annexed to the Board's Report.

It is mandatory for the Board of Directors of every company to present financial statement to the shareholders along with its report, known as the "Board's Report" at every annual general meeting. Apart from giving a complete review of the performance of the company for the year under report, material changes till the date of the report, the report highlights the significance of various national and international developments which can have an impact on the business and indicates the future strategy of the company. The Board's Report enables shareholders, lenders, bankers, government, prospective investors, all the stakeholders and the public to make an appraisal of the company's performance and reflects the level of corporate governance in the company.

The matters to be included in the Board's Report have been specified in Section 134 of the Companies Act, 2013 and Rule 8 of the Companies (Accounts) Rules, 2014. Apart from this, under Sections 67, 92, 129, 131, 135, 149, 160, 168, 177, 178, 188, 197, 204 of the Companies Act, 2013, relevant information has to be disclosed in 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 SEBI (LODR) ,2015.

### DISCLOSURE IN BOARD'S REPORT pursuant to the Companies Act, 2013

Disclosures under Section 134(3)	Issue of Equity Shares with differential rights	Issue of Sweat Equity Shares
Details of Employees Stock Option Scheme – section 62(1)(b)	Restrictions on purchase by company or giving of loans by it for	Disclosures pertaining to Consolidated Financial Statements
Voluntary revision of Financial Statements or Board's Report – Section 131(1)	Corporate Social Responsibility – Section 135	Re-Appointments of an Independent Director – Section 149(10)

Resignation of Director – Section 168(1)	Composition of Audit Committee – Section 177(8)	Details of Vigil Mechanism – Section 177(10)
Policy relating to the remuneration for the directors, key managerial personnel and other employees – Section 178(4)	Related party transactions – Section 188(2)	Disclosures pertaining to remuneration of directors and employees – Section 197(12)
Remuneration received by MD and WTD from holding or subsidiary companies – Section 197(14)	Secretarial Audit Report – Section 204(1)	Additional Disclosures by Producer Company

### Disclosures under Section 134(3)

Section 134 of the Act enjoins upon the Board a responsibility to make out its report to the shareholders and attach the said report to financial statements laid before the shareholders at the annual general meeting, in pursuance of Section 129 of the Act.

1.1 Disclosures under Section 134(3) In terms of Sub-section (3) of Section 134, the Board's Report shall include:

- (a) the web address**, if any, where annual return referred to in sub-section (3) of section 92 has been placed
- (b) Number of meetings of the Board: Board Report** should contain total number of Board Meetings held in respective financial year
- (c) Directors' Responsibility Statement:** Section 134(5) of the Act specifically provides that the Directors' Responsibility Statement shall set out the following affirmations:
  - (i) in the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures;
  - (ii) 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;
  - (iii) 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;

- (iv) the directors had prepared the annual accounts on a going concern basis; and
- (v) 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
- (vi) 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.

**(ca) details in respect of frauds reported by auditors under sub-section (12) of section 143 other than those which are reportable to the Central Government:**

The Board's Report shall contain a disclosure regarding the following details of frauds is being or has been committed against the company by its officers or employees, the auditor shall report the matter to the Central Government involving an amount of Rupees One Crore or above

- Nature of Fraud with description;
- Approximate Amount involved;
- Parties involved, if remedial action not taken; and
- Remedial action taken.

**(d) a statement on declaration given by independent directors under sub-section (6) of section 149:**

Every Independent Director shall give a declaration that he meets the criteria of independence laid down in sub-section (6) of section 149, which is to be given by him at the first meeting of the Board in which he participates as a director and thereafter at the first meeting of the Board in every financial year or whenever there is any change in the circumstances which may affect his status as an independent director. The Board's Report should contain a statement to the effect that the independent directors have given such a declaration.

**(e) Company's policy on directors' appointment and remuneration including criteria for determining qualifications, positive attributes, independence of a director and other matters provided under sub-section (3) of section 178:** The Board' Report of companies which are required to constitute Nomination and Remuneration Committee shall include:

- criteria for determining qualifications,
- positive attributes and independence of a director, and
- recommend to the Board a policy relating to the remuneration of directors, Key Managerial Personnel and other employees.

The Board's Report needs to disclose such criteria and also the policy relating to the remuneration.

This Section 178 is not applicable to a company incorporated under Section 8 of the Companies Act, 2013. Similarly, Section 178(2)/(3)/(4) is not applicable to Government Companies except with regard to appointment of senior management & other employees via Notification No. GSR 463(E), dated 05-06-2015.

In case of a company covered under sub-section (1) of section 178, company's policy on directors' appointment and remuneration including criteria for determining qualifications, positive attributes, independence of a director and other matters provided under sub-section (3) of section 178;

**(f) Explanations or comments by the Board on every qualification, reservation or adverse remark or disclaimer made—**

- by the auditor in his report; and
- by the Secretarial Auditor in his secretarial audit report;
- Auditor's report under section 143: Clause (h) of Section 143(3) provides that the auditor's report shall state any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith.
- Cost Audit Report under section 148: Section 148(5) of the Act and Rule 6 of the Companies (Cost Records and Audit) Rules, 2014 provides that the rights, duties and obligations applicable to the Auditor under Chapter X of the Act shall *mutatis mutandis* apply to a cost auditor appointed under Section 148 of the Act. It also provides that the cost auditor shall submit his report to the Board of Directors of the company. The cost auditor's report shall also state any qualification, reservation or adverse remark relating to the maintenance of cost accounts and other matters connected therewith.
- Secretarial Audit Report under Section 204(3): Section 204(3) of the Act provides that the Board of Directors, in their report made in terms of sub-section (3) of section 134, shall explain in full any qualification or observation or other remarks made by the company secretary in practice in his secretarial audit report. Thus, the Board should state detailed explanation in its board's report for all the observations and qualifications given by the Secretarial auditor in his secretarial audit report including the reasons for such material deviations and reasons that led to such deviations.
  - (i) by the auditor in his report; and
  - (ii) by the company secretary in practice in his secretarial audit report;

**(g) Particulars of loans, guarantees or investments under section 186:** The particulars of loans given, guarantees provided or investments in securities and acquisition made during the year under section 186 of the Act should be attached to the Board's Report.

**(h) Particulars of contracts or arrangements with related parties referred to in sub-section (1) of section 188 in the prescribed form;** The Report of the Board shall contain the details of contracts or arrangements entered with Related Parties as referred to in Section 188 (1) in Form AOC-2 pursuant to Rule 8(2) of Companies (Accounts) Rules, 2014.

**(i) The state of the company's affairs:** Information and data which are usually considered pertinent and necessary for the purpose of a proper appreciation of the state of affairs of a company relating to the period for which the financial statements have been prepared must be disclosed in the report. Relevant changes which have occurred, as compared to the position as stated in the previous year's Board's Report which have a material bearing on the performance of the company should be indicated in the Board's Report.

The figures of the previous year relating to achievement of targets of production and sales should also be given in the Board's Report to facilitate comparison and the reasons for any substantial deviation there from should be explained in brief.

**(j) the amounts, if any, which it proposes to carry to any reserves:** The first proviso to the section 123(1) of the Act provides that 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.

**(k) The amount, if any, which it recommends should be paid by way of dividend:** The Board's Report

shall disclose the amount per share and the percentage which the Board recommends to be paid as dividend under section 123 of the Act.

**(l) 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:** The Board's Report should include material changes and commitments, if any, affecting the financial position of the company and occurring between the date of balance sheet and the date of the report. The Directors' Report should, therefore, contain material changes pertaining to post-financial statement events impacting the operations and performance of the Company.

**(m) The conservation of energy, technology absorption, foreign exchange earnings and outgo, in such manner as may be prescribed:** 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. The Report of the Board shall contain the particulars of contracts or arrangements with related parties referred to in sub-section (1) of section 188 in the Form AOC-2.

The Board's Report should contain following information and details as per Rule 8(3) of the Companies (Accounts) Rules, 2014-

**A. Conservation of energy**

- (i) the steps taken or impact on conservation of energy;
- (ii) the steps taken by the company for utilising alternate sources of energy;
- (iii) the capital investment on energy conservation equipment;

**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.**

Provided that the requirement of furnishing information and details under this sub-rule shall not apply to a Government company engaged in producing defence equipment.

**(n) 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:** The company should provide about the overall risk management framework of the company, whether it has constituted risk management committee, the risk management policy of the company, the possible risks and steps taken to mitigate those risks in this section.

**(o) Details about the policy developed and implemented by the company on Corporate Social Responsibility initiatives taken during the year:** Section 135(4) of the Act provides that the Board of every company having net worth of ₹500 Crores or more or turnover of ₹1,000 Crores or more or net profit of ₹5 Crores or more during any financial year shall disclose contents of such Policy in its report and also place it on the company's website.

**(p) Board evaluation:** Every listed company and every other public company having a paid up share capital of twenty five crore rupees 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 (Rule 8(4) of the Companies (Accounts) Rules, 2014).

This clause shall not apply in case the directors are evaluated by the Ministry or Department of the Central Government which is administratively in charge of the company, or, as the case may be, the State Government as per its own evaluation methodology- Notification No. GSR 463(E), dated 5-6-2015.

**(q) such other matters as may be prescribed:-** Rule 8(5) of the Companies (Accounts) Rules, 2014, prescribes that the Board's Report shall also include following matters -

- (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—
    - o at the beginning of the year;
    - o maximum during the year;
    - o at the end of the year;
- (vi) the details of deposits which are not in compliance with the requirements of Chapter V of the Act;
- (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.

### Disclosures pertaining to Issue of Equity Shares with differential rights

Section 43 of the Act provides that a company limited by shares can issue equity shares with differential rights as to dividend, voting or otherwise in accordance with rules prescribed under Rule 4 of the Companies (Share Capital and Debentures) Rules, 2014.

Rule 4(4) of the Companies (Share Capital and Debentures) Rules, 2014, provides that the Board of Directors shall, *inter alia*, disclose in the Board's Report for the financial year in which the issue of equity shares with differential rights as to dividend, voting or otherwise was completed, the following details, namely:-

- (a) total number of shares allotted with differential rights;
- (b) details of the differential rights relating to voting rights and dividends;
- (c) percentage of shares with differential rights to the total post-issue equity share capital with differential rights issued at any point of time and percentage of voting rights which the equity share capital with differential voting rights shall carry to the total voting rights of the aggregate equity share capital;
- (d) price at which such shares have been issued;
- (e) particulars of promoters, directors or key managerial personnel to whom such shares are issued;
- (f) change in control, if any, in the company consequent to the issue of equity shares with differential voting rights;
- (g) diluted Earnings Per Share pursuant to the issue of each class of shares, calculated in accordance with the applicable accounting standards;
- (h) pre and post issue shareholding pattern along with voting rights in the format specified under sub-rule (2) of rule 4.

### Disclosures pertaining to Issue of Sweat Equity Shares

Section 54(1)(d) of the Act provides that where the equity shares of the company are listed on a recognised stock exchange, the sweat equity shares are issued in accordance with the regulations made by the SEBI and if they are not so listed, the sweat equity shares are issued in accordance with Rule 8 of Companies (Share Capital and Debentures) Rules, 2014.

In terms of Rule 8 of Companies (Share Capital and Debentures) Rules, 2014, the Board of Directors shall, *inter alia*, disclose in the Directors' Report for the year in which such shares are issued, the following details of issue of sweat equity shares namely:-

- (a) the class of director or employee to whom sweat equity shares were issued;
- (b) the class of shares issued as Sweat Equity Shares;
- (c) the number of sweat equity shares issued to the directors, key managerial personnel or other employees showing separately the number of such shares issued to them, if any, for consideration other than cash and the individual names of allottees holding one percent or more of the issued share capital;
- (d) the reasons or justification for the issue;
- (e) the principal terms and conditions for issue of sweat equity shares, including pricing formula;

- (f) the total number of shares arising as a result of issue of sweat equity shares;
- (g) the percentage of the sweat equity shares of the total post issued and paid up share capital;
- (h) the consideration (including consideration other than cash) received or benefit accrued to the company from the issue of sweat equity shares;
- (i) the diluted Earnings Per Share (EPS) pursuant to issuance of sweat equity shares.

#### **Disclosures of Details of Employees Stock Option Scheme - Section 62(1)(b)**

Section 62(1)(b) of the Act read with Rule 12(9) of the Companies (Share Capital and Debentures) Rules, 2014 provides that the Board of directors, shall, *inter alia*, disclose in the Directors' Report for the year, the following details of the Employees Stock Option Scheme:

- (a) options granted;
- (b) options vested;
- (c) options exercised;
- (d) the total number of shares arising as a result of exercise of option;
- (e) options lapsed;
- (f) the exercise price;
- (g) variation of terms of options;
- (h) money realized by exercise of options;
- (i) total number of options in force;
- (j) employee wise details of options granted to:-
  - (i) key managerial personnel;
  - (ii) any other employee who receives a grant of options in any one year of option amounting to five percent or more of options granted during that year;
  - (iii) identified employees who were granted option, during any one year, equal to or exceeding one percent of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant.

#### **Disclosures pertaining to Restrictions on purchase by company or giving of loans by it for purchase of its shares – Section 67**

Proviso to Section 67(3) read with Rule 16(4) of Companies (Share Capital and Debentures) Rules, 2014 provides that where the voting rights are not exercised directly by the employees in respect of shares to which the scheme for provision of money for purchase of or subscription for shares by employees or by trustees for the benefit of employees relates, the Board of Directors shall, *inter alia*, disclose in the Board's report for the relevant financial year the following details, namely:-

- (a) the names of the employees who have not exercised the voting rights directly;
- (b) the reasons for not voting directly;

- (c) the name of the person who is exercising such voting rights;
- (d) the number of shares held by or in favour of, such employees and the percentage of such shares to the total paid up share capital of the company;
- (e) the date of the general meeting in which such voting power was exercised;
- (f) the resolutions on which votes have been cast by persons holding such voting power;
- (g) the percentage of such voting power to the total voting power on each resolution;
- (h) whether the votes were cast in favour of or against the resolution.

### **Disclosures pertaining to Consolidated Financial Statements**

Rule 8(1) of the Companies (Accounts) Rules, 2014 specifies that the Board's Report

- shall be prepared on the basis of standalone financial statements of the company.
- 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.

Proviso to Section 129(3) read with Rule 5 of the Companies (Accounts) Rules, 2014 states that the company shall also attach along with its financial statement a separate statement containing the salient features of the financial statements of a company's subsidiary or subsidiaries, associate company or companies and joint venture or ventures in Form AOC-1.

### **Voluntary revision of Financial Statements or Board's Report - Section 131(1)**

Section 131(1) of the Act provides that revised financial statements or a revised report may be prepared in respect of any of the three preceding financial years where it appears to the directors of a company that the financial statements or the report of the Board, do not comply with the provisions of section 129 or section 134 and the detailed reasons for revision of such financial statements or report should be disclosed in the Board's report in the relevant financial year in which such revision is being made.

### **Disclosures pertaining to Corporate Social Responsibility – Section 135**

- The Board's report shall disclose the composition of the Corporate Social Responsibility Committee - Section 135(2).
- Contents of CSR policy as recommended by CSR Committee and approved by the Board - Section 135(4)(a).
- Section 135(5) provides that the Board of every company referred to in sub-section (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 three immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy. If the company fails to spend such amount, the Board shall, in its report, specify the reasons for not spending the amount.
- The Companies (Corporate Social Responsibility Policy) Rules, 2014 requires that the Board's Report shall include an annual report on CSR containing particulars specified in Annexure to the rules.

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.

### **Re-Appointment of an Independent Director - Section 149(10)**

Subject to the provisions of Section 152, an independent director shall hold office for a term up to five consecutive years on the Board of a company, but shall be eligible for reappointment on passing of a special resolution by the company and disclosure of such appointment in the Board's report.

Thus, if an independent director is appointed by passing a special resolution after completing a term of five years, the Board's report should contain a disclosure of such appointment.

### **Resignation of Director - Section 168(1)**

A director may resign from his office by giving notice in writing to the company and the Board. Section 168(1) requires the Board to place the fact of resignation of a director in report of directors laid in the immediately following general meeting by the Company.

### **Composition of Audit Committee - Section 177(8)**

The Board's report shall disclose the following –

- Composition of an Audit Committee
- Where the Board had not accepted any recommendation of the Audit Committee, the same shall be disclosed in the report along with the reasons therefor.

### **Details of Vigil Mechanism - Section 177(10)**

Section 177(9) read with Rule 7 of the Companies (Meeting of Board and its Powers) Rules, 2014 provides that every listed company and the following class or classes of companies shall establish a vigil mechanism for their directors and employees to report their genuine concerns or grievances-

- (a) Companies which accept deposits from the public;
- (b) Companies which have borrowed money from banks and public financial institutions in excess of fifty crore rupees.

### **Policy relating to the remuneration for the directors, key managerial personnel and other employees – Section 178(4)**

Section 178(3) and (4) provides that the Nomination and Remuneration Committee shall formulate and recommend to the Board a policy, relating to the remuneration for the directors, key managerial personnel and other employees. Such policy shall 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, key managerial personnel 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.

The policy so formulated shall be disclosed in the Board's report.

*Section 178(2)/(3)/(4) is not applicable to Section 8 companies and Government Companies except with regard to appointment of senior management & other employees via Notification No. GSR 463(E), dated 05-06-2015.*

**Related party transactions – Section 188(2)**

Every contract or arrangement entered into under Section 188(1) shall be referred to in the Board's report to the shareholders along with the justification for entering into such contract or arrangement in the prescribed form i.e., Form no. AOC-2 (pursuant to Section 134(3)(h) and Section 188(2)).

**Disclosures pertaining to remuneration of directors and employees –Section 197(12)**

Section 197(12) read with Rule 5 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014 provides that Board's Report of every listed company shall include:-

- (a) the ratio of the remuneration of each director to the median remuneration of the employees of the company for the financial year;
- (b) the percentage increase in remuneration of each director, Chief Financial Officer, Chief Executive Officer, Company Secretary or Manager, if any, in the financial year;
- (c) the percentage increase in the median remuneration of employees in the financial year;
- (d) the number of permanent employees on the rolls of company;
- (e) average percentile increase already made in the salaries of employees other than the managerial personnel in the last financial year and its comparison with the percentile increase in the managerial remuneration and justification thereof and point out if there are any exceptional circumstances for increase in the managerial remuneration;
- (f) affirmation that the remuneration is as per the remuneration policy of the company.
- (g) the expression "median" means the numerical value separating the higher half of a population from the lower half and the median of a finite list of numbers may be found by arranging all the observations from lowest value to highest value and picking the middle one;
- (h) if there is an even number of observations, the median shall be the average of the two middle values.

The Board's report shall include a statement showing the names of the top ten employees in terms of remuneration drawn and the name of every employee, who, -

- (i) if employed throughout the financial year, was in receipt of remuneration for that year which, in the aggregate, was not less than one crore and two lakh rupees;
  - (ii) if employed for a part of the financial year, was in receipt of remuneration for any part of that year, at a rate which, in the aggregate, was not less than eight lakh and fifty thousand rupees per month;
  - (iii) if employed throughout the financial year or part thereof, was in receipt of remuneration in that year which, in the aggregate, or as the case may be, at a rate which, in the aggregate, is in excess of that drawn by the managing director or whole-time director or manager and holds by himself or along with his spouse and dependent children, not less than two percent of the equity shares of the company.
- (2) The statement referred to above shall include the following as under:
- (i) designation of the employee;
  - (ii) remuneration received;
  - (iii) nature of employment, whether contractual or otherwise;

- (iv) qualifications and experience of the employee;
- (v) date of commencement of employment;
- (vi) the age of such employee;
- (vii) the last employment held by such employee before joining the company;
- (viii) the percentage of equity shares held by the employee in the company within the meaning of clause (iii) of sub-rule (2) above; and
- (ix) whether any such employee is a relative of any director or manager of the company and if so, name of such director or manager:

Provided that the particulars of employees posted and working in a country outside India, not being directors or their relatives, drawing more than sixty lakh rupees per financial year or five lakh rupees per month, as the case may be, as may be decided by the Board, shall not be circulated to the members in the Board's report, but such particulars shall be filed with the Registrar of Companies while filing the financial statements and Board's Report.

These particulars shall be made available to any shareholder on a specific request made by him in writing before the date of such Annual General Meeting wherein financial statements for the relevant financial year are proposed to be adopted by shareholders and such particulars shall be made available by the company within three days from the date of receipt of such request from shareholders:

Provided also that in case of request received even after the date of completion of Annual General Meeting, such particulars shall be made available to the shareholders within seven days from the date of receipt of such request, on a quarterly basis for public issue, rights issue, preferential issue, etc. , -

- (a) indicating deviations, if any, in the use of proceeds from the objects stated in the offer document or explanatory statement to the notice for the general meeting, as applicable;
- (b) indicating category wise variation (capital expenditure, sales and marketing, working capital, etc.) between projected utilisation of funds made by it in its offer document or explanatory statement to the notice for general meeting, as applicable and the actual utilisation of funds.

#### **Disclosures under SEBI (Share Based Employee Benefits) Regulations, 2014**

Regulation 14 of the Regulations provides that in addition to the information that a company is required to disclose, in relation to employee benefits under the Companies Act, 2013, the Board of directors of such a company shall also disclose the details of the scheme(s) being implemented, as specified by SEBI in this regard.

SEBI vide circular dated 16th June, 2015 has provided for following disclosure requirements in the Board's Report.

- The Board of directors in their report shall disclose any material change in the scheme(s) and whether the scheme(s) is / are in compliance with the regulations.
- Further, SEBI has prescribed specific details which shall be disclosed on the company's website and a web-link thereto shall be provided in the report of board of directors.

#### **Disclosure Requirements under the Sexual Harassment of Women at Workplace (Prevention, Prohibition & Redressal) Act, 2013**

- The Act mandates that all companies having more than 10 women employees shall disclose in annual report following details as per section 22 and 28 of the Act.

- Rule 14 of Sexual Harassment of Women at Workplace (Prevention, Prohibition & Redressal) Rules, 2013 provides that the annual report which the Complaints Committee shall prepare shall contain following information-
  - (a) Number of complaints of sexual harassment received in the year;
  - (b) Number of complaints disposed off during the year;
  - (c) Number of cases pending for more than ninety days;
  - (d) Number of workshops or awareness programme against sexual harassment carried out;
  - (e) Nature of action taken by the employer or District Officer

**APPROVAL OF THE BOARD’S REPORT**

The Board’s Report should be considered, approved and signed at a meeting of the Board, convened in accordance with the provisions of the Act and shall not be dealt with in any meeting held through video conferencing or other audio visual means (Rule 4 of the Companies (Meetings of Board and its Powers) Rules, 2014).

**Signing of Board’s Report [Section 134(6)].**

If Chairperson is authorised by the Board-	Where Chairperson is not authorised by the Board-	Further, as a good practice, the companies should get the annexure to the Board’s report also separately signed by the Chairman.
Chairperson of the Company	At least two directors, one of whom shall be a Managing Director, or by the director where there is one director	The Annual Report on CSR may be signed by the Chairman of the CSR Committee.

**Circulation of the Board’s Report**

Alongwith a signed copy of every financial statement, including consolidated financial statement if any, the Board’s Report shall be issued, circulated or published along with all notes annexed, the auditor’s report and Board’s report. [Section 134(7)]

**RIGHT OF MEMBERS TO RECEIVE COPIES OF FINANCIAL STATEMENTS, BOARD’S REPORT, ETC.**

Section 136 of the Act provides that, without prejudice to the provisions of Section 101, a copy of the financial statements, including consolidated financial statements, if any, 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

- every member of the company,
- every trustee for the debenture holder of any debentures issued by the company, and
- all persons other than such member or trustee, being the person so entitled, not less than 21 clear days before the date of the meeting.

## FILING OF THE BOARD'S REPORT

Section 137(1) of the Act provides that copies of financial statement along with all documents required to be annexed should be filed with the Registrar of Companies within 30 days along with the prescribed fees, after the financial statements, including consolidated financial statements have been adopted at the annual general meeting. The Board's Report has to be attached to the financial statements.

In case a company does not hold an annual general meeting in any year, a statement of facts and reasons along with financial statement and attachment shall be filed with registrar.

Further that pursuant to the provisions of section 117/ 179 of the Companies Act, and the Rules made thereunder the resolution for approving the Board's Report is also required to be filed to the Registrar within 30 days from the approval by the Board.

Third Proviso of Section 137(1) of the Act also provides that a One Person Company should 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 one hundred eighty days from the closure of the financial year.

In the case of a subsidiary which has been incorporated outside India (herein referred to as "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 of the fourth proviso shall 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.

## PROCEDURE FOR PREPARATION OF BOARD'S REPORT

1. Section 136(1) of the Companies Act, 2013 provides that every company, public or private shall forward to its member along with its annual financial statements, the Board's report. The Board's report is an important document in which the Board gives a complete review of the performance of the company during the year under review and other information as explained below.
2. The Board's report shall be prepared based on the stand alone financial statements of the company and the report shall contain a separate section wherein report on the performance and financial position of each of the subsidiaries, associates and joint venture companies included in the consolidated financial statement is presented.
3. Board's Report and the financial statement shall be approved in Board Meeting only. These matters shall not be dealt with in any meeting held through video conferencing or other audio visual means.
4. Section 134(3) read with rule 8(3) lists down various items to be included in the Board's Report as already detailed in the chapter.
5. Where it is proposed to pay dividend on equity or preference shares, the Board's Report shall contain the recommendation of the Board as to the rate of dividend for the year under review for the approval of members at the annual general meeting. The Board's proposal about dividend shall be in conformity with the relevant rules.
6. As there must be some interval of time between the end of the financial year and the day on which the Board finalised the Board's Report, the Board shall indicate in the report the up- to- date status and position affecting the financial impact on the operations of the company as well as material changes that have occurred which have a bearing on the working of the company. It would include events such as the following:-
  - a. Disposal of a substantial part of the undertaking ;

- b. Changes in the capital structure;
- c. Any serious breakdown which has happened and the steps taken to reduce its adverse impact ;
- d. Alteration in wage structure arising out of trade union negotiation;
- e. Material changes concerning purchase of raw materials and sale of the products, etc.

Subject to following the necessary precaution of not to disclose any information which is not in the interest of the business of the company or which may help the competitors, the Board's report shall give details of the changes, if any, that have occurred during the year under review, in the nature of the business of the company and in the class of business in which the company has interest and also in the nature of its subsidiary, if any.

7. The company shall disclose regarding the committees of the company viz. Corporate Social Responsibility Committee, Audit Committee, Nomination and Remuneration committee and Stakeholders Relationship Committee in the Board's Report as per requirement of Section 135, 177, 178 of the Act, if applicable.

Section 177(8) provides that 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 therefore.

8. The details of Loans, Guarantee and investment shall be mentioned in the Board's Report as per provisions of Section 186 of the Act.

9. The company shall disclose in its Board's report regarding all the particulars of contracts or arrangements with related parties referred to in section 188(1) in the Form AOC-2. [Rule 8 of Companies (Accounts) Rules, 2014]

10. It is provided that in Board's Report, a statement must be enclosed which shows the development and implementation of risk management policy of the company. The suggested items for this statement are as follows:

- a. Introduction
- b. Meaning and definitions Risk Management
- c. Types of Risks
- d. Risk Management
- e. Risk Assessment
- f. Risk Identification Activities
- g. Risk Handling
- h. Monitoring and Reporting
- i. Conclusion

11. Section 177(10) provides for disclosure of details of establishment of vigil mechanism by the company on its website, if any, and in the Board's report.

12. Section 197(12) read with Rule 5 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 provides for disclosures which are discussed earlier in the chapter.

13. Section 204(1) read with Rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 requires to annex the Secretarial Audit Report in the Form – MR-3 with the Board's Report of the listed company and the following specified public companies:

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

Such secretarial audit report under section 134, is required to be given by a Company Secretary in practice.

14. Section 134(3)(f) provides that the board of directors shall be bound to give full information and contain a suitable explanation in the Board's Report on any qualification, reservation or adverse remark made by the Auditors in their report on the accounts audited by them and by the company secretary in practice in his secretarial audit report.

15. Rule 8(3) provides that the Board's Report to include the particulars in respect of conservation of energy/technology absorption as already detailed in this Chapter. (Sample Board's Report is placed at Annexure IV)

### 3. ANNUAL RETURN

Annual Return is a significant document for the stakeholders of a company as it provides in a nutshell, very comprehensive information about various aspects of a company. It is perhaps the most important document required to be filed by every company with the Registrar of Companies. Apart from the Financial Statements, this is the only document to be compulsorily filed with the Registrar every year irrespective of any events / happenings in the company. While the Financial Statements give information on the financial performance of a company, it is the Annual Return which gives extensive disclosure and greater insight into the non-financial matters of the company and the people behind management of the company.

#### Applicability

As per section 92 of the Companies Act, 2013, every company is required to prepare the Annual Return in Form No. MGT-7 containing the particulars as they stood on the close of the financial year. Annual Return is to be filed with the Registrar within 60 days from the date on which Annual General Meeting (AGM) is actually held or from the last day on which AGM should have been held.

As provided in sub-section(2) of section 384, the provisions of section 92 regarding filing of annual return apply to a foreign company subject to such exceptions, modifications and adoptions as may be provided for in the Rules. Rule 7 of the Companies (Registration of Foreign Companies) Rules, 2014 provides that every foreign company shall prepare and file, within a period of sixty days from the last day of its financial year, to the Registrar annual return in Form FC-4 along with fee, containing the particulars as they stood on the close of the financial year.

#### Contents of Annual Return

Annual Return shall contain the following particulars in consonance with the Section 92(1) of the Act:

- (1) its registered office, principal business activities, particulars of its holding, subsidiary and associate companies;
- (2) its shares, debentures and other securities and shareholding pattern;
- (3) its members and debenture-holders along with changes therein since the close of the previous financial year;
- (4) its promoters, directors, key managerial personnel along with changes therein since the close of the previous financial year;
- (5) meetings of members or a class thereof, Board and its various committees along with attendance details;
- (6) remuneration of directors and key managerial personnel;
- (7) 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;
- (8) matters relating to certification of compliances, disclosures as may be prescribed;
- (9) details, as may be prescribed, in respect of shares held by or on behalf of the Foreign Institutional Investors and  
such other matters as may be prescribed.

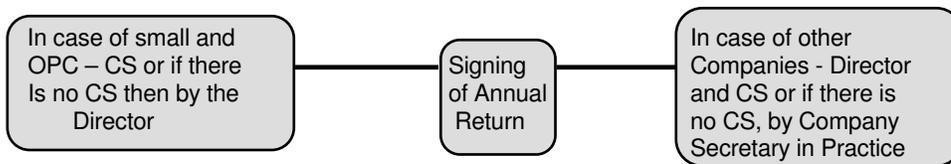
**Additional contents**

Secretarial Standards on Board Meetings (SS-1) provides that annual return shall disclose the number and dates of meetings of the board and committees held during the financial year indicating the number of meetings attended by each director. Further Secretarial Standard on General Meetings (SS-2) provides that the annual return shall disclose the date of Annual General Meeting (AGM) held during the financial year.

**Signing of Annual Return**

Under section 92(1) of the Act, the Annual Return is required to be signed both by a director and the Company Secretary, or where there is no Company Secretary, by a Company Secretary in Practice.

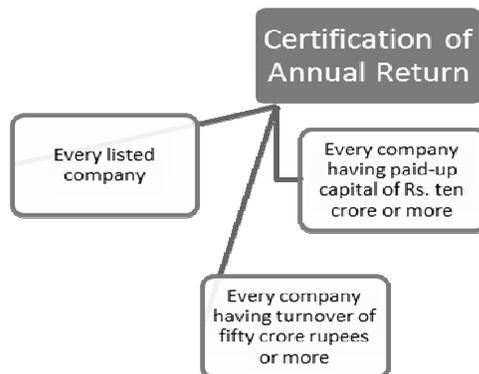
The Annual Return of One Person Company and Small Company shall be signed by the Company Secretary or where there is no company secretary, by the director of the company. The Act authorises the Central Government.



**Certification of Annual Return**

Certification of Annual Return under sub-section (2) of section 92 of the Act read with rule 11(2) of the Companies (Management and Administration) Rules, 2014, the Annual Return of a listed company or of a company having a paid up share capital of Rs. 10 Crores or more or turnover of Rs. 50 Crores or more shall be certified by a Company Secretary in Practice in the Form No. MGT- 8. The certificate shall state that the annual return discloses the facts correctly and adequately and that the company has complied with all the provisions of this Act.

In terms of sub-section (6) of section 92, if a Company Secretary in Practice 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 lakh.



### **Inclusion in Board's Report & Website**

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.

### **Filing of Annual Return with Registrar**

Every company is required to file with the Registrar a copy of the annual return, within sixty days from the date on which the AGM is held or where no AGM is held in any year within sixty days from the date on which the AGM should have been held together with the statement specifying the reasons for not holding the AGM, with such fees or additional fees as may be prescribed.

For foreign company the filing is to be done in FC-4 and other companies the same is to be done in MGT-7.

### **Preservation of Annual Return**

According to Rule 15 of the Companies (Management and Administration) Rules, 2014 copies of all annual returns prepared under section 92 and copies of all certificates and documents required to be annexed thereto shall be preserved for a period of eight years from the date of filing with the Registrar.

### **Contravention and Consequences**

In case the company fails to file its annual return, before the expiry of the period as specified above, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to five lakhs rupees.

Every officer of such company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

Further where a company secretary in practice certifies the annual return which is not in conformity with the requirements of this section or the rules made thereunder, he shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees.

## **4. WEBSITE DISCLOSURES**

Companies Act, 2013 does not mandate companies to have an active website, but SEBI (LODR), 2015 requires all the listed entities shall maintain a functional website containing the following information about the listed entity:-

- (a) details of its business;
- (b) financial information including complete copy of the annual report including balance sheet, profit and loss account, directors report etc;
- (c) contact information of the designated officials of the listed entity who are responsible for assisting and handling investor grievances;
- (d) email address for grievance redressal and other relevant details;
- (e) name of the debenture trustees with full contact details;
- (f) the information, report, notices, call letters, circulars, proceedings, etc concerning non-convertible redeemable preference shares or non convertible debt securities;
- (g) all information and reports including compliance reports filed by the listed entity;

- (h) information with respect to the following events:
  - (i) default by issuer to pay interest on or redemption amount;
  - (ii) failure to create a charge on the assets;
  - (iii) revision of rating assigned to the non convertible debt securities:

It is important that the listed entity ensures the contents of the website are correct and updated at any given point of time.

## **Disclosures under Companies Act, 2013 & Rules made thereunder**

### **1. Information Pertaining to Registered Office [Section 12(3)(c)]**

Every Company must get its e-mail id and website address, if any, printed on its letterheads, business letters, billheads, letter papers and in all its notices and other official publications.

### **2. Change of Object for raising money through Prospectus [Section 13(8)(i)]**

A company which has raised money by issuing prospectus and has still some unutilized amount of the money so raised shall not change its objects for which it raised money through the prospectus unless a special resolution is passed by the company. The details of such a resolution as may be prescribed shall be published on the Website of the company, if any, indicating there in the justification for such change.

### **3. Annual Return [Section 92 (3)]**

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

### **4. Unpaid Dividends [Section 124(2)]**

A company after transferring the amount of unpaid dividends to a separate bank account of "Unpaid Dividend Account" will have to prepare a statement containing the shareholder's names, their last known addresses, and the unpaid dividend to be paid to them on the company's Website, if any.

### **5. Corporate Social Responsibility [Section 135(4)(a)]**

The Board of every company having net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during any financial year, shall after taking into account the recommendations made by the Corporate Social Responsibility Committee, approve the Corporate Social Responsibility Policy for the company and disclose contents of such Policy in its report and also place it on the company's website, if any, in such manner as may be prescribed under the Rule 9 of the Companies (Corporate Social Responsibility Policy) Rules, 2014.

### **6. Placing of financial statements and other documents of a listed company on the website [Section 136(1)(a)]**

A listed company shall also place its financial statements including consolidated financial statements, if any, auditor's report and all other documents required by law to be attached thereto, on its website, which is maintained by or on behalf of the company. The third proviso to this section provides that every company having a subsidiary or subsidiaries shall publish separate audited accounts in respect of each of its subsidiary on its website, if any.

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

**7. Vigil Mechanism in Audit Committee for Listed Companies and other Prescribed Companies [Proviso to Section 177(10)]**

The vigil mechanism under subsection (9) of Section 177 pertaining to setting up of an Audit Committee 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. Provided that the details of establishment of such mechanism shall be disclosed by the company on its website, if any, and in the Board's report.

**8. Nomination and Remuneration Policy**

The Nomination and Remuneration Committee shall formulate the criteria and policy for determining qualifications, positive attributes and independence of a director

Provided that such policy shall be placed on the website of the company, if any, and the salient features of the policy and changes therein, if any, along with the web address of the policy, if any, shall be disclosed in the Board's report. Section 178(4)(c )]

**9. Compromises, Arrangements and Amalgamation [Proviso to Section 230(3)]**

A notice of meeting ordered by the Tribunal for the purpose of Compromise and Arrangements must be served upon the Creditors or class of Creditors, Shareholders or Debenture holders and other members. Such notice should also be published on the Website of the Company, if any.

**10. Code for Independent Directors [Schedule IV (IV)(6)]**

The terms and conditions of appointment of independent directors shall also be posted on the company's website

**11. Notice of candidature of a person for directorship [Rule 13(2) of the companies (Appointment and Qualification of Directors) Rules, 2014]**

The company shall, at least seven days before the general meeting, inform its members of the candidature of a person for the office of a director or the intention of a member to propose such person as a candidate for that office - by placing notice of such candidature or intention on the website of the company, if any.

**12. Notice of resignation of director [Rule 15 of the Companies (Appointment and Qualification of Directors) Rules, 2014]**

The Company shall within thirty days from the date of receipt of notice of resignation from a director, intimate the Registrar in Form DIR - 12 and post the information on its website, if any.

**13. Form and particulars of advertisement or circulars [Rule 4(3) of the Companies (Acceptance of Deposits) Rules, 2014]**

Every company inviting deposits from the public shall upload a copy of the circular on its website, if any.

**14. Variation of terms of contracts referred to in the prospectus or objects for which prospectus was issued [Rule 7(3) of the Companies (Prospectus and Allotment of Securities) Rules, 2014]**

The notice shall also be placed on the website of the company, if any.

**15. Other compliances for conversion of section 8 companies to any other kind [Rule 22(1)(b) of the Companies (Incorporation) Rules, 2014]**

The Company shall, within a week from the date of submitting the application to the Regional Director, publish a notice at its own expense, and a copy of the notice in Form No. INC. 19, shall be sent forthwith to the Regional Director and the said notice shall be published on the website of the company, if any, and as may be notified or directed by the Central Government.

**16. Change of objects for which money is raised through prospectus [Rule 32(3) of the Companies (Incorporation) Rules, 2014]**

Where there is change of objects for which money is raised through prospectus, a notice shall also be placed on the website of the company, if any pertaining to the same.

**17. Closure of register of members or debenture holders or other security holders [Rule 10(1) of the Companies (Management and Administration) Rules, 2014]**

A company closing the register of members or the register of debenture holders or the register of other security holders shall give at least seven days previous notice and in such manner, as may be specified by Securities and Exchange Board of India, if such company is a listed company or intends to get its securities listed, by advertisement at least once in a vernacular newspaper in the principal vernacular language of the district and having a wide circulation in the place where the registered office of the company is situated, and at least once in English language in an English newspaper circulating in that district and having wide circulation in the place where the registered office of the company is situated and publish the notice on the website as may be notified by the Central Government and on the website, if any, of the Company.

**18. Notice of meeting [Rule 18(3)(ix) of the Companies (Management and Administration) Rules, 2014]**

The notice of the general meeting of the company shall be placed on the website of the Company, if any.

**19. Voting through electronic means [Rule 20(3)(ii) of the Companies (Management and Administration) Rules, 2014]**

The notice of voting through electronic means shall also be placed on the website of the company, if any and of the agency forthwith after it is sent to the members

**20. Voting through Electronic Means [Rule 20(3)(xiv) of the Companies (Management and Administration) Rules, 2014]**

The results declared along with the scrutinizer's report shall be placed on the website of the company and on the website of the agency within two days of passing of the resolution at the relevant general meeting of members;

**21. Procedure to be followed for conducting business through postal ballot [Rule 22(4) of the Companies (Management and Administration) Rules, 2014]**

The notice of the postal ballot shall also be placed on the website of the company forthwith after the notice is sent to the members and such notice shall remain on such website till the last date for receipt of the postal ballots from the members.

**22. Postal Ballot [Rule 22(13) of the Companies (Management and Administration) Rules, 2014]**

The results of the poll shall be declared by placing it, along with the scrutinizer's report, on the website of the company.

### 23. Special notice [Rule 23(3) of the Companies (Management and Administration) Rules, 2014]

Where it is not practicable to give the notice in the same manner as the company gives it gives notice of any general meetings, the notice shall be published in English language in English newspaper and in vernacular language in a vernacular newspaper, both having wide circulation in the State where the registered office of the Company is situated and such notice shall also be posted on the website, if any, of the Company.

## POLICIES

The Companies incorporated under the Indian Company Law are required to frame different Policies/ maintain systems/ plans and devise Codes of/ for the Company/ Board of Directors and Senior Management Personnel/ Directors and Employees etc. pursuant to the provisions of the Companies Act, 2013 and other corporate laws. However, companies whose shares are listed on Stock Exchanges in India are additionally required to frame some other policies/ code as well, in compliance of the SEBI (LODR) and SEBI Rules and Regulations.

The Policies and Codes that are required to be framed by companies, needs also to be disclosed in the Board's Report forming part of the Annual Report and uploaded on Company's website, wherever applicable.

The table below lists the various Policies/ Codes to be framed, applicability, manner of framing and disclosure requirements etc.

S.No.	Name of Policy/ Code	Applicability	To be framed by		Disclosure	
			Committee	Board of Directors	Board Report	Website of Company
1.	Corporate Social Responsibility (CSR) Policy	Every company having net worth of Rs.500 crore or more OR turnover of ₹1,000 crore or more OR a net profit of ₹5 crore or more during any financial year	(i) Board shall constitute CSR Committee of the Board which shall formulate & recommend to the Board, CSR Policy which shall indicate the activities to be undertaken by the company as per Schedule VII of the CA, 2013,  (ii) recommend the amount of expenditure to	Board of Directors shall:  (i) Approve the Policy  (ii) ensure that the activities as are included in CSR Policy are undertaken by the company	Disclose the contents of the CSR Policy as per the particulars specified in the Annexure to Companies (CSR Policy) Rules, 2014	The contents to be given in the Board Report shall be displayed on the website of the Company.

			be incurred on the activities to be undertaken by the company and (iii) monitor CSR Policy of the company from time to time			
2.	Whistle Blower Policy – A Vigil mechanism for directors and employees to report genuine concerns or grievances about unethical behavior, actual or suspected fraud or violation of the company's code of conduct or ethics policy	Every listed company and all companies which: (i) accept deposits from the public; (ii) have borrowed money from banks and public financial institutions in excess of ₹50 Crores.	As the Audit Committee shall review the functioning of the Whistle Blower mechanism, the Policy can be routed through the Audit Committee.	Board	Details of establishment of such mechanism to be disclosed	Details of establishment of such mechanism to be disclosed, if any.
3.	Policy on directors' appointment and remuneration of the directors, KMP and other employees including criteria for determining qualifications, positive attributes, independence of a director and other matters.	Every Listed Company and all Public Companies having: paid up capital of ₹10 crores or more; OR turnover of ₹100 crores or more OR which have, in aggregate, outstanding loans or borrowings or debentures or deposits exceeding ₹50 crores or more.	Nomination & Remuneration Committee shall formulate a policy and recommend to the Board.	Approve the Policy	Yes	Yes

## **Various Policies to be framed as per SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015)**

As per the Listing Regulations, all listed entities are required to frame various policies which are detailed below:

### **B. Gist of policies to be adopted:**

- I. Policy for preservation of documents
- II. Policy for determining material subsidiary
- III. Policy on materiality of related party transactions
- IV. Policy for determination of materiality
- V. Archival Policy
- VI. Vigil Mechanism/ Whistle Blower policy
- VII. Policy on diversity of board of directors
- VIII. Dividend Distribution Policy

### **I. Policy for preservation of documents [Regulation 9]**

**Objective:** To classify the documents, records and registers of the Listed Company at least under two categories:

- (i) to be preserved permanently
- (ii) to be preserved for period of not less than 8 (eight) years.

The listed entity may preserve the above said documents in electronic mode.

### **II. Policy for determining material subsidiary [Regulation 16(1)(c)]**

**Objective:** To determine the material subsidiaries of a Listed Company and to provide the governance framework for such subsidiaries.

“material subsidiary” shall mean a subsidiary, whose income or net worth exceeds 10% of the consolidated income or net worth respectively, of the listed entity and its subsidiaries in the immediately preceding accounting year.

### **III. Policy on materiality of related party transactions and on dealing with related party transactions [Regulation 23]**

**Objective:** To ensure proper approval of related party transactions.

A transaction with a related party shall be considered material if the transaction(s) to be entered into individually or taken together with previous transactions during a financial year, exceeds 10% of the annual consolidated turnover of the listed entity as per the last audited financial statements of the listed entity.

All related party transactions have to be previously approved by the audit committee and require approval of the shareholders.

### **IV. Policy for determination of materiality [Regulation 30(4)(ii)]**

**Objective:** To protect the confidentiality of material/price sensitive information of a Listed Company

Every listed entity has to make disclosures of any events or information which, in the opinion of the board of

directors of the listed company, is material.

**Criteria for determination of materiality of events/ information:**

- (a) the omission of an event or information, which is likely to result in discontinuity or alteration of event or information already available publicly; or
- (b) the omission of an event or information is likely to result in significant market reaction if the said omission came to light at a later date;
- (c) If, the above two clauses are not applicable, an event/information may be treated as being material if in the opinion of the board of directors of listed entity, the event / information is considered material.

#### **V. Archival Policy [Regulation 30(8)]**

**Objective:** To ensure that all the information which, has been disclosed to stock exchange(s) under this regulation and such information which in the opinion of the board of directors of a listed company, is material has to be made available on the Company's website for public/members.

The material information of a listed company shall be hosted on its website for a minimum period of 5 (five) years and thereafter will be archived for a further period as specified in its Archival Policy.

#### **VI. Vigil Mechanism/ Whistle Blower Policy [Regulation 22]**

**Objective:** The Vigil Mechanism/Whistle Blower Policy is implemented to safeguard the unethical practices and to provide mechanism for reporting genuine concerns or grievances.

Every listed entity has to formulate a vigil mechanism for directors and employees to report genuine concerns.

The vigil mechanism has to provide for adequate safeguards against victimization of director(s) or employee(s) or any other person who avail the mechanism and also provide for direct access to the chairperson of the audit committee in appropriate or exceptional cases.

#### **VIII. Policy on diversity of board of directors**

**Objective:** To enhance the effectiveness of the Board by diversifying its composition and to obtain the benefit out of such diversity in better and improved decision making.

In order to ensure that the Company's boardroom has appropriate balance of skills, experience and diversity of perspectives that are imperative for the execution of its business strategy, the Company shall consider a number of factors, including but not limited to skills, industry experience, background, race and gender

#### **IX. Dividend Distribution Policy (Regulation 43A)**

**Objective:** The Policy broadly specifies the external and internal factors including parameters that may be considered while declaring dividend and the circumstances under which the shareholders of the Company may or may not expect dividend.

The top five hundred listed entities based on market capitalization (calculated as on March 31 of every financial year) shall formulate a dividend distribution policy which shall be disclosed in their annual reports and on their websites.

The dividend distribution policy shall include the following parameters:

- (a) the circumstances under which the shareholders of the listed entities may or may not expect dividend;
- (b) the financial parameters that shall be considered while declaring dividend;
- (c) internal and external factors that shall be considered for declaration of dividend;
- (d) policy as to how the retained earnings shall be utilized; and
- (e) parameters that shall be adopted with regard to various classes of shares:

Where in cases the listed entity proposes to declare dividend on the basis of parameters in addition to abovementioned clauses or proposes to change such additional parameters or the dividend distribution policy contained in any of the parameters, it shall disclose such changes along with the rationale for the same in its annual report and on its website.

The listed entities other than top five hundred listed entities based on market capitalization may disclose their dividend distribution policies on a voluntary basis in their annual reports and on their websites.

## ANNEXURES

### *ANNEXURE I*

#### **SPECIMEN BOARD RESOLUTION FOR PREPARATION OF ANNUAL REPORT IN ABRIDGED FORM FOR MAILING TO THE MEMBERS**

“RESOLVED THAT pursuant to the provisions of First proviso of sub – section (1) of Section 136 of the Companies Act, 2013 and Rule 10 of the Companies (Accounts) Rules 2014, the Annual Reports comprising of the Balance Sheet, Profit and Loss Account etc. of the company for the financial year ended 31st March 2013 be also prepared, finalised and audited in the prescribed Form No AOC – 3 for sending to the members of the company.”

“RESOLVED FURTHER THAT the draft audited statement containing salient features of financial statements for the year ended 31st March 2013, prepared in the prescribed Form No. AOC – 3 in accordance with First proviso of sub – section (1) of Section 136 of the Companies Act, 2013 and Rule 10 of the Companies (Accounts) Rules, 2014 as submitted to the meeting, be and are hereby approved and the same be authenticated by the directors of the company as required under Section 136 of the Act and be sent to the statutory auditors of the company for their report thereon and thereafter be sent to the members of the company for adoption at the ensuing annual general meeting of the company.”

### *Annexure II*

#### **SPECIMEN BOARD RESOLUTION FOR APPROVAL OF THE BOARD’S REPORT**

“RESOLVED THAT the draft Boards’ Report to the Shareholders of the company for the year ended 31st March 2015 prepared in accordance with the provisions of Section 134 of the Companies Act, 2013 together with its Annexures and also containing suitable explanation and fullest information on every reservation, qualification or adverse remarks contained in Auditor’s reports, as submitted to the meeting, be and is hereby approved and the same be signed by Shri..... Chairman of the company, by Shri..... Managing Director and Shri..... Director for and on behalf of the Board of Directors of the company.”

**Annexure III****SPECIMEN RESOLUTION TO BE PASSED AT A MEETING OF THE BOARD OF DIRECTORS FOR APPROVAL OF THE BOARD'S REPORT CONTAINING BOARD'S RESPONSE TO AUDITORS' COMMENTS AND QUALIFICATIONS**

"RESOLVED THAT, pursuant to Section 134 of the Companies Act, 2013 the draft of the Board's Report for the year ended....., 2013 as circulated earlier and as modified by incorporating the information and explanation given by the Board on every reservation, qualification or adverse remark contained in the Auditors' Report under Section 143 (2), and as laid on the table, be and is hereby approved and that the Board's Report be signed by the Chairman on behalf of the Board and that the Secretary of the company be directed to issue the same to the members of the company together with the printed copies of the audited accounts, and the Auditors' Report."

**ANNEXURE IV****Board's Report**

Your Directors are pleased to present 21st Annual Report and the audited financial statements for the financial year ended on 31st March, 2018.

Financial Results:

The financial performance of the Company, for the year ended on 31st March, 2018 is summarized below:

Particulars	Standalone		Consolidated	
	For the year ended 31st March 2018	For the year ended 31st March 2017	For the year ended 31st March 2018	For the year ended 31st March 2017
Sales and Other Income	23,956	21,494	45,831	42,254
Profit before Interest, Depreciation, Exceptional Expenses & Tax [PBIDET]	11,332	9,307	12,751	10,841
Less: Depreciation	455	243	773	465
Profit before Interest, Exceptional Expenses & Tax (PBIET)	10,877	9,064	11,978	10,376
Less: Interest	5	4	13	13
Profit Before Tax [PBT] Less: Provision for Tax Profit After Tax [PAT] Less: Minority Interest	10,872	9,060	11,965	10,363
Profit attributable to shareholders	-23	-585	850	532
Add: Profit brought forward from the previous year	10,895	9,645	11,115	9,831
Less: Additional depreciation upon revision in useful lives of tangible assets	-	-	220	186
	10,895	9,645	10,895	9,645
	24,149	18,247	24,149	18,247
	26	0	26	0

Profit available for appropriation, which is appropriated as follows:	35,018	27,892	35,018	27,892
Proposed Final Dividend	2,344	2,344	2,344	2,344
Corporate Dividend Tax on Dividend	477	399	477	399
Transfer to General Reserve	0	1,000	0	1,000
Balance carried to Balance Sheet	32,197	24,149	32,197	24,149
Total	35,018	27,892	35,018	27,892
Basic and Diluted Earning Per Share (EPS of FV Rs. 10/-) [in Rupees]	27.88	24.69	27.88	24.69

### Annual Report 2017-2018

The Company proposes to retain an amount of Rs. 32,197 lacs in the Statement of Profit and Loss. The consolidated financial highlights include the financials of ABC, XYZ, a partnership firm.

#### Results of operations:

During the year under review, the consolidated gross sales grew by 3.1%. On standalone basis, the Company has earned total revenue of ₹23,956 lacs. The PBIDT increased by 21.8 % to ₹11,332 lacs and the Profit Before Tax increased by 20% to ₹10,872 lacs. The Profit after Tax has increased to ₹10,895 lacs as compared to ₹9,645 lacs in the previous year and the EPS has increased from ₹24.69 in the previous year to ₹27.88. A detailed analysis of performance for the year has been included in the Management Discussion and Analysis, which forms part of the Annual Report.

#### Dividend:

Your Directors have recommended a dividend of ₹6/- [i.e. 60%] per equity share [last year ₹6/- per equity share] on 3,90,72,089 equity shares of ₹10/- each fully paid-up for the financial year ended on 31st March, 2018, amounting to ₹2,821 lakhs [inclusive of corporate dividend tax of ₹477 lakhs]. The dividend, if declared by the shareholders at the ensuing Annual General Meeting, will be paid to those shareholders, whose names stand registered in the Register of Members as on 29th July, 2018. In respect of shares held in dematerialized form, it will be paid to the members whose names are furnished by the National Securities Depository Limited and the Central Depository Services [India] Limited, as beneficial owners. The Dividend Payout ratio for the current year (inclusive of Corporate Dividend Tax) is 25.90 percent on profits.

During the year, the unclaimed dividend pertaining to the dividend for the year ended 31st March, 2008 was transferred to Investor Education and Protection Fund.

### Consolidated financial Statements

ABC, XYZ is under the majority control of the Company and hence the accounts of ABC, XYZ are consolidated with the accounts of the Company in accordance with the provisions of Accounting Standard [AS]- 21 on Consolidated Financial Statements issued by the Institute of Chartered Accountants of India, Companies Act, 2013 ["Act"] read with Schedule III of the Act and Rules made thereunder and the Listing Agreement with the Stock Exchanges. The audited Consolidated Financial Statements are provided in this Annual Report.

Though Company does not have any subsidiary Company, the Company has formed a policy relating to material subsidiaries, which is approved by the Board of Directors and can be accessed on the Company's website at the link: .....

### Related Party Transactions

All transactions entered by the Company during the financial year with related parties were in the ordinary course of business and on an arm's length basis. During the year, the Company had not entered into any transactions with related parties which could be considered as material in accordance with the policy of the Company on materiality of related party transactions.

The Policy on materiality of related party transactions and dealing with related party transactions as approved by the Board may be accessed on the Company's website at the link: ..... Disclosures on related party transactions are set out in Note No. 34 to the financial statements.

### Directors

#### i. Cessation:

Mr. P [DIN-XXXXXXXX], Director and Mr. Q [DIN-XXXXXXXX], Managing Director of the Company have resigned with effect from 14th July, 2017 and 14th April, 2018 respectively.

The Board places on record its appreciation for contributions and guidance provided by Mr. P and Mr. Q during their respective tenure as a Director / Managing Director of the Company.

#### ii. Retirement by rotation:

In accordance with the provisions of section 152[6] of the Act and in terms of Articles of Association of the Company, Dr. Sharvil P. Patel [DIN-XXXXXXXX] will retire by rotation at the ensuing Annual General Meeting and being eligible, offer himself for reappointment. The Board recommends his reappointment.

#### iii. Appointment of Additional / Whole Time Director:

Mr. R was appointed as an Additional Director and Whole time Director w.e.f. 14th May, 2018, subject to the approval of the Members at the ensuing Annual General Meeting. Mr. R is designated as the Key Managerial Personnel pursuant to the provisions of section 203 of the Act.

#### iv. Independent Directors:

The Independent Directors have submitted their declarations of independence, as required pursuant to the provisions of section 149(7) of the Act, stating that they meet the criteria of independence as provided in section 149(6).

#### v. Chairman:

Upon cessation of Mr. M [DIN-00131852] as the Director of the Company, Dr. N was appointed as the Chairman of the Board and Company w.e.f. 14th July, 2017.

#### vi. Key Managerial Personnel:

The following persons were designated as Key Managerial Personnel:

1. Mr. Q, Managing Director, [up to 14th April, 2018]
2. Mr. R, Whole Time Director, [w.e.f. 14th May, 2018]

3. Mr. O, Chief Financial officer and
4. Mr. J, Company Secretary

**vii. Board Evaluation:**

Pursuant to the provisions of the Act and Rules made thereunder and as provided under Schedule IV of the Act and SEBI (LODR), REG, 2015 the Board has carried out the annual performance evaluation of itself, the Directors individually as well as the evaluation of its committees. The manner in which the evaluation was carried out is provided in the Corporate Governance Report, which is part of this Annual Report.

**viii. Remuneration Policy:**

The Board has on the recommendations of Nomination and Remuneration Committee, framed a Policy on selection and appointment of Directors, Senior Management and their remuneration. The Remuneration Policy is stated in the Corporate Governance Report, which is part of this Annual Report.

### **Directors' Responsibility Statement**

In terms of section 134[3][c] of the Act, your Directors state that:

- i. in the preparation of the annual financial statements for the year ended on 31st March, 2016, applicable accounting standards read with requirements set out under schedule III of the Act, have been followed along with proper explanation relating to material departures, if any,
- ii. such accounting policies have been selected and applied consistently and judgments and estimates made that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company as at 31st March, 2018 and of the profit of the company for the year ended on that date
- iii. the annual financial statements are prepared on a going concern basis,
- iv. proper internal financial control are in place and that the financial controls are adequate and are operating vi. the systems to ensure compliance with the provisions of all applicable laws are in place and are adequate and operating effectively.

### **Board Meetings**

A calendar of meetings to be held in a year is decided in advance by the Board and circulated to the Directors. During the year, four Board and four Audit Committee Meetings were convened and held, the details of which are provided in the Corporate Governance Report, forming part of the Directors' Report. The gap between two consecutive meetings was not more than one hundred and twenty days as provided in section 173 of the Act.

### **Corporate Governance**

The Company has complied with the Corporate Governance requirements under the Act and as stipulated in Listing Regulations. A separate section on detailed report on the Corporate Governance practices followed by the Company under the Listing Agreement along with a certificate from M/s. DEF & Associates, Practicing Company Secretary, confirming the compliance, is part of the Annual Report.

***i. Statutory Auditor and their Report:***

M/s. D, Chartered Accountants, [Firm Registration No. 102511W] Statutory Auditor of the Company hold office until the conclusion of the ensuing 21st Annual General Meeting and are eligible for reappointment.

Pursuant to provisions of section 139 of the Companies Act, 2013 and the Rules made thereunder, the Board proposes to reappoint M/s. \_\_\_\_\_ & \_\_\_\_\_, Chartered Accountants as Statutory Auditor of the Company from the conclusion of the ensuing 21st Annual General Meeting till the conclusion of 26th Annual General Meeting. They have furnished a certificate confirming the eligibility under section 141 of the Companies Act, 2013 and Rules made thereunder.

The Board based on the recommendation of Audit Committee, recommends the reappointment of M/s \_\_\_\_\_, Chartered Accountants, as the Statutory Auditor of the Company.

The Board has duly reviewed the Statutory Auditor's Report on the Accounts. The observations and comments, appearing in the Auditor's Report are self-explanatory and do not call for any further explanation / clarification by the Board of Directors as provided under section 134 of the Act.

**ii. Cost Auditor:**

Pursuant to the provisions of section 148 [3] of the Act read with The Companies [Cost Records and Audit] Amendment Rules, 2014, the cost audit records maintained by the Company in respect of its product utralffe, is required to be audited. The Board had, on the recommendation of Audit Committee, appointed M/s UV & Associates, Cost Accountants [Firm Registration No.000338] to audit the cost records of for the financial year ended on 31st March, 2017 on a remuneration of ₹1.80 lacs As required under the Act and Rules made thereunder, the remuneration payable to the Cost Auditor is required to be placed before the Members General Meeting for ratification. Accordingly, a resolution to ratify the remuneration payable to M/s. UV & Associates for the financial year ending on 31st March, 2018 is included at Item No. 8 of the Notice convening 21 Annual General Meeting.

**iii. Secretarial Auditor and Secretarial Audit Report:**

Pursuant to the provisions of section 204 of the Act and The Companies [Appointment and Remuneration of Managerial Personnel] Rules, 2014, the Company has appointed M/s. DEF & Associates, Practicing Company Secretary to undertake Secretarial Audit for the financial year ended on 31st March, 2018. Secretarial Audit Report is attached to this report as Annexure-"A". The Board has duly reviewed the Secretarial Auditor's Report and the observations and comments, appearing in the report are self-explanatory and do not call for any further explanation / clarification by the Board of Directors as provided under section 134 of the Act.

**Corporate Social Responsibility [CSR]**

The Board of Directors of the Company has constituted a Corporate Social Responsibility [CSR] Committee under the Chairmanship of Dr. N. Other members of the Committee are Mr. Y and Prof. Z CSR Committee has recommended to the Board, a CSR Policy, indicating the activities to be undertaken by the Company, which is approved by the Board. The CSR Policy is posted on the website of the Company.

As part of its initiatives under Corporate Social Responsibility [CSR], the Company has contributed for healthcare, education and research in cancer and for eradicating poverty and malnutrition for the year under review. Other details of the CSR activities as required under section 135 of the Act are given in the CSR Report at Annexure-B.

**Business Risk Management:**

A well-defined risk management mechanism covering the risk mapping and trend analysis, risk exposure, potential impact and risk mitigation process is in place. The objective of the mechanism is to minimize the

impact of risks identified and taking advance actions to mitigate it. The mechanism works on the principles of probability of occurrence and impact, if triggered. A detailed exercise is being carried out to identify, evaluate, monitor and manage both business and non-business risks.

Discussion on risks and concerns are covered in the Management Discussion and Analysis Report, which forms part of this Annual Report.

### **Internal control systems and its adequacy**

The Company has internal control systems commensurate with the size, scale and complexity of its business operations. The scope and functions of internal auditor are defined and reviewed by the Audit committee. The internal auditor reports to the Chairman of the Audit Committee. Internal Auditors presents their quarterly report to the Audit Committee, highlighting various observations, system and procedure lapses and corrective actions are taken. The internal auditor also assesses opportunities for improvement of business processes, systems and controls, to provide recommendations, which can add value to the organization and it also follows up on the implementation of corrective actions and processes. The Management Auditor also ensures the compliance of the observations of internal and statutory auditors and presents his report to the Audit Committee.

### **Managing the Risks of fraud, corruption and unethical business practices**

#### ***i. Vigil Mechanism/ Whistle Blower Policy:***

The Company has established vigil mechanism and framed whistle blower policy for Directors and employees to report concerns about unethical behavior, actual or suspected fraud or violation of Company's Code of Conduct or Ethics Policy. Whistle Blower Policy is disclosed on the website of the Company.

#### ***ii. Business Conduct Policy:***

The Company has framed "ABC Business Conduct Policy". Every employee is required to review and sign the policy at the time of joining and an undertaking shall be given for adherence to the Policy. The objective of the Policy is to conduct the business in an honest, transparent and in an ethical manner. The policy provides for anti- bribery and avoidance of other corruption practices by the employees of the Company.

#### **Annual Return:**

The weblink of the Annual Return is \_\_\_\_\_.

Report as Annexure-"C". Constitution of Audit Committee:

The Board has reconstituted the Audit Committee whkh comprises of Mr. H as the Chairman and Dr. B.M. Hegde, Prof. Z and Mr. Y as the members. More details on the Committee are given in the Corporate Governance Report.

#### **Particulars of Employees:**

The information required under section 197 of the Act read with Rule 5[1] of The Companies [Appointment and

#### **Remuneration of Managerial Personnel] Rules, 2014 are given in Annexure-"D".**

Energy Conservation, Technology Absorption and Foreign Exchange Earnings and Outgo:

Information on conservation of energy, technology absorption, foreign exchange earnings and outgo, as required to be disclosed under section 134[3][m] of the Act read with the Companies [Accounts] Rules, 2014, are provided in the Annexure-"E" and forms part of this Report.

**General Disclosure:**

Your Directors state that the Company has made disclosures in this report for the items prescribed in section 134[3] of the Act and Rule 8 of The Companies [Accounts] Rules, 2014 to the extent the transactions took place on those items during the year.

**Acknowledgement:**

Your Directors wish to place on record their sincere appreciation for significant contributions made by the employees at all levels through their dedication, hard work and commitment, enabling the Company to achieve good performance during the year under review.

Your Directors also take this opportunity to place on record the valuable co-operation and support extended by the banks, government, business associates and the shareholders for their continued confidence reposed in the Company and look forward to having the same support in all future endeavors.

For and on behalf of the Board Place:

Ahmedabad

N

Date : 14th May, 2018

Chairman

## LESSON ROUND UP

- The annual report is a comprehensive report provided by most public companies to disclose their corporate activities over the past year.
- According to Regulation 34 of SEBI (LODR) Regulation, 2015 a listed entity shall submit the annual report to the stock exchange within twenty one working days of it being approved and adopted in the AGM.
- The listed entity shall send annual report to the holders of securities, not less than twenty-one days before the annual general meeting.
- Disclosures in the Board report are derived from various places, apart from disclosures specified in section 134 of the Act.
- Section 134 of the Act enjoins upon the Board a responsibility to make out its report to the shareholders and attach the said report to financial statements laid before the shareholders at the annual general meeting
- As per section 92 of the Companies Act, 2013, every company is required to prepare the Annual Return in Form No. MGT-7 containing the particulars as they stood on the close of the financial year.
- Annual Return is to be filed with the Registrar within 60 days from the date on which Annual General Meeting (AGM) is actually held or from the last day on which AGM should have been held.

## GLOSSARY

Holding Company	"holding company", in relation to one or more other companies, means a company of which such companies are subsidiary companies (Sec 2(46) of Companies Act, 2013) Explanation.—For the purposes of this clause, the expression "company" includes any body corporate.
Subsidiary Company	"subsidiary company" or "subsidiary", in relation to any other company (that is to say the holding company), means a company in which the

holding company—

(i) controls the composition of the Board of Directors; or

(ii) exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies:

**Provided** that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.

*Explanation.*—For the purposes of this clause,—

(a) a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (i) or sub-clause (ii) is of another subsidiary company of the holding company;

(b) the composition of a company's Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors;

(c) the expression "company" includes any body corporate;

(d) "layer" in relation to a holding company means its subsidiary or subsidiaries; (Sec 2(87) of Companies Act, 2013))

## SELF TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

1. What information is required to be disclosed in Annual Report?
2. Draft a Directors' Report of your company.
3. What forms the Directors' Responsibility Statement?
4. What points should be kept in mind while preparing Annual Report?

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# Lesson 10

## An overview of Inter-Corporate Loans, Investments, Guarantees and Security, Related Party Transactions

### LESSON OUTLINE

- Loans and investments by a company
- Investments held in company's own name
- Related Party Transactions
- Lesson Round-up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

Under the Companies Act, 2013 Inter-Corporate Loans and Investment plays a very vital role for the growth of industries as this results in the flow of funds for the group companies or other companies who are in the need of funds.

This chapter provides an overview of related party transactions, loans and investment by companies, 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.

As a prospecting company secretary you are expected to guide the Board on the subject matter, hence acquaintance of the same is essential.

## INTRODUCTION

The power to invest the funds of the company is the prerogative of the Board of Directors. This power is derived by the Board under Section 179 of the Act. However, the Companies Act, 2013 contains provisions for restrictions on investments that a company can make and loans it can provide. Moreover, giving corporate guarantee or security is also as good as giving a loan, because the person to whom guarantee or security is given can decide to enforce the guarantee or security in certain conditions and in such a situation, the company will have to pay the amount. Thus apart from loan and investments, restrictions are also placed on the guarantees which the company can give or security it can provide for a loan.

Provisions in respect of giving of loans, making investments, giving guarantee or providing security or acquiring securities of any other body corporate have been considerably modified by the Companies Act, 2013. As of now, an overall limit of 60% of paid-up share capital plus free reserves and securities premium account or 100% of free reserves and securities premium account, whichever is more, has been fixed.

### Let us understand some terminologies used in Section 186 of the Companies Act 2013

#### Free reserves

As per section 2(43) “free reserves” means such reserves which, as per the latest audited balance Sheet of a company, are available for distribution as dividend:

Provided that—

- (i) any amount representing unrealised gains, notional gains or revaluation of assets, whether shown as a reserve or otherwise e, or
- (ii) any change in carrying amount of an asset or of a liability recognised in equity, including surplus in profit and loss account on measurement of the asset or the liability at fair value,

shall not be treated as free reserves;

#### Paid-up share capital

As per Section 2(64) of the Act, “paid-up share capital” or “share capital paid-up” **means** such aggregate amount of money credited as paid-up as is equivalent to the amount received as paid up in respect of shares issued and also includes any amount credited as paid-up in respect of shares of the company, but does not include any other amount received in respect of such shares, by whatever name called;

**The definition of paid up share capital is exhaustive. Paid up share capital includes both equity and preference share capital.**

#### “body corporate” or “corporation

As per Section 2(11) “body corporate” or “corporation” includes a company incorporated outside India, but does not include—

- (i) a co-operative society registered under any law relating to co-operative societies; and
- (ii) any other body corporate (not being a company as defined in this Act),

which the Central Government may, by notification, specify in this behalf;

#### Company principally engaged in the business of acquisition of Shares etc.

As per explanation to section 186 - 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 fifty per cent. of its total assets, or if its income derived from investment business constitutes not less than fifty per cent. as a proportion of its gross income.

### **Investment Company & Infrastructure facilities**

As per explanation to Section 186

- (a) the expression “investment company” means a company whose principal business is the acquisition of shares, debentures or other securities;
- (b) the expression “infrastructure facilities” means the facilities specified in Schedule VI.

As per Schedule VI, the term “infrastructural projects” or “infrastructural facilities” includes the following projects or activities:—

(1) Transportation (including inter modal transportation), includes the following:—

- (a) roads, national highways, state highways, major district roads, other district roads and village roads, including toll roads, bridges, highways, road transport providers and other road-related services;
- (b) rail system, rail transport providers, metro rail roads and other railway related services;
- (c) ports (including minor ports and harbours), inland waterways, coastal shipping including shipping lines and other port related services;
- (d) aviation, including airports, heliports, airlines and other airport related services;
- (e) logistics services.

(2) Agriculture, including the following, namely:—

- (a) infrastructure related to storage facilities;
- (b) construction relating to projects involving agro-processing and supply of inputs to agriculture;
- (c) construction for preservation and storage of processed agro-products, perishable goods such as fruits, vegetables and flowers including testing facilities for quality.

(3) Water management, including the following, namely:—

- (a) water supply or distribution;
- (b) irrigation;
- (c) water treatment.

(4) Telecommunication, including the following, namely:—

- (a) basic or cellular, including radio paging;
- (b) domestic satellite service (i.e., satellite owned and operated by an Indian company for providing telecommunication service);
- (c) network of trunking, broadband network and internet services.

(5) Industrial, commercial and social development and maintenance, including the following, namely:—

- (a) real estate development, including an industrial park or special economic zone;
- (b) tourism, including hotels, convention centres and entertainment centres;

- (c) public markets and buildings, trade fair, convention, exhibition, cultural centres, sports and recreation infrastructure, public gardens and parks;
  - (d) construction of educational institutions and hospitals;
  - (e) other urban development, including solid waste management systems, sanitation and sewerage systems.
- (6) Power, including the following:—
- (a) generation of power through thermal, hydro, nuclear, fossil fuel, wind and other renewable sources;
  - (b) transmission, distribution or trading of power by laying a network of new transmission or distribution lines.
- (7) Petroleum and natural gas, including the following:—
- (a) exploration and production;
  - (b) import terminals;
  - (c) liquefaction and re-gasification;
  - (d) storage terminals;
  - (e) transmission networks and distribution networks including city gas infrastructure.
- (8) Housing, including the following:—
- (a) urban and rural housing including public / mass housing, slum rehabilitation, etc;
  - (b) other allied activities such as drainage, lighting, laying of roads, sanitation and facilities.
- (9) Other miscellaneous facilities/services, including the following:—
- (a) mining and related activities;
  - (b) technology related infrastructure;
  - (c) manufacturing of components and materials or any other utilities or facilities required by the infrastructure sector like energy saving devices and metering devices;
  - (d) environment related infrastructure;
  - (e) disaster management services;
  - (f) preservation of monuments and icons;
  - (g) emergency services (including medical, police, fire and rescue).
- (10) such other facility service as may be prescribed.

### **Securities**

As per Section 2(81) “securities” means the securities as defined in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956;

As per Section 2(h) of the Securities Contracts (Regulation) Act, 1956, “**securities**” include—

- (i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;
- (ia) derivative;

- (ib) units or any other instrument issued by any collective investment scheme to the investors in such schemes;
- (ic) security receipt as defined in clause (zg) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
- (id) units or any other such instrument issued to the investors under any mutual fund scheme;
- (ii) Government securities;
  - (iia) such other instruments as may be declared by the Central Government to be securities; and
- (iii) rights or interest in securities;

### **LOANS AND INVESTMENTS BY COMPANIES (Section 186)**

#### **Not more than two layers of investment companies - Section 186(1)**

A company shall unless otherwise prescribed, make investment through not more than two layers of investment companies. [Sub-section (1) of section 186]

However, the aforesaid provisions shall not affect,—

- (i) a company from acquiring any other company incorporated in a country outside India if such other company has investment subsidiaries beyond two layers as per the laws of such country;
- (ii) a subsidiary company from having any investment subsidiary for the purposes of meeting the requirements under any law or under any rule or regulation framed under any law for the time being in force. [Proviso to sub-section (1) of section 186]

Therefore, Section 186 (1) restricts a company from making investment through more than 2 layers of investment companies.

As stated above, for the purpose of Section 186 of the Act, Investment Company means a company whose principal business is the acquisition of shares, debentures or other securities.

The definition of Investment Company is exhaustive. Further, the restriction under section 186(1) is about investment through Investment Companies only.

Therefore, investment through any company other than the Investment Company is not covered under sub-section (1) of Section 186 of the Act.

#### **LIMITS FOR LOANS, GUARANTEES, SECURITY AND INVESTMENT - SECTION 186(2)**

No Company shall, directly or indirectly:

- (a) give any loan to any person or other body corporate;
- (b) give any guarantee, or provide security, in connection with a loan to any other body corporate or person; and
- (c) acquire, by way of subscription, purchase or otherwise the securities of any other body corporate;

exceeding 60% of its paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account, whichever is more unless the same is previously authorised by a special resolution passed in a general meeting.

**Explanation.**—For the purposes of this sub-section, the word "person" does not include any individual who is in the employment of the company.

## NON APPLICABILITY OF SECTION 186

### Exemptions

Sub-section (11) of section 186 provides that nothing contained in this section, except sub-section (1), shall apply—

- (a) to any loan made, any guarantee given or any security provided or any investment made by a banking company, or an insurance company, or a 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 pursuance of clause (a) of sub-section (1) of section 62 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 Chapter III-B of the Reserve Bank of India Act, 1934 and whose principal business is acquisition of securities.

### Exemption from Applicability of Section 186 to Government Company

In view of the Central Government's notification dated 5<sup>th</sup> June 2015 under Section 462 of the Companies Act, 2013, **Section 186 shall not apply to:**

- (a) a Government company engaged in defence production;
- (b) a Government company, other than a listed company, in case such company obtains approval of the Ministry or Department of the Central Government which is administratively in charge of the company, or, as the case may be, the State Government before making any loan or giving any guarantee or providing any security or making any investment under the section.

**Note:** Except the government companies falling under the above mentioned conditions, all other companies are required to comply with the provisions of Section 186. In cases where there is no share capital, computation shall be based upon the free reserves of the company, if any.

## PENALTY FOR CONTRAVENTION OF SECTION 186

If a company contravenes the provisions of this section, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to two years and with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees. [Section 186(13)]

## MEANING OF THE TERM INVESTMENT

The word 'Investments' in common parlance would include any property or right in which money or capital is invested. However, for the purpose of this study, the term 'Investments' is used in a limited sense to mean the investment of money in shares, stock, debentures, or other securities.

## PROCEDURES INVOLVED IN MAKING LOAN GIVING GUARANTEE AND PROVIDING SECURITY

**Loan/investment to be made with the approval of all the directors at the Board Meeting [Section 186(5)]**

No loan or investment shall be made 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 directors present at the meeting.

Note: Every proposal for making loan to any other body corporate, exceeding 60% of its paid-up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account whichever is more, shall be approved at the meeting of the Board with the consent of all the directors present at the meeting and also to be approved by the shareholders at the general meeting by way of special resolution. [Section 186(3)]

#### **Prior approval by Special Resolution [Section 186 (3)]**

**Section 186(3) read with Rule 13 of Companies (Meetings of Board and its Powers) Rules, 2014, states that**

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 limits specified under sub-section (2) (above mentioned), no investment or loan shall be made or guarantee shall be given or security shall be provided unless previously authorised by a special resolution passed in a general meeting. [Section 186(3)]

Where a loan or guarantee is given or where a security has been provided by a company to its wholly owned subsidiary company or a joint venture company, or acquisition is made by a holding company, by way of subscription, purchase or otherwise of, the securities of its wholly owned subsidiary company, the requirement of section 186(3) Act shall not apply i.e. prior special resolution shall not be required.

A resolution passed at a general meeting in terms of sub-section (3) of section 186 to give any loan or guarantee or investment or providing any security or the acquisition under sub-section (2) of section 186 shall specify the total amount up to which the Board of Directors are authorized to give such loan or guarantee, to provide such security or make such acquisition.

**The company is required to disclose the details of such loans or guarantee or security or acquisition in the financial statement.**

The company shall disclose to the members in the financial the full particulars in accordance with the provisions of sub-section (4) of section 186.

No company, which is registered under section 12 of the Securities and Exchange Board of India 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.

Pursuant to the above provisions no stock broker, sub-broker, share transfer agent, banker to issue, Registrar to an issue, Merchant Baker, underwriter, portfolio manager, investment advisor or any intermediary associated with capital market and which is registered under section 12 of the SEBI Act, shall make loans or investments or give guarantees or provide security in excess of the limits specified above. [Rule 11 of Companies (Meetings of Board and its Powers) Rules, 2014]

#### **Disclosure in financial statements [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 utilised by the recipient of the loan or guarantee or security.

#### **Prior Approval of Financial Institution [Section 186(5)]**

The company has to obtain prior approval of the public financial institution concerned where any term loan is

subsisting. Section 186(5) provides that 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, the prior approval of Public Financial Institution shall not be required where the aggregate of loans and investments so far made, the amounts for which guarantee or security so far provided to or in all other bodies corporate, alongwith the investments, loans, guarantee or security proposed to be made or given does not exceed the limit of 60% specified above and there is no default in repayment of loan installments or payment of interest thereon as per the terms and conditions of such loan to the public financial institution. [Proviso Section 186(5)]

#### **Rate of interest [Section 186(7)]**

Loan given under this section shall carry the rate of interest not lower than the prevailing yield of one year, three year, five year or ten year Government Security closest to the tenor of the loan.

In case of section 8 companies, section 186 (7), following proviso shall be applicable:-

Provided that nothing contained in this sub-section shall apply to a company in which twenty-six per cent. or more of the paid-up share capital is held by the Central Government or one or more State Governments or both, in respect of loans provided by such company for funding Industrial Research and Development projects in furtherance objects as stated in its memorandum of association.”.- (Notification No. GSR 466(E) dated 5-06-2015, as amended by notification no GSR 584(E) , dated 13-06-2017.)

#### **Default subsists with respect to repayment of deposits [Section 186(8)]**

No company, which is in default in repayment of any deposits accepted before or after the commencement of the Companies Act, 2013 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.

This prohibition will operate in respect of any default made under Section 73 to 76 and the Rules made thereunder and not only on the default of repayment of deposit or payment of interest thereon.

### **REGISTER OF LOANS MADE, GUARANTEES GIVEN, SECURITIES PROVIDED AND INVESTMENTS MADE**

Sub-section (9) of section 186 provides that every company giving loan or giving a guarantee or providing security or making an acquisition under this section shall keep a register which shall contain such particulars and shall be maintained in manner prescribed under Rule 12 of Companies (Meetings of Boards and its Powers) Rules, 2014.

Rule 12 states that every company giving loan or giving guarantee or providing security or making an acquisition of securities shall, from the date of its incorporation, maintain a register in Form MBP 2 and enter therein separately, the particulars of loans and guarantees given, securities provided and acquisitions made as aforesaid.

The entries in the register shall be made chronologically in respect of each such transaction within seven days of making such loan or giving guarantee or providing security or making acquisition.

The register shall be kept at the registered office of the company and the register shall be preserved permanently and shall be kept in the custody of the company secretary of the company or any other person authorised by the Board for the purpose. The entries in the register (either manual or electronic) shall be authenticated by the company secretary of the company or by any other person authorised by the Board for the purpose.

The extracts from the register maintained may be furnished to any member of the company on payment of such fee as may be prescribed in the Articles of the company which shall not exceed ten rupees for each page.

### **INVESTMENTS TO BE HELD IN COMPANY'S OWN NAME**

According to Sub-section (1) of Section 187, 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.

The requirement that the investment made by the company must be held in its own name is confined to only those investments which are made by it on its own behalf and not on behalf of someone else. In a case where the company is a trustee, the investment is supposed to be made on behalf of the beneficiaries of the trust and not on its own behalf. Therefore, the investments by the company as a trustee and held in the name of the beneficiaries is allowed.

As per proviso to section 187(1), the company may hold any shares in its subsidiary company in the name of any nominee or nominees of the company, if it is necessary to do so, to ensure that the number of members of the subsidiary company is not reduced below the statutory limit.

Where the shares of a company were registered in the joint names of the company and one of its directors, it was held that the director was a nominee of the company for that purpose and could only act jointly as he had no rights of his own. [Exchange Travel (Holdings) Ltd. Re, (1991) BCLC 728 (Ch D)].

### **Exemptions from applicability of Section 187(1)**

1. In terms of the provisions of Section 187(2), Section 187(1) does not prevent a company:
  - (a) from depositing with the bank, being the bankers of the company, any shares or securities for the collection of any dividend or interest payable thereon; or
  - (b) from depositing with or transferring to, or holding in the name of, the State Bank of India or a scheduled bank, being the bankers of the company, shares or securities, in order to facilitate the transfer thereof. However, if within a period of 6 months from the date on which the shares or securities are transferred by the company to, or are first held by the company in the name of, the State Bank of India or a scheduled bank as aforesaid, no transfer of such shares or securities takes place, the company shall, as soon as practicable, after the expiry of that period, have the shares or securities re-transferred to it from the State Bank of India or the scheduled bank or, as the case may be, again hold the shares or securities in its own name; or
  - (c) from depositing with, or transferring to, any person any shares or securities, by way of security for the re-payment of any loan advanced to the company or the performance of any obligation undertaken by it.
  - (d) from holding investments in the name of a depository when such investments are in the form of securities held by the company as a beneficial owner.

Thus, it is not necessary for the company to hold the shares or stocks or debentures in its own name if they are deposited with the bank as aforesaid. A resolution of the Board of directors in this behalf is sufficient. The bank is entitled to have the shares or debentures registered in its own name with the specific purpose of collecting dividend or interest from the company whose shares or debentures are deposited with the bank. The company holding the investment in the name of the bank is only required to enter into a separate agreement with the bank that the latter will collect dividend and interest and credit the company with the amounts so collected. It may be noted that the deposit of shares, stocks and debentures with the bank need not be by way of a pledge but may be made for the specific object of enabling the banker to act as agent of the company to collect dividend and interest.

## REGISTER OF INVESTMENTS NOT HELD IN COMPANY'S OWN NAME

According to sub-section (3) of section 187 where in pursuance of clause (d) of sub-section (2), 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.

Therefore, a company is only required to maintain a register for securities not held in the name of the company, when the investments are held in the name of a depository.

Accordingly when any shares or securities in which investments have been made by a company are not held by it in its own name as a beneficial owner when such investments are held in the name of a depository pursuant to Section 187(2)(d), the company shall forthwith enter in a register maintained by it for the purpose, the prescribed particulars.

## Companies (Meetings of Board and its Powers) Rules, 2014

Rule 14 of Companies (Meetings of Board and its Powers) Rules, 2014 states the following:

- (1) Every company shall, from the date of its registration, maintain a register in Form MBP 3 and enter therein, chronologically, the particulars of investments in shares or other securities beneficially held by the company but which are not held in its own name and 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.
- (2) The company shall also record whether such investments are held in a third party's name for the time being or otherwise.
- (3) 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 of the company or if there is no company secretary, any director or any other officer authorised by the Board for the purpose.
- (4) The entries in the register shall be authenticated by the company secretary of the company or by any other person authorised by the Board for the purpose.

## PUNISHMENT

According to section 187(4), if a company contravenes the provisions of section 187, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees, or with both.

## RELATED PARTY TRANSACTIONS

According to Section 2(76) of Companies Act 2013, “**related party**”, with reference to a company, means—

- (i) a director or his relative;
- (ii) a key managerial personnel or his relative;
- (iii) a firm, in which a director, manager or his relative is a partner;
- (iv) a private company in which a director or manager or his relative is a member or director;

- (v) a public company in which a director or manager is a director and holds along with his relatives, more than two per cent (2%) of its paid-up share capital;
- (vi) any body corporate whose Board of Directors, managing director or manager is accustomed to act in accordance with the advice, directions or instructions of a director or manager;
- (vii) any person on whose advice, directions or instructions a director or manager is accustomed to act: Provided that nothing in sub-clauses (vi) and (vii) shall apply to the advice, directions or instructions given in a professional capacity;
- (8) any body corporate which is—
  - a holding, subsidiary or an associate company of such company ;
  - a subsidiary of a holding company to which it is also a subsidiary;or
  - an investing company or the venturer of the company.

Explanation.—For the purpose of this clause, “the investing company or the venturer of a company” means a body corporate whose investment in the company would result in the company becoming an associate company of the body corporate

*(According to Notification no. GSR 464(E), dated 05/06/2015 in case of Private Companies this sub- clause shall not apply with respect to section 188.)*

- (i) such other person as may be prescribed;

Related Party: According to Rule 3 Companies (Specification of Definitions Details) Rules, 2014 for the purposes of sub-clause (ix) of clause (76) of section 2 of the Act, a director other than an independent director or key managerial personnel of the holding company or his relative with reference to a company, shall be deemed to be a related party.

***List of relatives in terms of Section 2(77)***

Relative means anyone who is related to another if-

- (1) they are members of Hindu Undivided Family;
- (2) they are husband and wife; or
- (3) one person is related to other in accordance with Rule 4 of Companies (Specifications of Details) Rules, 2014.

A person shall be deemed to be the relative of another, if he or she is related to another in the following manner, namely-

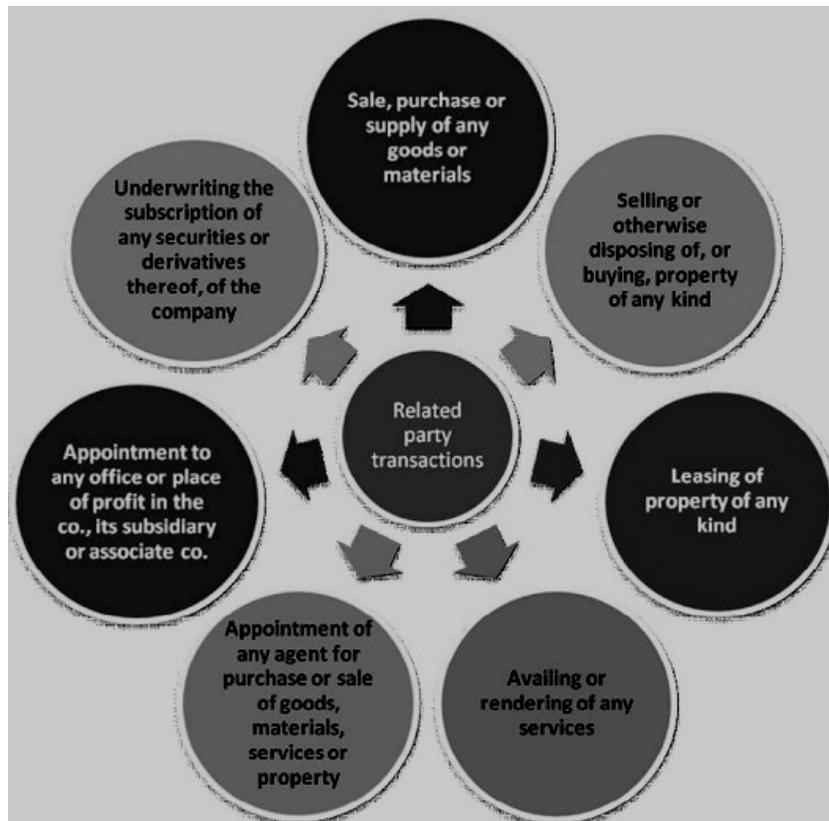
- (1) Father:  
Provided that the term “Father” includes step-father.
- (2) Mother:  
Provided that the term “Mother” includes the step-mother.
- (3) Son:  
Provided that the term “Son” includes the step-son.
- (4) Son’s wife
- (5) Daughter
- (6) Daughter’s husband

- (7) Brother:  
Provided that the term “Brother” includes the step-brother;
- (8) Sister  
Provided that the term “Sister” includes the step-sister.

### Nature of Related Party Transactions

The scope of dealing with Related Party Transactions has been widened in Companies Act, 2013. Section 188 (1) of the Act provides that except with the consent of the Board of Directors given by a resolution at a meeting of the Board and subject to such conditions as prescribed under Rule 15 of the Companies (Meetings of board and its Powers) Rules, 2014, no company shall enter into any contract or arrangement with a related party with respect to—

- (i) sale, purchase or supply of any goods or materials;
- (ii) selling or otherwise disposing of, or buying, property of any kind;
- (iii) leasing of property of any kind;
- (iv) availing or rendering of any services;
- (v) appointment of any agent for purchase or sale of goods, materials, services or property;
- (vi) such related party's appointment to any office or place of profit in the company, its subsidiary company or associate company; and
- (vii) underwriting the subscription of any securities or derivatives thereof, of the company:



### Information to the Board for Related Party Transactions

Rule 15 of the Companies (Meetings of Board and its Powers) Rules, 2014 provides that a company shall enter into any contract or arrangement with a related party subject to the following conditions, namely:-

- (1) The agenda of the Board meeting at which the resolution is proposed to be moved shall disclose-
  - (a) the name of the related party and nature of relationship;
  - (b) the nature, duration of the contract and particulars of the contract or arrangement;
  - (c) the material terms of the contract or arrangement including the value, if any;
  - (d) any advance paid or received for the contract or arrangement, if any;
  - (e) the manner of determining the pricing and other commercial terms, both included as part of contract and not considered as part of the contract;
  - (f) whether all factors relevant to the contract have been considered, if not, the details of factors not considered with the rationale for not considering those factors; and
  - (g) any other information relevant or important for the Board to take a decision on the proposed transaction.
- (2) Where any director is interested in any contract or arrangement with a related party, such director shall not be present at the meeting during discussions on the subject matter of the resolution relating to such contract or arrangement.

### PRIOR APPROVAL OF THE COMPANY BY A RESOLUTION

*First Proviso to the Section 188 (1) of the Act* provides that no contract or arrangement, in the case of a company having a paid-up share capital of not less than such amount, or transactions not exceeding such sums, as prescribed, shall be entered into except with the prior approval of the company by a resolution.

Rule 15 of the Companies (Meetings of board and its Powers) Rules, 2014 provides that except with the prior approval of the company by a resolution, a company shall not enter into a transaction or transactions, where the transaction or transactions to be entered into,-

- (a) as contracts or arrangements with respect to clauses (a) to (e) of sub-section (1) of section 188, with criteria as mentioned below-
  - (i) sale, purchase or supply of any goods or materials, directly or through appointment of agent, amounting to ten percent or more of the turnover of the company or rupees one hundred crore, whichever is lower, as mentioned in clause (a) and clause (e) respectively of sub-section (1) of section 188;
  - (ii) selling or otherwise disposing of or buying property of any kind, directly or through appointment of agent, amounting to ten percent or more of net worth of the company or rupees one hundred crore, whichever is lower, as mentioned in clause (b) and clause (e) respectively of sub-section of section 188;
  - (iii) leasing of property of any kind amounting to ten percent or more of the net worth of the company or ten percent or more of the turnover of the company or rupees one hundred crore, whichever is lower, as mentioned in clause (c) of sub-section (1) of section 188;

- (iv) availing or rendering of any services, directly or through appointment of agent, amounting to ten percent more of the turnover of the company or rupees fifty crore, whichever is lower as mentioned in clause (d) and clause (e) respectively of sub-section (1) of section 188:

The limits specified in sub-clause (i) to (iv) shall apply for transaction or transactions to be entered into either individually or taken together with the previous transactions during a financial year.

- (b) is for appointment to any office or place of profit in the company, its subsidiary company or associate company at a monthly remuneration exceeding two and a half lakh rupees as mentioned in clause (f) of sub-section (1) of section 188.
- (c) is for remuneration for underwriting the subscription of any securities or derivatives thereof, of the company exceeding one percent of the net worth as mentioned in clause (g) of sub-section (1) of section 188.

The turnover or net worth referred in the above sub-rules shall be computed on the basis of the audited financial statements of the preceding financial year.

*Exceptions:* The requirement of passing the resolution under first proviso shall not be applicable for transactions entered into between a holding company and its wholly owned subsidiary whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval.

In case of wholly owned subsidiary, if the resolution is passed by the holding company, it shall be sufficient for the purpose of entering into the transaction between the wholly owned subsidiary and the holding company.

In case of Government companies above mentioned First Proviso to Section 188 (1) of the Act shall not apply to-

- (a) a Government company in respect of contracts or arrangements entered into by it with any other Government company;
- (b) a Government company other than a listed company, in respect of contracts or arrangements other than those referred to in clause (a), in case such company obtains approval of the Ministry or Department of the Central Government which is administratively in charge of the company, or, as the case may be the State Government before entering into such contract or arrangement.  
*[Notification No. GSR 463(E) dated 5-6-2015]*

Information to be provided: The explanatory statement to be annexed to the notice of a general meeting convened pursuant to section 101 shall contain the following particulars, namely:-

- (a) name of the related party;
- (b) name of the director or key managerial personnel who is related, if any;
- (c) nature of relationship;
- (d) nature, material terms, monetary value and particulars of the contract or arrangements;
- (e) any other information relevant or important for the members to take a decision on the proposed resolution.

## RELATED PARTY NOT TO VOTE ON RESOLUTION

Second Proviso to Section 188 (1) of the Act provides that no member of the company shall vote on such resolution, to approve any contract or arrangement which may be entered into by the company, if such member is a related party.

This shall not apply to a company in which ninety per cent. or more members, in number, are relatives of promoters or are related parties.

- Exemption to Private Companies: In case of private companies second proviso shall not apply (Notification No. GSR 464(E) dated 5-6-2015).
- Exemption to Government Companies: In case of Government companies above mentioned *Second* Proviso to the section 188 (1) of the Act shall not apply to -
  - (a) a Government company in respect of contracts or arrangements entered into by it with any other Government company;
  - (b) a Government company other than a listed company, in respect of contracts or arrangements other than those referred to in clause (a), in case such company obtains approval of the Ministry or Department of the Central Government which is administratively in charge of the company, or, as the case may be the State Government before entering into such contract or arrangement. (Notification No. GSR 463(E) dated 5-6-2015).

## Meaning of Ordinary Course of Business

### ***Non Applicability of Section 188(1)***

Section 188(1) shall not apply to any transactions entered into by the company in its ordinary course of business other than transactions which are not on an arm's length basis.

**Meaning of Ordinary Course of business:** The phrase "in the ordinary course of business" has been used in various places under the Act for example under Sections 67, 179, 180, 185, 186, 188 etc. and predominantly, it is used context of related party/ related party transactions. Generally "in the ordinary course of business" understood as the ordinary course of business will cover the usual transactions, customs and practices of a business and of a company.

Whether a particular act is done in the course of business or not is really a question of fact and must be determined according to the evidence led and the circumstances of the case. It must be found as to whether the particular act has any connection with the normal business that the company is carrying on and whether it is so related to the business of the company that it can be considered to be performed in the ordinary course of the business of that company. *Seksaria Biswan Sugar Factory Ltd. v Commissioner of Income-tax*, (Central) Bombay (1950) 18 ITR 139 (Bom): AIR 1950 Bom 200]

In *Unisys Corporation v. Hercules Incorporated et al.*, 24 A.D.2d 365 (1996) : 638 N.Y.S 2d 461, the Appellate Division of the Supreme Court of the State of New York has held the meaning of the phrase, "in the ordinary course of business", as follows:

"Something which is done as a matter of corporate historical practice is, as a matter of law, done "in the ordinary course of business".

### **Meaning of arm's length transaction**

As per the explanation (2) to Section 188(1) of the Act, the expression "arm's length transaction" means a transaction between two related parties that is conducted as if they were unrelated, so that there is no conflict of interest.

The phrase 'on an arm's length basis' is in fact 'at arm's length' or 'an arm's length relationship' which means avoiding intimacy or close contact. The phrase 'at arm's length' in relation to dealings between two parties is used to refer to dealings when neither party is controlled by the other.

Arm's length is the condition or fact that the parties to a transaction are independent and on an equal footing. Arm's length transaction is a transaction between unrelated persons or organizations, in which there is no improper influence exercisable by one party over another, and no conflict of interests of or relating to dealings between two parties who are not related or not on close terms and who are presumed to have roughly equal bargaining power; not involving a confidential relationship. Parties are said to deal at "arm's length" when they conduct the business without being subject to the other's control or overmastering influence.

An arm's length transaction is a transaction between companies or people that do not have close contact or any financial connections and be or deal at arm's length means without a close relationship with a person or a company. The burden to establish that a transaction was at arm's length would be on the company and there must be sufficient and pertinent material to prove that the terms of the transaction with a related party were purely commercial and the same as in the case of a transaction between the company and a non-related party and there were no extra-commercial considerations. The company should create and preserve appropriate and adequate documentation indicating that the transaction is an arm's length one, particularly with regard to price and terms of supply (such as credit, discount, etc). In my opinion, comparable prices of the competitor's goods is not necessary to be ascertained but what is necessary is prices charged to other customers (if there is any).

The requirement of passing the resolution under first proviso shall not be applicable for transactions entered into between a holding company and its wholly owned subsidiary whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval.

### **DISCLOSURE IN BOARD'S REPORT**

Section 188(2) provides that every related party contracts or arrangements shall have to be disclosed in the Board's report and referred to shareholders along with the justification for entering into such type of transactions in the prescribed form i.e., Form no. AOC-2 (pursuant to Section 134(3)(h) and Section 188(2)).

### **CONSEQUENCES OF ENTERING RELATED PARTY CONTRACTS OR ARRANGEMENTS BY THE DIRECTOR OR THE EMPLOYEE WITHOUT THE CONSENT OF THE BOARD OR APPROVAL BY RESOLUTION**

- Section 188(3) provides that where any contract or arrangement is entered into by a director or any other employee, without obtaining the consent of the Board or approval by a resolution in the general meeting under sub-section (1) and if it is not ratified by the Board or, as the case may be, by the shareholders at a meeting within three months from the date on which such contract or arrangement was entered into, such contract or arrangement shall be voidable at the option of the Board or, as the case may be, of the shareholders and if the contract or arrangement is with a related party to any director, or is authorised by any other director, the directors concerned shall indemnify the company against any loss incurred by it.

- Section 188(4) states that it shall be open to the company to proceed against a director or any other employee who had entered into such contract or arrangement in contravention of the provisions of this section for recovery of any loss sustained by it as a result of such contract or arrangement.

### **PENALTIES FOR NON COMPLIANCE**

Section 188(5) provides that any director or any other employee of a company, who had entered into or authorised the contract or arrangement in violation of the provisions of this section shall,—

- (i) in case of listed company, be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both;and
- (ii) In case of any other company, be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees.

### **ROLE OF AUDIT COMMITTEE IN RELATED PARTY TRANSACTIONS**

Section 177(4)(iv) of the Companies Act, 2013 provides that the terms of reference of Audit Committee shall include approval or any subsequent modification of transactions of the company with related parties;

Provided that the Audit Committee may make omnibus approval for related party transactions proposed to be entered into by the company subject to such conditions as may be prescribed;

Thus, it is the responsibility of audit committee to approve the transactions of the company with related parties.

As per Rule 6A of Companies (Meeting of Board and its Powers) Second Amendment Rules, 2015, the audit committee may make omnibus approval for all related party transactions proposed to be entered into by the company subject to the following conditions, namely -

(1) The Audit Committee shall, after obtaining approval of the Board of Directors, specify the criteria for making the omnibus approval which shall include the following, namely:-

- (a) maximum value of the transactions, in aggregate, which can be allowed under the omnibus route in a year;
- (b) the maximum value per transaction which can be allowed;
- (c) extent and manner of disclosures to be made to the Audit Committee at the time of seeking omnibus approval;
- (d) review, at such intervals as the Audit Committee may deem fit, related party transaction entered into by the company pursuant to each of the omnibus approval made;
- (e) transactions which cannot be subject to the omnibus approval by the Audit Committee.

(2) The Audit Committee shall consider the following factors while specifying the criteria for making omnibus approval, namely:-

- (a) repetitiveness of the transactions (in past or in future);
- (b) justification for the need of omnibus approval.

(3) The Audit Committee shall satisfy itself on the need for omnibus approval for transactions of repetitive nature and that such approval is in the interest of the company.

(4) The omnibus approval shall contain or indicate the following:-

- (a) name of the related parties;
- (b) nature and duration of the transaction;
- (c) maximum amount of transaction that can be entered into;
- (d) the indicative base price or current contracted price and the formula for variation in the price, if any; and
- (e) any other information relevant or important for the Audit Committee to take a decision on the proposed transaction:

Provided that where the need for related party transaction cannot be foreseen and aforesaid details are not available, audit committee may make omnibus approval for such transactions subject to their value not exceeding rupees one crore per transaction.

(5) Omnibus approval shall be valid for a period not exceeding one financial year and shall require fresh approval after the expiry of such financial year.

(6) Omnibus approval shall not be made for transactions in respect of selling or disposing of the undertaking of the company.

Any other conditions as the Audit Committee may deem fit.

### **Provisions under SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015**

Meaning of related party transaction: According to SEBI (Listing Obligations And Disclosure Requirements) Regulations, 2015 Regulation 2(1) (zc) defines that "related party transaction" means a transfer of resources, services or obligations between a listed entity and a related party, regardless of whether a price is charged and a "transaction" with a related party shall be construed to include a single transaction or a group of transactions in a contract.

Provided that this definition shall not be applicable for the units issued by mutual funds which are listed on a recognised stock exchange(s).

Meaning of related party: Regulation 2(1)(zb) of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 defines that "related party" means a related party as defined under sub-section (76) of section 2 of the Companies Act, 2013 or under the applicable accounting standards<sup>1</sup>.

Provided this definition shall not be applicable for the units issued by mutual fund which are listed on recognised stock exchange(s).

Provided that any person or entity belonging to the promoter or promoter group of the listed entity and holding 20% or more of shareholding in the listed entity shall be deemed to be a related party. (Notified on 9<sup>th</sup> May, 2018 effective from April 1, 2019)

According to Regulation 2(1) (zd) of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 "relative" means relative as defined under Section 2(77) of the Companies Act, 2013 and rules

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<sup>1</sup> Applicable accounting standards would be Ind AS-24 or AS-18, as the case may be.

prescribed there under.

Provided this definition shall not be applicable for the units issued by mutual fund which are listed on recognised stock exchange(s).

**Provisions to be complied with in case of related party transaction:** Regulation 23 of the SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 provides that:

- (1) The listed entity shall formulate a policy on materiality of related party transactions and on dealing with related party transactions which shall also be placed on the website of the company. A transaction with a related party shall be considered material if the transaction(s) to be entered into individually or taken together with previous transactions during a financial year, exceeds ten percent of the annual consolidated turnover of the listed entity as per the last audited financial statements of the listed entity.

*A transaction involving payments made to a related party with respect to brand usage or royalty shall be considered material if the transaction(s) to be entered into individually or taken together with previous transactions during a financial year, exceed two percent of the annual consolidated turnover of the listed entity as per the last audited financial statements of the listed entity. (The amendment shall come into force w.e.f. the half year ending March 2019)*

- (2) All related party transactions shall require prior approval of the audit committee.
- (3) Audit committee may grant omnibus approval for related party transactions proposed to be entered into by the listed entity subject to the following conditions, namely-
  - (a) the audit committee shall lay down the criteria for granting the omnibus approval in line with the policy on related party transactions of the listed entity and such approval shall be applicable in respect of transactions which are repetitive in nature;
  - (b) the audit committee shall satisfy itself regarding the need for such omnibus approval and that such approval is in the interest of the listed entity;
  - (c) the omnibus approval shall specify:
    - (i) the name(s) of the related party, nature of transaction, period of transaction, maximum amount of transactions that shall be entered into,
    - (ii) the indicative base price / current contracted price and the formula for variation in the price if any; and
    - (iii) such other conditions as the audit committee may deem fit:

Provided that where the need for related party transaction cannot be foreseen and aforesaid details are not available, audit committee may grant omnibus approval for such transactions subject to their value not exceeding rupees one crore per transaction.

- (d) the audit committee shall review, at least on a quarterly basis, the details of related party transactions entered into by the listed entity pursuant to each of the omnibus approvals given.
  - (e) Such omnibus approvals shall be valid for a period not exceeding one year and shall require fresh approvals after the expiry of one year:
- (4) All material related party transactions shall require approval of the shareholders through resolution and *the related parties shall abstain from voting [this shall be replaced by “no related party shall vote to approve” (the amendment shall come into force w.e.f. the half year ending March 2019)]* on

such resolutions whether the entity is a related party to the particular transaction or not.

- (5) The provisions of sub-regulations (2), (3) and (4) shall not be applicable in the following cases:
  - (a) transactions entered into between two government companies;
  - (b) transactions entered into between a holding company and its wholly owned subsidiary whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval.
- (6) The provisions of this regulation shall be applicable to all prospective transactions.
- (7) For the purpose of this regulation, all entities falling under the definition of related parties shall *abstain from voting* [*this shall be replaced by "not vote to approve the relevant transaction" (the amendment shall come into force w.e.f. the half year ending March 2019)*] irrespective of whether the entity is a party to the particular transaction or not.
- (8) *The listed entity shall submit within 30 days from the date of publication of its standalone and consolidated financial results for the half year, disclosures of related party transactions on a consolidated basis, in the format specified in the relevant accounting standards for annual results to the stock exchanges and publish the same on its website.(the amendment shall come into force w.e.f. the half year ending March 2019)*

## Conclusion

The related party transaction can be categorized into two categories on the basis of the status of the Company i.e. for listed Company and for unlisted Company.

In case of an unlisted Company, the transaction shall be treated as related party transaction if:-

- the company must be one party and the other party to the contract or arrangement is a related party as defined in section 2(76) of the Act in relation to the company; and
- there must be a contract or arrangement of any one or more of the kinds specified in section 188(1) of the Act; and
- the transaction entered into with the related party is not in the ordinary course of business or such transaction is not on an arm's length.

In case of a listed Company, the transaction shall be treated as related party transaction if:-

- the entity falling in any of the categories of related party as provided in section 2(76) of the Act: or
- An entity, even if such entity is not falling within the ambit of section 2(76) of the Act, but has been defined as "related party" under the applicable accounting standards; and
- Such contract or arrangement falls under any one or more of the categories as specified in section 188(1) of the Act; or
- Even if such transaction is not one or more of the categories as specified in section 188(1) of the Act, but such transaction involves transfer of resources, services or obligations between a listed company and a related party, regardless of whether a price is charged.

### LESSON ROUND-UP

- 'Investments' has been used in a limited sense in the lesson to mean the investing of money in shares, stock, debentures or other securities.
- The power to invest the funds of the company is the prerogative of the Board of Directors. However, the Board must not misuse its powers. The Companies Act, 2013 contains provisions for restrictions on investments that a company can make and loans it can provide. Restrictions are also placed on the guarantees which the company can give or security it can provide for a loan.
- The provisions for restrictions on investments and loans by companies would also apply to Section 8 companies and guarantee companies not having a share capital.
- Approvals for making investments and loans would have to be taken in accordance with the specific provisions of the Companies Act. A blanket approval of the shareholders for the purpose would not suffice.
- The Companies Act provides for the particulars to be provided in the register of loans made, guarantees given, securities provided and investments made and the manner in which it is to be kept.
- Provisions have also been given in relation to inspection of such register and penalties imposable in case of defaults in maintaining the required registers.
- No member of the company shall vote on such resolution, to approve any contract or arrangement which may be entered into by the company, if such member is a related party. This shall not apply to a company in which ninety per cent. or more members, in number, are relatives of promoters or are related parties.
- The Audit Committee may make omnibus approval for related party transactions proposed to be entered into by the company subject to such conditions as may be prescribed.
- As per the Act, 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. This requirement is confined to only those investments which are made by it on its own behalf and not on behalf of someone else. However, in certain circumstances, the Act exempts the companies from complying with the above provisions.
- When any shares or securities in which investments have been made by a company are not held by it in its own name as a beneficial owner when such investments are held in the name of a depository pursuant to permissible conditions given in the Act, the company shall forthwith enter in a register maintained by it for the purpose, particulars as specified in the Act.
- In case of default, the company is punishable with fine and every officer of the company who is in default shall be punishable with imprisonment or with fine or with both.

### GLOSSARY

Derivatives	A derivative is a contract between two parties which derives its value/price from an underlying asset. The most common types of derivatives are futures, options, forwards and swaps.
Public Financial Institution	Public financial institution means— (i) the Life Insurance Corporation of India, established under section 3 of the Life Insurance Corporation Act, 1956 (31 of 1956); (ii) the Infrastructure Development Finance Company Limited; (iii) specified company referred to in the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002; (iv) institutions notified by the Central Government

(v) such other institution as may be notified by the Central Government in consultation with the Reserve Bank of India:

Provided that no institution shall be so notified unless—

(A) it has been established or constituted by or under any Central or State Act other than this Act or the previous company law; or

(B) not less than fifty-one per cent of the paid-up share capital is held or controlled 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;

[Sec 2(72) of Companies Act, 2013]

Office or place of Profit

i. where such office or place is held by a director, if the director holding it receives from the company anything by way of remuneration over and above the remuneration to which he is entitled as director, by way of salary, fee, commission, perquisites, any rent-free accommodation, or otherwise;

ii. where such office or place is held by an individual other than a director or by any firm, private company or other body corporate, if the individual, firm, private company or body corporate holding it receives from the company anything by way of remuneration, salary, fee, commission, perquisites, any rent-free accommodation, or otherwise;

(Explanation to section 188(1) of Companies Act, 2013)

**SELF-TEST QUESTIONS**

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)*

1. Discuss the law relating to loans and investments by companies.
2. Which companies are exempt from the provisions with regard to loans and investments by companies?
3. What particulars are required to be entered in the Register of Loans and Investments?
4. Your company, is a public limited company which wishes to make investments in the shares of another company. The total investment exceeds the statutory limit stipulated by the Act. What are the formalities to be complied with in this regard?

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# Lesson 11

## Registers and Records

### LESSON OUTLINE

- Register to be maintained under Companies Act, 2013
- Returns
- Preservations of Records
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

Every company has to maintain certain registers and records for statutory, statistical, disclosure, and information management/MIS purposes. They also have to file returns with the regulatory authorities to intimate them as to material changes in the working of the company. The objective behind keeping such registers and records is not only a statutory requirement, but these are also helpful for the smooth functioning of the company. These records make the company's working more systematic. The company is required to keep these records within the vicinity of the place prescribed for it by the laws.

Maintenance, Authentication, Preservation of records and returns, forms an important part of secretarial practice of Company Secretary.

After reading this lesson, prospective Company Secretaries will be able to understand the legal and secretarial aspect of maintenance, authentication, preservation and inspection of statutory book/registers prescribed under various provisions of the Company Law, along with other non-statutory books.

### Introduction- Register to be Maintained under Companies Act, 2013

The Companies Act 2013, lays down that every company must maintain and keep books, registers and copies of returns, documents etc. at its registered office. 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 –

- Register of sweat equity shares. [Section 54 and Rule 8(14) of Companies (Share Capital and Debentures) Rules, 2014]
- Register of Employee Stock Options. [Section 62(1)(b) Rule 12 of Companies (Share Capital and Debentures) Rules, 2014]
- Register of securities bought back. [Section 68(9) and Rule 17(12) of companies (Share Capital and Debenture) Rules, 2014]
- Register of deposits. [Section 73 and Rule 14 Companies (Acceptance of Deposits) Rules, 2014]
- Register of charges. [Section 85 and Rule 7 of Companies (Registration of Charges) Rules 2014]
- Register of members. [Section 88(1)(a) and Rule 3 of Companies (Management and Administration) Rules, 2014]
- Register of debenture holders. [Section 88(1)(b) & (c) and Rule 4 of Companies (Management and Administration) Rules, 2014]
- Foreign register. [Section 88 (4) and Rule 7 of Companies (Management and Administration) Rules, 2014].
- Register of Renewed and Duplicate Share Certificates. [Rule 6 of the Companies (Share Capital and Debentures) Rules, 2014]
- Register of Significant beneficial owners in a company. (Section 90 of Companies Act).
- Register of Postal Ballot. [Section 110 and Rule 22 of the Companies (Management and Administration) Rules, 2014]
- Books containing minutes of General Meeting and of Board and of Committees of Directors. [Section 118]
- Books of account. [Section 128]
- Register of Directors/ Key Managerial Personnel. [Section 170(1)]
- Register of investments in securities not held in company's name. [Section 18 and Rule 14 of Companies (Meetings of Board and its Powers) Rules, 2014]
- Register of loans, guarantees given and security provided or making acquisition of securities (Section 186(9) and Rule 12 Companies (Meetings of Boards and its Powers) Rules 2014]

- Register of contracts with companies/firms in which directors are interested. [Section 189(5) and Rule 16 of Companies (Meetings of Boards and its Powers) Rules, 2014]

### **Register of Sweat Equity Shares [Section 54 and Rule 8(14) of Companies (Share Capital and Debentures) Rules, 2014]**

Every company which issues sweat equity shares should maintain a register of sweat equity shares and enter therein particulars of sweat equity shares issued. A Register of Sweat Equity Shares shall be maintained by the company in **Form No. SH-3** and shall forthwith enter therein the particulars of Sweat Equity Shares issued under section 54. The register should contain the particulars of date of the special resolution authorizing the issue of sweat equity shares; date of Board resolution for allotment; name of the allottee; status of the allottee, i.e. whether director or employee; folio number/certificate number; reference to entry in register of members; date of issue of such shares, number of shares issued, face value of the share, price at which the shares are issued, consideration paid, if any, by the employee/director, particulars of consideration other than cash, the lock-in period of these shares and the date of expiry thereof. The Register of Sweat Equity Shares shall be maintained at the registered office of the company or such other place as the Board may decide. Entries in the register shall be authenticated by the Company Secretary of the company or by any other person authorized by the Board for the purpose.

The register should be open for inspection during the business hours of the company, subject to such reasonable restrictions as the company may impose by its articles or in general meetings so that not less than 2 hours in each working day of the company are allowed for inspection. Members can inspect the register without payment of any fee. Copies of the register can be demanded by any person who inspects the register.

### **Register of Employee Stock Options [Section 62(1)(b) Rule 12 of Companies(Share Capital and Debentures) Rules, 2014]**

The company which has issued Employee stock options shall maintain a Register of Employee Stock Options in Form No. SH.6 and shall forthwith enter therein the particulars of option granted under clause (b) of sub-section (1) of section 62.

The Register of Employee Stock Options shall be maintained at the registered office of the company or such other place as the Board may decide.

The entries in the register shall be authenticated by the company secretary of the company or by any other person authorized by the Board for the purpose.

### **Register of Securities bought back**

[Section 68 (9) and Rule 17 (12) of Companies (Share Capital and Debentures) Rules, 2014]

Where a company buys back its shares or other specified securities under Section 68, it shall maintain a register of the shares or securities so bought, the consideration paid for the shares or securities bought back, the date of cancellation of shares or securities, the date of extinguishing and physically destroying the shares or securities.

The company shall maintain a register of shares or other securities which have been bought-back in Form No. SH-10.

The register of shares or securities bought-back shall be maintained at the registered office of the company and shall be kept in the custody of the secretary of the company or any other person authorized by the board

in this behalf.

The entries in the register shall be authenticated by the secretary of the company or by any other person authorized by the Board for the purpose

**Register of Deposits Rule [Section 73 and Rule 14 of Companies (Acceptance of Deposits) Rules, 2014]**

Every company other than a banking company which accepts any deposits should, from the date of such acceptance, maintain year-wise one or more separate registers for deposits accepted/renewed, in which there shall be entered separately in the case of each depositor the following particulars, namely:

- (a) Name, address and PAN of the depositor/s;
- (b) Particulars of guardian, in case of a minor;
- (c) Particulars of the nominee;
- (d) Deposit receipt number;
- (e) Date and amount of each deposit;
- (f) Duration of the deposit and the date on which each deposit is repayable;
- (g) Rate of interest or such deposits to be payable to the depositor;
- (h) Due date(s) for payment of interest;
- (i) Mandate and instructions for payment of interest and for non-deduction of tax at source, if any;
- (j) Date or dates on which payment of interest will be made;
- (k) Details of deposit insurance including extent of deposit insurance;
- (l) Particulars of security or charge created for repayment of deposits;
- (m) Any other relevant particulars;

The register should be maintained deposit receipt number-wise. Entries in the register should be made forthwith from the date of issuance of the deposit receipt.

Entries in the register shall be made within seven days from the date of issuance of the deposit receipt and such entries shall be authenticated by a director or secretary of the company or by any other officer authorized by the Board for this purpose.

The register or registers referred to in sub-rule (1) shall be preserved in good order for a period of not less than eight years from the financial year in which the latest entry is made in the register.

The register is not open for inspection.

**Register of Charges [Section 85; Rule 10 of Companies (Registration of Charges) Rules, 2014]**

Section 85(1) read with Rule 10 of Companies (Registration of Charges) Rules, 2014 provides that every company shall keep at its registered office a register of charges in **Form No. CHG-7** and enter therein particulars of all the charges registered with the Registrar on any of the property, assets or undertaking of the company and the particulars of any property acquired subject to a charge as well as particulars of any modification of a charge and satisfaction of charge.

- The entries in the register of charges maintained by the company shall be made forthwith after the

creation, modification or satisfaction of charge, as the case maybe.

- Entries in the register shall be authenticated by a director or the secretary of the company or any other person authorised by the Board for the purpose.
- The register of charges shall be preserved permanently and the instrument creating a charge or modification thereon shall be preserved for a period of eight years from the date of satisfaction of charge by the company. Provided that a copy of the instrument creating the charge shall also be kept at the registered office of the company along with the register of charges.
- The register of charges and instrument of charges, shall be open for inspection during business hours—
  - (a) by any member or creditor without any payment of fees; or
  - (b) by any other person on payment of prescribed fees, subject to such reasonable restrictions as the company may, by its articles, impose.

### **Register of Members [Section 88(1)(a) and Rule 3 of Companies (Management and Administration)] Rules, 2014**

1. Every company limited by shares shall, from the date of its registration, maintain a register of its members indicating separately for each class of equity and preference shares held by each member residing in or outside India in Form No.MGT-1.
2. In the case of a company not having share capital, the register of members shall contain the following particulars, in respect of each member, namely:-
  - (a) name of the member; address (registered office address in case the member is a body corporate); e-mail address; Permanent Account Number or CIN; Unique Identification Number, if any; Father's/Mother's/Spouse's name; Occupation; Status; Nationality; in case member is a minor, name of the guardian and the date of birth of the member; name and address of nominee;
  - (b) date of becoming member;
  - (c) date of cessation;
  - (d) amount of guarantee, if any;
  - (e) any other interest, if any; and
  - (f) instructions, if any, given by the member with regard to sending of notices, etc:

The register of members along with the index shall be preserved permanently and shall be kept in the custody of the company secretary of the company or any other person authorized by the Board for such purpose.

For details please read the lesson 3, i.e., Members and Shareholders.

### **Register of Debenture Holders and any other Security Holders**

[Section 88(1)(b)&(c) and Rule 4 of Companies (Management and Administration) Rules, 2014]

Every company which issues or allots debentures or any other security shall maintain a separate register of debenture holders or security holders, as the case may be, for each type of debentures or other securities in Form No.MGT-2.

The register should contain information relating to name, father's /husband's name; address and occupation, if any, of each debenture holder; date of allotment; date of registration with the Registrar of Companies; the debentures held by each holder distinguishing each debenture by its number except where such debentures are held with a depository; distinctive number and certificate number of debentures; the amount paid or agreed to be considered as paid on those debentures; date of payment; date on which the name of each person was entered in the register as a debenture holder; date on which any person ceased to be a debenture holder; date of transfer of debentures; serial number of instrument of transfer; transferor's name and folio number; transferee's name and folio number, transfer number, number of debentures transferred and their distinctive numbers; date of transfer; and instructions, if any, for payment of interest.

In the case of debentures held in dematerialised mode, the name and particulars of the depository should be entered in the register as registered owner. The names of beneficial owners on whose behalf such debentures are held in dematerialized form should not be entered.

Entries in the register should be made simultaneously with the allotment or transfer of debentures and entries in the index should be made forthwith.

The register and index should be maintained at the registered office of the company unless in a general meeting a special resolution is passed authorizing the keeping of the register at any other place within the same city, town or village in which the registered office is situated and an advance copy of the proposed special resolution is given to the Registrar of Companies.

The register of debenture holders or any other security holders along with the index shall be preserved for a period of eight years from the date of redemption of debentures or securities, as the case may be, and shall be kept in the custody of the company secretary of the company or any other person authorized by the Board for such purpose.

**Foreign Register [Section 88(4) and Rule 7 of Companies (Management and Administration) Rules, 2014]**

In terms of sub-section (4) of Section 88, a company, if authorized by its Articles of Association, can also keep any part of the Register in any other country. Hence, in all such countries, where the Company has large number of shareholders, a Register of Members containing information about the members from that particular country may be kept. To be called "foreign register", this Register should contain the names and particulars of the members, debenture holders, other security holders or beneficial owners residing in that country.

The Rules provides as under with regard to the foreign register, the company shall, within thirty days from the date of the opening of any foreign register, file with the Registrar notice of the situation of the office in Form No.MGT-3 along with the fee where such register is kept; and in the event of any change in the situation of such office or of its discontinuance, shall, within thirty days from the date of such change or discontinuance, as the case may be, file notice in Form No.MGT-3 with the Registrar of such change or discontinuance. [Rule 7(2)]

A foreign register shall be deemed to be part of the company's register of members or of debenture holders or of any other security holders or beneficial owners, as the case may be. The foreign register shall be maintained in the same format as the Principal Register. [Rule 7(3) and 7(4)]

A foreign register shall be open to inspection and may be closed, and extracts may be taken there from and copies thereof may be required, in the same manner, mutatis mutandis, as is applicable to the principal register. [Rule 7 (5)]

Entries in the foreign register maintained under sub-section (4) of section 88 shall be made simultaneously after the Board of Directors or its duly constituted committee approves the allotment or transfer of shares, debentures or any other securities, as the case may be. [Rule7(7)]

The company shall—

- (a) transmit to its registered office in India a copy of every entry in any foreign register within fifteen days after the entry is made; and
- (b) keep at such office a duplicate register of every foreign register duly entered up from time to time. [Rule7 (8)]

If a foreign register is maintained, a duplicate thereof should be maintained at the registered office of the company or at such other place where the register of members or debenture holders is kept. Every such duplicate register is deemed to be part of the principal register. The office where the foreign register is maintained should forthwith from the date of making any entry, transmit to the registered office of the company in India a copy of every entry made in any foreign register.

- If a foreign register is kept by a company in any country outside India, the decision of the Tribunal in regard to the rectification of the register shall be binding. [Rule7(6)]
- The company may discontinue the keeping of any foreign register; and thereupon all entries in that register shall be transferred to some other foreign register kept by the company in the same part of the world or to the principal register. [Rule 7(11)]

The foreign register shall be kept in the custody of the company secretary or person authorised by the Board.

The foreign register of members shall be preserved permanently, unless it is discontinued and all the entries are transferred to any other foreign register or to the principal register. Foreign register of debenture holders or any other security holders shall be preserved for a period of eight years from the date of redemption of such debentures or securities.

### **Register of Renewed and Duplicate Share Certificates [Rule 6(3) of the Companies (Share Capital and Debentures) Rules, 2014]**

Every company with a share capital should, from the date of its registration, maintain a register of renewed and duplicate certificates.

The word 'renewed' includes consolidation and sub-division of shares and issue of certificate in lieu thereof.

Particulars of every share certificate issued shall be recorded in a Register of Renewed and Duplicate Share Certificates. Such register shall be maintained in **Form No. SH-2** indicating against the name(s) of the person(s) to whom the certificate is issued, the number and date of issue of the share certificate in lieu of which the new certificate is issued, and the necessary changes indicated in the Register of Members by suitable cross-references in the "Remarks" column. Such register shall be kept at the registered office of the company or at such other place where the Register of Members is kept. The register shall be preserved permanently and shall be kept in the custody of the Company Secretary of the company or any other person authorized by the Board for the purpose. All entries made in the Register of Renewed and Duplicate Share Certificates shall be authenticated by the company secretary or such other person as may be authorized by the Board for purposes of sealing and signing the share certificate. The register is not open for inspection.

### **Register of Significant beneficial owners in a company (Section 90)**

Every individual, who acting alone or together, or through one or more persons or trust, including a trust and

persons resident outside India, holds beneficial interests, of not less than twenty-five per cent. or such other percentage as may be prescribed, in shares of a company or the right to exercise, or the actual exercising of significant influence or control as defined in clause (27) of section 2, over the company, shall make a declaration to the company, specifying the nature of his interest and other particulars, in such manner and within such period of acquisition of the beneficial interest or rights and any change thereof, as may be prescribed:

The Central Government may prescribe a class or classes of persons who shall not be required to make declaration.

Every company shall maintain a register of the interest declared by individuals, as above, and changes therein which shall include the name of individual, his date of birth, address, details of ownership in the company and such other details as may be prescribed. Such register maintained shall be open to inspection by any member of the company on payment of such fees as may be prescribed.

**Register of Postal Ballot [Section 110 and Rule 22(10) of the Companies (Management and Administration) Rules, 2014]**

Every company which is required to or which proposes to get any resolution passed through postal ballot should maintain a separate register for each postal ballot to record the assent or dissent received through postal ballot.

The scrutinizer shall maintain a register either manually or electronically to record their assent or dissent received, mentioning the particulars of name, address, folio number or client ID of the shareholder, number of shares held by them, nominal value of such shares, whether the shares have differential voting rights, if any, details of postal ballots which are received in defaced or mutilated form and postal ballot forms which are invalid.

Entries in the register should be made immediately after the opening of postal ballots. Separate folios should be maintained for each resolution passed through postal ballot. The register should be kept at the registered office of the company after the Scrutinizer has submitted his report.

The register, postal ballot forms and all other related records are not available for inspection.

All postal ballot forms should be authenticated by the Scrutinizer. Entries in the register should be authenticated by the Scrutinizer.

The register, postal ballot forms and all other related records should be kept in the safe custody of the Scrutinizer till the Chairman signs the Minutes Book in which the result of the voting by postal ballot is recorded.

The secretary of the company, managing director or whole-time director or the director so authorised and the Scrutinizer should make adequate arrangements for safe custody of the register and proof of dispatch of Notices and all envelopes received by post or by hand, until the Scrutinizer submits his report to the Chairman.

The Scrutinizer should return the postal ballot forms and any related documents or records to the designated person of the company for safekeeping until the resolution has been implemented.

The Scrutinizer's report and office copies of the notices should be preserved in good order until the resolution has been implemented or for a period of 10 years, whichever is later.

**Books containing Minutes of proceedings of General Meeting, meeting of Board of Directors and other meeting and resolution passed by postal ballot [Section 118]**

Section 118 provides that every company shall prepare, sign and keep minutes of proceedings of every general meeting, including the meeting called by the requisitionists and all proceedings of meeting of any class of share holders or creditors or Board of Directors or committee of the Board and also resolution passed by postal ballot within thirty days of the conclusion of every such meeting concerned.

In case of meeting of Board of Directors or of a committee of Board, the minutes shall contain name of the directors present and also name of dissenting director or a director who has not concurred the resolution. The Chairman shall exercise his absolute discretion in respect of inclusion or non-inclusion of the matters which is regarded as defamatory of any person, irrelevant or detrimental to company's interest in the minutes. Minutes kept shall be evidence of the proceedings recorded in a meeting.

*As per 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. Accordingly SS-1 & SS-2 needs to be adhered to.*

Rule 25 contains provisions with regards to minutes of meetings. A distinct minute book shall be maintained for each type of meeting namely:

- (i) general meetings of the members;
- (ii) meetings of the creditors;
- (iii) meetings of the Board; and
- (iv) meetings of the committees of the Board.

It may be noted that resolutions passed by postal ballot shall be recorded in the minute book of general meetings as if it has been deemed to be passed in the general meeting. In no case the minutes of proceedings of a meeting or a resolution passed by postal ballot shall be pasted to any such book.

In case of every resolution passed by postal ballot, a brief report on the postal ballot conducted including the resolution proposed, the result of the voting thereon and the summary of the scrutinizer's report shall be entered in the minutes book of general meetings along with the date of such entry within thirty days from the date of passing of resolution. Minutes of proceedings of each meeting shall be entered in the books maintained for that purpose along with the date of such entry within thirty days of the conclusion of the meeting. Each page of every such book shall be initialled or signed and the last page of the record of proceedings of each meeting or each report in such books shall be dated and signed by:

- in the case of minutes of proceedings of a meeting of the Board or of a committee thereof, by the chairman of the said meeting or the Chairman of the next succeeding meeting;
- in the case of minutes of proceedings of a general meeting, by the Chairman of the same meeting within the aforesaid period of thirty days or in the event of the death or inability of that Chairman within that period, by a director duly authorized by the Board for the purpose;
- in case of every resolution passed by postal ballot, by the Chairman of the Board within the aforesaid period of thirty days or in the event of there being no chairman of the Board or the death or inability of that chairman within that period, by a director duly authorized by the Board for the purpose.

Minute books of general meetings shall be kept at the registered office of the company. Minutes of the Board and committee meetings shall be kept at the registered Office or at such other place as may be approved by the Board.

Minutes books shall be preserved permanently and kept in the custody of the company secretary of the company or any director duly authorized by the Board for the purpose and shall be kept in the registered office or such place as the members may decide by passing special resolution pursuant to requirement of section 88 read with section 94 of the Act. This section shall not apply to Section 8 company as a whole except that minutes may be recorded within 30 days of the conclusion of every meeting in case of companies where the articles of association provide for confirmation of minutes by circulation.

### **Provisions under Secretarial Standards**

The Secretarial Standards also provide following guidelines for Preservation of Minutes and other Records [see para 8 of SS-1 and para 18 of SS-2]:-

- (a) Minutes of all Meetings shall be preserved permanently in physical or in electronic form with Timestamp.
- (b) Where, under a scheme of arrangement, a company has been merged or amalgamated with another company, Minutes of all Meetings of the transferor company, as handed over to the transferee company, shall be preserved permanently by the transferee company, notwithstanding that the transferor company might have been dissolved.
- (c) Office copies of Notices, Agenda, Notes on Agenda and other related papers shall be preserved in good order in physical or in electronic form for as long as they remain current or for eight financial years, whichever is later and may be destroyed thereafter with the approval of the Board.
- (d) Office copies of Notices, Agenda, Notes on Agenda and other related papers of the transferor company, as handed over to the transferee company, shall be preserved in good order in physical or electronic form for as long as they remain current or for eight financial years, whichever is later and may be destroyed thereafter with the approval of the Board and permission of the Central Government, where applicable.

### **Books of Account [Section128]**

#### **Requirement of keeping Books of Account (Section128)**

- Maintenance of books of account would mean records maintained by the company to record the specified financial transaction. It has been specifically provided that every company shall keep proper books of account. This section specifies the main features of proper books of account as under –
- The company must keep the books of account with respect to items specified in clauses (i) to (iv) of Section 2(13) of the Companies Act, 2013, which defines “books of account”.
- The books of account must show all money received and expended, sales and purchases of goods and the assets and liabilities of the company.
- The books of account must be kept on accrual basis and according to the double entry system of accounting.
- The books of account must give a true and fair view of the state of the affairs of the company or its branches.

- “Books of account” as defined in Section 2(13) includes records maintained in respect of—
  - (i) all sums of money received and expended by a company and matters in relation to which the receipts and expenditure take place;
  - (ii) all sales and purchases of goods and services by the company;
  - (iii) the assets and liabilities of the company; and
  - (iv) the items of cost as may be prescribed under section 148 in the case of a company which belongs to any class of companies specified under that section.

All or any of the books of account may be kept at such other place in India as the Board of directors may decide. When the Board so decides to keep books and other papers at any other place in India, a notice to this effect shall be given to the Registrar in Form AOC-5 giving full address of that other place within seven days of Board’s decision.

The maintenance of books of account and other books and papers in electronic mode is permitted and is optional. Such books of accounts or other relevant books or papers maintained in electronic mode shall remain accessible in India so as to be usable for subsequent use. Details are provided under Rule 3 of the Companies (Accounts) Rules, 2014.

The books of account, together with vouchers relevant to any entry in such books, are required to be preserved in good order by the company for a period of not less than eight years immediately preceding the relevant financial year. In case of a company incorporated less than eight years before the financial year, the books of account for the entire period preceding the financial year together with the vouchers shall be so preserved. The provisions of Income-tax Act shall also be complied with in this regard. As per proviso to sub-section 5, where an investigation has been ordered in respect of a company under Chapter XIV of the Act related to inspection, inquiry or investigation, the Central Government may direct that the books of account may be kept for such period longer than 8 years, as it may deem fit and give directions to that effect.

The person responsible to take all reasonable steps to secure compliance by the company with the requirement of maintenance of books of account etc. shall be: [Section 128(6)]

- (a) Managing Director,
- (b) Whole-Time Director in charge of finance,
- (c) Chief Financial Officer, or
- (d) Any other person of a company charged by the Board with the duty of complying with provisions of section 128.

### **Register of Directors and Key Managerial Personnel**

[Section 170(1) & Rule 17 of Companies (Appointment and Qualification of Directors) Rules, 2014]

Every company shall keep at its registered office a register of its directors and key managerial personnel containing the following particulars:

- (a) Director Identification Number (Optional for KMP);
- (b) present name and surname in full;
- (c) any former name or surname in full;

- (d) father's name, mother's name and spouse's name(if married) and surnames in full;
- (e) date of birth;
- (f) residential address (present as well as permanent);
- (g) nationality (including the nationality of origin, if different);
- (h) occupation;
- (i) date of the board resolution in which the appointment was made;
- (j) date of appointment and reappointment in the company;
- (k) date of cessation of office and reasons therefor;
- (l) office of director or key managerial personnel held or relinquished in any other body corporate;
- (m) membership number of the Institute of Company Secretaries of India in case of Company Secretary;
- (n) PAN mandatory for KMP who is not having DIN.

Entries should be made in the register chronologically with a separate folio maintained in respect of each such person. The register should be maintained at the registered office of the company.

The register should be open for inspection during the business hours of the company, subject to such reasonable restrictions as the company may impose by its articles or in general meeting so that not less than 2 hours in each working day of the company are allowed for inspection. Members can inspect the register without payment of any fee and any other person can inspect the register on payment of the requisite fee. No person is entitled to copies of the register or any portion thereof.

Entries in the register should be authenticated by the secretary of the company or by any other person authorized by the Board for the purpose, by appending his signature to each entry.

The register should be preserved permanently and should be kept in the custody of the secretary of the company or any other person authorized by the Board for the purpose.

In addition to the details of the directors or key managerial personnel, the company shall also include in the aforesaid Register the details of securities held by them in the company, its holding company, subsidiaries, subsidiaries of the company's holding company and associate companies relating to:

- (a) the number, description and nominal value of securities;
- (b) the date of acquisition and the price or other consideration paid;
- (c) date of disposal and price and other consideration received;
- (d) cumulative balance and number of securities held after each transaction;
- (e) mode of acquisition of securities;
- (f) mode of holding – physical or in dematerialized form; and
- (g) whether securities have been pledged or any encumbrance has been created on the securities.

Members or debenture holders can inspect the register without payment of any fee. A member or debenture holder inspecting the register can make extracts from the register during the course of inspection. However, no person is entitled to copies of the register or any portion thereof.

Entries in the register should be authenticated by the secretary of the company or by any other person authorized by the Board for the purpose, by appending his signature to each entry.

The register should be preserved permanently and should be kept in the custody of the secretary of the company or any other person authorized by the Board for the purpose. This section shall not apply to Government company in which entire share capital is held by central Government, or by any State Government or Governors or by the Central Government or by one or more state Governments.

### Register of Investments in Securities not held in Company's Name

[Section 187 and Rule 14 of Companies (Meetings of Board and its Powers) Rules 2014

1. Every company shall, from the date of its registration, maintain a register in **Form No. MBP-3** and enter therein, chronologically, the particulars of investments in shares or other securities beneficially held by the company but which are not held in its own name and 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.
2. Further, the company shall also record whether such investments are held in a third party's name for the time being or otherwise.
3. 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 of the company or if there is no company secretary, any director or any other officer authorised by the Board for the purpose.
4. Entries in the register shall be authenticated by the company secretary of the company or by any other person authorized by the Board for the purpose.

The said 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.

### Register of loans, guarantees given and security provided or making acquisition of securities [Section 186 (9) and Rule 12 Companies (Meetings of Boards and its Powers) Rules, 2014]

1. Every company giving loan or giving guarantee or providing security or making an acquisition of securities shall, from the date of its incorporation, maintain a register in Form No. MBP-2 and enter therein separately, the particulars of loans and guarantees given, securities provided and acquisitions made as aforesaid.
2. The entries in the register shall be made chronologically in respect of each such transaction within seven days of making such loan or giving guarantee or providing security or making acquisition.
3. The register shall be kept at the registered office of the company and the register shall be preserved permanently and shall be kept in the custody of the company secretary of the company or any other person authorised by the Board for the purpose.
4. The entries in the register (either annual or electronic) shall be authenticated by the company secretary of the company or by any other person authorized by the Board for the purpose.
5. A register can be maintained either manually or in electronic mode.
6. The extract from the register may be furnished to any member of the company on payment of fee as may be prescribed in the Articles of the company which shall not exceed ten rupees for each page.

In case of Government Company - Section 186 shall not apply to:-

- (a) a Government company engaged in defence production;

- (b) a Government company, other than a listed company, in case such company obtains approval of the Ministry or Department of the Central Government which is administratively in charge of the company, or, as the case may be, the State Government before making any loan or giving any guarantee or providing any security or making any investment under the section.

### Register of contracts with companies/firms in which directors are interested

[Section 189(5) and Rule 16 of Companies (Meetings of Boards and its Powers) Rules, 2014]

- 1 Every company is required to keep one or more registers in Form MBP 4 giving separately the particulars of all contracts or arrangements and shall enter therein the particulars of-
  - (a) company or companies or bodies corporate, firms or other association of individuals, in which any director has any concern or interest as mentioned in sub-section (1) of section 184. But the particulars of the company or companies or bodies corporate in which a director himself together with any other director holds two percent or less of the paid-up share capital would not be required to be entered in the register.
  - (b) contracts or arrangements with a body corporate or firm or other entity as mentioned under sub-section(2) of section 184, in which any director is, directly or indirectly, concerned or interested; and
  - (c) contracts or arrangements with a related party with respect to transactions to which section 188 applies.
2. The entries in the register shall be made at once, whenever there is a cause to make entry, in chronological order and shall be authenticated by the company secretary of the company or by any other person authorized by the Board for the purpose. [(Rule 16(2)).
3. Such register shall be kept at the registered office of the company and the register shall be preserved permanently and shall be kept in the custody of the company secretary of the company or any other person authorized by the Board for the purpose. [Rule 16(3)].
4. The company shall provide extracts from such register to a member of the company on his request, within seven days from the date on which such request is made upon the payment of such fee as may be specified in the articles of the company but not exceeding ten rupees per page.

Such register or registers are required to be placed before the next meeting of the Board and signed by all the directors present at the meeting.

Every director within thirty days of his appointment or relinquishment is required to disclose his concern or interest in other associations, which are required to be included in the register. The register be kept at the registered office of the company and also open for inspection during business hours.

In case of Section 8 Company - Section 189 shall apply only if the transaction with reference to section 188 on the basis of terms and conditions of the contract or arrangement exceeds one lakh rupees.

### Annual Return

As per section 92 of the Act, every company shall prepare a return in E-form MGT 7 containing the required particulars as they stood on the close of the financial year and signed by a director and the company secretary, or where there is no company secretary, by a company secretary in practice. Whereas annual return in relation to One Person Company 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.

The Annual Return shall contain the following particulars:

- (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) its members and debenture-holders along with changes therein since the close of the previous financial year;
- (d) its promoters, directors, key managerial personnel along with changes therein since the close of the previous financial year;
- (e) meetings of members or a class thereof, Board and its various committees along with attendance details;
- (f) remuneration of directors and key managerial personnel;
- (g) 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;
- (h) matters relating to certification of compliances, disclosures as may be prescribed;
- (i) details, as may be prescribed, in respect of shares held by or on behalf of the Foreign Institutional Investors; and

such other matters as may be prescribed,

In case of One Person Company 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.

Provided further that the Central Government may prescribe abridged form of annual return for "One Person Company, small company and such other class or classes of companies as may be prescribed.]

The annual return, filed by a listed company or, by a company having paid-up capital of ten crore rupees or more or turnover of fifty crore rupees or more, shall be certified by a company secretary in practice, stating that the annual return discloses the facts correctly and adequately and that the company has complied with all the provisions of this Act

## **PRESERVATION OF REGISTERS AND RECORDS**

### **Provisions under SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015**

In case of listed entities SEBI(LODR), requires certain policies to be adopted by the companies for the purpose of preserving documents

#### ***A. Policy for preservation of documents***

Regulation 9 of the SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 provides following for preservation of documents:

The listed entity shall have a policy for preservation of documents, approved by its board of directors, classifying them in at least two categories as follows-

- (a) documents whose preservation shall be permanent in nature;
- (b) documents with preservation period of not less than eight years after completion of the relevant

transactions:

Provided that the listed entity may keep documents specified in clauses (a) and (b) in electronic mode.

### **B. Preservation of documents as per the Archival Policy**

Further, Regulation 30 of the SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 provides for disclosure of material events or information, which shall be disclosed with or without any application of the guidelines for materiality as specified under sub-regulation (4) of Regulation 30.

As per sub-regulation (8) of Regulation 30 every listed entity shall disclose on its website all such events or information as provided under the provisions of Regulation 30 and such disclosures shall be hosted on the website of the listed entity for a minimum period of five years and thereafter as per the archival policy of the listed entity, as disclosed on its website.

## LESSON ROUND-UP

- 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.
- Every company incorporated under the Act is required to keep at its registered office, *inter alia*, the following statutory books and registers—
- Register of securities bought back. [Section 68 and Rule 17(12) of Companies (Share Capital and Debenture) Rules, 2014]
- Register of deposits. [Section 73 and Rule 14 Companies (Acceptance of Deposits) Rules, 2014]
- Register of charges. [Section 81 and Rule 7 of Companies Registration of Charges Rules, 2014]
- Register of members [Section 88 (1) and Rule 3(1) of Companies (Management and Administration) Rules, 2014]
- Register of debenture holders [Section 88 (1)]
- “Foreign register” containing the names and particulars of the members, debenture holders, other security holders or beneficial owners residing outside India. [Section 88(4)]
- Register of Renewed and Duplicate Share Certificates. [Rule 6 of the Companies (Share Capital and Debentures) Rules, 2014]
- Register of sweat equity shares. [Section 54 and Rule 8(14) of Companies (Share Capital and Debentures) Rules, 2014]
- Register of Significant Beneficial Owner
- Register of Postal Ballot. [Section 110 and Rule 22 of the Companies (Management and Administration) Rules, 2014]
- Books containing minutes of general meeting and of Board and of committees of Directors. [Section 118]
- Books of account. [Section 128]
- Register of Directors/ key managerial personnel. [Section 170(1)]
- Register of investments in securities not held in company’s name. [Section 187 and Rule 14 of Companies





# Lesson 12

## An overview of Corporate Reorganisation

### LESSON OUTLINE

- Regulatory framework for merger/ amalgamation
- Provisions of Companies Act, 2013
- Power to Compromise or make arrangements with members or creditors
- Merger and amalgamation of certain companies
- Merger and amalgamation of a company with a foreign company
- Power to acquire shares of shareholders dissenting from scheme or contract approved by majority
- Purchase of minority shareholding
- Power of Central Government to provide for amalgamation of companies
- Lesson Round Up
- Glossary
- Self-Test Question

### LEARNING OBJECTIVES

While implementing the strategic decision of merger/amalgamation, the transferor/transferee company has to comply with a number of regulations viz., the Companies Act, 2013 and rules made there under, Income Tax Act, 1961, SEBI(LODR), Regulations, 2015, The Indian Stamp Act, 1899, the Competition Act, 2002 etc. It involves conducting of various meetings including board/general meetings, creditors' meetings, valuation and calculation of swap ratio, obtaining of various approvals from regulators like Stock Exchanges, National Company Law Tribunal (NCLT), Competition Commission of India, etc., drafting of documents such as preparation of scheme, notices/explanatory statements, filing of various documents including e-forms with ROC, filing of scheme of amalgamation with NCLT, etc.

After reading this lesson you will be able to understand the broad regulatory framework with respect to compromise/arrangement, mergers/demergers.

## REGULATORY FRAMEWORK FOR MERGER/AMALGAMATION

The Regulatory Framework of Mergers and Amalgamations (M&A) covers

1. Income Tax Act, 1961
2. SEBI (Listing Obligation & Disclosure Requirements) Regulations, 2015
3. The Indian Stamp Act, 1899
4. SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011
5. The Companies Act, 2013 and The Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 made under Chapter XV of the Companies Act 2013
6. Competition Act, 2002

### 1. Income Tax Act 1961

The Income Tax Act, 1961 covers aspects such as tax reliefs to amalgamating/amalgamated companies, carry forward of losses, exemptions from capital gains tax, etc. For example, when a scheme of merger or demerger involves the merger of a loss making company or a hiving off of a loss making division, it is necessary to check the relevant provisions of the Income Tax Act and the Rules for the purpose of ensuring, *inter alia*, the availability of the benefit of carrying forward the accumulated losses and setting of such losses against the profits of the Transferee Company. Taxation aspects of the Merger and Amalgamation have more elaborately given under the relevant module.

### 2. SEBI (Listing Obligations & Disclosure Requirements) Regulations, 2015

Regulation 37 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, provides that the listed entity shall not file any scheme of arrangement under sections 391-394 and 101 of the Companies Act, 1956 or under Sections 230-234 and Section 66 of Companies Act, 2013, whichever applicable, with any Court or Tribunal unless it has obtained observation letter or No-objection letter from the stock exchange(s).

Generally, stock exchanges raise several queries and on being satisfied that the scheme does not violate any laws concerning securities such as the Takeover Code or the SEBI (ICDR) Regulations, Stock Exchanges accord their approval.

The listed entity shall place the Observation letter or No-objection letter of the stock exchange(s) before the Court or Tribunal at the time of seeking approval of the scheme of arrangement. The validity of the 'Observation Letter' or No-objection letter of stock exchanges shall be six months from the date of issuance, within which the draft scheme of arrangement shall be submitted to the Court or Tribunal.

In addition to the above, Securities and Exchange Board of India has also provided some compliances with regard to the merger and amalgamation.

Rule 19 of the Securities Contracts (Regulation) Rules, 1957 provides basic compliance requirement for listing of securities on stock exchanges and SEBI has the power to relax listed companies from such compliances.

SEBI has issued Circular No. CFD/DIL3/CIR/2017/21 dated March 10, 2017 which *inter-alia* regulate the scheme of arrangement/ amalgamation/ merger/ etc. as filed with Stock Exchange(STX) for their NOC/ observation letter and also the provides for certain requirements to be complied with for being eligible to get

relaxation under Rule 19 of Securities Contracts (Regulation) Rules, 1957 and get the specified securities, issued by the transferee company, pursuant to a Scheme, listed on the stock exchange. Circular provides for the format of Detailed Compliance Report (DCR) to be filed with STX at the time obtaining their NOC/Observation letter duly certified by the Company Secretary, Chief Financial Officer and the Managing Director, confirming compliance with various regulatory requirements specified for schemes of arrangement and all accounting standards.

### 3. The Indian Stamp Act 1899

It is necessary to refer to the Stamp Act to check the stamp duty payable on transfer of undertaking through a merger or demerger.

The Constitution of India confers the power on the state legislature to make the laws in regard to the matters of stamp duty other than the documents specified in schedule I. The State in exercise of its legislative powers under Article 246 of the Constitution read with Entry 63 of List II (Seventh Schedule) of the Constitution levy the Stamp Duty.

Stamp duty is levied on the instrument evidencing a transfer *inter-vivos*, i.e. a conveyance. As per Section 2(10) of the Indian Stamp Act, 1899, "**Conveyance**" includes a conveyance oil sale and **every instrument** by which property whether movable or immovable, is transferred *inter vivos* and which is not otherwise specifically provided for by Schedule 1.

As per Section 2(14) of the Indian Stamp Act, 1899, "**Instrument**" includes every **document** by which any right or liability is, or purports to be, created, transferred, limited, extended, extinguished or record.

The term Section 3(18) of the General Clauses Act, 1897, "**Document**" shall include any matter written, expressed or described upon any substance by means of letters, figures or marks, or by more than one of those means **which is intended to be used**, or which may be used, **for the purpose or recording that matter**.

The definition(s) as reproduced above are inclusive in nature and are not self-explanatory. Hence, to avoid any ambiguity and confusion in this regard, with time, certain States has amended their Stamp Act and included Order of Court approving scheme of arrangement within the meaning of 'conveyance'. Maharashtra, Gujarat, Karnataka, Rajasthan, Chhattisgarh, Madhya Pradesh and Andhra Pradesh are the states which have specifically included an amalgamation order of a High Court as "Conveyance".

In *Re. Sahayanidhi (Virudhunagar) Ltd.v. AR.S Subramanya Nadar*, (1950) 20 Com Cases 214 (Mad) Hon'ble Madras High Court held that, "the documents (scheme of amalgamation or reconstruction) purport to transfer movable property in the shape of book debts and promissory notes and the consideration for such transfer is partly in the shape of a cash payment and partly in the shape of covenants entered into by the transferee. We are therefore of the opinion that these two documents fall within Article 23 of Schedule I and are to be stamped as such."

In *Re. Hindustan Lever v. State of Maharashtra* (2004) 9 SCC 438 apex court held that, "This definition of instrument is not amended by the Maharashtra Act of 17 of 1993. The word "Instrument" is defined to mean, every document by which any right or liability is, or purports to be created, transferred, limited, extended, extinguished or recorded, but does not include bill of exchange, cheque, promissory note, bill of lading, letter of credit, policy of insurance, transfer of shares, debenture proxy and receipt. The recital in the scheme of amalgamation as well as the order of the High Court under Section 394 of the Companies Act, 1956, declares, that, upon such order of High Court the undertaking of the transferor company shall stand

transferred to the transferee company with all its movable, immovable and tangible assets to the transferee company without any further act or deed..... Thus the amalgamation scheme sanctioned by the Court would be an "instrument" within the meaning of Section 2(i). By the said "instrument" the properties are transferred from the transferor company to the transferee company, the basis of which is the compromise or arrangement arrived at between the two companies.

In *Re. Gemini Silk Ltd. v. Gemini Overseas Ltd.* [2003] 114 Comp. Cas. 92 (cal.) Hon'ble Calcutta High Court held that, "An order sanctioning a scheme of reconstruction has its genesis in an agreement between the shareholders of the transferor and the transferee-company. The intended transfer is a voluntary act of contracting parties. The transfer has all the trappings of a sale. The transfer is effected by an order of court and the order of court is an instrument by which the transfer is effected. Once the order is held to be an instrument, the irresistible conclusion is that it is a conveyance. Thus an order sanctioning a scheme of reconstruction or amalgamation under section 394 is covered by definition of words 'conveyance' and 'instrument' under the Indian Stamp Act, 1899 and, therefore, liable to stamp duty. "

In the case of *Madhu Intra Ltd v. Registrar of Companies* 2006 130 Comp Cas 510 Cal the Division Bench of Hon'ble High Court of Calcutta made the following observations, even if the order under Section 394 is to be taken to be a 'conveyance' or an 'instrument' the transfer of assets and liabilities effected thereby is purely by operation of law which on account of Section 2(d) of the Transfer of Property Act also excludes the operation of Section 6(e) thereto. Notwithstanding the definition of the expression 'instrument' in Section 2(14) of the Indian Stamp Act, the un-amended provisions of the Indian Stamp Act in relation to such definition and the definition of 'conveyance' and/ or 'instrument' does not apply to an order under Section 394 of the Companies Act for the purpose of stamp-duty

In our view, the transfer of assets and liabilities of the transferor company to the transferee company takes place on an order being made under Sub-section (1) of Section 394 by operation of Sub-section (2) thereof.

In February 2012 the Hon'ble High Court of Calcutta made the following observations in the case of *Emami Biotech Limited and Others.....*

By sanctioning of amalgamation scheme, the property including the liabilities are transferred as provided in Section 394 of the Companies Act and on that transfer instrument, stamp duty is levied. It, therefore, cannot be said that the State Legislature has no jurisdiction to levy such duty.

It must be respectfully observed in the context that in the light of the judgment in *Hindustan Lever*, the view expressed in *Madhu Intra* does not hold good. The judgement in *Madhu Intra* did not notice the Supreme Court pronouncement in *Hindustan Lever*. If the Division Bench of this court had noticed *Hindustan Lever* and had still rendered the opinion in *Madhu Intra*, it would have been binding on the company Judge of this court. But in *Madhu Intra* not noticing *Hindustan Lever* and it being apparent that the question has been answered otherwise by the Supreme Court, it is the Supreme Court view that has to be followed.

In *Re. Delhi Towers Limited v. GNCT of Delhi* [2010] 159 Comp Case 129 (Del.) Hon'ble Delhi Court held that, "there can therefore be no manner of doubt, that even if the legislature had not effected the amendment and included the clause in sub-section (g) of Section 2 of the Bombay Stamp Act, it made no difference to the legal issue at all. A scheme of amalgamation approved by a court in exercise of jurisdiction under the Companies Act, 1956 and given effect to thereafter, where under property is conveyed from one company to another, is covered within the un-amended definition of the term 'conveyance' in the Bombay Stamp Act as well. The same would therefore be eligible to stamp duty under section 3 of the Indian Stamp Act."

In the case of *Li Taka Pharmaceuticals Ltd. v. State of Maharashtra And Other* [AIR 1997 Bom 7] Hon'ble

Bombay High Court held that an order under section 394 is founded or based upon compromise or arrangement between the two companies of transferring assets and liabilities of one company to another company known as "transferor-company" and that order is an "instrument" as defined under section 2(1) of the Bombay Stamp Act which includes every document by which any right or liability is transferred.

Apart from the above cited case laws also in *Ambica Quarry works v. State of Gujrat*, AIR 1987 SC 1073; *Orient Paper Industry Ltd. v. State of Orissa*, AIR 1991 SC 672; *State of Orissa v. Sudhansu Sekhar Misra*, AIR 1968 SC 647; *Krishna Kumar v. Union Bank of India*, AIR 1990 SC 1782, The Hon'ble Supreme Court of India in the series of judgments in the above cited cases has held that an order of amalgamation is subject to Stamp Duty in the context of the provisions of the Bombay Stamp Act where the chargeability and the basis of chargeability of an order of amalgamation have been expressly spelt out, in the absence of such express provisions regarding chargeability and basis of chargeability of an order of amalgamation in the Stamp Acts of other states, it is legally doubtful whether orders of amalgamation in such States would be subject to Stamp Duty.

#### **PRESENT SCENARIO WITH REGARDS TO PAYMENT OF STAMP DUTY IN VARIOUS STATES**

Some of the States like Maharashtra, Gujarat, Karnataka, Rajasthan etc which have enacted their own Stamp Acts have made specific provisions with respect to payment of Stamp Duty on Order of the High Court under Section 394 in their Acts/Schedules, while some other states like Madhya Pradesh, Andhra Pradesh etc which have adopted the Indian Stamp Act, 1899 have made state amendments to levy Stamp duty on the High Court Order. The remaining states which neither have their own Stamp Act nor have they made any State Amendment in the adopted Indian Stamp Act, 1899, levy Stamp duty as per the decision of High Court, if any, covering their states, or follow the decision of Supreme Court as laid down in the case of Hindustan Lever.

#### **CONCLUSION**

The law relating to payment of Stamp Duty on the Order of High Court in case of Merger lacks uniformity in India and levy of Stamp Duty will depend upon the Stamp Duty Law of the Concerned State. Also in cases where the Transferor Company has its assets in different states things may get more complicated. The method of arriving at the figure of Stamp Duty also varies from State to State. Non -payment of Stamp Duty can cause legal hurdles at the time of registration of properties in the name of Transferee Company. Payment of Stamp Duty is an important aspect to be considered before going in for a merger especially in those cases where the asset of the Transferor Company poses a significant value.

#### **4. SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011**

If an acquisition is contemplated by way of issue of new shares, or the acquisition of existing shares or voting rights, of a listed company, to or by an acquirer, the provisions of the Takeover Code are applicable. The Takeover Code regulates both direct and indirect acquisitions of shares or voting rights in, and control over a target company. The key objectives of the Takeover Code are to provide the shareholders of a listed company with adequate information about an impending change in control of the company or substantial acquisition by an acquirer, and provide them with an exit option in case they do not wish to retain their shareholding in the company.

#### **5. Competition Act 2002**

The provisions of Competition Act and the Competition Commission of India (Procedure in regard to the Transaction of Business relating to Combinations) Regulations, 2011 are to be complied with.

## 6. PROVISIONS OF THE COMPANIES ACT 2013

### COMPANIES ACT 2013

Chapter XV of Companies Act, 2013 comprising Section 230 to 240 contains provisions on 'Compromises, Arrangements and Amalgamations'. The scheme of Chapter XV goes as follows.

1. Section 230-231 deals with compromise or arrangements.
2. Section 232 deals with mergers and amalgamation including demergers.
3. Section 233 deals with amalgamation of small companies.
4. Section 234 deals with amalgamation of company with foreign company.
5. Section 235 deals with acquisition of shares of dissenting shareholders.
6. Section 236 deals with purchase of minority shareholding.
7. Section 237 deals with power of Central Government to provide for amalgamation of companies in public interest.
8. Section 238 deals with registration of offer of schemes involving transfer of shares.
9. Section 239 deals with preservation of books and papers of amalgamated companies.
10. Section 240 deals with liability of officers in respect of offences committed prior to merger, amalgamation, etc.

### The Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 made under Chapter XV of the Companies Act, 2013

The scope of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 made under Chapter XV of the Companies Act, 2013 includes detailed procedural aspects relating to substantive law.

### POWER TO COMPROMISE OR MAKE ARRANGEMENTS WITH MEMBERS OR CREDITORS

#### Tribunal to order meeting of members/creditors, etc.

Section 230(1) states that when a compromise or arrangement is proposed—

- (a) between a company and its creditors or any class of them; or
- (b) between a company and its members or any class of them,

the Tribunal may, on the application of the (i) company, or (ii) any creditor or (iii) member of the company, or (iv) in the case of a company which is being wound up, of the liquidator, appointed under this Act or under Insolvency and Bankruptcy Code, 2016 order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal directs.

For the purposes of this sub-section, arrangement includes a reorganisation of the company's share capital by the consolidation of shares of different classes or by the division of shares into shares of different classes, or by both these methods.

#### Affidavit by the applicant to disclose certain material facts

Section 230(2) states that the company or any other person, by whom an application is made under sub-section (1), shall disclose to the Tribunal by affidavit—

- (a) all material facts relating to the company, such as the latest financial position of the company, the latest

auditor's report on the accounts of the company and the pendency of any investigation or proceedings against the company;

(b) reduction of share capital of the company, if any, included in the compromise or arrangement;

(c) any scheme of corporate debt restructuring consented to by not less than seventy-five per cent of the secured creditors in value, including—

- (i) a creditors' responsibility statement in the prescribed form;
- (ii) safeguards for the protection of other secured and unsecured creditors;
- (iii) report by the auditor that the fund requirements of the company after the corporate debt restructuring as approved shall conform to the liquidity test based upon the estimates provided to them by the Board;
- (iv) where the company proposes to adopt the corporate debt restructuring guidelines specified by the Reserve Bank of India, a statement to that effect; and
- (v) a valuation report in respect of the shares and the property and all assets, tangible and intangible, movable and immovable, of the company by a registered valuer.

### **Notice of the meeting**

Section 230(3) states that when a meeting is proposed to be called in pursuance of an order of the Tribunal under sub-section (1), a notice of such meeting shall be sent to all the creditors or class of creditors and to all the members or class of members and the debenture-holders of the company, individually at the address registered with the company which shall be accompanied by

- a statement disclosing the details of the compromise or arrangement,
- a copy of the valuation report, if any, and
- explaining their effect on creditors, key managerial personnel, promoters and non-promoter members, and the debenture-holders, and
- the effect of the compromise or arrangement on any material interests of the directors of the company or the debenture trustees, and
- such other matters as may be prescribed;

Such notice and other documents shall also be placed on the website of the company, if any, and in case of a listed company, these documents shall be sent to the Securities and Exchange Board and stock exchange where the securities of the companies are listed, for placing on their website and shall also be published in newspapers in such manner as may be prescribed.

When the notice for the meeting is also issued by way of an advertisement, it shall indicate the time within which copies of the compromise or arrangement shall be made available to the concerned persons free of charge from the registered office of the company.

### **Notice to provide for voting by themselves or through proxy or through postal ballot**

Sub-section (4) of section 230 states that a notice under sub-section (3) shall provide that the persons to whom the notice is sent may vote in the meeting either themselves or through proxies or by postal ballot to the adoption of the compromise or arrangement within one month from the date of receipt of such notice.

**Who can object to the scheme?**

Any objection to the compromise or arrangement shall be made only by persons holding not less than ten per cent of the shareholding or having outstanding debt amounting to not less than five per cent of the total outstanding debt as per the latest audited financial statement.

**Notice to be sent to the regulators seeking their representations**

Section 230(5) states that a notice under sub-section (3) along with all the documents in such form as may be prescribed shall also be sent to the Central Government, the Income-tax authorities, the Reserve Bank of India, the Securities and Exchange Board, the Registrar, the respective stock exchanges, the Official Liquidator, the Competition Commission of India established under sub-section (1) of section 7 of the Competition Act, 2002, if necessary, and such other sectoral regulators or authorities which are likely to be affected by the compromise or arrangement and shall require that representations, if any, to be made by them shall be made within a period of thirty days from the date of receipt of such notice, failing which, it shall be presumed that they have no representations to make on the proposals.

**Approval and sanction of the scheme**

Section 230(6) states that when at a meeting held in pursuance of sub-section (1), majority of persons representing three-fourths in value of the creditors, or class of creditors or members or class of members, as the case may be, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and if such compromise or arrangement is sanctioned by the Tribunal by an order, the same shall be binding on the company, all the creditors, or class of creditors or members or class of members, as the case may be, or, in case of a company being wound up, on the liquidator appointed under this Act or under the Insolvency and Bankruptcy Code, 2016, as the case may be and the contributories of the company.

**Order of the Tribunal sanctioning the scheme to provide for the following matters [Section 280(7)]**

An order made by the Tribunal under sub-section (6) shall provide for all or any of the following matters, namely:—

- (a) where the compromise or arrangement provides for conversion of preference shares into equity shares, such preference shareholders shall be given an option to either obtain arrears of dividend in cash or accept equity shares equal to the value of the dividend payable;
- (b) the protection of any class of creditors;
- (c) if the compromise or arrangement results in the variation of the shareholders' rights, it shall be given effect to under the provisions of section 48;
- (d) if the compromise or arrangement is agreed to by the creditors under sub-section (6), any proceedings pending before the Board for Industrial and Financial Reconstruction established under section 4 of the Sick Industrial Companies (Special Provisions) Act, 1985 shall abate;
- (e) such other matters including exit offer to dissenting shareholders, if any, as are in the opinion of the Tribunal necessary to effectively implement the terms of the compromise or arrangement.

**Accounting treatment proposed in the scheme to be in conformity with accounting standards**

No compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company's auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133.

### **Order of Tribunal to be filed with the Registrar**

Section 230(8) states that the order of the Tribunal shall be filed with the Registrar by the company within a period of thirty days of the receipt of the order.

### **Tribunal may dispense with calling of meeting of creditors**

Section 230(9) states that the Tribunal may dispense with calling of a meeting of creditors or class of creditors where such creditors or class of creditors, having at least ninety per cent value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement.

### **Compromise in respect of buy back is to be in compliance with section 68**

As per Section 230(10), no compromise or arrangement in respect of any buy-back of securities under this section shall be sanctioned by the Tribunal unless such buy-back is in accordance with the provisions of section 68.

### **Compromise includes takeover (This sub-section is not yet notified)**

Section 230(11) states that any compromise or arrangement may include takeover offer made in such manner as may be prescribed. In case of listed companies, takeover offer shall be as per the regulations framed by the Securities and Exchange Board.

*Do provisions of section 66 apply with respect to reduction of capital effected in pursuance of order of Tribunal under section 230?*

Provisions of section 66 shall not apply to the reduction of share capital effected in pursuance of the order of the Tribunal under this section.

## **POWER OF THE TRIBUNAL TO ENFORCE COMPROMISE OR ARRANGEMENT**

As per section 231(1), when the Tribunal makes an order under section 230 sanctioning a compromise or an arrangement in respect of a company, it—

- (a) shall have power to supervise the implementation of the compromise or arrangement; and
- (b) may, at the time of making such order or at any time thereafter, give such directions in regard to any matter or make such modifications in the compromise or arrangement as it may consider necessary for the proper implementation of the compromise or arrangement.

Sub-section (2) states that if the Tribunal is satisfied that the compromise or arrangement sanctioned under section 230 cannot be implemented satisfactorily with or without modifications, and the company is unable to pay its debts as per the scheme, it may make an order for winding-up the company and such an order shall be deemed to be an order made under section 273.

## **MERGER AND AMALGAMATION OF COMPANIES**

### **Tribunal's power to call meeting of creditors or members, with respect to merger or amalgamation of companies**

Section 232(1) states that when an application is made to the Tribunal under section 230 for the sanctioning of a compromise or an arrangement proposed between a company and any such persons as are mentioned in that section, and it is shown to the Tribunal—

- (a) that the compromise or arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of the company or companies involving merger or the amalgamation of any two or more companies; and
- (b) that under the scheme, the whole or any part of the undertaking, property or liabilities of any company (hereinafter referred to as the transferor company) is required to be transferred to another company (hereinafter referred to as the transferee company), or is proposed to be divided among and transferred to two or more companies,

the Tribunal may on such application, order a meeting of the creditors or class of creditors or the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal may direct and the provisions of sub-sections (3) to (6) of section 230 shall apply *mutatis mutandis*.

#### **Circulation of documents for members'/creditors' meeting**

Section 232(2) states that when an order has been made by the Tribunal under sub-section (1), merging companies or the companies in respect of which a division is proposed, shall also be required to circulate the following for the meeting so ordered by the Tribunal, namely:—

- (a) the draft of the proposed terms of the scheme drawn up and adopted by the directors of the merging company;
- (b) confirmation that a copy of the draft scheme has been filed with the Registrar;
- (c) a report adopted by the directors of the merging companies explaining effect of compromise on each class of shareholders, key managerial personnel, promoters and non-promoter shareholders laying out in particular the share exchange ratio, specifying any special valuation difficulties;
- (d) the report of the expert with regard to valuation, if any;
- (e) a supplementary accounting statement if the last annual accounts of any of the merging company relate to a financial year ending more than six months before the first meeting of the company summoned for the purposes of approving the scheme.

#### **Sanctioning of scheme by Tribunal**

Section 232(3) states that the Tribunal, after satisfying itself that the procedure specified in sub-sections (1) and (2) has been complied with, may, by order, sanction the compromise or arrangement or by a subsequent order, make provision for the following matters, namely:—

- (a) the transfer to the transferee company of the whole or any part of the undertaking, property or liabilities of the transferor company from a date to be determined by the parties unless the Tribunal, for reasons to be recorded by it in writing, decides otherwise;
- (b) the allotment or appropriation by the transferee company of any shares, debentures, policies or other like instruments in the company which, under the compromise or arrangement, are to be allotted or appropriated by that company to or for any person:

##### ***No transferee company can hold shares in its own name or under any trust***

A transferee company shall not, as a result of the compromise or arrangement, hold any shares in its own name or in the name of any trust whether on its behalf or on behalf of any of its subsidiary or associate companies and any such shares shall be cancelled or extinguished;

- (c) the continuation by or against the transferee company of any legal proceedings pending by or against any transferor company on the date of transfer;

- (d) dissolution, without winding-up, of any transferor company;
  - (e) the provision to be made for any persons who, within such time and in such manner as the Tribunal directs, dissent from the compromise or arrangement;
  - (f) where share capital is held by any non-resident shareholder under the foreign direct investment norms or guidelines specified by the Central Government or in accordance with any law for the time being in force, the allotment of shares of the transferee company to such shareholder shall be in the manner specified in the order;
  - (g) the transfer of the employees of the transferor company to the transferee company;
  - (h) when the transferor company is a listed company and the transferee company is an unlisted company,—
    - (A) the transferee company shall remain an unlisted company until it becomes a listed company;
    - (B) if shareholders of the transferor company decide to opt out of the transferee company, provision shall be made for payment of the value of shares held by them and other benefits in accordance with a pre-determined price formula or after a valuation is made, and the arrangements under this provision may be made by the Tribunal.
- The amount of payment or valuation under this clause for any share shall not be less than what has been specified by the Securities and Exchange Board under any regulations framed by it;
- (i) where the transferor company is dissolved, the fee, if any, paid by the transferor company on its authorised capital shall be set-off against any fees payable by the transferee company on its authorised capital subsequent to the amalgamation; and
  - (j) such incidental, consequential and supplemental matters as are deemed necessary to secure that the merger or amalgamation is fully and effectively carried out.

#### **Auditor's certificate as to conformity with accounting standards**

No compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company's auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133.

#### **Transfer of property or liabilities**

Sub-section (4) of Section 232 states that an order under this section provides for the transfer of any property or liabilities, then, by virtue of the order, that property shall be transferred to the transferee company and the liabilities shall be transferred to and become the liabilities of the transferee company and any property may, if the order so directs, be freed from any charge which shall by virtue of the compromise or arrangement, cease to have effect.

#### **Certified copy of the order to be filed with the Registrar**

Section 232(5) states that every company in relation to which the order is made shall cause a certified copy of the order to be filed with the Registrar for registration within thirty days of the receipt of certified copy of the order.

#### **Effective date of the scheme**

Section 232(6) states that the scheme under this section shall clearly indicate an appointed date from which

it shall be effective and the scheme shall be deemed to be effective from such date and not at a date subsequent to the appointed date.

#### **Annual statement certified by CA/CS/CWA to be filed with Registrar every year until the completion of the scheme**

Section 232 (7) states that every company in relation to which the order is made shall, until the completion of the scheme, file a statement in such form and within such time as may be prescribed with the Registrar every year duly certified by a chartered accountant or a cost accountant or a company secretary in practice indicating whether the scheme is being complied with in accordance with the orders of the Tribunal or not.

#### **Punishment**

Section 232(8) states that if a transferor company or a transferee company contravenes the provisions of this section, the transferor company or the transferee company, as the case may be, shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees and every officer of such transferor or transferee company who is in default, shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees, or with both.

#### **Explanation under Section 232**

For the purpose of the Section, —

- (i) in a scheme involving a merger, where under the scheme the undertaking, property and liabilities of one or more companies, including the company in respect of which the compromise or arrangement is proposed, are to be transferred to another existing company, it is a merger by absorption, or where the undertaking, property and liabilities of two or more companies, including the company in respect of which the compromise or arrangement is proposed, are to be transferred to a new company, whether or not a public company, it is a merger by formation of a new company;
- (ii) references to merging companies are in relation to a merger by absorption, to the transferor and transferee companies, and, in relation to a merger by formation of a new company, to the transferor companies;
- (iii) a scheme involves a division, where under the scheme the undertaking, property and liabilities of the company in respect of which the compromise or arrangement is proposed are to be divided among and transferred to two or more companies each of which is either an existing company or a new company; and
- (iv) property includes assets, rights and interests of every description and liabilities include debts and obligations of every description.

#### **MERGER AND AMALGAMATION OF CERTAIN COMPANIES**

Section 233 prescribes simplified procedure for Merger or amalgamation of —

- two or more small companies, or
- between a holding company and its wholly-owned subsidiary company or
- such other class or classes of companies as may be prescribed.

#### **Merger of small companies/holding and subsidiary companies**

Accordingly, sub-section (1) of Section 233 states that notwithstanding the provisions of section 230 and

section 232, a scheme of merger or amalgamation may be entered into between two or more small companies or between a holding company and its wholly-owned subsidiary company or such other class or classes of companies as may be prescribed, subject to the following, namely:—

- (a) a notice of the proposed scheme inviting objections or suggestions, if any, from the Registrar and Official Liquidators where registered office of the respective companies are situated or persons affected by the scheme within thirty days is issued by the transferor company or companies and the transferee company;
- (b) the objections and suggestions received are considered by the companies in their respective general meetings and the scheme is approved by the respective members or class of members at a general meeting holding at least ninety per cent of the total number of shares;
- (c) each of the companies involved in the merger files a declaration of solvency, in the prescribed form, with the Registrar of the place where the registered office of the company is situated; and
- (d) the scheme is approved by majority representing nine-tenths in value of the creditors or class of creditors of respective companies indicated in a meeting convened by the company by giving a notice of twenty-one days along with the scheme to its creditors for the purpose or otherwise approved in writing.

#### **Transferee company to file a copy of scheme approved**

Section 233(2) states that the transferee company shall file a copy of the scheme so approved in the manner as may be prescribed, with the Central Government, Registrar and the Official Liquidator where the registered office of the company is situated.

#### **Central Government to issue confirmation order, where there are no objections or suggestions from Registrar or Official Liquidator**

Section 233(3) states that on the receipt of the scheme, if the Registrar or the Official Liquidator has no objections or suggestions to the scheme, the Central Government shall register the same and issue a confirmation thereof to the companies.

#### **Objections if any by the Registrar or Official Liquidator to be communicated to the central government**

Section 233(4) provides that if the Registrar or Official Liquidator has any objections or suggestions, he may communicate the same in writing to the Central Government within a period of thirty days. If no such communication is made, it shall be presumed that he has no objection to the scheme.

#### **Application by Central Government to the Tribunal**

Section 233(5) states that if the Central Government after receiving the objections or suggestions or for any reason is of the opinion that such a scheme is not in public interest or in the interest of the creditors, it may file an application before the Tribunal within a period of sixty days of the receipt of the scheme under sub-section (2) stating its objections and requesting that the Tribunal may consider the scheme under section 232.

#### **Tribunal's Action to Central Government's application**

Section 233(6) states that on receipt of an application from the Central Government or from any person, if the Tribunal, for reasons to be recorded in writing, is of the opinion that the scheme should be considered as per the procedure laid down in section 232, the Tribunal may direct accordingly or it may confirm the scheme by passing such order as it deems fit:

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

#### **Registrar having jurisdiction over transferee company has to be communicated**

Section 233(7) states that a copy of the order under sub-section (6) confirming the scheme shall be communicated to the Registrar having jurisdiction over the transferee company and the persons concerned and the Registrar shall register the scheme and issue a confirmation thereof to the companies and such confirmation shall be communicated to the Registrars where transferor company or companies were situated.

#### **Effect of registration of the scheme**

Section 233(8) states that registration of the scheme under sub-section (3) or sub-section (7) shall be deemed to have the effect of dissolution of the transferor company without process of winding-up.

#### **Section 233(9) states that the registration of the scheme shall have the following effects, namely:—**

- (a) transfer of property or liabilities of the transferor company to the transferee company so that the property becomes the property of the transferee company and the liabilities become the liabilities of the transferee company;
- (b) the charges, if any, on the property of the transferor company shall be applicable and enforceable as if the charges were on the property of the transferee company;
- (c) legal proceedings by or against the transferor company pending before any court of law shall be continued by or against the transferee company; and
- (d) where the scheme provides for purchase of shares held by the dissenting shareholders or settlement of debt due to dissenting creditors, such amount, to the extent it is unpaid, shall become the liability of the transferee company.

#### **Transferee Company not to hold any share in its own name or trust and all such shares are to be cancelled or extinguished**

Section 233(10) states that a transferee company shall not on merger or amalgamation, hold any shares in its own name or in the name of any trust either on its behalf or on behalf of any of its subsidiary or associate company and all such shares shall be cancelled or extinguished on the merger or amalgamation.

#### **Transferee Company to file an application with Registrar along with the scheme registered**

Section 233(11) provides that the transferee company shall file an application with the Registrar along with the scheme registered, indicating the revised authorised capital and pay the prescribed fees due on revised capital. The fee, if any, paid by the transferor company on its authorised capital prior to its merger or amalgamation with the transferee company shall be set-off against the fees payable by the transferee company on its authorised capital enhanced by the merger or amalgamation.

#### **MERGER OR AMALGAMATION OF A COMPANY WITH A FOREIGN COMPANY**

Section 234(2) states that subject to the provisions of any other law for the time being in force, a foreign company, may with the prior approval of the Reserve Bank of India, merge into a company registered under this Act or vice versa and the terms and conditions of the scheme of merger may provide, among other things, for the payment of consideration to the shareholders of the merging company in cash, or in Depository Receipts, or partly in cash and partly in Depository Receipts, as the case may be, as per the scheme to be drawn up for the purpose.

For the purposes of sub-section (2), the expression “foreign company” means any company or body corporate incorporated outside India whether having a place of business in India or not.

Section 234(1) states that the provisions of this Chapter unless otherwise provided under any other law for the time being in force, shall apply *mutatis mutandis* to schemes of mergers and amalgamations between companies registered under this Act and companies incorporated in the jurisdictions of such countries as may be notified from time to time by the Central Government. The Central Government may make rules, in consultation with the Reserve Bank of India, in connection with mergers and amalgamations provided under this section.

**Rule 25A of the of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016,**

(1) A foreign company incorporated outside India may merge with an Indian company after obtaining prior approval of Reserve Bank of India and after complying with the provisions of sections 230 to 232 of the Act and these rules.

(2) (a) A company may merge with a foreign company incorporated in any of the jurisdictions specified in Annexure B after obtaining prior approval of the Reserve Bank of India and after complying with provisions of sections 230 to 232 of the Act and these rules.

(b) The transferee company shall ensure that valuation is conducted by valuers who are members of a recognised professional body in the jurisdiction of the transferee company and further that such valuation is in accordance with internationally accepted principles on accounting and valuation. A declaration to this effect shall be attached with the application made to Reserve Bank of India for obtaining its approval under clause (a) of this sub-rule.

(3) The concerned company shall file an application before the Tribunal as per provisions of section 230 to section 232 of the Act and these rules after obtaining approvals specified in sub-rule (1) and sub-rule (2), as the case may be.

Explanation 1. For the purposes of this rule the term “company” means a company as defined in clause (20) of section 2 of the Act and the term “foreign company” means a company or body corporate incorporated outside India whether having a place of business in India or not.

Explanation 2. For the purposes of this rule, it is clarified that no amendment shall be made in this rule without consultation of the Reserve Bank of India.

**POWER TO ACQUIRE SHARES OF SHAREHOLDERS DISSENTING FROM SCHEME OR CONTRACT APPROVED BY MAJORITY**

**Offer to dissenting shareholders**

Where a scheme or contract involving the transfer of shares or any class of shares in a company (the transferor company) to another company (the transferee company) has, within four months after making of an offer in that behalf by the transferee company, been approved by the holders of not less than nine-tenths in value of the shares whose transfer is involved, other than shares already held at the date of the offer by, or by a nominee of the transferee company or its subsidiary companies, the transferee company may, at any time within two months after the expiry of the said four months, give notice in the prescribed manner to any dissenting shareholder that it desires to acquire his shares.

**MEANING OF DISSENTING SHAREHOLDERS [Section 235(1)]**

As per the explanation to Section 235, dissenting shareholder includes a shareholder who has not assented to the scheme or contract and any shareholder who has failed or refused to transfer his shares to the transferee company in accordance with the scheme or contract.

**ACQUISITION OF SHARES OF DISSENTING SHAREHOLDERS [Section 235(2)]**

After the notice under section 235(1) of the Act, the transferee company shall, unless on an application made by the dissenting shareholder to the Tribunal, within one month from the date on which the notice was given and the Tribunal thinks fit to order otherwise, be entitled to and bound to acquire those shares on the terms on which, under the scheme or contract, the shares of the approving shareholders are to be transferred to the transferee company.

**PROCESS OF ACQUISITION OF SHARES FROM DISSENTING SHAREHOLDERS [Section 235(3)]**

Where a notice has been given by the transferee company under Section 235(1) and the tribunal has not, on an application made by the dissenting shareholder, made an order to the contrary, the transferee company shall, on the expiry of one month from the date on which the notice has been given, or, if an application to the Tribunal by the dissenting shareholder is then pending, after that application has been disposed of, send a copy of the notice to the transferor company together with an instrument of transfer, to be executed on behalf of the shareholder by any person appointed by the transferor company and on its own behalf by the transferee company, and pay or transfer to the transferor company the amount or other consideration representing the price payable by the transferee company for the shares which, by virtue of this section, that company is entitled to acquire, and the transferor company shall—

- (a) thereupon register the transferee company as the holder of those shares; and
- (b) within one month of the date of such registration, inform the dissenting shareholders of the fact of such registration and of the receipt of the amount or other consideration representing the price payable to them by the transferee company.

**UTILIZATION OF FUNDS [Section 235(4)]**

Any sum received by the transferor company under this section shall be paid into a separate bank account, and any such sum and any other consideration so received shall be held by that company in trust for the several persons entitled to the shares in respect of which the said sum or other consideration were respectively received and shall be disbursed to the entitled shareholders within sixty days.

**PURCHASE OF MINORITY SHAREHOLDING****Definition of Acquirer and Person acting in concert**

The expressions “acquirer” and “person acting in concert” shall have the meanings respectively assigned to them in clause (b) and clause (e) of sub regulation (1) of regulation 2 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997.

As per Section 236(1) of the Act, in the event of an acquirer, or a person acting in concert with such acquirer, becoming registered holder of ninety per cent or more of the issued equity share capital of a company, or in the event of any person or group of persons becoming ninety per cent majority or holding ninety per cent. of the issued equity share capital of a company, by virtue of an amalgamation, share exchange, conversion of securities or for any other reason, such acquirer, person or group of persons, as the case may be, shall notify the company of their intention to buy the remaining equity shares.

As per Section 236(2) of the Act, the acquirer, person or group of persons under sub-section (1) shall offer to the minority shareholders of the company for buying the equity shares held by such shareholders at a price determined on the basis of valuation by a registered valuer in accordance with such rules as may be prescribed.

Without prejudice to the provisions of sub-sections (1) and (2), the minority shareholders of the company may offer to the majority shareholders to purchase the minority equity shareholding of the company at the price determined as in accordance with Rule 27 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016, which is as under:

The registered valuer shall determine the price (hereinafter called as offer price ) to be paid by acquirer, person or group of persons referred to in sub-section (1) of section 236 of the Act for purchase of equity shares of the minority shareholders of the company, in accordance with the following:

In case of a listed company;

- (i) The offer price shall be determined in the manner as may be specified by the Securities And Exchange Board of India under the relevant regulations framed by it, as may be applicable; and
- (ii) The registered valuer shall also provide a valuation report on the basis of valuation addressed to the board of directors of the company giving justification for such valuation.

In the case of an unlisted company and a private company,

- (i) the offer price shall be determined after taking into account the following factors :-
  - (a) the highest price paid by the acquirer, person or group of persons for acquisition during last twelve months;
  - (b) the fair price of shares of the company to be determined by the registered valuer after taking into account valuation parameters including return on net worth, book value of shares, earning per share, price earning multiple vis-à-vis the industry average, and such other parameters as are customary for valuation of shares of such companies; and
- (ii) the registered valuer shall also provide a valuation report on the basis of valuation addressed to the board of directors of the company giving justification for such valuation.

The majority shareholders shall deposit an amount equal to the value of shares to be acquired by them under sub-section (2) or sub-section (3), as the case may be, in a separate bank account to be operated by company whose shares are being transferred for at least one year for payment to the minority shareholders and such amount shall be disbursed to the entitled shareholders within sixty days. Provided that such disbursement shall continue to be made to the entitled shareholders for a period of one year, who for any reason had not been made disbursement within the said period of sixty days or if the disbursement have been made within the aforesaid period of sixty days, fail to receive or claim payment arising out of such disbursement.

In the event of a purchase under this section, company whose shares are being transferred shall act as a transfer agent for receiving and paying the price to the minority shareholders and for taking delivery of the shares and delivering such shares to the majority, as the case may be.

In the absence of a physical delivery of shares by the shareholders within the time specified by the company, the share certificates shall be deemed to be cancelled, and company whose shares are being transferred shall be authorised to issue shares in lieu of the cancelled shares and complete the transfer in accordance with law and make payment of the price out of deposit made under sub-

section (4) by the majority in advance to the minority by despatch of such payment.

In the event of a majority shareholder or shareholders requiring a full purchase and making payment of price by deposit with the company for any shareholder or shareholders who have died or ceased to exist, or whose heirs, successors, administrators or assignees have not been brought on record by transmission, the right of such shareholders to make an offer for sale of minority equity shareholding shall continue and be available for a period of three years from the date of majority acquisition or majority shareholding.

Where the shares of minority shareholders have been acquired in pursuance of this section and as on or prior to the date of transfer following such acquisition, the shareholders holding seventy-five per cent. or more minority equity shareholding negotiate or reach an understanding on a higher price for any transfer, proposed or agreed upon, of the shares held by them without disclosing the fact or likelihood of transfer taking place on the basis of such negotiation, understanding or agreement, the majority shareholders shall share the additional compensation so received by them with such minority shareholders on a pro rata basis.

When a shareholder or the majority equity shareholder fails to acquire full purchase of the shares of the minority equity shareholders, then, the provisions of this section shall continue to apply to the residual minority equity shareholders, even though,—

- (a) the shares of the company of the residual minority equity shareholder had been delisted; and
- (b) the period of one year or the period specified in the regulations made by the Securities and Exchange Board under the Securities and Exchange Board of India Act, 1992 (15 of 1992), had elapsed.

#### **POWER OF CENTRAL GOVERNMENT TO PROVIDE FOR AMALGAMATION OF COMPANIES IN PUBLIC INTEREST [Section 237]**

- If the Central Government is satisfied that it is essential in the public interest that two or more companies should amalgamate, the Central Government may, by order notified in the Official Gazette, provide for the amalgamation of those companies into a single company with such constitution, with such property, powers, rights, interests, authorities and privileges, and with such liabilities, duties and obligations, as may be specified in the order.
- The order under sub-section (1) may also provide for the continuation by or against the transferee company of any legal proceedings pending by or against any transferor company and such consequential, incidental and supplemental provisions as may, in the opinion of the Central Government, be necessary to give effect to the amalgamation.
- Every member or creditor, including a debenture holder, of each of the transferor companies before the amalgamation shall have, as nearly as may be, the same interest in or rights against the transferee company as he had in the company of which he was originally a member or creditor, and in case the interest or rights of such member or creditor in or against the transferee company are less than his interest in or rights against the original company, he shall be entitled to compensation to that extent, which shall be assessed by such authority as may be prescribed and every such assessment shall be published in the Official Gazette, and the compensation so assessed shall be paid to the member or creditor concerned by the transferee company.
- Any person aggrieved by any assessment of compensation made by the prescribed authority under sub-section (3) may, within a period of thirty days from the date of publication of such assessment in the Official Gazette, prefer an appeal to the Tribunal and thereupon the assessment of the

compensation shall be made by the Tribunal.

- No order shall be made under this section unless—
  - (a) a copy of the proposed order has been sent in draft to each of the companies concerned;
  - (b) the time for preferring an appeal under sub-section (4) has expired, or where any such appeal has been preferred, the appeal has been finally disposed off; and
  - (c) the Central Government has considered, and made such modifications, if any, in the draft order as it may deem fit in the light of suggestions and objections which may be received by it from any such company within such period as the Central Government may fix in that behalf, not being less than two months from the date on which the copy aforesaid is received by that company, or from any class of shareholders therein, or from any creditors or any class of creditors thereof.

The copies of every order made under this section shall, as soon as may be after it has been made, be laid before each House of Parliament.

#### **REGISTRATION OF OFFER OF SCHEMES INVOLVING TRANSFER OF SHARES [Section 238]**

In relation to every offer of a scheme or contract involving the transfer of shares or any class of shares in the transferor company to the transferee company under section 235,—

- (a) every circular containing such offer and recommendation to the members of the transferor company by its directors to accept such offer shall be accompanied by such information and in the manner as prescribed under Rule 28 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 which states that every circular containing the offer of scheme or contract involving transfer of shares or any class of shares and recommendation to the members of the transferor company by its directors to accept such offer, shall be accompanied by such information as set out in Form No. CAA.15. The circular shall be presented to the Registrar for registration.
- (b) every such offer shall contain a statement by or on behalf of the transferee company, disclosing the steps it has taken to ensure that necessary cash will be available; and
- (c) every such circular shall be presented to the Registrar for registration and no such circular shall be issued until it is so registered:

Provided that the Registrar may refuse, for reasons to be recorded in writing, to register any such circular which does not contain the information required to be given under clause (a) or which sets out such information in a manner likely to give a false impression, and communicate such refusal to the parties within thirty days of the application.

An appeal shall lie to the Tribunal against an order of the Registrar refusing to register any circular under sub-section (1).

The director who issues a circular which has not been presented for registration and registered under clause (c) of sub-section (1), shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees.

#### **PRESERVATION OF BOOKS AND PAPERS OF AMALGAMATED COMPANIES [Section 239]**

The books and papers of a company which has been amalgamated with, or whose shares have been acquired by, another company under this Chapter shall not be disposed of without the prior permission of the Central Government and before granting such permission, that Government may appoint a person to

examine the books and papers or any of them for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion or formation, or the management of the affairs, of the transferor company or its amalgamation or the acquisition of its shares.

### **Liability of Officers in Respect of Offences Committed Prior to Merger, Amalgamation, etc. [Section 240]**

Notwithstanding anything in any other law for the time being in force, the liability in respect of offences committed under this Act by the officers in default, of the transferor company prior to its merger, amalgamation or acquisition shall continue after such merger, amalgamation or acquisition.

## **“MAJORITY RULE AND MINORITY RIGHTS”**

### **The Principle of Non-interference (Rule in *Foss v. Harbottle*)**

The general principle of company law is that every member holds equal rights with other members of the company in the same class. The scale of rights of members of the same class must be held evenly for smooth functioning of the company. In case of difference(s) 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 v. Harbottle* 67 E.R. 189; (1843) 2 Hare 461 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.

## **CASE LAW**

In *Foss v. Harbottle*, two shareholders, Foss and Turton brought an action on behalf of themselves and all other shareholders against the directors and solicitor of the company alleging that by their concerted and illegal transactions they had caused the company's property to be lost to the company. It was also alleged that there was no qualified Board. Foss and Turton claimed damages to be paid by the defendants to the company. It was held by the court that the action could not be brought by the minority shareholders although there was nothing to prevent the company itself, acting through the majority of its shareholders, bringing action. The wrong done to the company was not which could be ratified by the majority of members. The company (i.e. the majority) is the proper plaintiff for wrong done to the company, so the majority of members are competent to decide whether to commence proceedings against the directors. The reasons for rule were nicely stated by Melish L.J. in *MacDougall v. Gardiner*, (1875) 1 Ch. D. 13 (C.A.) at p. 25 in the following words:

“If the thing complained of is a thing which in substance the majority of company are entitled to do, or if something has been done irregularly which the majority of the company are entitled to do regularly, or if something has been done illegally which the majority of the company are entitled to do legally, there can be no use in having litigation about it, the ultimate end of which is only that a meeting has to be called, and then ultimately the majority gets its wishes.”

In *Rajahmundry Electric Supply Co. v. Nageshwara Rao* AIR 1956 SC 213, the Supreme Court observed that:

“The courts will not, in general, intervene at the instance of shareholders in matters of internal administration, and will not interfere with the management of the company by its directors so long as they are acting within the powers conferred on them under articles of the company. Moreover, if the directors are supported by the majority shareholders in what they do, the minority shareholders can, in general do nothing about it.”

From the above it follows then that a company being a separate legal person from the members who compose it, the company is the proper person to bring an action.

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

In *Edwards v. Halliwell* (1950) 2 All. E.R. 1064, Jenkins, L.J. restated the rule in the following terms: “The rule in *Foss v. Harbottle* comes to no more than this. First, the proper plaintiff in respect of wrong alleged to be done to company is prima facie the company itself. Secondly, where the alleged wrong is a transaction which might be made binding on the company by a simple majority of members, no individual member is allowed to maintain an action in respect of that matter for the simple reason that, if a mere majority of the members of the company is in favour of what has been done, then cadit quaestio... (cannot be questioned). If on the other hand, a simple majority of members of the company or association is against what has been done, then there is no valid reason why the company itself should not sue”.

### Justification and Advantages of the Rule in *Foss v. Harbottle*

The justification for the rule laid down in *Foss v. Harbottle* is that the will of the majority prevails. On becoming a member of a company, a shareholder agrees to submit to the will of the majority. The rule really preserves the right of the majority to decide how the company’s affairs shall be conducted. If any wrong is done to the company, it is only the company itself, acting, as it must always act, through its majority, that can seek to redress and not an individual shareholder.

Moreover, a company is a person at law, the action is vested in it and cannot be brought by a single shareholder. Where there is a corporate body capable of filing a suit for itself to recover property either from its directors or officers or from any other person then that corporate body is the proper plaintiff and the only proper plaintiff [*Gray v. Lewis*, (1873) 8 Ch. Appl. 1035].

The main advantages that flow from the Rule in *Foss v. Harbottle* are of a purely practical nature and are as follows:

1. **Recognition of the separate legal personality of company:** If a company has suffered some injury, and not the individual members, it is the company itself that should seek to redress.
2. **Need to preserve right of majority to decide:** The principle in *Foss v. Harbottle* preserves the right of majority to decide how the affairs of the company shall be conducted. It is fair that the wishes of the majority should prevail.

3. **Multiplicity of futile suits avoided:** Clearly, if every individual member were permitted to sue anyone who had injured the company through a breach of duty, there could be as many suits as there are shareholders. Legal proceedings would never cease, and there would be enormous wastage of time and money.
4. **Litigation at suit of a minority futile if majority does not wish it:** If the irregularity complained of is one which can be subsequently ratified by the majority it is futile to have litigation about it except with the consent of the majority in a general meeting. In *Mac Dougall v. Gardiner*, (1875) 1 Ch. 13 (C.A.), the articles empowered the chairman, with the consent of the meeting, to adjourn a meeting and also provided for taking a poll if demanded by the shareholders. The adjournment was moved, and declared by the chairman to be carried; a poll was then demanded and refused by the chairman. A shareholder brought an action for a declaration that the chairman's conduct was illegal. Held, the action could not be brought by the shareholder; if the chairman was wrong, the company alone could sue.

Application of *Foss v. Harbottle* Rule in Indian context — The Delhi High Court in *ICICI v. Parasrampuriah Synthetic Ltd.* SSL, July 5, 1998 has held that an automatic application of *Foss v. Harbottle* Rule to the Indian corporate realities would be improper. Here the Indian corporate sector does not involve a large number of small individual investors but predominantly financial institutions funding at least 80% of the finance. It is these financial institutions which provide entire funds for the continuous existence and corporate activities. Though they hold only a small percentage of shares, it is these financial institutions which have really provided the finance for the company's existence and, therefore, to exclude them or to render them voiceless on an application of the principles of *Foss v. Harbottle* Rule would be unjust and unfair.

#### **EXCEPTION TO THE RULE IN FOSS V. HARBOTTLE**

The rule in *Foss v. Harbottle* is not absolute but is subject to certain exceptions. In other words, the rule of supremacy of the majority is subject to certain exceptions and thus, minority shareholders are not left helpless, but they are protected by:

- (a) the common law; and
- (b) the provisions of the Companies Act, 2013.

The cases in which the majority rule does not prevail are commonly known as exceptions to the rule in *Foss v. Harbottle* and are available to the minority. In all these cases an individual member may sue for declaration that the resolution complained of is void, or for an injunction to restrain the company from passing it. The said rule will not apply in the following case:

#### **Prevention of Oppression and Mismanagement**

The minority shareholders are empowered to bring action with a view to preventing the majority from oppression and mismanagement. These are the statutory rights of the minority shareholders and find detailed discussion later in the study.

In *Bennet Coleman & Co. and Ors. v. Union of India & Ors.*, (1977) 47 Com Cases 92 (Bom), the Division Bench of the Bombay High Court held that Sections 397 and 398 of the Companies Act, 1956 are intended to avoid winding up of the company if possible and keep it going while at the same time relieving the minority shareholders from acts of oppression and mismanagement or preventing its affairs from being conducted in a manner prejudicial to public interest. Thus, the Court has wide powers to supplant the entire corporate management by resorting to non-corporate management which may take the form of appointing an

administrator or a special officer or a committee of advisers etc., who will be in charge of the affairs of the company.

The exceptions to the rule in *Foss v. Harbottle* are not limited to those covered above. Further exceptions may be admitted where the rules of justice require that an exception to the rule should be made.

It should be noted that the ordinary civil courts are not deprived of the jurisdiction to decide the matters except where the Companies Act expressly excludes it such as matters relating to winding up [*Panipat Woollen & General Mills Co.Ltd. v. R.L. Kaushik*, (1969) 39 Com Cases 249 (Punj & Har)].

## “MAJORITY RULE AND MINORITY RIGHTS” UNDER COMPANIES ACT

In India, the Companies Act attempts to maintain a balance between the rights of majority and minority shareholders by admitting in the rule of the majority but limiting it at the same time by a number of well-defined minority rights, and thus protecting the minority shareholders.

Companies Act, 1956 provided for protection of the minority shareholders from oppression and mismanagement by the majority under Section 397 (Application to Company Law Board for relief in cases of oppression) and 398 (Application to Company Law Board for relief in cases of mismanagement).

Oppression as per Section 397(1) of Companies Act, 1956 was defined as 'when affairs of the company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members' while the term mismanagement was defined under Section 398(1) as 'conducting the affairs of the company in a manner prejudicial to public interest or in a manner prejudicial to the interests of the company or there has been a material change in the management and control of the company, and by reason of such change it is likely that affairs of the company will be conducted in a manner prejudicial to public interest or interest of the company'.

Right to apply to the Company Law Board in case of oppression and/or mismanagement was provided under Section 399 to the minority shareholders meeting the ten percent shareholding or hundred members or one-fifth members limit, as the case may be. However, the Central Government was also provided with the discretionary power to allow any number of shareholders and/or members to apply for relief under Section 397 and 398 in case the limit provided under Section 399 was not met.

Chapter XVI of the Companies Act, 2013 deals with the provisions relating to prevention of oppression and mismanagement of a company. Oppression and mismanagement of a company mean that the affairs of the company are being conducted in a manner that is oppressive and biased against the minority shareholders or any member or members of the company. To prevent the same, there are provisions for the prevention and mismanagement of a company.

The Ministry of Corporate Affairs vide its Notification S.O.1934 (E) dated 1st June 2016 notified section 241 to 245 of the Companies Act, 2013. Section 246 was notified vide Notification S.O.2912 (E) dated 9th September, 2016. These provisions are discussed in detail hereunder.

## PREVENTION OF OPPRESSION AND MISMANAGEMENT

### Meaning of Oppression

The words “oppression” and “mismanagement” are not defined in the Act. The meaning of these words for the purpose of Company Law should be used in a broad generic sense and not in any strict literal sense.

The meaning of the term “oppression” as explained by Lord Cooper in the Scottish case of *Elder v. Elder & Western Ltd.*, (1952) Scottish Cases 49, which has been cited with approval by Wanchoo, J (afterwards C.J.)

of the Supreme Court in *Shanti Prasad v. Kalinga Tubes*, (1965) 1 Comp. L.J. 193 at 204 is as under :

“The essence of the matter seems to be that the conduct complained of should at the lowest, involve a visible departure from the standards of fair dealing, on which every shareholder who entrusts his money to the company is entitled to rely.”

#### CASE LAW

An attempt to force new and more risky objects upon an unwilling minority may in circumstances amount to oppression. This was held in *Re. Hindustan Co-operative Insurance Society Ltd.*, AIR. 1961 Cal. 443 wherein the life insurance business of a company was acquired in 1956 by the Life Insurance Corporation of India on payment of compensation. The directors, who had the majority voting power, refused to distribute this amount among shareholders, rather they passed a special resolution changing the objects of the company to utilise the compensation money for the new objects. This was held to be an “Oppression”. The court observed: “The majority exercised their authority wrongfully, in a manner burdensome, harsh and wrongful. They attempted to force the minority shareholders to invest their money in different kind of business against their will. The minority had invested their money in a life insurance business with all its safeguards and statutory protections. But they were being forced to invest where there would be no such protections or safeguards”.

A similar relief was allowed by the House of Lord in *Scottish Co-operative Wholesale Society v. Mayer* (1959) AC 324. In this case, the society created a subsidiary company to enable it to enter in the rayon industry. Subsequently when the need for the subsidiary ceased to exist, the society adopted a policy of running down its business which depressed the value of its shares. The two petitioners who were managing directors and minority shareholders in the company successfully pleaded “oppression”. The court ordered the society to purchase the minority shares at the value at which they stood before the oppressive policy started [This decision has also been followed in *Re. H.R. Harmer Ltd.*, (1959) 1 WLR 62].

Minor acts of mismanagement, however, are not to be regarded as oppression. As far as possible, shareholders should try to resolve their differences by mutual readjustment. Moreover, the courts will not allow these special remedies to become a vexatious source of litigation. For example, in *Lalita Rajya Lakshmi v. Indian Motor Co.* A.I.R. 1962 Cal 127, the petitioner alleged that the Board of directors were guilty of certain acts detrimental to the minority of the shareholders. The allegations were that the income of the company was deliberately shown less by excessive expenditure; that passengers travelling without ticket on the company’s buses were not checked; that petrol consumption was not properly checked; that second hand buses of the company had been disposed of at low price, that dividends were being declared at too low a figure. It was held that even if each of these allegations were proved to the satisfaction of the court, there would have been no oppression.

A member can complain of oppression only in his capacity as a member and not in his capacity as director or creditor [In *Re. Bellador Silk Ltd.*, (1965) 1 All ER 667].

The legal representatives of a deceased member whose name is still on the register of members are entitled to file a petition under Sections 397 and 398 of the Companies Act, 1956, for relief against oppression or mismanagement, *Worldwide Agencies Pvt. Ltd. and Another v. Mrs. Margaret T. Desor and Others*, Com Cases Vol. 67 (1990), 807 (S.C.).

A shareholder dies and his heirs apply for transmission of shares while their application for succession certificate was pending before the Civil Court. The legal heirs alleged illegal allotment of shares by respondent to themselves, reducing the legal heirs to minority. It has held that the legal heirs are entitled to

file a petition alleging oppression and mismanagement. [*Rajkumar Devraj & Aur. v. Jai Mahal Hotels Pvt. Ltd. & Others* (CLB) CA. No. 133 of 2006 in C.P. No. 30 of 2006.

It should not, however, be supposed that these special remedies against oppression or mismanagement are available only to minorities. "In an appropriate case, if the court is satisfied about the act of oppression or mismanagement, relief can be granted even if the application is made by a majority, who have been rendered completely ineffective by the wrongful acts of a minority group. "Accordingly, a relief under the section was allowed to a majority group by Mitra, J., of the Calcutta High Court in *In Re. Sindhri Iron Foundry (P) Ltd.* (1963) 68 CWN 118. His Lordship observed that "if the court 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 to the hands of unauthorised persons who have taken wrongful possession and who claim to be the shareholders and directors there is no reason why the court should not make appropriate order to put an end to such matters.

Referring to the argument that the majority could always call a meeting and put things in order by passing resolutions, his Lordship said:

"The facts in this case show very clearly, that there is no chance of redress in the domestic forum of the company. If a Board meeting was to be called, one group would contend that there were five directors, whereas the other group would urge that there were seven. If a meeting of the shareholders was to be convened, according to one group there would be only sixteen shareholders, while according to the other the number would exceed twenty-five ... There would be complete chaos and confusion ... " (*Ibid.*, p. 335).

"This ingenious remedy has not only permitted redressal of many abuses, but its mere availability has had a deterrent effect upon management." [George H. Hornstein: *The Future of Corporate Control*, (1950) 63 HLR 476].

It was held in the case of *Ajit Singh Ahuja v. Sapphire (India) (P) Ltd.* [(2009) 1 Comp LJ 313 (CLB)] that in a case of oppression, a member has to specifically plead on five facts – (a) what is the alleged act of oppression; (b) who committed the act of oppression; (c) how it is oppressive; (d) whether it is in the affairs of the company; and (e) whether the company is party to the commission of the act of oppression.

Oppression must be a continuous process. This is suggested by the words, 'are being conducted in a manner...' used in Section 397. Hence isolated acts of oppression or mismanagement will not give rise to an action under Section 397 of the Act. In *Shanti Pd. Jain's Case*, the court said:... "events have to be considered not in isolation but as a part of a consecutive story. There must be continuous acts on the part of the majority shareholders, continuing up-to-date of petition".

However in *Tea Brokers P. Ltd. v. Hemendra Prosad Barooah* (1998) 5 Comp LJ 963 (Cal.) the Division Bench of Calcutta High Court observed that:

'This is undoubtedly, a right and privilege which a member enjoys in his capacity as a member of the company... such an act may be even a single act done on one particular occasion if the effect of such an act will be of a continuing nature and the member concerned is deprived of his rights and privilege for all time to come in future'.

In *Ramshankar Prasad v. Sindu Iron Foundry (P) Ltd.*, AIR 1966 Cal 512, it was held that a petition under Section 397, would be maintainable even if the oppression was of a short duration and of a singular conduct if its effects persisted indefinitely [followed in *Maharashtra Power Development Corporation. Ltd. v. Dabhol Power Co. Ltd.* (2003) 56 CLA 263 (Bom.)].

In *Bhagirath Agarwala v. Tara Properties P. Ltd.* (2003) 51 CLA 57 (Cal.), also the removal of a director and allotment of shares were set aside as they were done at a meeting which was covered without complying with the requirements of Section 286 and also reflected an oppressive policy. The allotment was made only to one member without simultaneous offer to others on pro rata basis. A single act of issue of additional shares can have a continuous effect. It can constitute oppression. A relief can be had against it. There is no bar of limitation in such a case. [*Ashok Kumar Oswal v. Panchsher Textile Mfg. & Trading Co. Ltd.* (2002) 110 Com Cases 800 (CLB-PB)].

Past acts of oppression will not entitle a plaintiff to seek the remedy under Section 397. The purpose of this section is not so much to take up the past as to redeem the future. A catalogue of charges of the past alleged misdeeds will not attract the section [*Thakur Prem Singh v. Thakur Hotel (Simla) Co. (P) Ltd.*, AIR 1963 Punj. 63; *Raghunath Swarup Mathur v. Har Swarup Mathur*, (1970) 40 Com Cases 282 (All)].

## Provisions under Companies Act, 2013

### APPLICATION TO TRIBUNAL FOR RELIEF IN CASE OF OPPRESSION & MISMANAGEMENT (SECTION 241)

#### A. BY ANY MEMBER OF A COMPANY

Section 241 of the Companies Act, 2013 states that any member of a company, who has right to apply under section 244, may apply to the Tribunal for complains that—

- (a) 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, whether by -
  - an 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,

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,

However, such material change shall not be a change brought about by, or in the interests of, any creditors, including debenture holders or any class of shareholders of the company.

#### B. BY CENTRAL GOVERNMENT

The Central Government, if it is of the opinion that the affairs of the company are being conducted in a manner prejudicial to public interest, it may itself apply to the Tribunal for an order.

### RIGHT TO APPLY UNDER SECTION 244 (SECTION 244)

Sub – section (1) of Section 244 states that following members of a company shall have the right to apply under section 241, namely:—

- (a) *In the case of a company having a share capital -*

- (i) not less than one hundred members of the company, or
  - (ii) not less than one-tenth of the total number of its members, Whichever is less; or
  - (iii) any member or members holding not less than one tenth of the issued share capital of the company, subject to the condition that the applicant or applicants has or have paid all calls and other sums due on his or their shares;
- (b) In the case of a company not having a share capital -
- (i) not less than one-fifth of the total number of its members shall have the right to apply under section 241.

For the purposes of this sub-section, 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 under sub-section (1), 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.

## **POWER OF TRIBUNAL**

### **Power of Tribunal to waive requirements to apply specified under Section 244**

Proviso to section 244 states that the Tribunal may, on an application made to it in this behalf, waive all or any of the requirements specified in clause (a) or clause (b) of sub – section (1) of Section 244 so as to enable the members to apply under Section 241.

### **Power of Tribunal to issue orders [Section 242(1)]**

On any application made under section 241, the Tribunal is of the opinion—

- (a) that the company's affairs have been or are being conducted in a manner prejudicial or oppressive to any member or members or prejudicial to public interest or in a manner prejudicial to the interests of the company; and
- (b) that to wind up the company would unfairly prejudice such member or members, but that otherwise the facts would justify the making of a winding-up order on the ground that it was just and equitable that the company should be wound up, the Tribunal may, with a view to bringing to an end the matters complained of, make such order as it thinks fit.

### **Filing of copy of Order of Tribunal [Section 242(3)]**

Section 242(3) provides that a certified copy of the order of the Tribunal under section 242(1) shall be filed by the company with the Registrar within 30 days of the order of the Tribunal.

### **Details in Order passed by Tribunal [Section 242(2)]**

An order made by the Tribunal under sub – section (1) shall provide for—

- (a) the regulation of conduct of affairs of the company in future;
- (b) the purchase of shares or interests of any members of the company by other members thereof or by the company;
- (c) in the case of a purchase of its shares by the company as aforesaid, the consequent reduction of its share capital;

- (d) restrictions on the transfer or allotment of the shares of the company;
- (e) the termination, setting aside or modification, of any agreement, howsoever arrived at, between the company and the managing director, any other director or manager, upon such terms and conditions as may, in the opinion of the Tribunal, be just and equitable in the circumstances of the case;
- (f) the termination, setting aside or modification of any agreement between the company and any person other than those referred to in clause (e):

Provided that no such agreement shall be terminated, set aside or modified except after due notice and after obtaining the consent of the party concerned;

- (g) the setting aside of any transfer, delivery of goods, payment, execution or other act relating to property made or done by or against the company within three months before the date of the application under this section, which would, if made or done by or against an individual, be deemed in his insolvency to be a fraudulent preference;
- (h) removal of the managing director, manager or any of the directors of the company;
- (i) recovery of undue gains made by any managing director, manager or director during the period of his appointment as such and the manner of utilisation of the recovery including transfer to Investor Education and Protection Fund or repayment to identifiable victims;
- (j) the manner in which the managing director or manager of the company may be appointed subsequent to an order removing the existing managing director or manager of the company made under clause (h);
- (k) appointment of such number of persons as directors, who may be required by the Tribunal to report to the Tribunal on such matters as the Tribunal may direct;
- (l) imposition of costs as may be deemed fit by the Tribunal;
- (m) any other matter for which, in the opinion of the Tribunal, it is just and equitable that provision should be made.

#### **Interim Order [Section 242(4)]**

The Tribunal may, on the application of any party to the proceeding, make any interim order which it thinks fit for regulating the conduct of the company's affairs upon such terms and conditions as appear to it to be just and equitable.

#### **Alteration in Memorandum or Articles**

Where an order of the Tribunal makes any alteration in the memorandum or articles of a company, then, the company shall not have power, except to the extent, if any, permitted in the order, to make, without the leave of the Tribunal, any alteration whatsoever which is inconsistent with the order, either in the memorandum or in the articles. *[Section 242(5)]*

The alterations made by the order in the memorandum or articles of a company shall, in all respects, have the same effect as if they had been duly made by the company in accordance with the provisions of this Act and the said provisions shall apply accordingly to the memorandum or articles so altered. *[Section 242(6)]*

A certified copy of every order altering, or giving leave to alter, a company's memorandum or articles, shall within thirty days after the making thereof, be filed by the company with the Registrar who shall register the same. *[Section 242(7)]*

However, if a company contravenes the provisions of sub-section (5) of Section 242, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees, or with both.

### **CONSEQUENCE OF TERMINATION OR MODIFICATION OF AGREEMENTS (SECTION 243)**

Where an order made under Section 242 terminates, sets aside or modifies an agreement—

- (a) such order shall not give rise to any claims whatever against the company by any person for damages or for compensation for loss of office or in any other respect either in pursuance of the agreement or otherwise;
- (b) no managing director or other director or manager whose agreement is so terminated or set aside shall, for a period of five years from the date of the order terminating or setting aside the agreement, without the leave of the Tribunal, be appointed, or act, as the managing director or other director or manager of the company.

Provided that the Tribunal shall not grant leave under this clause unless notice of the intention to apply for leave has been served on the Central Government and that Government has been given a reasonable opportunity of being heard in the matter.

### **CLASS ACTION SUITS (Section 245)**

The initiation of class action suits is one of the major changes introduced by the Companies Act, 2013. The major objective behind the provision of class action suits is to safeguard the interests of the minority shareholders. So, class action suits are expected to play an important role to address numerous prejudicial and abusive acts committed by the Board of Directors and other managerial personnel as it has been statutorily recognized under the Companies Act, 2013.

#### **What is a class action suit?**

A class action suit is a lawsuit where a group of people representing a common interest may approach the Tribunal to sue or be sued. It is a procedural instrument that enables one or more plaintiffs to file and prosecute litigation on behalf of a larger group or class having common rights and grievances.

#### **Application of Class Action and Reliefs [Section 245(1)]**

Sub - section (1) of section 245 states that such number of members, depositor or any class of them, as the case may be, may, file an application before the Tribunal for seeking all or any of the following orders, namely:—

- (a) to restrain the company from committing an act which is ultra vires the articles or memorandum of the company;
- (b) to restrain the company from committing breach of any provision of the company's memorandum or articles;
- (c) to declare a resolution altering the memorandum or articles of the company as void if the resolution was passed by suppression of material facts or obtained by mis-statement to the members or depositors;
- (d) to restrain the company and its directors from acting on such resolution;
- (e) to restrain the company from doing an act which is contrary to the provisions of this Act or any other

law for the time being in force;

- (f) to restrain the company from taking action contrary to any resolution passed by the members;
- (g) to claim damages or compensation or demand any other suitable action from or against—
  - (i) the company or its directors for any fraudulent, unlawful or wrongful act or omission or conduct or any likely act or omission or conduct on its or their part;
  - (ii) the auditor including audit firm of the company for any improper or misleading statement of particulars made in his audit report or for any fraudulent, unlawful or wrongful act or conduct; or
  - (iii) any expert or advisor or consultant or any other person for any incorrect or misleading statement made to the company or for any fraudulent, unlawful or wrongful act or conduct or any likely act or conduct on his part;
- (h) to seek any other remedy as the Tribunal may deem fit.

Such application may be filed by the members, depositor or any class of them, as the case may be, 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.

Sub-section (10) of Section 245 states that subject to the compliance of this section, an application may be filed or any other action may be taken under this section by any person, group of persons or any association of persons representing the persons affected by any act or omission, specified in sub-section (1).

#### **Liability of Audit Firm and its Partners [Section 245(2)]**

Where the members or depositors seek any damages or compensation or demand any other suitable action from or 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 of particulars in the audit report or who acted in a fraudulent, unlawful or wrongful manner.

#### **Required Number of Applicants [Section 245(3)]**

The requisite number of members provided in sub-section (1) of Section 245, shall be as under:—

##### **A. In case, application by Members:**

- (a) In the case of a company having a share capital -
  - (i) not less than one hundred members of the company, or
  - (ii) not less than such percentage of the total number of its members as may be prescribed,

Whichever is less; or

  - (iii) any member or members holding not less than such percentage of the issued share capital of the company as may be prescribed, subject to the condition that the applicant or applicants has or have paid all calls and other sums due on his or their shares;
- (b) In the case of a company not having a share capital -
  - (ii) not less than one-fifth of the total number of its members.

##### **B. In case, application by Depositors:**

- (i) Not less than one hundred depositors of the company, or

- (ii) Not less than such percentage of the total number of depositors as may be prescribed,  
*Whichever is less shall have right to apply.*
- (iii) Any depositor or depositors to whom the company owes such percentage of total deposits of the company as may be prescribed shall also have right to apply.

An application may be filed or any other action may be taken under this section by any person, group of persons or any association of persons representing the persons affected by any act or omission, specified in sub-section (1).

#### **Requirement for Consideration of Application [ Section 245(4)]**

In considering an application for class action, the Tribunal shall take into account, in particular—

- (a) whether the member or depositor is acting in good faith in making the application for seeking an order;
- (b) any evidence before it as to the involvement of any person other than directors or officers of the company on any of the matters provided in clauses (a) to (f) of subsection (1);
- (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 this section;
- (d) any evidence before it as to the views of the members or depositors of the company who have no personal interest, direct or indirect, in the matter being proceeded under this section;
- (e) where the cause of action is an act or omission that is yet to occur, whether the act or omission could be, and in the circumstances would be likely to be—
  - (i) authorised by the company before it occurs; or
  - (ii) ratified by the company after it occurs;
- (f) where the cause of action is an act or omission that has already occurred, whether the act or omission could be, and in the circumstances would be likely to be, ratified by the company.

#### **In case of admission of application**

Section 245(5) provides that if an application filed for class action is admitted, then the Tribunal shall have regard to the following, namely:—

- (a) public notice shall be served on admission of the application to all the members or depositors of the class in such manner as may be prescribed;
- (b) all similar applications prevalent in any jurisdiction should be consolidated into a single application and the class members or depositors should be allowed to choose the lead applicant and in the event the members or depositors of the class are unable to come to a consensus, the Tribunal shall have the power to appoint a lead applicant, who shall be in charge of the proceedings from the applicant's side;
- (c) two class action applications for the same cause of action shall not be allowed;
- (d) 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.

### Effects of Order

Order shall be binding: 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. [Section 245(6)]

Punishment for non-compliance: Any company which fails to comply with an order passed by the Tribunal under this section shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years and with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees. [Section 245(7)]

### Frivolous or vexatious Application [Section 245(8)]

Where any application filed before the Tribunal is found to be frivolous or vexatious, it shall, for reasons to be recorded in writing, reject the application and make an order that the applicant shall pay to the opposite party such cost, not exceeding one lakh rupees, as may be specified in the order.

### Exemption to Banking Company [Section 245(9)]

This Section is not applicable to Banking Company. Nothing contained in under section 245 of the companies Act, 2013 shall apply to a banking company.

### APPLICATION OF CERTAIN PROVISIONS TO PROCEEDINGS UNDER SECTION 241 OR SECTION 245 – (SECTION 246)

According to Section 246, the provisions of sections 337 to 341 (both inclusive) shall apply mutatis mutandis, in relation to an application made to the Tribunal under section 241 or section 245.

- Penalty for fraud by officers (Section 337):
- Liability for proper account not kept (Section 338):
- Liability for fraudulent conduct of business (Section 339):
- Power of Tribunal to assess damages against delinquent directors, etc. (Section 340):
- Liability under Sections 339 and 340 to extend to partners or directors in Firms or
- Companies (Section 341).

### WINDING UP OF COMPANIES

Winding up of a company is defined as a process by which the life of a company is brought to an end and its property administered for the benefit of its members and creditors. In words of Professor Gower, "Winding up of a company is the process whereby its life is ended and its Property is administered for the benefit of its members & creditors. An Administrator, called a liquidator is appointed and he takes control of the company, collects its assets, pays its debts and finally distributes any surplus among the members in accordance with their rights."

According to Halsbury's Laws of England, "Winding up is a proceeding by means of which the dissolution of a company is brought about & in the course of which its assets are collected and realised; and applied in payment of its debts; and when these are satisfied, the remaining amount is applied for returning to its members the sums which they have contributed to the company in accordance with Articles of the Company." Winding up is a legal process.

Under the process, the life of the company is ended & its property is administered for the benefits of the members & creditors. A liquidator is appointed to realise the assets & properties of the company. After payments of the debts, if any surplus of assets is left out they will be distributed among the members according to their rights. Winding up does not necessarily mean that the company is insolvent. A perfectly solvent company may be wound up by the approval of members in a general meeting.

There are differences between winding up and dissolution. At the end of winding up, the company will have no assets or liabilities. When the affairs of a company are completely wound up, the dissolution of the company takes place. On dissolution, the company's name is struck off the register of the companies and its legal personality as a corporation comes to an end.

### **Legal provisions for Winding Up of Companies**

Section 2(94A) of the Companies Act 2013 provides the following definition of Winding up.

Winding up" means winding up under this Act or liquidation under the Insolvency and Bankruptcy Code, 2016, as applicable."Winding up" means winding up under this Act or liquidation under the Insolvency and Bankruptcy Code, 2016, as applicable.

The procedures for Winding up of companies are provided under Chapter XX of the Companies Act, 2013 and Insolvency and Bankruptcy Code of India 2016.

The Insolvency and Bankruptcy Code, 2016 is an act to consolidate and amend the laws relating to reorganisation and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner for maximisation of value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders including alteration in the order of priority of payment of Government dues and to establish an Insolvency and Bankruptcy Board of India, and for matters connected therewith or incidental thereto. The Insolvency and Bankruptcy Code, 2016 (IBC) was passed by the Parliament on 11 May 2016, received Presidential assent on 28 May 2016 and was notified in the official gazette on the same day.

### **Winding Up by the Tribunal**

Section 270 of the Companies Act, 2013 provides that the provisions of Part I of Chapter XX of the Companies Act, 2013 shall apply to the winding up of a company by the Tribunal under this Act.

### **Circumstances in Which Company May be Wound Up by Tribunal**

Section 271 of the Companies Act, 2013 provides that a company may, on a petition under section 272, be wound up by the Tribunal under following circumstances-

- (a) if the company has, by special resolution, resolved that the company be wound up by the Tribunal;
- (b) 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;
- (c) if on an application made by the Registrar or any other person authorised 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;
- (d) 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; or

(e) if the Tribunal is of the opinion that it is just and equitable that the company should be wound up."

### **Petition for Winding Up**

Section 272(1) of the Companies Act, 2013 provides that subject to the provisions of this section, a petition to the Tribunal for the winding up of a company shall be presented by—

- (a) the company;
- (b) any contributory or contributories;
- (c) all or any of the persons specified in clauses (a) and (b);
- (d) the Registrar;
- (e) any person authorised by the Central Government in that behalf; or
- (f) in a case falling under clause (b) of section 271, by the Central Government or a State Government.

A contributory shall be entitled to present a petition for the winding up of a company, notwithstanding that he may be the holder of fully paid-up shares, or that the company may have no assets at all or may have no surplus assets left for distribution among the shareholders after the satisfaction of its liabilities, and shares in respect of which he is a contributory or some of them were either originally allotted to him or have been held by him, and registered in his name, for at least six months during the eighteen months immediately before the commencement of the winding up or have devolved on him through the death of a former holder. [Section 272(2)]

The Registrar shall be entitled to present a petition for winding up under section 271, except on the grounds specified in clause (a) or clause (e) of that sub-section: Provided that the Registrar shall obtain the previous sanction of the Central Government to the presentation of a petition:

Provided further that the Central Government shall not accord its sanction unless the company has been given a reasonable opportunity of making representations. [Section 272(3)]

A petition presented by the company for winding up before the Tribunal shall be admitted only if accompanied by a statement of affairs in such form and in such manner as may be prescribed. [Section 272(4)]

A copy of the petition made under this section shall also be filed with the Registrar and the Registrar shall, without prejudice to any other provisions, submit his views to the Tribunal within sixty days of receipt of such petition. [Section 272(4)]

### **Powers of Tribunal**

Section 273(1) of the Companies Act, 2013 provides the Tribunal may, on receipt of a petition for winding up under section 272 pass any of the following orders, namely:—

- (a) dismiss it, with or without costs;
- (b) make any interim order as it thinks fit;
- (c) appoint a provisional liquidator of the company till the making of a winding up order;
- (d) make an order for the winding up of the company with or without costs; or

(e) any other order as it thinks fit:

Provided that an order under this sub-section shall be made within ninety days from the date of presentation of the petition:

Provided further that before appointing a provisional liquidator under clause (c), the Tribunal shall give notice to the company and afford a reasonable opportunity to it to make its representations, if any, unless for special reasons to be recorded in writing, the Tribunal thinks fit to dispense with such notice:

Provided also that the Tribunal shall not refuse to make a winding up order on the ground only that the assets of the company have been mortgaged for an amount equal to or in excess of those assets, or that the company has no assets.

Section 273(2) of the Companies Act, 2013 provides where a petition is presented on the ground that it is just and equitable that the company should be wound up, the Tribunal may refuse to make an order of winding up, if it is of the opinion that some other remedy is available to the petitioners and that they are acting unreasonably in seeking to have the company wound up instead of pursuing the other remedy.

### **Company Liquidators**

Section 275 (1) and (2) of the Companies Act, 2013 provides that for the purposes of winding up of a company by the Tribunal, the Tribunal at the time of the passing of the order of winding up, shall appoint a Provisional Liquidator or the Company Liquidator, as the case may, from amongst the insolvency professionals registered under the Insolvency and Bankruptcy Code, 2016.

### **Voluntary Winding up**

Chapter V of the Insolvency and Bankruptcy Code of India 2016 deals with the Voluntary Liquidation of Corporate Persons.

#### **Section 59**

- (1) A corporate person who intends to liquidate itself voluntarily and has not committed any default may initiate voluntary liquidation proceedings under the provisions of this Chapter.
- (2) The voluntary liquidation of a corporate person under sub-section (1) shall meet such conditions (3) and procedural requirements as may be specified by the Board.
- (3) Without prejudice to sub-section (2), voluntary liquidation proceedings of a corporate person registered as a company shall meet the following conditions, namely:—
  - (a) a declaration from majority of the directors of the company verified by an affidavit stating that—
    - (i) they have made a full inquiry into the affairs of the company and they have formed an opinion that either the company has no debt or that it will be able to pay its debts in full from the proceeds of assets to be sold in the voluntary liquidation; and
    - (ii) the company is not being liquidated to defraud any person;
  - (b) the declaration under sub-clause (a) shall be accompanied with the following documents, namely:—
    - (i) audited financial statements and record of business operations of the company for the previous two years or for the period since its incorporation, whichever is later;
    - (ii) a report of the valuation of the assets of the company, if any prepared by a registered valuer;

- (c) within four weeks of a declaration under sub-clause (a), there shall be—
- (i) a special resolution of the members of the company in a general meeting requiring the company to be liquidated voluntarily and appointing an insolvency professional to act as the liquidator; or
  - (ii) a resolution of the members of the company in a general meeting requiring the company to be liquidated voluntarily as a result of expiry of the period of its duration, if any, fixed by its articles or on the occurrence of any event in respect of which the articles provide that the company shall be dissolved, as the case may be and appointing an insolvency professional to act as the liquidator: Provided that the company owes any debt to any person, creditors representing two thirds in value of the debt of the company shall approve the resolution passed under sub-clause (c) within seven days of such resolution.
- (4) The company shall notify the Registrar of Companies and the Board about the resolution under sub-section (3) to liquidate the company within seven days of such resolution or the subsequent approval by the creditors, as the case may be.
  - (5) Subject to approval of the creditors under sub-section (3), the voluntary liquidation proceedings in respect of a company shall be deemed to have commenced from the date of passing of the resolution under sub-clause (c) of sub-section (3).
  - (6) The provisions of sections 35 to 53 of Chapter III and Chapter VII shall apply to voluntary liquidation proceedings for corporate persons with such modifications as may be necessary.
  - (7) Where the affairs of the corporate person have been completely wound up, and its assets completely liquidated, the liquidator shall make an application to the Adjudicating Authority for the dissolution of such corporate person.
  - (8) The Adjudicating Authority shall on an application filed by the liquidator under sub-section (7), pass an order that the corporate debtor shall be dissolved from the date of that order and the corporate debtor shall be dissolved accordingly.
  - (9) A copy of an order under sub-section (8) shall within fourteen days from the date of such order, be forwarded to the authority with which the corporate person is registered.

#### ***Provisions applicable to every mode of winding up***

Part III of Chapter XX of the Companies Act, 2013 provides for following Sections which are applicable to every mode of winding up.

- 324 - Debts of all Descriptions to be Admitted to Proof
- 326 - Overriding Preferential Payments
- 327 - Preferential Payments
- 328 - Fraudulent Preference
- 329 - Transfers Not in Good Faith to be Void
- 330 - Certain Transfers to be Void
- 331 - Liabilities and Rights of Certain Persons Fraudulently Preferred
- 332 - Effect of Floating Charge
- 333 - Disclaimer of Onerous Property

- 334 - Transfers, etc., After Commencement of Winding Up to be Void
- 335 - Certain Attachments, Executions, etc., in Winding Up by Tribunal to be Void
- 336 - Offences by Officers of Companies in Liquidation
- 337 - Penalty for Frauds by Officers
- 338 - Liability Where Proper Accounts not Kept
- 339 - Liability for Fraudulent Conduct of Business
- 340 - Power of Tribunal to Assess Damages Against Delinquent Directors, etc.
- 341 - Liability Under Sections 339 and 340 to Extend to Partners or Directors in Firms or Companies
- 342 - Prosecution of Delinquent Officers and Members of Company
- 343 - Company Liquidator to Exercise Certain Powers Subject to Sanction
- 344 - Statement that Company is in Liquidation
- 345 - Books and Papers of Company to be Evidence
- 346 - Inspection of Books and Papers by Creditors and Contributories
- 347 - Disposal of Books and Papers of Company
- 348 - Information as to Pending liquidations
- 349 - Official Liquidator to Make Payments into Public Account of India
- 350 - Company Liquidator to Deposit Monies into Scheduled Bank
- 351 - Liquidator Not to Deposit Monies into Private Banking Account
- 352 - Company Liquidation Dividend and Undistributed Assets Account
- 353 - Liquidator to Make Returns, etc.
- 354 - Meetings to Ascertain Wishes of Creditors or Contributories
- 355 - Court, Tribunal or Person, etc., Before Whom Affidavit May be Sworn
- 356 - Powers of Tribunal to Declare Dissolution of Company Void
- 357 - Commencement of Winding Up by Tribunal
- 358 - Exclusion of Certain Time in Computing Period of Limitation

## OVERVIEW OF REGISTERED VALUERS

### Who shall conduct the valuation?

Section 247(1) of the Companies Act, 2013 states that where a valuation is required to be made in respect of any property, stocks, shares, debentures, securities or goodwill or any other assets or net worth of a company or its liabilities under the provision of the Companies Act, 2013, it shall be valued by a person having such qualifications and experience and registered as a valuer in such manner, on such terms and conditions as may be prescribed and appointed by the audit committee or in its absence by the Board of Directors of that company.

(2) The valuer appointed under sub-section (1) shall,—

- (a) make an impartial, true and fair valuation of any assets which may be required to be valued;
- (b) exercise due diligence while performing the functions as valuer;
- (c) make the valuation in accordance with such rules as may be prescribed; and
- (d) not undertake valuation of any assets in which he has a direct or indirect interest or becomes so interested at any time during a period of three years prior to his appointment as valuer or three years after the valuation of assets was conducted by him.

### **In case of contravention made by the Valuer**

Sub - section (3) of Section 247 states that if a valuer contravenes the provisions of the section 247 or the rules made thereunder, the valuer shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees:

Provided that if the valuer has contravened such provisions with the intention to defraud the company or its members, he shall be punishable with imprisonment for a term which may extend to one year and with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

### **Liability of Valuer**

Sub - section (4) of Section 247 states that where a valuer has been convicted under sub-section (3), he shall be liable to—

- (i) refund the remuneration received by him to the company; and
- (ii) pay for damages to the company or to any other person for loss arising out of incorrect or misleading statements of particulars made in his report.

### **Regulatory authority for Registered Valuer**

The Central Government delegated its powers and functions under section 247 of the Companies Act, 2013 to the Insolvency and Bankruptcy Board of India (IBBI) and specified the IBBI as the Authority under the Companies (Registered Valuers and Valuation) Rules, 2017.

### **Institute of Company Secretaries of India – Registered Valuer Organisation (ICSI-RVO)**

#### **What is ICSI – RVO?**

As specified above, Section 247 of the Companies Act, 2013 provides that where a valuation is required to be made in respect of any assets it shall be valued by a person who, having the necessary qualifications and experience, and being a valuer member of a recognised valuer organisation, is registered as a valuer with the Authority. Accordingly, to enable the members of the Institute/others to practice as Registered Valuers, the Institute incorporated **ICSI-RVO**.

**ICSI- RVO** is a Section 8 company which has been formed with the intent to enrol, register, educate, train, promote, develop and regulate Registered Valuers Rules while establishing and promoting high standards of practice and professional conduct and furthermore, to promote good professionalism, ethical conduct and competency of Registered Valuers for ensuring quality of valuation work.

The IBBI vide Registered Valuers Organisation Recognition No. IBBI/RVO/2018/003 recognised ICSI RVO as a Registered Valuers Organisation for the Asset Class(es):-

- (i) Land and Building
- (ii) Plant and Machinery
- (iii) Securities or Financial Assets

### Who can offer Valuation services?

For conducting valuations required under the Companies Act, 2013 and the Insolvency and Bankruptcy Code, 2016, a person is to be registered with the IBBI as a registered valuer. For registering with IBBI, a person must have necessary qualification and experience, has to be enrolled as a valuer member with a Registered Valuer Organisation (RVO), has to complete a recognised educational course conducted by the RVO, and pass valuation examination conducted by IBBI.

IBBI, being the Authority, in pursuance of the first proviso to rule 5 (1) of the Companies (Registered Valuers and Valuation) Rules, 2017 specified the details of educational course for the Asset Class of 'Securities or Financial Assets'. These courses shall be delivered by the RVOs in not less than 50 hours.

A person, who is rendering valuation services under the Companies Act, 2013, may continue to do so without a certificate of registration up to 31st March, 2018, thereafter with effect from 1st April, 2018 for conducting valuations required under the Companies Act, 2013 and the Insolvency and Bankruptcy Code, 2016, a person is to be registered with the IBBI as a registered valuer.

In pursuance of the Rule 5 (3) of the Companies (Registered Valuers and Valuation) Rules, 2017, IBBI, being the Authority, has also published the syllabus, format and frequency of the valuation examination for the Asset Class of 'Securities or Financial Assets'. A person wishing to be a valuer needs to pass this valuation examination.

## REGISTRATION OFFICES AND FEES

### Registration of Documents

Section 403 states that any document, required to be submitted, filed, registered or recorded, or any fact or information required or authorised to be registered under the Companies Act, 2013, shall be submitted, filed, registered or recorded within the time specified in the relevant provision on payment of such fee as may be prescribed. The fees is prescribed under the Companies (Registration Offices and fees) Rules, 2014.

However, in case of failure to submit, file or register or record the above stated documents, within the period provided in the relevant section, it may, without prejudice to any other legal action or liability under the Companies Act, 2013, be submitted, filed, registered or recorded as the case may be :-

- (a) In case of documents provided under Section 92 or 137 [First proviso to Section 403]
  - after expiry of the period so provided *under Section 92 or 137*,
  - on payment of such additional fee as may be prescribed –
    - (i) which shall not be less than one hundred rupees per day, and
    - (ii) different amounts may be prescribed for different classes of companies.
  
- (b) In case of any other documents [*Second proviso to Section 403*]:-
  - after expiry of the period so provided under relevant Section,
  - on payment of such additional fee as may be prescribed and different fees may be prescribed for different classes of companies.

### **Continuous Default**

Third proviso to Section 403 states that where there is default on two or more occasions in submitting, filing, registering or recording of the document, fact or information, it may, without prejudice to any other legal action or liability under the Companies Act, 2013, be submitted, filed, registered or recorded, as the case may be, on payment of a higher additional fee, as may be prescribed:-

- which shall not be lesser than twice the additional fee provided under the first or the second proviso to Section 403, as applicable.

### **Punishment on Failure**

Further, sub-section (2) of Section 403 states that where a company fails or commits any default to submit, file, register or record any document, fact or information under sub-section (1) of Section 403 before the expiry of the period specified in the relevant section, the company and the officers of the company who are in default, shall, without prejudice to the liability for the payment of fee and additional fee, be liable for the penalty or punishment provided under the Companies Act, 2013 for such failure or default.

## **COMPANIES TO FURNISH INFORMATION OR STATISTICS**

### **Power of Central Government to Direct Companies to Furnish Information or Statistics**

Section 405 of the Companies, Act, 2013 states that the Central Government may, by order, require companies or any class of companies, to furnish such information or statistics with regard to their or its constitution or working, and within such time, as may be specified in the order.

Every such order shall be published in the Official Gazette and may be addressed to companies or to any class of companies, in such manner, as the Central Government may think fit and the date of such publication shall be deemed to be the date on which requirement for information or statistics is made on such companies or class of companies, as the case may be.

For the purpose of satisfying itself that any information or statistics furnished by a company or companies in pursuance of any order stated above is correct and complete, the Central Government may by order require such company or companies to produce such records or documents in its possession or allow inspection thereof by such officer or furnish such further information as that Government may consider necessary.

### **Failure to furnish information or statistics by the companies required by the Central Government**

If any company fails to comply with an order specified above, or knowingly furnishes any information or statistics which is incorrect or incomplete in any material respect, the company shall be punishable with fine which may extend to twenty-five thousand rupees and every officer of the company who is in default, shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to three lakh rupees, or with both.

### **In case of Foreign Companies**

Where a foreign company carries on business in India, all references to a company in this section shall be deemed to include references to the foreign company in relation, and only in relation, to such business.

## **LESSON ROUND-UP**

- Section 230(1) states that when a compromise or arrangement is proposed—
  - between a company and its creditors or any class of them; or

- between a company and its members or any class of them,
- the Tribunal may, on the application of the (i) company, or (ii) of any creditor or (iii) member of the company, or (iv) in the case of a company which is being wound up, of the liquidator, order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal directs.
- Section 230(6) states that when at a meeting held in pursuance of sub-section (1), majority of persons representing three-fourths in value of the creditors, or class of creditors or members or class of members, as the case may be, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and if such compromise or arrangement is sanctioned by the Tribunal by an order, the same shall be binding on the company, all the creditors, or class of creditors or members or class of members, as the case may be, or, in case of a company being wound up, on the liquidator and the contributories of the company.
- Section 230(8) states that the order of the Tribunal shall be filed with the Registrar by the company within a period of thirty days of the receipt of the order.
- Section 232(1) states that when an application is made to the Tribunal under section 230 for the sanctioning of a compromise or an arrangement proposed between a company and any such persons as are mentioned in that section, and it is shown to the Tribunal—
- that the compromise or arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of the company or companies involving merger or the amalgamation of any two or more companies; and
- that under the scheme, the whole or any part of the undertaking, property or liabilities of any company (hereinafter referred to as the transferor company) is required to be transferred to another company (hereinafter referred to as the transferee company), or is proposed to be divided among and transferred to two or more companies, the Tribunal may on such application, order a meeting of the creditors or class of creditors or the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal may direct and the provisions of sub-sections (3) to (6) of section 230 shall apply mutatis mutandis.
- Section 233 prescribes simplified procedure for Merger or amalgamation of
  - two or more small companies or
  - between a holding company and its wholly-owned subsidiary company, or
  - such other class or classes of companies as may be prescribed
- Section 234(2) states that subject to the provisions of any other law for the time being in force, a foreign company, may with the prior approval of the Reserve Bank of India, merge into a company registered under this Act or vice versa and the terms and conditions of the scheme of merger may provide, among other things, for the payment of consideration to the shareholders of the merging company in cash, or in Depository Receipts, or partly in cash and partly in Depository Receipts, as the case may be, as per the scheme to be drawn up for the purpose.
- Section 237(1) states that when the Central Government is satisfied that it is essential in the public interest that two or more companies should amalgamate, the Central Government may, by order notified in the Official Gazette, provide for the amalgamation of those companies into a single company with such constitution, with such property, powers, rights, interests, authorities and privileges, and with such liabilities, duties and obligations, as may be specified in the order.



# Lesson 13

## An Introduction to MCA 21 and filing in XBRL

### LESSON OUTLINE

- Important Aspects of MCA-21
- MCA Services
- Pre-requisites for e-filing
- Pre-certification of e-forms
- Lesson Round up
- Self-Test Questions

### LEARNING OBJECTIVES

Keeping in tune with the e-governance initiatives the world over, Ministry of Corporate Affairs (MCA), Govt. of India has initiated the MCA-21 project in the year 2006, to enable an easy and secure access to MCA services in a manner that best suits the corporate entities and professionals and of course, the public.

The significant changes brought about by the introduction of MCA-21 project and the e-filing has introduced a sea-change in the process of filing, storage of records and inspection of records of registered companies. Professionals associated with the corporate sector, the individual investors, the Investor Protection Groups and the Prosecuting Agencies of the Government now have easy access to vital data to regulate the affairs of the companies and can also launch prosecutions against the erring companies and their directors/board of management. It is envisaged that since all the relevant data about the concerned companies are filed online and these get stored as master database in the electronic repository, due attention should be given towards filling and filing of the e-forms.

This chapter covers all the important aspects relating to various e-services like e-stamping, e-inspection, filling and filing the e-forms etc. The students may refer to [mca.gov.in](http://mca.gov.in) for the format of various e-Forms

## **E-GOVERNANCE AND MCA -21**

With the advent of Information and Communication Technology in all sectors today, Governments across the globe including the Government of India are taking major initiatives to integrate IT in all their processes. Electronic Governance is the application of Information Technology to the Government functioning in order to bring about Simple, Moral, Accountable, Responsive and Transparent (SMART) Governance. E-governance is a highly complex process requiring provision of hardware, software, networking and re-engineering of the procedures for better delivery of services.

MCA-21 is an ambitious e-governance initiative of Government of India that builds on the Government's vision of National e-governance in the country. As part of the Government's focus on governance norms to meet the expectations arising from globalization, MCA project was launched as a flagship initiative of Ministry of Corporate Affairs (MCA). MCA-21 has resulted in improved procedures for better delivery of services by the Ministry of Corporate Affairs. This reform of administration has not only improved efficiency and transparency in the government operations, but has also enabled the Ministry to concentrate more on policy matters.

This E- governance initiative, in partnership with Private Player, is a fine example of public private partnership, and is built on a BOOT (Built, Operate, Own and Transfer) model. Infosys is currently maintaining this project.

## **MCA- 21 AND ITS LEGAL VALIDITY**

Section 398 of the Companies Act, 2013 has provision related to filing of applications, documents, and inspections in electronic form.

Section 398(1) provides that notwithstanding anything to the contrary contained in this Act, and without prejudice to the provisions contained in section 6 of the Information Technology Act, 2000, the Central Government may make rules so as to require from such date as may be prescribed in the rules that-

Such applications, balance sheet, prospectus, return, declaration, memorandum, articles, particulars of charges, or any other particulars or document as may be required to be filed or delivered under this Act or the rules made there under, shall be filed in the electronic form and authenticated in such manner as may be prescribed;

Such document, notice, any communication or intimation, as may be required to be served or delivered

Under this Act, in the electronic form and authenticated in such manner as may be prescribed;

Such inspection of the memorandum, articles, register, index, balance sheet, return or any other particulars or document maintained in the electronic form, as is otherwise available for inspection under this Act or the rules made there under, may be made by any person through the electronic form in such manner as may be prescribed;

such fees, charges or other sums payable under this Act or the rules made there under shall be paid through the electronic form and in such manner as may be prescribed; and

The Central Government has provided all the e-forms as an annexure to the relevant Rules.

Rule 7 of Companies (Registration offices and fees) Rules, 2014 relates to manner and conditions of filing provides that Every application, financial statement, prospectus, return, declaration, memorandum, articles, particulars of charges, or any other particulars or documents or any notice, or any communication or intimation required to be filed or delivered or served under the Act and rules made there under, shall be filed or delivered or served in computer readable electronic form, in portable document format (pdf) or in such other format as has been specified in any rule or form in respect of such

application or form or document or declaration to the concerned Registrar through the portal maintained by the Central Government on its web-site or through any other website notified by the Central Government.

## **IMPORTANT ASPECTS OF MCA-21**

### **Organization of ROC Office under MCA**

The ROC office working from its present address will virtually become the Back Office of the Ministry. Since the number of companies/entities may find it difficult to switch over to e-Filing at the initial stage,

### **Front Office and Back Office**

#### **Front Office**

The major components involved in this comprehensive e-governance project are front office and back office.

Front Office represents the interface of the corporate and public users with the MCA-21 system. This comprises of Virtual Front Office and Registrar's Front Office.

#### **Virtual front office**

Virtual front office is one of the various channels available to stakeholders (companies and the professionals) to enable them to do the statutory filing with ROC Offices across the country. It merely represents a computer facility for filing of digitally signed e-forms by accessing the MCA portal through internet ([www.mca.gov.in](http://www.mca.gov.in)). It also presupposes availability of related facilities to convert documents into PDF format and scanning of documents wherever required.

#### **Registrar's Front Office (RFO)**

To facilitate the change over from Physical Document Filing to Digital Document Filing, the Ministry started offices known as the Registrar Front Office. It is one of the various channels available to stakeholders to enable them to do the statutory filing with ROC Offices across the country. Registrar's Front Offices are managed and operated by the operator RFO has all facilities which are required for online filing like trained manpower, broadband connectivity, scanner, printer and related computer accessories. This office managed by MCA and TCS/Infosys officials provides free of cost service in all aspects of MCA 21 e-governance projects.

#### **Back Office**

Back Office represents the offices of Registrar of Companies, Regional Directors and Headquarters and takes care of internal processing of the forms filed by the corporate user as per MCA norms and guidelines. The e- forms are routed dynamically to the concerned authority for processing depending upon the assigned role. All the e-forms along with attachments are stored in the electronic depository, which the staff of MCA can view depending upon the access rights.

#### **Certified Filing Centre (CFC)**

In order to provide the Companies to do their e Filing, Professional Institutes (ICSI, ICAI, ICAI-cost), their Regional Councils/ Local chapters, individual practicing members and firms of professionals were authorised to create and set-up the required facilities for facilitating the e Filing process. The Certified Filing Centres, thus set-up by the Professionals are over and above the 53 Registrar's Front Office set-up by the Ministry under the programme. While the services available from the Facilitation Centers set-up by the Ministry are without any charge, the services provided by these Certified Filing Centers entail payment of service charges.

## **SUBSTANTIAL BENEFITS OF MCA21**

### **Elimination of interface with the offices of ROCs, RDs and the MCA**

MCA-21 has been designed virtually to eliminate the physical interface between the companies and the offices of ROCs, RDs and even MCA. It has not only saved time and energy of the company representatives but also enabled them to focus on other creative tasks. Time consuming works of professionals i.e. the tasks of incorporation of new companies, conducting searches of important documents, obtaining certificates of creation, modification and satisfaction of charges, filing of statutory forms and returns etc. have now become very quick and easy.

The problem of becoming defaulter by the company for non-filing of Annual returns due to long queues at ROC offices is now eliminated with e-filing. Conducting search was very painful in physical maintenance of statutory records. E-filing is panacea to all these problems.

### **Effective use of database**

With the help of database collected, the vital information has been collected, segregated in such a way that it can be used by various stakeholders for various purposes. It will help in transparency in operations and benefits to players in stock markets as well as easy and prominent exposure of defaulters.

The following websites are created:

– Website for Investor Education and Protection Fund: <http://iepf.gov.in>

Ministry of Corporate Affairs has set up the Investor Education and Protection Fund (IEPF) with the dedicated purpose of empowering investors through education and awareness building. It has been established under Section 205 C of the Companies Act, 1956 and now under Section 125 of the Companies Act 2013 for promotion of investors awareness and protection of the interests of investors.

There was no unified website providing information on all financial instruments. Moreover, almost all individual websites that exist provide information from their own respective perspectives and not what and how the small investors want it. This website would fulfill the need for an information resource for small investors on all aspects of the financial markets and would attempt to do it in the small investors language.

It would provide information about IEPF and the various activities that have been undertaken/ funded by it. It would also provide information relevant for investors, including about various instruments for investment, regulatory system and grievance redressal mechanism.

– [www.watchoutinvestors.com](http://www.watchoutinvestors.com):

Over the years, thousands of unscrupulous entities have defrauded the investors. Investors have lost confidence in the market consequent to a series of mishaps. In many cases, though penal regulatory action has been taken against such entities, the information about such action is in a difficult-to-access, difficult-to-use format. Absence of any organized database prevents regulators and investors from taking any pre-emptive action [www.watchoutinvestors.com](http://www.watchoutinvestors.com) alerts various entities and about persons with information that one should be aware of before investing. It is sponsored and aided by Investor education and protection fund and Securities and exchange board of India.

[www.watchoutinvestors.com](http://www.watchoutinvestors.com) is a national web-based registry covering entities including companies and intermediaries and, wherever available the persons associated with such entities, who have been indicted for an economic default and/or for non-compliance of laws/guidelines and/or who are no longer in the specified activity.

### **Better supervision and monitoring of compliance**

MCA-21 has ensured better supervision and control of the MCA over Companies with regard to compliance with the provisions of the Companies Act. Thus, enforcement of law has become easier and will ultimately benefit the investors, the stakeholders and the concerned Regulatory bodies. With specific details of companies and their directors available in the electronic form, it ensures proactive & effective compliance of relevant law(s) and also in turn fosters corporate governance.

### **Mutually beneficial system**

The focus of the MCA-21 program is on bringing about a fine balance between trade facilitation on one hand and enforcement requirements on the other.

### **Speed, transparency and efficiency**

MCA-21 project aims to bring speed, transparency and efficiency in the delivery of the services rendered by the MCA to all the stakeholders through a set of pre-defined service levels.

### **Effective due diligence**

Banks and Financial Institutions can conduct a through scrutiny of the documents filed by the company before advancing loan(s) and other financial assistance to such a company.

### **Efficient services by professionals**

Professionals will be able to offer efficient services to their client companies.

### **Environment Friendly**

MCA-21 has also proved to be environment friendly since paper work involved in filing of forms and documents has been eliminated.

## **MCA SERVICES**

The MCA21 application is designed to fully automate all processes related to the proactive enforcement and compliance of the legal requirements under the Companies Act, 1956, Companies Act, 2013 and Limited Liability Partnership Act, 2008. This helps the business community to meet their statutory obligations.

### **Benefits**

The MCA21 application offers the following:

1. Enables the business community to register a company and file statutory documents quickly and easily.
2. Provides easy access of public documents
3. Helps faster and effective resolution of public grievances
4. Helps registration and verification of charges easily
5. Ensures proactive and effective compliance with relevant laws and corporate governance
6. Enables the MCA employees to deliver best of breed services

### **Services offered**

*Obtain Digital Signature Certificate* - The Information Technology Act, 2000 has provisions for use of Digital Signatures on the documents submitted in electronic form in order to ensure the security and authenticity of the documents filed electronically. This is secure and authentic way to submit a document

electronically. As such, all filings done by the companies/LLPs under MCA21 e-Governance programme are required to be filed using Digital Signatures by the person authorised to sign the documents. A user can acquire Digital Signature Certificate(DSC), register DSC and update particulars of the DSC through the MCA Portal.

Apply for Director Identification Number (DIN) - The concept of a Director Identification Number (DIN) was introduced for the first time with the insertion of Sections 266A to 266G of Companies (Amendment) Act, 2006, since then the system has evolved and Companies Act 2013 also makes a provision for obtaining DIN. As such, all the existing and intending Directors have to obtain DIN within the prescribed time-frame as notified.

View master details of any company/LLP registered with Registrar of Companies - A facility has been made available to the general public to view master details of any company/LLP registered with Registrar of Companies. This facility may be availed by clicking "View Company Master Data". A user can view Master Data of a Company or an LLP, signatory details of a particular company, details of companies and directors under prosecution, details of Companies and LLP's registered in the last 30 days, master data of directors specifying the name of Companies/LLP's they are director/ partner in, director/designated partner's details, etc.

Index of Charges - A similar facility has also been made available in respect of the 'Register of Charges' for the companies/LLPs by clicking on to the 'View Index of Charges' and for the viewing the details of the signatories of any company/LLP by clicking on 'View Signatory Details'.

#### **1. LLP Services**

A user can check LLP name, find LLPIN (Limited Liability Partnership Identification Number), avail services related to incorporation of an LLP, services related to annual e-Filing for an LLP, services related to change in LLP information and services related to closure of an LLP.

#### **2. LLP Services for Business User**

A business user can enter or update partner details of an LLP, enter Form 3 or Form 3 & 4 details for LLP filing and verify partner details for filing Annual Return.

#### **3. E-Filing**

A user can download LLP Forms or Company Forms from the Portal, submit application for PAN and TAN, upload e-forms, download Submitted Form for resubmission, check annual filing status of the company, upload details of security holders or debenture holders or depositors.

#### **4. Company Services**

A user can check company name, find CIN (Corporate Identity Number), services related to incorporation of a company, avail services related to compliance filing of a company, services related to change in company information, services related to charge management, informational services and services related to closure of a company.

#### **5. Complaints**

A user can raise service related complaints, track the complaints created, create investor/serious complaint, track the status of complaints created as 'investor/serious complaint', give feedback or suggestions to MCA-21 and raise employee grievances.

#### **6. Document Related Services**

A user can get certified copies of Forms and documents of a company, view forms and documents online etc.

### **7. Fee and Payment Services**

A user can avail services through Enquire Fees, pay later, link NEFT payment, pay miscellaneous fee, pay stamp duty and track the payment status.

### **8. Public Search of Trademark**

A user can search whether trademark has been registered or applied for a particular name by a company.

### **9. Investor Services**

A user can search amount unclaimed/unpaid amount due to be transferred to the Investor Education and Protection Fund (IEPF), upload investor details, confirm uploaded files.

### **Track SRN/Transaction Status**

A user can track the transaction status of the uploaded forms i.e., whether they are approved or pending for approval or required for resubmission or are rejected.

## **E-SERVICES**

### **CENTRAL REGISTRATION CENTRE (CRC)**

The Central Registration Centre (CRC) is an initiative of Ministry of Corporate Affairs (MCA) in Government Process Re-engineering(GPR) with the specific objective of providing speedy incorporation related services in line with global best practices.

CRC is presently tasked to process applications for RUN service for reserving a name and forms related to new companies incorporations (SPICe/ SPICe MOA/ SPICe AOA /INC-22 andDIR-12).

### **INCORPORATION OF COMPANY**

After filing an application electronically through e-form, a company can be incorporated. Once company gets incorporated, CIN is allotted by the Registrar to the company.

### **Corporate Identity Number(CIN)/Foreign Company Registration Number (FCRN)**

Every company is allocated a Corporate Identity Number (CIN). CIN can be found from the MCA-21 portal through search based on:

- ROC Registration No.
- Existing Company Name
- Old Name of Company (in case of change of name, user is required to enter old name and the system displays corresponding current name).
- Inactive CIN [In case of change of CIN, the user is required to enter previous (inactive) CIN Number].

Each Indian company (Listed or Unlisted) has a unique 21 Digit CIN. This is required to be quoted on all e-forms. Once this number is filled, company details are automatically filled in E-Forms issued by MCA by using pre-fill function.

As stated above, CIN is a 21 digit number assigned to every company incorporated on or after November 1, 2000. The Corporate Identity Number allotted to a company indicates listing status, economic activity(industry), state, year of incorporation, ownership and sequential number assigned by ROC (Registration Number).

1 <sup>st</sup> Digit	Listing Status
Next 5 digits	Economic Activity (industry)
Next 2 digits	State
Next 4 digits	Year of Incorporation
Next 3 digits	Ownership. Status of the company ( Private (PTC)/ public ( PLC) / government companies (GOI) etc.....
Last 6 digits	Sequential number assigned by ROC (Registration Number)

### **Foreign Company Registration Number (FCRN)**

Every Foreign Company has been allotted a Foreign Company Registration Number (FCRN).

Corporate Identity Number (CIN), work as a unique identifier of an Indian company. Foreign Company Registration Number (FCRN) is a unique identifier in the case of a Foreign Company.

### **Director Identification Number (DIN)**

DIN is an identification number which the Central Government may allot to any individual, intending to be appointed as director or to any existing directors of a company, for the purpose of his identification

All existing and any person intending to be appointed as a director are required to obtain the Director Identification Number (DIN). DIN is also mandatory for directors of Indian Companies who are not citizens of India. However, DIN is not mandatory for directors of foreign company having branch offices in India. Every individual, who is intending to be appointed as Director of a company or designated partner of a limited liability partnership is required to make an application electronically in Form DIR -3 to Central Government for obtaining Director Identification Number (DIN) or in case the company is being incorporated through Form SPICe, a maximum of three directors can apply for DIN. DIN is a unique identification number and once obtained is valid for life time of a director. A single DIN is required to be obtained irrespective of the number of directorships.

### **RUN FACILITY**

The MCA Affairs has simplified the Company Name Approval Process from 26th January 2017 by introducing a new simple web-based application called RUN (Reserve Unique Name) for Company Registration. RUN (Reserve Unique Name) is a simple and easy process for reserving a name for a new company or for change of name of an existing Company.

This facility can be availed only by a registered user of MCA portal. The complete name of proposed company, including suffix like (OPC) Private Limited / Private Limited / Limited, should be submitted at the time of application for approval. Also, the object of the proposed Company is also to be submitted through RUN application.

In case of change of name of an existing Company the Corporate Identification Number (CIN) of the existing company should be submitted at the time of application through RUN Process to reserve a new name.

### **INTEGRATED PROCESS OF NAME RESERVATION, COMPANY INCORPORATION, DIN ALLOTMENT AND ISSUANCE OF PAN & TAN THROUGH SPICe (FORM INC-32) BY MCA-21**

An integrated process through which reservation of name, incorporation of a new company, application for allotment of DIN and/or application for PAN and TAN can be applied simultaneously through a single application e-Form i.e. Form INC-32 (SPICe).

After filing the SPICe Form and making payment the user is required to visit the MCA portal and access the service 'Submit application for PAN and TAN'. He has to download Form 49A (PAN) and 49B (TAN)

and upload them on the same screen after attaching his DSC. He has to upload these forms (PAN & TAN) within 2 days of filing the SPICe form failing which the entire SPICe form would be marked as 'Invalid and Not to be taken on record'.

Once the e-Form is processed and found complete, company would be registered and CIN would be allocated. DIN gets issued to the proposed Directors who do not have a valid DIN. Maximum three proposed Directors are allowed using this integrated form for filing application of allotment of DIN while incorporating a company. Also PAN and TAN would get issued to the Company.

On approval of SPIC e forms, the Certificate of Incorporation (COI) is issued with PAN as allotted by the Income Tax Department. An electronic mail with Certificate of Incorporation (COI) as an attachment along with PAN and TAN is also sent to the user. Further PAN card shall be issued by the Income Tax Department.

After receipt of Certificate of Incorporation (with PAN indicated there in as allotted by the Income Tax Department), in case of non-receipt of PAN card, stakeholders shall check the status at [www.TIN-NSDL.com](http://www.TIN-NSDL.com)

### **Digital Signature Certificate (DSC)**

The e-forms are required to be authenticated by the authorized signatories using digital signatures as defined under the Information Technology Act, 2000. A digital signature is the electronic signature duly issued by a certifying authority that shows the authority of the person signing the same. It is an electronic equivalent of a written signature. Every user who is required to sign an e-form for submission with MCA is required to obtain a Digital Signature Certificate. For MCA-21, the following four types of users are identified as users of Digital Signatures and are required to obtain digital signature certificate:

1. MCA (Government) Employees.
2. Professionals (Company Secretaries, Chartered Accountants, Cost Accountants and Lawyers) who interact with MCA and companies in the context of Companies Act.
3. Authorized signatories of the Company including Managing Director, Directors, Manager or Secretary.
4. Representatives of Banks and Financial Institutions.

A person requiring a Digital Signature Certificate can approach any of the Certifying authorities identified by the MCA, with original supporting documents and self-attested copies, for issuance of Digital Signature Certificate. DSCs can also be obtained, wherever offered by CA, using Aadhare KYC based authentication, and herein supporting documents are not required. Such Certifying Authorities are authorized to issue a Digital Signature Certificate with a validity of one or two years.

Registration of DSC is a onetime activity on the MCA portal. For registration of DSC, steps are given on the MCA Portal.

All companies (Public Company, Private Company, Company not having share capital, Company limited by share or guarantee, Unlimited Company) must comply with this requirement of registration of DSC by the director, manager and secretary.

Foreign directors are required to obtain Digital Signature Certificate from an Indian Certifying Authority (List of Certifying Authorities is available on the MCA portal). The process of registration of DSC is same as applicable to others.

### **Payment of Stamp Duty**

Stamp duty is a state subject. It is payable on Memorandum and Articles of Association of every

Company. In some states, duty is also payable on the authorized capital mentioned in the Memorandum of Association of the Company. States have authorized MCA to collect the stamp duty on their behalf and to remit the same to them.

### **Introduction of e-stamping facility by MCA and dispensation of physical submission thereof**

For the purpose of making all transactions faster, improving service delivery and making office of the Registrar paperless, the process of physical submission of documents has been dispensed with. The Central Government shall initially collect the stamp duty on behalf of State Governments and Union Territories for specific purpose of e-filing of documents under the provisions of the Companies Act, 2013 and to remit the same directly to their accounts in accordance with the approved payment and accounting procedures.

At present, e-Forms to which e -Stamping is applicable are –

- (i) Form SH-7
- (ii) Form FC-1
- (iii) Form GNL-4

The procedure for collection of stamp duty came in to force w.e.f. 13th day of September, 2009. With effect from 1st April 2010, companies are compulsorily required to make payment electronically for stamp duty in respect of all the States which have authorised to the Central Government to collect the Stamp duty on their behalf. In respect of the State from whom the authorization is yet to be received, the Company shall continue to pay stamp duty outside the MCA portal.

However, the payment of stamp duties in specific cases for some forms will be governed by the respective state laws for payment of same. ( For example, stamp rates on share certificates or increasing the authorized capital will vary from state to state)

The companies are not required to make physical submission of documents on which stamp duty is paid electronically through MCA portal. However, in respect of the documents on which stamp duty is not paid through MCA portal, the Companies are required, in addition to their electronic filing, to submit physical copies of such stamped documents with Registrar of Companies also.

Simultaneously, there are documents other than those specified above which are not covered for payment of stamp duty through MCA portal and on which stamp duty payable in the respective State is equal to or less than one hundred rupees. Such stamped documents are required to be scanned by the company and filed electronically for evidencing by the Registrar and need not be submitted physically except those required to be filed for compounding of offence or adjudication of penalties or applications to Central Government or Regional Director in the physical form separately.

Rule 7 of Companies (Registration offices and fees) Rules, 2014 states in any law for the time being in force , the company shall retain such documents duly stamped in original permanently for the documents relating to incorporation and matters incidental there to, changes in any of the clauses of the Memorandum and Article of Association and in other cases for a minimum period of eight years from the date of filing of the documents and shall be required to produce the same as and when the same is required for inspection and verification by the competent authority under any law for the time being in force.

The rates of stamp duty in the respective states may be revised through finance bill therefore, students are advised to refer to the latest rates of stamp duty.

Stamp duty can be paid through MCA-21 system with any of the option such as net banking, credit card, debit card, NEFT or offline with banks.

### STP Forms (Rule 10)

STP stands for “Straight Through Process”. Some e-forms are identified as informatory in nature. These forms are filed under Straight through process may be examined by the Registrar at any time on suo-moto or on receipt of any information or complaint from any source at any time after its filing. It means the information given in the e-forms is being taken on file maintained by the Registrar of Companies through electronic mode on the basis of statement of correctness given by the filing Company and further verification by the practicing professionals.

### Re-submission (Rule 10)

Where the Registrar, on examining any such application or e-Form or document, finds it necessary to call for further information or finds such application or e-Form or document to be defective or incomplete in any respect, he shall give intimation of such information called for or defect or incompleteness noticed electronically, by placing it on the website and bye-mail on the last intimated e-mail address of the person or the company, which has filed such application or e-Form or document, directing him or it to furnish such information or to rectify such defects or incompleteness or to re-submit such application or e-Form or document. In case the e-mail address of the person or company in question is not available, such intimation shall be given by the Registrar by post at the last intimated address or registered office of such person or company, as the case may be. The Registrar shall preserve the fact of such intimation in the electronic record.

The Registrar shall give an opportunity allowing thirty days time to such person or such company for furnishing any further information, or documents called for, in respect of application or e-form or document, filed electronically in GNL-4, for rectification of the defects or incompleteness or for re-submission of such application or e-Form or document.

The Registrar shall allow fifteen days' time to the person or company, which has filed the application or e-Form or document for furnishing further information or for rectification of the defects or incompleteness or for re-submission of such application or e-form or document.

In case where such further information called for has not been provided or has been furnished partially or defects or incompleteness has not been rectified or has been rectified partially or has not been rectified as required within the period allowed, the Registrar shall either reject or treat the application or e-form or document, as the case may be, as invalid in the electronic record, and shall inform the person or company, as the case may be. Where any document has been recorded as invalid by the Registrar, the document may be rectified by the person or company only by fresh filing a long with payment of fee and additional fee, as applicable at the time of fresh filing, without prejudice to any other liability under the Act. [Rule 10 of the Companies (Registration Offices and Fees) Rules 2014]

The Registrar shall allow fifteen days, time for re-submission in case of reservation of a name through web service- RUN for rectifications of defects if any.

### Refund

The user is required to make various payments to avail MCA21 services. A number of instances have been observed where the users make multiple payments or incorrect payment or excess payment while using these services. In order to allow the stakeholders to claim refund of such payments, refund process has been introduced by MCA.

The Person is to file the 'Refund Form' available on MCA21 portal for claiming refund.

The refund of MCA21 fees is available in the following cases:

- (a) **Multiple Payments**—This includes cases where service seeker does multiple filings of e Form No. or e Form No. SH-7 and makes payments more than once (multiple times) for the same

service. However, refund shall not be allowed in respect of approved e Forms.

- (b) **Incorrect Payments**—This includes cases where the service seeker has made payment in respect of an e Form or Stamp duty through an incorrect option under Pay miscellaneous fee facility.
- (c) **Excess Payment**—This includes cases where any excess fee has been paid by the service seeker due to some incorrect data entered in the e Form or incorrect data in MCA 21 system due to migration of data from legacy system.

No refund is permitted of the stamp duty, the person is required to approach the concerned state/ union territory. Refund process is not applicable for the following services/ e Forms:

- Public Inspection of documents
- Request for Certified Copies
- Payment for transfer deeds
- Stamp duty fee (D series SRN)
- IEPF Payment
- STP Forms i.e, Form 14-LLP (even for cases when the same were non STP earlier)
- Form No. DIR-3/ There is no fee for filing the refund form.

The refund form is to be filed within the stipulated time period. Also, there shall be deduction in the amount to be refunded based on time period within which refund e-Form is filed.

The mode of payment of refund shall be through cheque only. Later, provision for payment of refund through ECS will also be made available.

### **Online Inspection of Documents**

The documents filed online, once taken on record by ROC Offices are available for public viewing on payment of requisite fees. These documents, which are in domain of public documents, include documents relating to incorporation, charges, annual returns and balance sheets and change in directors. A certified copy of the documents can also be obtained by any one so interested. For this purpose there is also an option to mention the number of pages in the document for which a certified copy is required as well as the number of copies required.

### **Inspection, production and evidence of documents kept by Registrar—Rule 14 of Companies (Registration offices and fees) Rules, 2014**

The inspection of the documents maintained in the electronic registry so set up by MCA and which are otherwise available for inspection under the Act or rules made there under, shall be made by any person in electronic form.

### **Inspection of documents**

Rule 15 of Companies (Registration offices and fees) Rules, 2014

Any person may –

- Inspect any document kept by the Registrar, being documents filed or registered by him in pursuance of this Act or making a record of any fact required or authorized to be recorded or registered in pursuance of this Act, on payment for each inspection of fee.
- Require a certificate of incorporation of any company, or a copy or extract of any other document or any part of any other document to be certified by the Registrar, on payment of fee.

It is further provided that no person shall be entitled under section 399 to inspector obtain copies of resolutions referred to in clause (g) of sub- section (3) of section 117 of the Act.

## **ALL ABOUT FILLING AND FILING OF E-FORMS**

### **E-forms**

An e-form is only a re-engineered conventional form notified and represents a document in electronic format for filing with MCA authorities through the Internet. This may be either a form filed for compliance or information purpose or an application seeking approval from the MCA. Due to technical updates, these forms updates regularly, even though their user interface may not change. User always uses latest e-forms from the MCA Portal.

Filing and filing of forms is an important part of the secretarial function of a company secretary. Normally, where company appoints a company secretary, he is designated as the officer responsible for compliance under the Companies Act and other allied legislations. Therefore, for any lapse in complying with the various provisions of the Companies Act or such other legislations, for the compliance of which the company secretary has been made responsible, he becomes liable as “officer in default”.

Filing and filing of forms, returns and applications under various provisions demand intimate knowledge of substantive as well as procedural law. The Registrar of Companies (RoC) registers the documents filed with them within the prescribed time, if found in order. Often, a large number of documents filed with the RoC are not taken on record due to technical lapses which result in avoidable correspondence and frequent visits to the office of RoC. In order to avoid such errors, every care should be taken to ensure that the forms are properly filled and adequate documents are attached to them before filing.

Company Secretaries, under electronic filing system are required to be familiar with computer, internet, MCA21 electronic filing system, pdf files and using digital signatures.

## **PREREQUISITES FOR E-FILING ON MCA-21**

Digital Signature certificate (DSC) of either Class 2 and Class 3 signing certificate category issued by a licensed Certifying Authority (CA) needs to be obtained for e-Filing on the MCA Portal.

Digital Signatures are legally admissible in a Court of Law, as provided under the provisions of IT Act, 2000. The Certifying Authorities are authorized to issue a Digital Signature Certificate with a validity of one or two years.

### **Hardware and Software Requirements under e - filing**

The minimum system requirements for e-filing on MCA-21 are as under:

- any computer or laptop
- An efficient operating system
- Latest Browser.
- Adobe Reader from version 9.4 to version 10.1.4
- Scanner (above 300-600 DPI) for converting the attachments in the PDF format; and
- Java Runtime Environment (JRE) updated version

## **IMPORTANT TERMS USED IN E-FILING**

### **Pre-fill**

Pre-fill is functionality in an e-Form that is used for filling automatically, the requisite data from the system

without repeatedly entering the same. For example, by entering the CIN of the company, the name and registered office address of the company shall automatically be pre-filled by the system without any fresh entry.

### **Attachment**

An attachment refers to a document that is sent as an enclosure with an e-Form by means of an attached file.

The objective of the attachment is to provide details relevant to the e-Form for processing. While some attachments are optional, some are mandatory in nature.

The attachments to an e-Form have to be in Adobe PDF format only and My MCA portal has a facility to convert any document format to PDF format. My MCA portal does not accept big attachments and the users are advised to keep the attachment size to minimum (Not exceeding 2.6 MB of the total size of the Form including attachments).

### **Modify**

Once the user has done “Check Form” the form gets locked and it cannot be edited. If the user wishes to make any alteration, the form can be overwritten by clicking the “Modify” button.

If the user wants to modify the form after pre-scrutiny failure, the user can get the e-form and whichever fields have to be changed only those may be modified by using the “Modify” button.

### **Radio Button**

Frequent use of radio buttons has been done in the e-Form. While filling the e-Form one is required to select applicable option out of two or more radio buttons given against each point.

### **Check Box**

Applicable Check box is required to tick out of the two or more boxes wherever it appears in the e-Form.

### **Drop Down Box**

Drop down box is a box wherein at the end, a downward arrow is provided. On clicking the arrow various applicable choices appear. One is required to highlight the applicable choice and that will be filled in the box.

### **Text Box**

Text box is meant to provide details on the relevant point by the person filling the e-form. Space provided is generally adequate for the text to be written. However, if the space is not sufficient for a particular matter, information can be given in the annexure to the form indicating the same in the box.

### **Country Code**

Sometimes the applicant is required to fill up the country code in the e-Form. This is available in the instruction kit.

### **Stock Exchange Code**

All the stock exchanges of the country have been divided into two categories A and B. Listed companies are required to mention the stock exchange where the shares are listed with the help of the code.

### **Check Form**

By clicking “Check Form”, the user will be in a position to find out whether the mandatory fields in an e-

Form are duly filled-in. For example, if the user enters alphabets in “Date of Appointment of Director” field, he/she will be asked to correct the entered information.

If the size of e-Form including attachment is of bigger size then the attachment may be filed through an addendum.

### **Pre-Scrutiny**

Pre-scrutiny is a functionality that is used for checking whether certain core aspects are properly filled in the e- Form. The user has to make the necessary attachments in PDF format before submitting the e-Form for pre scrutiny.

After this affix digital signature.

### **Submit**

An e-Form can be submitted after it has been digitally signed. The process of submission of an e-Form in case of off-line filling is presented below:

- (a) User logs in to MCA21 portal and uses e-Form upload service
- (b) User browses the e-Form and clicks on “Submit” button
- (c) User will be shown errors, if any
- (d) If e-Form is successfully submitted, user will get confirmation message and will be lead to the fee payment screen.

The digital certificate is validated to ensure that the certificate has not expired and the current status of the same is valid and that the certificate has not been revoked or suspended.

### **Addendum to e-Form**

The user may have to submit some additional supporting documents that are not submitted during the e-Form (application) filing but are required for the processing of the e-Form. MCA may also ask the applicant to provide some additional documents in support of the e-Formal ready filed so as to expedite the processing of the same.

The user can initiate this on their own by checking the track transaction status on My MCA portal or on being notified by MCA through email. Payment of fees is not required for filing an addendum.

The supporting documents that the applicant uploads, as an addendum, gets duly associated with the e-Form that was submitted earlier with the given Service Request Number (SRN).\*

The normal process of filing an addendum is presented below:

- (a) The applicant enters SRN for which document needs to be attached.
- (b) The applicant attaches relevant document and clicks “Submit”.
- (c) The system verifies that the status of entered SRN is “In Progress” and the submitted document gets accepted.

### **Service Request Number (SRN)**

Each transaction under e-filing is uniquely identified by a Service Request Number (SRN). On filing of an e-form, the system generates and provides an in e character alpha numeric string starting with an alphabet (A-Z), called a Service Request Number (SRN). A user can check the status of the

document/transaction, by entering the SRN.

### **PRE-CERTIFICATION OF CERTAIN E-FORMS [RULE 8(12)]**

Apart from authentication of e-forms by authorized signatories using digital signatures, some e-forms are also required to be pre-certified by practicing professionals. Pre-certification means certification of correctness of any document by a professional before the same is filed with the Registrar.

Ministry of Corporate Affairs has entrusted practicing professionals registered as Members of professional bodies namely ICAI, ICSI and ICWAI with the responsibility of ensuring integrity of documents filed by them with MCA in electronic mode including filing of financial statements in XBRL mode.

This pre-certification is to be carried out by *inter-alia*, Company Secretaries or chartered accountant or as the case may be the Cost Accountant in whole-time practice. The forms filled by companies, other than OPC and small companies which has to be pre-certified by practising professionals include the following :

1. RUN Web based Name search facility
2. FORM No. INC-22 (Notice of situation or change of situation of registered office)
3. FORM No. INC-27 (Conversion of Public Company into Private Company or Private Company into Public Company and Conversion of Unlimited Liability Company into a Company limited by shares or guarantee or Conversion of Guarantee Company into a Company limited by shares)
4. FORM No. INC-28 (Notice of Order of the Court or any other competent authority)
5. FORM No. PAS- 2 (Information Memorandum)
6. FORM No. PAS-3 (Return of allotment)
7. FORM No. SH-7 (Notice to Registrar of any alteration of share capital)
8. FORM No. SH-11 (Return in respect of buy back of securities)
9. FORM No. CHG-1 (Application for registration of creation, modification of charge (other than those related to debentures) including particulars of modification of charge by Asset Reconstruction Company in terms of Securitization and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002 (SARFAESI))
10. FORM No. CHG-4 (Particulars for satisfaction of charge thereof)
11. FORM No. CHG-9 (Application for registration of creation or modification of charge for debentures or rectification of particulars filed in respect of creation or modification of charge for debentures)
12. FORM No. MGT-7 (Annual Return)
13. FORM No. MGT-10 (Changes in shareholding position of promoters and top ten Shareholders)
14. FORM No. MGT-14 (Filing of Resolutions and agreements to the Registrar)
15. FORM No. DIR-3 (Application for allotment of Director Identification Number)
16. FORM No. DIR-3C (Intimate information of directors, managing director, manager and secretary by an Indian Company)
17. FORM No. DIR-5 (Application for surrender of Director Identification Number)
18. FORM No. DIR-6 (Intimation of change in particulars of Director to be given to the Central Government)
19. FORM No. DIR-12 (Particulars of appointment of Directors and the key managerial personnel)

and the changes among them)

20. FORM No. MR-1 (Return of appointment of managerial personnel)
  21. FORM No. MR-2 (Form of application to the Central Government for approval of appointment or reappointment and remuneration or increase in remuneration or waiver for excess or over payment to managing director or whole time director or manager and commission or remuneration to directors)
  22. FORM No. URC-1 (Application by a company for registration under section 366—Conversion from firm into company and LLP into company)
  23. FORM No. GNL-1 (Form for filing an application with Registrar of Companies)
  24. FORM No. GNL-3 (Particulars of person(s) or Key managerial personnel charged or specified for the purpose of sub- clause (iii) or (iv) of clause 60 of Section 2)
  25. FORM No. GNL-4 (Form for filing addendum for rectification of defects or incompleteness)
  26. FORM No. NDH-1 (Return of statutory compliances)
  27. FORM No. NDH-2 (Application for extension of time)
  28. FORM No. NDH-3 (Half yearly Return)
  29. FORM No. MSC-1 (Application to ROC for obtaining the status of dormant company)
  30. FORM No. MSC-3 (Return of dormant companies)
  31. FORM No. MSC-4 (Application for seeking status of active company)
  32. Form No. AOC-4 XBRL (Form for filing XBRL document in respect of financial statement and other documents with the Registrar)
- Form STK-2 (Application by company to ROC for removing its name from register of companies)

### **Necessity of Pre-certification**

Introduction of pre-certification by an independent professional in the e-Form aimed at reducing the workload of the Registrar of Companies. Once an e-Form has been pre-certified by a professional towards its authenticity based on the particulars contained in the books of accounts and records of the company, ROC is entitled to take on record the e-Form. Professionals are responsible for submitting/certifying documents (to be signed digitally by them) and system would accept most of these documents online without approval by Registrar of Companies or other officers of the Ministry. If a professional gives a false certificate or omits any material information knowingly, he is liable to punishment under section 447 and 448 of the Companies Act, 2013 besides disciplinary action by the Institute which issued the Certificate of Practice.

### **Fees (Rule 12 of Registration Offices and Fees)**

The documents required to be submitted, filed, registered or recorded or any factor information required or authorized to be registered under the Act shall be submitted, filed, registered or recorded on payment of the fee or on payment of the fee or on payment of such additional fee as applicable, as mentioned in Table annexed to these rules.

For the purpose of filing the documents or applications for which no e-form is prescribed under the various rules prescribed under the Act, the document or application shall be filled through Form No.GNL.1 or GNL.2 along with fee as applicable and in case a single form is prescribed for multiple purposes, the fee shall be paid for each of the purpose contained in the single form.

For the purpose of filing information to sub- clause (60) of section 2 of the Act, such information shall be

filed in

Form No. GNL.3 along with fee as applicable.

### **Mode of Payment (Rule13 of Registration Offices and Fees)**

The fees, charges or other sums payable for filing any application, form, return or any other document in pursuance of the Act or any rule made there under shall be paid by means of credit card; or internet banking; or remittance at the counter of the authorised banks or any other mode as approved by the Central Government.

### **GUIDELINES FOR FILLING AND FILING-FORMS**

While preparing the forms, documents, returns to be filed with the Registrar, the following points are to be kept in view:

- (a) Each time we are required to file an e-Form, we should download the Form from the MCA site to avoid the wastage of time at a later stage because the forms are under revision and a slight change in the form will result in it not getting uploaded at the stage of submitting on the portal.
- (b) An e-Form contains certain standardized features. It starts with the Corporate Identity Number (CIN), which works as a unique identifier of a company (in the case of an Indian Company). In the case of foreign company, the foreign company Registration Number is required to be filled-up. By entering the number, the company details to the extent these are available in static form in the database are automatically filled in by using the pre-fill functionality.
- (c) The e-Form contains a number of mandatory fields, marked with the red color star(\*) which are required to be filled in. Certain other fields are non-mandatory in nature, which may be filled in as maybe relevant in any particular case.
- (d) An e-Form contains tool tips for context sensitive help.
- (e) An instruction kit is available for each e-Form, which contains details of the instructions for properly filling the e-Form. It is important to go through it before filing the e-form.
- (f) An e-Form may be filled in either online or offline mode. Online filling implies that the e-Form is filled while being still connected to MCA portal through the Internet. Offline filling denotes that the e-Form is downloaded into the user's computer and filled later without being connected to the Internet.
- (g) An e-Form may require certain mandatory attachments to be filed along with it. Optional attachments may also be filed with an e-Form. The list of such attachments is displayed in the e-Form.
- (h) All documents/forms/returns, etc., are to be submitted in English or Hindi and where a document is in any language other than English and Hindi, a translation of that document or portion in to either English or Hindi certified by a responsible officer of the company to be correct, shall be attached to each copy of the document which is furnished to the Registrar. All such documents shall be converted into pdf format.
- (i) Next to attachment, there is a declaration that is sought from the person filing the e-Form to the effect that the information given in the e-Form and the attachments is correct and complete.
- (j) Most of the e-Forms require the digital signature of the Managing Director or Director, Manager or Secretary of the company for successful filing/submission.
- (k) Scanned documents take more space and as far as possible MS-word file converted into pdf file is preferred.
- (l) All electronic forms require, the date of board meeting to be specified under the head

verification. In the said column, the date of the board meeting at which the person is authorised to sign and submit form shall be specified. Where it is mentioned in the form that it has to be signed by specific person, it should be so digitally signed.

- (m) Further, the digital signature of a third party may also be required in certain cases. In the case of an e- Form for creation or modification of charges, such digital signature is also required from the Bank or Financial Institution.
- (n) In certain cases, a certificate from the Chartered Accountant or Cost Accountant or Company Secretary in whole-time practice is also required to authenticate the particulars contained in the e-Form. For example, this requirement is mandatory in the case of an e-Form for appointment of director, change in the situation of the registered office, etc.
- (o) There are built-in facilities to check the filled in e-Form for requisite validations, to do pre-scrutiny and to modify the e-Form when the same is required to be re-submitted.
- (p) Certain documents need physical filing in addition to e-filing. It needs to be noted that those should preferably be free from corrections and erasure. If there is any correction or erasure, it should be duly authenticated by the person signing the document or the return.
- (q) After the filling part is complete, the e-Form is ready for submitting into the MCA central documentary repository and when the Submitted button is pressed, the e-Form gets uploaded into the MCA central document repository.
- (r) Thereafter, the requisite fees as applicable for the e-Form should be paid either on-line or off-line.
- (s) Once the e-Form has been accepted and payment of fees has been acknowledged, a work item is created and assigned to the appropriate MCA employee based on pre-defined assignment rules as part of MCA back office work flow automation.
- (t) In the case of an e-Form, the authorized officer affixes his/ her digital signature for registering/ approving/rejecting the same.
- (u) After the processing of the e-Form is completed, an acknowledgement email is sent to the user regarding its approval/rejection.

Once the e-form is filled, there would be need to validate the e-form using Pre-scrutiny button. Then the relevant digital signatures have to be affixed and the form be saved. Internet connection is required to carryout the pre-fill and pre-scrutiny functions .The filled up e-form as per relevant instruction kit needs to be uploaded on the MCA21 portal. On successful upload, the Service request number would be generated and it would be directed to make payment of the statutory fees. Once the payment has been made the status of payment made and filing status can be tracked on the MCA21 portal by using the "Track Your Payment Status" and "Track Your Transaction Status" link respectively.

### **IMPORTANT ASPECTS TO BE CONSIDERED AT THE TIME OF ANNUAL FILING**

As a part of annual filing, each year companies incorporated under the Companies Act, 2013 are required to file the following documents along with the relevant e-forms with the Registrar of Companies:

#### **XBRL Filing**

XBRL (Extensible Business Reporting Language) is a language for the electronic communication of business and financial data which is revolutionizing business reporting around the world. It helps in the preparation, analysis and communication of business information. It offers cost savings, greater efficiency and improved accuracy and reliability to all those involved in supplying or using financial data.

The Ministry of Corporate Affairs has mandated the following select class of companies mentioned below

to file financial statements in XBRL (eXtensible Business Reporting Language) mode and by using the XBRL taxonomy:

- (i) all companies listed with any Stock Exchange(s) in India and their Indian subsidiaries; or
- (ii) all companies having paid-up capital of Rupees five crore and above; or
- (iii) all companies having turnover of Rupees one hundred crore and above; or
- (iv) all companies who were required to file their financial statements for FY 2010-11, using XBRL mode.

However, the companies in banking, insurance, power sector, non-banking financial companies and housing finance companies are exempted from XBRL filing till further orders.

Key benefits of XBRL filing are as under:

- (i) Relevant data has tags and selective information can be fetched for specific purposes by various government and regulatory agencies
- (ii) It is in conformity with Global Reporting Standards, which helps in improved data mining and relevant information search.

### **Steps for filing Financial Statements in XBRL mode**

Irrespective of the fact, whether the company has a net profit less than 5 crores or a turnover less than 100 crores, the company shall still file in xbrl mode only. In short, "Once an XBRL, Always am XBRL"

#### **1. Creation of XBRL instance document**

Companies have the option to create their own XBRL documents in house or to engage a third party to convert their financial statements into XBRL form. The first step in creation of an instance document is to do tagging of the XBRL taxonomy elements with the various accounting heads in the books of accounts of the company.

This would create the mapping of the taxonomy elements with the accounting heads so that the accounting information can be converted into XBRL form. Each schedule of the balance sheet/ P&I Statement is known as an element and each schedule item or sub-schedule is known as child member.

Mapping is the process of comparing the concepts in the financial statements to the elements in the published taxonomy, assigning a taxonomy element to each accounting concept published by the company.

Selecting the appropriate elements for some financial statement elements may require a significant amount of judgment. For that reason those in the company who are most familiar with the financial statements should be associated with mapping of accounting concepts to taxonomy elements. The mapping should be reviewed before proceeding further as the complete reporting would be dependent on the mapping.

In case any information is present in the financial statements for which corresponding tag/ element is not available in the taxonomy, then the same needs to be captured in the next-best-fit element in the taxonomy or should be included under the corresponding "Others" element. This should be followed only in case the relevant tag is not available in the taxonomy. It should not to be used generally.

Further, it is imperative to include foot note w. r. t. the same while preparing the instance document. For tagging or capturing the information which is often included in brackets in the labels in the company's financial statements, can either be captured as footnote or if detailed tags are available, the same should be tagged with the detailed tags in the taxonomy.

The complete information as contained in the annual accounts and related documents; and the information required to be filed with the Registrar of Companies should be reported in the XBRL instance documents to be submitted with MCA.

Initially, all tagging and mapping shall be done on the basic template (.RXO) file or the offline (.XLS) template provided and after all compilation is completed, such file shall be created as .XML document which shall be duly validated and pre-scrutinised shall be attached to the AOC-4 Form

For preparing instance document, the taxonomy as applicable for the relevant financial year is to be used.

1. Download XBRL validation tool from MCA Portal
2. Load the instance document in the validation tool
3. Validate the instance document.
4. This stage has to be carefully dealt, since the internal validation tool may only highlight the arithmetic errors, and only the MCA tool will give the .XML error required to be handled for filing.
5. Pre-scrutiny of the instance document
6. Convert to pdf and verify the contents of the instance document. (This step is essential to ensure that the disclosures contained in XBRL document are as per Audited Financial Statement adopted in the AGM and the textual information entered in the instance document are clearly viewable)
7. Attach instance document to the Form 23AC-XBRL and 23ACA-XBRL or From AOC-4(XBRL)
8. Submitting the XBRL Form on the MCA portal
9. Viewing of balance sheet and profit and loss submitted in XBRL form on MCA portal.

#### **Common Points for all the annual e-Forms**

- Balance sheet and Profit and Loss Account are to be filed as two separate documents with different e forms. Now, the financial statements comprising the Balance sheet and profit and loss and cash flow, if any are filed in a single form AOC-4)
- Annual Return, Balance Sheet and Profit and Loss Account are filed as attachments because scanned images considerably increase the size of document, besides being more expensive. (annual return is a form not an attachment and list of shareholders is the attachment to Annual return). Annual return by itself is an exhaustive forms which captures all relevant data of the company.
- It is suggested that these e-Forms should be filled offline and got printed before filing as these forms are taken on record through electronic mode without any processing at the RoC office. The Company must ensure that the particulars filed are correct. Further, generally, there is no provision of resubmission of these e- Forms.
- In case of a company having share capital, the authorized capital as on the date of filing of the e-form and in case of company without share capital, the number of members as on the date of filing of the form should be entered in thee-Forms.
- After filling, the e-form should be pre-scrutinised by clicking the Pre scrutiny button or else, it shall be rejected at the time of uploading of form.
- No attachment can be submitted through the addendum service in respect of these e-forms.

## DESCRIPTION OF E-FORMS

The Central Government has provided all the e-forms as an annexure to the relevant Rules. Important aspects with respect to each e-form are provided hereunder:

### The following E-Forms are required to be filed with Registrar under The Companies Act, 2013

- (1) **E-Form DIR-3C-** Intimation of Director Identification Number by the company to the Registrar DIN services

e-Form DIR-3C is required to be filed pursuant to Section 157 of the Companies Act, 2013 & Rule 10A (2) of the Companies (Appointment and Qualification of Directors) Rules, 2014. Time limit (days) for filing – Within 15 days of the receipt of intimation under section 156

Purpose of the eForm - Every director shall inform all the companies in which he/ she is a director, of the DIN allotted to him/her in Form DIR-3B within 30 days of the receipt of intimation of approval of DIN. Similarly, the Secretary and Manager of a company shall inform the company of their Income-tax Permanent Account Number (PAN). Company needs to further inform about DIN of the directors to the Registrar in Form DIR-3C within 15 days of receiving the intimation.

- (2) **E-Form CRA-2-** Form of intimation of appointment of cost auditor by the company to Central Government.

e-Form CRA-2 is required to be filed pursuant to section 148(3) of The Companies Act, 2013 and rule 6(2) and 6(3A) of The Companies ( Cost Records and Audit) Rules, 2014.

Time limit (days) for filing - In case of Original filing - Within 30 days of the date of board meeting [earliest date] or 180 days of the commencement of the financial year, whichever is earlier.

In case of filing due to casual vacancy due to resignation, death or removal - Within 30 days of the occurrence of such vacancy.

Purpose of the eForm - Every company covered under the Companies (Cost Records and Audit) Rules, 2014 including all units and branches shall, in respect of each of its financial year commencing on or after the 1st day of April, 2014, maintain cost records as per the requirements of CRA-1. Further company covered under class of company required to appoint cost auditor, shall appoint such cost auditor within one hundred and eighty days from the commencement of the financial year. It shall also inform the Central government about appointment of cost auditor within thirty days of the board meeting appointing cost auditor or within one hundred and eighty days of commencement of the financial year, whichever is earlier.

Any casual vacancy in the office of a cost auditor, whether due to resignation, death or removal, shall be filled by the Board of Directors within thirty days of occurrence of such vacancy and the company shall inform the Central Government in Form CRA-2 within thirty days of such appointment of cost auditor.

**Attachments** – Copy of Board resolution of the company.

- (3) **E-Form CG-1-** Form for filing application or documents with Central Government

e-Form CG-1 is required to be filed in pursuant to the Companies Act, 2013.

Purpose of the eForm - A company can seek approval from the Central Government by filing application under Companies Act, 2013 in eForm CG-1.

- (4) **E-Form ADT-2-** Application for removal of auditor(s) from his/their office before expiry of term

e-Form ADT-2 is required to be filed pursuant to Section 140(1) of the Companies Act, 2013 and rule 7(1) of the Companies (Audit and Auditors) Rules, 2014.

Time limit (days) for filing – Within 30 days of passing Board resolution.

Purpose of the eForm - eForm ADT-2 is an application by the company seeking approval from the Regional Director/ Registrar of Companies for Removal of Auditor from the office before the expiry of the term of office.

**Attachments –**

- Details of the grounds for seeking removal of auditor
- Copy of the special resolution
- Minutes of the annual general meeting or extraordinary general meeting

**(5) E-Form INC-18-** Application to Regional director for conversion of section 8 company into company of any other kind

eForm INC-18 is required to be filed in pursuant to Section 8 (4) (ii) of the Companies Act, 2013 and Rule 21(3) of Companies (Incorporation) Rules, 2014.

Purpose of the eForm- An existing company registered under section 8 seeks to convert itself into a company of any other kind shall make an application to the Regional Director for conversion of its status. Once the approval is given by the Regional Director, the company shall cease to enjoy all the privileges/ concessions obtained by it on account of being a Section 8 company.

**Attachments –**

- Memorandum of association
- Articles of association
- Certified true copy of board resolution(s) authorizing conversion
- Certified true copy of the special resolution passed for approval for conversion into any other kind and notice convening the general meeting along with the relevant explanatory statement annexed thereto
- Certificate from CA/CS/CWA (in practice) certifying that the conditions laid down in the Act and rules, have been complied with
- Statement of assets and liabilities of the company as on the date not earlier than thirty days of that date duly certified by the auditor
- Copy of valuation report by a registered valuer about the market value of assets
- Audited financial statements, the Board's reports, annual returns and the audit reports for each of the two financial years immediately preceding the date of the application or, where the company has functioned only for one financial year, for such year
- NOC from all the creditors is mandatory in case yes is selected in field 7.

**(6) E-Form INC-23-** Application to Regional Director for approval to shift the Registered Office from one state to another state or from jurisdiction of one Registrar to another Registrar within the same State

e-Form INC-23 is required to be filed in pursuant to Section 12(5) & 13(4) of the Companies Act, 2013 and rule 28 & 30 of the Companies (Incorporation) Rules, 2014.

Purpose of the e-Form- In order to shift the registered office of the company from one state to another or from jurisdiction of one Registrar of Companies to another, an application in e-Form INC-23 has to be made to the Regional Director (Central Government) for his confirmation/ approval.

## Attachments –

- Memorandum of Association and Articles of Association.
- Certified true copy of notice of the general meeting along with relevant explanatory statement.
- Certified true copy of special resolution sanctioning shifting of registered office.
- Certified true copy of the minutes of the general meeting authorizing such alteration.
- Proof of service of the application to the Registrar, Chief Secretary of the state, SEBI or any other regulatory authority, if applicable.

In case registered office is shifted from one state to another state the following attachments are mandatory:

- Power of attorney/vakalatnama/Board resolution.
- List of creditors and debenture holders.
- Affidavit from Directors in terms of rules.
- Affidavit verifying the application.
- Affidavit by the company secretary of the company and the directors in regards to the correctness of list of creditors and affairs of the company.
- Affidavit by directors about no retrenchment of employees.
- Affidavit verifying the list of creditors.
- It is mandatory to attach in case if there is any prosecution is pending against the company or if any inquiry, inspection or investigation is initiated against the company.
- Copy of newspaper advertisement for notice of shifting the registered office. It is mandatory to attach copy of newspaper publication in case if the registered office is shifting within the state.
- Copy of objections (if received any)

**(7) E-Form ADJ- Memorandum of Appeal**

e-Form ADJ is required to be filed in pursuant to section 454(5) of the Companies Act, 2013 and Rule 4(1) of Companies (Adjudication of Penalties) Rules, 2014.

Time limit (days) for filing- Within a period of sixty days from the date of receipt of the order of adjudicating officer by the aggrieved party.

Purpose of the eForm - An adjudicating officer(s), not below the rank of Registrar, appointed by Central Government can impose any penalty on the company and the officer who is in default stating any non-compliance or default under the provisions of the Companies Act, 2013. Person aggrieved by such order may prefer an appeal to the Regional Director having jurisdiction in the matter by filing eForm ADJ.

## Attachments –

- Certified copy of the order against which appeal is sought is mandatory in all cases.
- A copy of authorization in favour of authorized representative and also written consent of such authorized person is also required to be attached where party is represented by such authorized person.
- Order of condonation of delay is mandatory in case there is any delay in filing the order.

**(8) E-Form RD-1-** Applications made to Regional Director

eForm RD-1 is required to be filed pursuant to the Companies Act, 2013.

Purpose of the eForm- A company can seek approval from Regional Director by filing application in eForm RD-1 for certain mentioned purposes under Companies Act, 2013.

**Attachments –**

For issue of license u/s 8

In case of new association -

- Memorandum of association (MoA).
- Articles of association (AoA).
- Declaration as per rule 19 of the Companies (Incorporation) Rules, 2014.
- Details application in Form INC-12
- Statement of brief description of the work, if already done by the association and work proposed to be done.
- Statement of the grounds on which application is made
- Other necessary attachments as per rules 19 of the Companies (Incorporation) Rules, 2014

In case of company already registered -

- Detailed application in Form INC-12
- Assets and liability statement as per rule 20 of the Companies (Incorporation) Rules, 2014
- Last two years' accounts, balance sheet and report on working of the association as submitted to the members of the association
- Statement of brief description of the work, if already done by the association and work proposed to be done.
- Other necessary attachments as per rules 20 of the Companies (Incorporation) Rules, 2014

Rectification of name -

- Copy of board resolution Removal of auditor -
- Copy of ordinary resolution
- Copy of special notice
- Copy of the representation if any made by the statutory auditor

**(9) E-Form CHG-8-** Application to Central Government for extension of time for filing particulars of registration of creation / modification / satisfaction of charge OR for rectification of omission or misstatement of any particular in respect of creation/modification/ satisfaction of charge

e-Form CHG-8 is required to be filed in pursuant to Section 77(1) & 87 of the Companies Act, 2013 and Rule 12(2) of the Companies (Registration of Charges) Rules, 2014.

Purpose of the e-Form-Application to Central Government for extension of time for Filing particulars of registration of creation / modification / satisfaction of charge

Rectification of omission or misstatement of any particular in respect of creation/modification/ satisfaction of charge

Attachments –

- A documentary evidence of creating/modifying/satisfying the charge.
- The letter of authorisation from the authorised representative of a foreign company – In case of a foreign company
- Copy of resolution of the Board authorising the filing of the application and appointing the authorized representative – In case of Company
- In case of omission or misstatement of a charge:
  - An Affidavit stating omission or misstatement of a charge
  - Confirmation from the charge holder

**(10) E-Form INC-6-** One Person Company- Application for Conversion

e-Form INC-6 is required to be filed pursuant to Section 18 of Companies Act, 2013 and Rule 7(4) of the Companies (Incorporation) Rules, 2014.

Time limit (days) for filing –

In case of Mandatory Conversion – Within 6 months from the effective date on which the above threshold limit was exceeded.

In case of Voluntarily Conversion– Within 30 days from the date of passing special resolution.

Purpose of the e-Form - This e-Form is required to be filed in case of conversion of OPC into private or public or conversion of private into OPC. In case paid up share capital of an One Person Company exceeds fifty lakh rupees or its average annual turnover during the relevant period exceeds two crore rupees, it shall make an application in Form INC-6 within 6 months from the effective date on which the above threshold limit was exceeded. However if any One Person Company wants to convert itself into private/public company then also it can voluntarily apply through Form INC-6 after two years of its incorporation. A private company can also make an application for conversion into One Person Company by filing Form INC-6.

**Attachments -**

- Altered Memorandum of association
- Altered Articles of association
- Copy of the duly attested latest financial statement.
- Copy of board resolution authorizing giving of notice

It is mandatory to attach a certificate from Chartered Accountant if the conversion is, because of exceeding average annual turnover.

In case of conversion of private company into OPC, following attachments are mandatory:

- Affidavit
- Certified true copy of minutes, list of creditors and list of members.
- Copy of NOC of every creditor.
- Consent of the nominee in Form No. INC-3 along with all enclosures
- Copy of PAN card of the nominee and member.
- Proof of identity of the nominee and member.
- Residential proof of the nominee and member.

**(11) E-Form INC-24-** Application for approval of Central Government for change of name

e-Form INC-24 is required to be filed pursuant to Section 13(2) of the Companies Act, 2013 and rule 29(2) of the Companies (Incorporation) Rules, 2014.

Purpose of the e-Form - An existing company seeking for change of name shall apply to Central Government (RoC) by filing an application in e-Form INC-24. For changing the name, company is required to have a name reserved by filing Form RUN and shall have passed the special resolution.

**Attachments –**

- Certified true copy of minutes of the general meeting of the members where the special resolution was passed for change of name of the company is required to be attached.
- Copy of any approval order obtained from the concerned authorities (such as RBI, IRDA, SEBI etc.) or the concerned department.
- If change of name is due to change in main activity of the company, a certificate from chartered accountant regarding turnover details from new activity should be enclosed.

**(12) E-Form MSC-1-** Application to Registrar for obtaining the status of dormant company

e-Form MSC-1 is required to be filed pursuant to sub-section (1) of Section 455 of the Companies Act, 2013 and Rule 3 of Companies (Miscellaneous) Rules, 2014.

Time limit (days) for filing - Within 30 days of passing of special resolution

Purpose of the e-Form - A company is formed and registered for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years, or has not filed financial statements and annual returns during the last two financial years may make an application in eForm MSC-1 to the Registrar of Companies for obtaining the status of a dormant company.

**(13) E-Form MSC-4-** Application for seeking status of active company

e-Form MSC-4 is required to be filed pursuant to Section 455(5) of the Companies Act, 2013 and Rule 8 of Companies (Miscellaneous) Rules, 2014.

Purpose of the e-Form - A dormant company can file an application to Registrar in eForm MSC-4 for seeking the status of an active company.

**Attachments:**

- Certified true copy of board resolution authorizing making of this application.
- Certified true copy of special resolution authorizing for obtaining dormant status.
- Auditor's certificate.
- Statement of affairs duly certified by Chartered Accountant or Auditor(s) of the company.
- Copy of approval or no objection certificate (NOC) from the regulatory authority in case company is regulated by such authority.
- Latest financial statement and annual return of the company is mandatory to attach in case the same is filed to Registrar.
- Consent of the lender if any loan is outstanding.
- Certificate regarding no dispute in the management or ownership.

**(14) E-Form GNL-1-** Applications made to Registrar of Companies

e-Form GNL-1 is required to be filed pursuant to rule 12(2) of Registrar of Companies (Registration Offices and Fees) Rules, 2014 and the Companies Act, 2013.

Purpose of the e-Form- User can file application seeking approval from Registrar of Companies by filing application in eForm GNL-1 for following purposes under Companies Act, 2013:-

Compounding of offences

Extension of AGM up to 3 months

Scheme of arrangement, amalgamation

Others

**Attachments:**

- Board resolution passed for the purpose of making an application for any of the documents as applicable
- Scheme of arrangement, amalgamation Extension of period of annual general meeting
- Copy of notice received from RoC or any other competent authority if the application for compounding of offence is filed in pursuance to notice received from RoC or any other competent authority
- Detailed application is required to be attached in all the cases of filing

In case of compounding of offence, the detailed application should contain the following details:

- General profile and history of the company containing details such as name, date of incorporation, main objects of the company
- Facts of the case mentioning nature of offence and period of default
- Whether the offence is made good, if yes then how and when (i.e. the date where applicable)
- Prayer to compounding authority for compounding of offense

In case of extension of annual general meeting, the detailed application should contain the following details:

- Reasons of extension
- Period for which extension is required (Note: It should not exceed three months)

**(15) E-Form INC-12- Application for grant of License under section 8**

eForm INC-12 is required to be filed pursuant to section 8(1) and 8(5) of the Companies Act, 2013 and rule 19 and 20 of Companies (Incorporation) Rules, 2014.

Purpose of the eForm - Any person/association desirous of being incorporated as a company without the addition of the word 'Limited' or 'Private Limited' as the case may be before charitable objects which are in the overall interest of the community and intends to apply its profits and income in promoting its objects and prohibits payment of dividend shall make an application to Central Government in eForm INC-12. The application can also be filed by an existing company for the purpose of converting itself into such company. Consequent upon approval of application, a license under section 8 will be issued by the Central Government.

**Attachments:**

- Memorandum of Association as per Form no. INC-13
- Articles of Association

- Declaration as per Form No. INC-14
- Declaration as per Form No. INC-15
- Estimated income and expenditure for next three years

It is mandatory to attach following in case of grant of license to an existing company:

- Certified true copy of resolution passed in general meeting and board meeting
- Last one / two year's financial statement(s), board's report(s) and Audit report(s)
- Assets and liabilities statements with their values as per applicable rule

Approval/ concurrence/ NOC of the concerned authority is mandatory to be attached in case the company is regulated by such authority.

Entrenched articles of association is mandatory to be attached in case articles are entrenched.

**(16) Form– FTE-** Application for striking off the name of company under the Fast Track Exit (FTE) Mode

Purpose of the eForm- Application for striking off the name of company under the Fast Track Exit Mode. This Form can be filed only by an Active company or by a dormant company or by company marked as defaulting. Upon approval of this Form, status of the company shall be changed to 'Struck off' from the register of companies. Any company desirous of getting its name struck off from Registrar of Companies under section 560 shall file Form FTE only.

**Attachments:**

- A duly certified statement of account by a chartered accountant in whole-time practice or statutory auditor of the company (As per annexure C of the Guidelines) (Mandatory) Copy of Board resolution showing authorisation given for filing this application(Mandatory)
- Affidavit (to be given individually by director(s)) (As per annexure A of the Guidelines) (Mandatory)
- Indemnity bond (to be given individually or collectively by director(s) (As per annexure B of the Guidelines) (Mandatory)

In case application is not digitally signed by the company representative, physical copy of application duly signed by the director, Managing Director, manager or secretary authorised by the Board of Directors (Mandatory in case 'No' selected in field 10) Copy of no objection certificate (NOC) from concerned administrative Ministry/Department/ State Government (Mandatory in case of a Government company)Any other information can be provided as an optional attachment

**(17) E-Form RUN – Reserve Unique Name**

It is a simple and easy to use web service for reserving a name for a new company or for change of name for any existing company.

Purpose of the eForm – 'RUN' is one of the Government Process Re-engineering (GPR) initiatives for making the incorporation process speedy, smooth, simple and reducing number of procedures involved for starting a business, w.e.f. 26th January 2018 on the occasion of 69th Republic Day new web based (there is no requirement to download e-form like INC-1, after filling up the earlier form and attaching DSC (after successful pre-scrutiny) you were required to upload the same), has been launched for reserving name of new company or for change in name of existing company earlier there was INC-1 for reservation of name of new company or for change in name of existing company.

Time limit (days) for filing:

An approved name is valid for a period of

- (i) 20 days from the date of approval (in case name is being reserved for a new company) or
- (ii) 60 days from the date of approval (in case of change of name of an existing company)

**Attachments:**

- It is mandatory to attach relevant documents and No Objection Certificates (NOCs) only when a name which requires the approval of a sectoral Regulator or NOC etc. if applicable, as per the Companies(Incorporation) Rules, 2014, is being applied for.

**(18) E-Form INC-3-** One Person Company- Nominee consent form

eForm INC-3 is required to be filed in pursuant to section 3(1) of the Companies Act, 2013 and rule 4(2), (3), (4), (5) & (6) of Companies (Incorporation) Rules, 2014.

Purpose of the eForm- One Person Company is required to indicate the name of the other person as nominee in its memorandum with his prior written consent, who shall become the member of the company in case of subscriber's/member's death or incapacity to contract and such consent of the nominee shall be submitted to Registrar in this eForm INC-3.

**Enclosures:**

Copy of PAN card

Proof of identity

Residential Proof

All the enclosures along with this form shall be submitted as an attachment to other forms INC-2, INC-4 or INC-6 as the case may be. User is required to provide copy of residential proof not older than two months.

**(19) E-Form INC-4-** One Person Company- Change in Member/Nominee

eForm INC-4 is required to be filed pursuant to Section 3(1) of the Companies Act, 2013 and Rule 4(4), (5), (6) of Companies (Incorporation) Rules, 2014.

Time limit (days) for filing – Within 30 days of notice of withdrawal of consent/change in nominee/cessation of member

Purpose of the eForm - Member of One Person Company is required to nominate a person, after obtaining his/her prior written consent, who will become the member of such OPC in the event of member's death or incapacity to contract. This form is filed in case there is any change in the nominee of the OPC by personal withdrawal of consent by the nominee himself, or change in the nominee by the member, or in case of cessation of member due to various reasons.

**Attachments:**

- Consent of the nominee in signed Form INC-3 along with all the enclosures. (Mandatory)
- Certified copy of PAN card of the new nominee and/or new member. (Mandatory)
- Proof of identity of the new nominee and/or new member. (Mandatory)
- Residential proof of the new nominee and/or new member. (Mandatory)

It is mandatory to attach notice of withdrawal of consent in case withdrawal is by nominee.

It is mandatory to attach copy of intimation for change in nominee in case intimation about change in the name of the nominee.

It is mandatory to attach proof of cessation of member in case of intimation of cessation of member.

**(20) E-Form INC-22-** Notice of situation or change of situation of registered office

eForm INC-22 is required to be filed pursuant to Section 12(2) & 12(4) of the Companies Act, 2013 and rule 25 & 27 of the Companies (Incorporation) Rules, 2014.

Time limit (days) for filing:

- (i) In case of a New Company – 30 days from the Date of Incorporation
- (ii) In case of an Existing Company – 15 days from date of shifting the registered office

Purpose of the eForm- The Company is required to furnish to the Registrar verification of its registered office in eForm INC-22 within a period of thirty days from the date of its incorporation. The company can also specify the address of registered office at the time of filing incorporation eForms. For this, the applicant shall upload eForm INC-22 as linked form to eForm INC-32. In case of One Person Company, the particulars of the registered office address can be filed in eForm INC-2 only. And any change in situation of the registered office thereafter, the company is required to notify to Registrar in eForm INC-22 within fifteen days of such change.

**Attachments:**

In case of New Company -

- Proof of registered office address (Conveyance/ Lease deed/ Rent Agreement etc. along with the rent receipts is required to be attached).
- Copies of the utility bills (proof of evidence of any utility service like telephone, gas, electricity etc. depicting the address of the premises not older than two months is required to be attached).
- Proof that the company is permitted to use the address as the registered office of the Company ..... (Authorization from the owner or occupant of the premises along with proof of ownership or occupancy and it is mandatory if registered office is owned by any other entity/ person (not taken on lease by company).

In case of existing company –

- Proof of Registered Office address (Conveyance/Lease deed/ Rent Agreement etc. alongwith the rent receipts).
- Copies of the utility bills (proof of evidence of any utility service like telephone, gas, electricity etc. depicting the address of the premises not older than two months is required to be attached). Altered Memorandum of association. This is mandatory to attach in case of shifting of registered office from one state to another within the jurisdiction of same RoC or from one state to another outside the jurisdiction of existing RoC.
- A proof that the Company is permitted to use the address..... Authorization from the owner or occupant of the premises along with proof of ownership or occupancy and it is mandatory if registered office is owned by any other entity/ person (not taken on lease by company).
- Certified copy of order of competent authority. It is mandatory to attach in case of shifting of registered office from one RoC to another within the same state or from one state to another within the jurisdiction of same RoC or from one state to another outside the jurisdiction of existing RoC.
- List of all the companies (specifying their CIN) having the same registered office address, if any. In case of change in registered office of a company within local limits of city, town or village or

outside local limits of city, town or village but within same state and with same RoC, then the company is required to file eForm MGT-14 (if applicable) and eForm INC-22.

In case the registered office of the company is shifted from the jurisdiction of one RoC office to another RoC office within the same state or otherwise then the company is required to file both eForm INC-23 for RD's approval and eForm INC-28 (old Form 21) for notice of RD's approval order and eForm INC-22 only once.

**(21) E-Form INC-27-** Conversion of public company into private company or private company into public company

eForm INC-27 is required to be filed pursuant to section 14 and 18 of the Companies Act, 2013 and rule 33 and 37 of Companies (Incorporation) Rules, 2014.

Time limit (days) for filing:

- (i) Conversion of private company into public company - 15 days from the date of passing the special resolution
- (ii) Conversion of public company into private company - 30 days from the date of receiving the order
- (iii) Conversion of Unlimited Liability Company into Limited Liability Company - 60 days from the date of passing the special resolution

Purpose of the eForm - For the purpose of conversion from private to public company, a private company is required to pass special resolution and file intimation in Form INC-27. A Public company can also get converted into a private company by filing Form INC-27 subject to passing the special resolution and approval of the competent authority. Further, an unlimited liability company can also convert itself into Limited Liability Company by filing form INC-27 subject to fulfillment of other requirements as notified.

**Attachments:**

- Minutes of the member's meeting where approval was given for conversion and alteration of the articles of association.
- Copy of Special Resolution
- Copy of Altered Articles of Association;
- Copy of Altered Memorandum of Association in case of conversion of Unlimited Liability Company to Limited Liability Company.
- Declaration of all Directors as per Rule 37(3)(e) and Rule 37(3)(g) in case of conversion of Unlimited Liability Company to Limited Liability Company.
- Complete list of creditors and debenture holders in case of conversion of Unlimited Liability Company to Limited Liability Company.
- Declaration of Solvency in case of conversion of Unlimited Liability Company to Limited Liability Company.
- Declaration regarding no complaints as per Rule 37(4) in case of conversion of Unlimited Liability Company to Limited Liability Company.
- Copy of Statutory Auditors Certificate in case of conversion of Unlimited Liability Company to Limited Liability Company.
- Copy of Newspaper publication in case of conversion of Unlimited Liability Company to Limited

Liability Company.

- Order of competent authority in case of conversion from public company to private company.
- Certified copy of order for condonation of delay in case form is filed after the prescribed due date

**(22) E-Form SH-7-** Notice to Registrar of any alteration of share capital

eForm SH-7 is required to be filed pursuant to Section 64 (1) of the Companies Act, 2013 and rule 15 of Companies (Share Capital & Debentures) Rules, 2014.

Time limit (days) for filing –

- (i) Increase in share capital independently by company – within 30 days from date of meeting.
- (ii) Increase in number of members – within 30 days from date of meeting.
- (iii) Increase in share capital with Central Government order within 30 days from date of receipt of order.
- (iv) Consolidation or division etc. within 30 days from effective date entered in field 7
- (v) Redemption of redeemable preference shares within 30 days from actual date of redemption.

Purpose of the eForm- Whenever a company alters its share capital/ number of members independently or increases the share capital by conversion of debentures/loans due to order of Central Government, then a return shall be filed with the registrar within 30 days of such alteration or increase. The return shall also be filed where the company redeems any redeemable preference shares.

**Attachments:**

- Certified true copy of the resolution for alteration of capital is mandatory in case of increase in share capital independently by company.
- Copy of order of central government is mandatory in case of increase in share capital with central Government order.
- Copy of the order of the tribunal is mandatory in case of increase in share capital with Central Government.
- Certified true copy of board resolution authorizing redemption of redeemable preference shares is displayed and mandatory in case of redemption of redeemable preference shares.
- Altered memorandum of association is mandatory in case of increase in share capital independently or by order of Central Government or increase in number of members.
- Altered articles of association is mandatory in case the same are altered.
- Working for calculations of ratios (in case of conversions) is mandatory in case of increase in share capital with central government order.

**(23) E-Form DIR-12-** Particulars of appointment of Directors and the key managerial personnel and the changes among them

eForm DIR-12 is required to be filed in pursuant to Sections 7(1)(c), 168 & 170 (2) of the Companies Act, 2013 and Rule 17 Of Companies (Incorporation) Rules, Rule 8, 15 & 18 of Companies (Appointment and Qualification of Directors) Rules, 2014.

Time limit (days) for filing - Appointment/ Cessation/ Change in designation of directors and the key managerial personnel – Within 30 days from the date of appointment/Cessation/change in designation.

Purpose of the eForm- Every company, whether new or existing, is required to file an eForm DIR-12 for particulars of its directors and key managerial personnel of the company with the Registrar, within 30 days from the date of appointment/ resignation and of any change taking place in their designations.

**Attachments:**

- Declaration of the appointee director, managing director, in Form No. DIR-2 is mandatory to attach in case of appointment of a Director / Manager / Company Secretary / CEO / CFO.
- Notice of resignation is mandatory to attach in case of cessation of a Director /Manager/ Company Secretary / CEO / CFO.
- Evidence of cessation is mandatory to attach in case of cessation of a Director / Manager/ Company Secretary / CEO / CFO.
- Interest in other entities of director it is mandatory to attach in case number of entities entered is more than one.

**(24) E-Form FC-2-** Return of alteration in the documents filed for registration by foreign company

eForm FC-2 is required to be filed pursuant to Section 380(3) of the Companies Act, 2013 and Rule 3(4) of the Companies (Registration of Foreign Companies) Rules, 2014.

**Purpose of the eForm**

Every foreign company on alterations in the charter or statute or any other instrument governing the company, alterations in the particulars of Director/Secretaries of the foreign company, any change in the registered or principal office of the company in the country of incorporation, any change in the particulars of authorized representative(s) of the company and any change in other places of business in India of the company, has to file eform FC-2 within 30 days of the alterations made. This eForm is required to be filed with Registrar of Companies and a copy is routed to concerned RoC of the respective state by the system. An alert is generated at the concerned RoC to inform of the filing done at RoC, Delhi.

Time limit (days) for filing - Within 30 days from Date of the alteration.

**Attachments:**

- Certified true copy of the Board resolution, if any
- Copy of the general meeting resolution
- Copy of approval letter (it is mandatory if any approval is required for such alteration).
- Translated version of the documents in English (in case documents attached are not in English).
- Particulars of alterations in the place of business in India of the company
- Particulars of alteration in details of the directors or secretaries
- Particulars of alterations in details of the company authorized representative

**(25) E-Form FC-3-** Annual accounts along with the list of all principal places of business in India established by foreign company

eForm FC-3 is required to be filed pursuant to Section 381 of the Companies Act, 2013 and Rule 4, 5 and 6 of Companies (Registration of Foreign Companies) Rules, 2014.

Time limit (days) for filing - 9 months from the close of financial year

### **Purpose of the eForm**

Every foreign company is required to prepare and file financial statements within a period of six months of the close of the financial year of the foreign company to which the financial statements relate to Delhi RoC in eForm number FC-3. It shall also prepare and file a list of places of business in India established by a foreign company as on date of the balance sheet in the same form. However, the Registrar can extend the said period to not more than three months on application made in writing.

### **Attachments:**

- Copy of latest consolidated financial statement of parent company (Mandatory).
- Copy of balance sheet and profit and loss account duly authenticated under section 381(1) (Mandatory).
- Statement of related party transactions
- Statement of repatriation of profits
- Statement of transfer of funds
- Approval letter obtained for every establishment in India by a foreign company
- In case the document is in any other language other than English, certified translation in English language is mandatory

**(26) E-Form CHG-1-** Application for registration of creation, modification of charge (other than those related to debentures)

eForm CHG-1 is required to be filed pursuant to Section 77, 78 and 79 and Section 384 and Rule 3(1) of the Companies Rules, 2014.

Time limit (days) for filing – within thirty days of creation of charge

### **Purpose of the eForm**

All the companies are required to file particulars for registration of charges created or modified within specified period to concerned Registrar of Companies. The charge can be created on various types of assets situated in or outside India and may be created in favour of lenders such as Banks or financial institutions. Every charge that is created or modified by the company is required to be filed in eForm CHG-1 to concerned RoC in case of Indian Company and RoC, Delhi in case of a foreign company.

### **Attachments:**

- Instrument(s) of creation or modification of charge.
- Instrument(s) evidencing .....which is already subject to charge .....such acquisitions, in case if there is any acquisition of property which is already subjected to charge.
- Particulars of all joint charge holders, if number of charge holder is more than one.

**(27) E-Form CHG-4-** Particulars for satisfaction of charge thereof

eForm CHG-4 is required to be filed pursuant to Section 82(1) of the Companies Act, 2013 and Rule 8(1) of Companies (Registration of Charges) Rules, 2014.

Time limit (days) for filing-Within 30 days of date of satisfaction of Charge

### **Purpose of the eForm**

Every company shall intimate the RoC of the payment or satisfaction (in full) of any charge relating to the company within 30 days from the date of such payment or satisfaction. Indian companies will file eForm CHG-4 with their concerned RoC and the foreign companies will file eForm CHG-4 with the Delhi RoC.

### **Attachments:**

- Letter of the charge holder stating that the amount has been satisfied is a mandatory attachment in all cases.
- Any other information can be provided as an optional attachment(s).

### **(28) E-Form CHG-6- Notice of appointment or cessation of receiver or manager**

eForm CHG-6 is required to be filed pursuant to section 84(1), 384 of the Companies Act, 2013 and Rule 9(1) of Companies (Registration of Charges) Rules, 2014.

Time limit (days) for filing –Within 30 Days of date of appointment or cessation

### **Purpose of the eForm**

Where any person obtains an order of the Court for appointment of any receiver or manager of the property of any company, subject to a charge or appoints such person or receiver under the power of any instrument, shall notify the RoC in eFormCHG-6 within 30 days of such order/appointment. The person appointed as receiver or manager shall also notify the RoC in eForm CHG-6 about the cessation of such appointment within 30 days of such cessation.

### **Attachments:**

- In case the appointment of receiver/manager is pursuant to an instrument then attach a copy of instrument.
- In case the appointment of receiver/manager is in pursuant to a court order then attach a copy of court order.
- List of specified property of the company in case the appointment relates to specified property of the company
- List of specified property of the company in case the appointment relates to income arising from specified property of the company.

### **(29) E-Form CHG-9- Application for registration of creation or modification of charge for debentures or rectification of particulars filed in respect of creation or modification of charge for debentures**

eForm CHG-9 is required to be filed pursuant to Sections 71(3), 77, 78 & 79 and Section 384 of the Companies Act, 2013 and Rule 3 of Companies (Registration of Charges) Rules, 2014.

Time limit (days) for filing –

- (i) Creation of new charge/ Modification of charge – Within 30 days of date of Creation/
- (ii) Modification of Charge

### **Purpose of the eForm**

All the companies are required to file particulars for registration of charges created or modified for the purpose of securing debentures or rectification of particulars filed in respect of creation or modification of charge on debentures within specified period to concerned Registrar of Companies. Every charge that is created or modified by the company is required to be filed in eForm CHG-9 to concerned RoC in case of

Indian Company and RoC, Delhi in case of a foreign company. E-Form CHG-9 can also be filed by the company or any person interested in charge for rectifying any omission or misstatement done in any previous filing.

**Attachments:**

- Certified true copy of resolution authorizing the issue of the debenture series is a mandatory in case of creation of charge.
- Instrument containing details of the charge created or modified is mandatory in all cases.
- Order of the Central Government is mandatory in case eForm is being filed for rectification of charges.

**(30) E-Form GNL-3-** Particulars of person(s) or Key managerial personnel charged or specified for the purpose of sub-clause (iii) or (iv) of clause 60 of section 2

eForm GNL-3 is required to be filed pursuant to Section 2(60) of the Companies Act, 2013. Time limit (days) for filing - Particulars of Key managerial personnel(s) or director(s) or charged or specified – Within 30 days from date of board resolution.

**Purpose of the eForm**

When a company charges any person with the responsibility of complying with the provisions of the Act, it has to file Form GNL-3, provided the person so charged has given his consent in this behalf to the Board. The consent of the charged person is taken on the same form. The withdrawal of the consent for the charged person is also filed through the same form. The purpose is to identify persons within the company for complying with the provisions of the Companies Act.

**Attachments:**

- Copy of board resolution passed for appointment or revocation is a mandatory attachment.

**(31) E-Form DIR-3-** Application for allotment of Director Identification Number

e-Form DIR-3 is required to be filed pursuant to Section 153 of the Companies Act, 2013 & Rule 9(1) of the Companies (Appointment and Qualification Of Directors) Rules, 2014.

**Purpose of the e-Form**

Any person intending to become a director in an existing company is required to make an application to MCA for allotment of a unique identification, namely, Director Identification Number (DIN) through this e-Form.

**Attachments:**

The following are the mandatory attachments to be filed in all cases:-

1. Proof of Identity of applicant

- In case of Indian nationals, Income-tax PAN
- In case of foreign nationals, passport
- Proof of identity enclosed with e-Form DIR-3 should also contain the date of birth of the applicant and the same should match the date of birth filled in the application form. In case the proof of identity does not indicate the date of Birth then additional proof of date of Birth, duly certified/ attested, should be attached.

2. Proof of residence of applicant

- Address proofs like passport, election (voter identity) card, and ration card, driving license, electricity bill, telephone bill or aadhaar shall be attached and should be in the name of applicant only.
- In case of Indian applicant, documents should not be older than 2 months from the date of filing of the e-Form.
- In case of foreign applicant, address proof should not be older than 1 year from the date of filing of the e-Form.

3. In case of proofs which are in languages other than Hindi / English, the proofs should be translated in Hindi / English from professional translator carrying his details (name, signature, address) and seal. In the case of foreign nationals, translation done by the notary of home country is also acceptable.

**(32) E-Form DIR-6-** Intimation of change in particulars of Director to be given to the Central Government e-Form DIR-6 is required to be filed pursuant to Rule 12(1) of the Companies (Appointment and Qualification of Directors) Rules, 2014.

Time limit (days) for filing: Within 30 days of the change in particulars.

**Purpose of the eForm**

A director having an approved DIN is required to intimate to MCA in case of change(s) in his particular(s) as stated in eForm DIR-3 /Old form DIN1 within a period of 30 days of any such change.

**Attachments:**

The following attachments are mandatory to be filed in all cases:

- Proof of change in particulars
- Proof of Identity of director/ designated partner
- In case of Indian nationals, Income-tax PAN is a mandatory requirement for proof of identity.
- In case of foreign nationals, passport is a mandatory requirement for proof of identity.
- Proof of residence of director/ designated partner
- Address proofs like bank statements, electricity bill, telephone bill, utility bills etc. shall be attached. In case of Indian director/ designated partner, documents should not be older than 2 months from the date of filing of the eForm.
- In case of foreign director/ designated partner, address proof should not be older than 1 year from the date of filing of the eForm.
- In case of proofs which are in languages other than Hindi/ English, the proofs should be translated in Hindi / English from professional translator carrying his details (name, signature, address) and seal.

**(33) E-Form DIR-9-** A Report by a company to ROC for intimating the disqualification of the director

eForm DIR-9 is required to be filed pursuant to Section 164(2) read with Rule 14(2) of the Companies(Appointment and Qualification of Directors) Rules, 2014.

Time limit (days) for filing: Within 30 days of the failure.

**Purpose of the eform DIR-9**

Whenever a company fails to file the financial statements or annual returns, or fails to repay any deposit,

interest, dividend, or fails to redeem its debentures, as specified in sub-section(2) of section 164, the company shall immediately file Form DIR-9, to the Registrar furnishing therein the names and addresses of all the directors of the company during the relevant financial years.

**(34) E-Form SPICe (INC-32)- Simplified Proforma for Incorporating Company Electronically (SPICe)**

eForm SPICe (INC-32) is required to be filed in pursuance of sections 4, 7, 12, 152 and 153 of the Companies Act, 2013 read with rules made there under.

**Purpose of the eForm**

E-Form SPICe (INC-32) deals with the single application for reservation of name, incorporation of a new company and/or application for allotment of DIN and/or application for PAN and TAN. This eForm is accompanied by supporting documents including details of Directors & subscribers, MoA and AoA etc. Once the eForm is processed and found complete, company would be registered and CIN would be allocated. Also DINs gets issued to the proposed Directors who do not have a valid DIN. Maximum three Directors are allowed for using this integrated form for filing application of allotment of DIN while incorporating a company. Also PAN and TAN would get issued to the Company.

**Attachments:**

1. Memorandum of Association – Mandatory only in the following cases:

- Section 8 company selected in field 1 (a) or - all or any of the non-individual first subscribers as entered in filed 6(b) are based outside India or
- Part I company selected in field 1 (a) or - Number of subscribers entered in the field 6(a)
- 'Total number of first subscribers (non-individual + individual)' are more than seven
- Section 8 company selected in field 1 (a) or
- all or any of the non-individual first subscribers as entered in filed 6(b) are based outside India or
- Part I company selected in field 1 (a) or
- Number of subscribers entered in the field 6(a)
- 'Total number of first subscribers
- If the address for correspondence is the address of registered office of the company, then following attachments are mandatory:

2. Articles of Association – Mandatory only in the following cases:

- (non-individual + individual) are more than seven

3. Affidavit and declaration by first subscriber(s) and director(s) – Mandatory in all cases

4. Proof of office address

5. Copies of utility bills that are not older than two months. If proposed name require approval of Central government then attach the following:

6. Copy of approval in case the proposed name contains any word(s) or expression(s) which requires approval from central government. If the proposed name is based on a registered trademark or is subject matter of an application pending for registration under the Trade Marks Act, then it is mandatory to attach:

7. Approval of the owner of the trademark or the applicant of such trademark for registration of Trademark If proposed name requires approval from any sectoral regulator, then it is mandatory to attach (if already received):

8. In principle approval from the concerned regulator If any subscriber to the proposed company is Foreign company and/or company incorporated outside India, then it is mandatory to attach:

9. Copy of certificate of incorporation of the foreign body corporate and resolution passed

Note: It is optional to attach Copy of certificate of incorporation in case the subscriber to the proposed company is Body Corporate.

If any subscriber to the proposed company is a Company itself, then it is mandatory to attach:

10. Resolution passed by Promoter Company. In case the name is similar to any existing company, then it is mandatory to attach:

11. A certified true copy of No objection certificate by way of board resolution /resolution

In case any of the director has any interest in the proposed company, then it is mandatory to attach:

12. Interest of first director(s) in other entities In case of an OPC, it is mandatory to attach:

13. Consent of nominee

14. Proof of identity and residential address of the nominee

If any one of the subscriber does not have a DIN, it is mandatory to attach:

15. Proof of identity and residential address of the subscribers

If any of the director (including subscriber cum director) does not have DIN, then it is mandatory to attach:

16. Proof of identity and residential address of such director.

17. Resolution of unregistered companies in case of Chapter XXI (Part I) Companies Authorized to Register, under the Act.

Any other information can be provided as an optional attachment. A separate declaration in format of INC-8 is not required to be attached. It is recommended to name the attachments with proper name.

For e.g. If PAN is attached as proof of identity then recommended name of the attachment is "PAN – Proof of Identity". This should be followed while attaching any attachment.

#### **Declaration**

- In the Declaration section, enter the applicant name and professional details.
- Select a professional (Chartered Accountant/ Company Secretary/ Cost Accountant/Advocate) from the list of drop down values who has been engaged for giving declaration under section 7(1) and such declaration is attached.
- Enter valid membership number and certificate number of the practicing professional.

#### **(35) E-Form SPICe MOA (INC-33)- e Memorandum of Association**

eForm SPICe MOA (INC-33) is required to be filed pursuant to Schedule I (see Sections 4 and 5) to the Companies Act, 2013.

#### **Purpose of the eForm**

Memorandum of Association

**(36) E-Form SPICe AOA (INC-34)-** e Articles of Association E-Form SPICe AOA (INC-34) is required to be filed pursuant to Schedule I (see Sections 4 and 5) to the Companies Act, 2013.

**Purpose of the eForm**

This document describes the System Requirements Specifications of Form SPICe AOA (INC-34). This document lays down the software requirements for the application that have been captured through a detailed study of the business functions.

**(37) E-Form URC-1-** Application by a company for registration under section 366

eForm URC-1 is required to be filed pursuant to Section 366 of the Companies Act, 2013 and Rule 3(2) of the Companies (Authorised to Registered) Rules, 2014.

Time limit (days) for filing - within 60 days from date of application of Form 2.1.

**Purpose of the eForm**

Any partnership firm, limited liability partnership, cooperative society, society or any other business entity formed under any other law for the time being in force consisting of seven or more members, may at any time register itself under Companies Act, 2013 as a Part I Company. For this purpose, eForm URC-1 shall be filed along with eForm INC-32.

**Attachments**

The following attachments are mandatory:

1. Particulars of members/partners along with the details of shares held by them
2. Declaration of two or more directors verifying the particulars of all members/ partners
3. Affidavit from all the members/partners for dissolution of the entity
4. Copy of the instrument constituting or regulating the entity
5. Copy of certificate of registration of the entity
6. Copy of Newspaper advertisement
7. Certificate from a CA/CS/CWA certifying the compliance with all the provisions of Stamp Act, to the extent applicable

**Conditional:**

8. Consent of majority of members is mandatory to be attached in case company is limited by shares or Unlimited company.
9. Consent of at least three-fourth of members agreeing for registration under this part is mandatory to be attached in case company is limited by guarantee.
10. No objection certificate from the concerned Registrar of Firms or Registrar of Companies (LLP) is mandatory to be attached in case type of entity is Firms/ LLP.
11. No objection certificate/Consent given by secured creditors is mandatory to be attached in case of any secured debt outstanding as on the date of application.
12. Copy of the resolution declaring the amount of guarantee is mandatory in case company is limited by guarantee.

Statement of accounts of the company, prepared not later than 6 days preceding the date of application

duly certified by auditor, if applicable

**(38) E-Form FC-1-** Information to be filed by foreign company

eForm FC-1 is required to be filed pursuant to Section 380(1)(a) to (h) and Rule 3(3) of the Companies (Registration of Foreign Companies) Rules, 2014.

Time limit (days) for filing - Within 30 days from the date of establishment of registered/principle place of business in India.

**Purpose of the eForm**

A foreign company shall file the particulars of the principal place of business in eform FC-1 within 30 days of establishment of place of business in India alongwith the required documents to RoC, Delhi. The Registrar of the corresponding state shall have access to these documents filed with the RoC, Delhi.

**Attachments:**

- Certified copy of the charter, statutes, or memorandum and articles of the company or other instrument constituting or defining the constitution of the company (Mandatory).
- List of directors and secretary of the foreign company (Mandatory).
- Power of attorney or board resolution in favour of the authorized representative(s) (Mandatory).
- Reserve bank of India approval letter (It is mandatory to attach attested copy of such (approval)).
- Copy of permission letter of other Authority(s)/Regulator(s), if any is required to be attached.

It is mandatory to attach following in case number entered is more than seven of respective field:

- Particulars of the persons covered u/s 379
- Details of the places of business other than principal place of business in India
- Details of the places of business established at any earlier occasion(s)
- Particulars of the authorized representatives
- Interest of authorized person(s) in other entities
- Particulars of subsidiary, holding or associate companies of the foreign company in India
- Particulars of related party of the foreign company

**(39) eForm CRA-4-** Form for filing Cost Audit Report with the Central Government.

eForm CRA-2 is required to be filed pursuant to section 148(6) of Companies Act, 2013 and rule 6(6) of the Companies (Cost Records and Audit) Rules, 2014.

**Purpose of the eForm**

Every cost auditor appointed shall submit the cost audit report to company within one hundred eighty days from the closure of the financial year in form CRA-3. Further company shall submit that cost audit report to the Central Government along with full information and explanation on every reservation or qualification marked by auditor within thirty days from the date of receipt of cost audit report in form CRA-4.

Time limit (days) for filing - Within 30 days of the date of receipt of the cost audit report from cost auditor.

**Attachments:**

- XBRL document in respect of the cost audit report and company's information and explanations

on every qualification and reservation contained therein

**(40) E-Form DPT-3- Return of deposits**

eForm DPT-3 is required to be filed pursuant to rule 16 of the of the Companies (Acceptance of Deposits) Rules, 2014.

Time limit (days) for filing - 30th June of every year

**Purpose of the eForm**

Every company to which the Companies (Acceptance of Deposits) Rules, 2014 apply, shall on or before the 30th day of June, of every year, file a return of deposit with the Registrar and furnish the information contained therein as on the 31st day of March of that year duly audited by the auditor of the company.

**Attachments:**

- Auditor's certificate
- Copy of trust deed – Mandatory if company has trust deed and details of same are mentioned in the form
- Copy of instrument creating charge – Mandatory if company has trust deed and details of same are mentioned in the form
- List of depositors - List of deposits matured, cheques issued but not yet cleared to be shown separately – Mandatory if company has balance of deposits outstanding at the end of the year.

**(41) eForm ADT-1- Information to the Registrar by Company for appointment of Auditor**

eForm ADT-1 is required to be filed pursuant to Section 139 (1) of the Companies Act, 2013and pursuant to rule 4(2) of the Companies (Audit and Auditors) Rules, 2014.

Time limit (days) for filing - 15 days from the date of appointment

**Purpose of the eForm**

On appointment/ reappointment of an auditor at the annual general meeting, the company shall file a notice of such appointment / reappointment with the Registrar within fifteen days of the meeting in which the auditor is appointed/re-appointed.

**Attachments:**

- Copy of the intimation sent by company
- Copy of written consent given by auditor
- Copy of resolution passed by the company

**(42) E-Form ADT-3- Notice of Resignation by the Auditor**

eForm ADT-3 is required to be filed pursuant to Section 140(2) of the Companies Act, 2013and Rule 8 of the Companies (Audit and Auditors) Rules, 2014.

Time limit (days) for filing - 30 days from the date of resignation.

**Purpose of the eForm**

Auditor resigning from the company shall file within 30 days from the date of resignation, a statement in Form ADT-3 with the registrar.

**Attachments:**

- Resignation letter.

**(43) E-Form DPT-4-** Statement regarding deposits existing on the commencement of the Act

eForm DPT-4 is required to be filed pursuant to section 74 (1) of the Companies Act, 2013 and rule 20 of the Companies (Acceptance of Deposits) Rules, 2014.

**Purpose of the eForm**

In respect of any deposit accepted by a company before the commencement of the Companies Act, 2013, the amount of such deposit or any interest thereon if remains unpaid as on the date of commencement this Act then such company shall file a statement of such details in Form DPT-4 within three months.

**Attachments:**

- Auditor's certificate

**(44) eForm INC-5-** One Person Company- Intimation of exceeding threshold

eForm INC-5 is required to be filed pursuant to Rule 6(4) of the Companies (Incorporation) Rules, 2014.

Time limit (days) for filing - 60 days from the date of exceeding the threshold.

**Purpose of the eForm**

One Person Company is required to give an intimation to the Registrar in Form No INC-5 informing that it has ceased to be a One Person Company by exceeding the threshold limit by virtue of either increase in its paid up share capital beyond fifty lakh rupees or increase in its average annual turnover during the relevant period beyond two crore rupees. OPC shall file this intimation within sixty days from the date of exceeding threshold and it will take necessary steps to convert itself into a private company or a public company as the case may be.

**Attachments:**

- Certified true copy of board resolution where person giving notice has been authorized
- Copy of the duly attested latest financial statements
- Certificate from a Chartered Accountant in practice for calculation of average annual turnover during the relevant period – This certificate is mandatory to attach if the threshold limit is exceeded on account of average annual turnover

**(45) E-Form PAS-3-** Return of allotment

eForm PAS-3 is required to be filed pursuant to Section 39(4) and 42(9) of the Companies Act, 2013 and rule 12 and 14 Companies (Prospectus and Allotment of Securities) Rules, 2014.

Time limit (days) for filing - 30 days from the date of allotment

**Purpose of the form**

To file return of allotment of shares and securities.

**Attachments:**

- List of allottees, separate list for each allotment is mandatory, please refer the format below in Annexure B

- Copy of Board or Shareholders' resolution approving allotment of shares is mandatory in all cases
- Valuation Report from the registered valuer is mandatory in case obtained from valuer.
- Copy of Contract/Complete particulars of contract duly stamped is mandatory to attach in case securities are issued other than cash
- Complete record of private placement offers and acceptances in Form PAS-5 is mandatory in case of private placement
- Copy of the special resolution authorizing the issue of bonus shares is mandatory in case of bonus issue.

**(46) E-Form SH-8-** Letter of offer

eForm SH-8 is required to be filed pursuant to Section 68 of the Companies Act 2013 rule 17(2) of the Companies (Share Capital & Debentures) Rules, 2014.

**Purpose of the eForm**

eForm SH-8 is required to be filled by the company for presenting letter of offer for buy back of its own shares or other securities. Letter of offer shall be filed by a company authorized by a special resolution for buyback of its own shares or other securities with the Registrar of Companies in eForm SH-8 before buy back.

**Attachments:**

The following attachments are mandatory:

- Details of the promoters of the company.
- Declaration by auditor(s).
- Certified true copy of the board resolution authorizing buy back.
- Copy of the notice of the general meeting issued under section 68(3) along with the explanatory Statement thereto,
- Audited financial statements of last three years.

Rest is based on applicability as mentioned in the eForm:

- Buy back details of last three years is mandatory in case company has done any buyback in the last three years.
- Management discussion and analysis is mandatory in case of listed company.
- List of holding and subsidiary companies of the company if applicable
- Unaudited financial statements if applicable
- Statutory approvals received (if any)
- Details of the auditor, legal advisors, bankers and trustees (if any)

**(47) E-Form SH-9-** Declaration of Solvency

eForm SH-9 is required to be filed pursuant to Section 68(6) of Companies Act 2013 and Rule 17(3) of the Companies (Share Capital & Debentures) Rules, 2014.

**Purpose of the form**

Declaration of Solvency

**Attachments:**

- Copy of Board resolution of the company
- Statement of assets and liabilities
- Auditor's report
- Affidavit as per rule 17(3)
- Copy of Special Resolution, if it was passed

**(48) E-Form SH-11-** Return in respect of buy-back of securities

eForm SH-11 is required to be filed pursuant to Section 68(10) of the Companies Act 2013 and pursuant to rule 17(13) of the Companies (Share Capital and Debentures) Rules, 2014.

Time limit (days) for filing - 30 days from the date of completion of buy back .

**Purpose of the eForm**

A company has to file return of buy back in eForm SH-11 to the Registrar within thirty days of completion of buy back containing the particulars of the buyback of shares and other securities.

**Attachments:**

The following attachments are mandatory:

- Description of shares or other specified securities bought back
- Particulars relating to holders of securities before buy-back
- Certified true copy of special resolution passed at the general meeting is mandatory in case date is entered in field 8(b)
- Certified true copy of board resolution authorizing buy back
- Balance Sheet of the company
- Compliance certificate for the buy-back rules as per the sub-rule (14)

**(49) E-Form MGT-14-** Filing of Resolutions and agreements to the Registrar

eForm MGT-14 is required to be filed pursuant to Section 94(1), 117(1) of the Companies Act, 2013 and Section 192 of the Companies Act, 1956 and rules made there under.

Time limit (days) for filing - Within 30 Days from the date of passing the resolution/postal ballot.

**Purpose of the eForm**

A company or liquidator has to file with the concerned RoC certain resolutions and agreements. These are to be filed after being passed at the meeting of the Board /Shareholders / Creditors of the company. The particulars of such resolutions or / and agreement are to be filed through this eForm. The provisions of Section 94 and 117 are applicable regarding registration of certain resolutions and agreements with RoC. The eForm has to be filed with RoC within 30 days of passing of the resolution or of the making of the agreement.

**Attachments:**

- Certified true copy of resolution(s) along with copy of explanatory statement under section 102 (Mandatory in case resolution or postal ballot is selected at serial no 3).
- Altered memorandum of association (Mandatory in case any change in MOA).

- Altered articles of association (Mandatory in case of any change in AOA).
- Copy of agreement (Mandatory in case agreement is selected at serial no 3).

**(50) E-Form DIR-11-** Notice of resignation of a director to the Registrar

eForm DIR-11 is required to be filed pursuant to Section 168 (1) of the Companies Act, 2013 and Rule 16 of Companies (Appointment and Qualification of Directors) Rules, 2014.

**Purpose of the eForm**

Director may resign from his office by giving a notice in writing to the company and he may also forward a copy of his resignation along with detailed reasons for the resignation to the Registrar within thirty days of resignation in eForm DIR-11. The resignation of a director shall take effect from the date on which the notice is received by the company or the date, if any, specified by the director in the notice, whichever is later.

**Attachments:**

The following attachments are mandatory:

- Notice of resignation filed with the company
- Proof of dispatch
- Acknowledgement received from company, if any and is mandatory if yes selected in option at serial no 6.
- Time limit (days) for filing - 30 days from Effective date of resignation.

**(51) E-Form GNL-2-** Form for submission of documents with the Registrar.

eForm GNL-2 is required to be filed pursuant to the Companies Act, 2013 and the Companies Act, 1956.

**Purpose of the eForm**

Company can file certain documents with the Registrar of Companies by filing this eForm GNL-2 and in case there is no eForm prescribed for filing any document with Registrar, then company can file such documents through this eForm.

- Copy of prospectus or information memorandum or private placement offer letter or record of private to be kept by the company
- Form 149 or form 152 or form 153 or form 154 or form 156 or form 157 or form 158 or form 159 of the Companies (Court) Rules, 1959
- Form SH-9: Declaration of solvency (Not applicable)
- Return of deposits or circular for inviting deposits or circular in the form of advertisement for inviting deposits

**(52) E-Form FC-4-** Annual Return of a foreign company

eForm FC-4 is required to be filed pursuant to Section 384(2) of the Companies Act 2013 and Rule 7 of Companies (Registration of Foreign Companies) Rules, 2014.

**Purpose of the eForm**

Every foreign company shall prepare and file annual return of the company in eForm FC-4 within 60 days from the close of financial year.

Time limit (days) for filing - 60 days from the date of balance sheet entered in field 4.

**Attachments:**

- Details of Promoters, Directors and Key managerial personnel and changes there in since close of previous financial year. (Mandatory)
- Details of directors and key managerial personnel and their remuneration.(Mandatory)
- Details of the meeting of the members or class thereof, board and its various committees along with attendance details. (Mandatory)
- Particulars of members and debenture holders along with changes therein since the close of previous financial year. (Mandatory)
- Particulars of Holding, subsidiary and associate companies and firms. (Mandatory in case number of entities prescribed at serial no 6 is more than seven)
- Details of Penalties / punishment/ Compounding of offences, if any. (optional)

**(53) E-Form MSC-3- Return of dormant companies**

eForm MSC-3 is required to be filed pursuant to Section 455 (5) of The Companies Act 2013, and Rule 7 of Companies Rules, 2014.

Time limit (days) for filing - 30 days from financial year end date

**Purpose of the eForm**

A dormant company shall file a return annually in eForm No. MSC-3 along with the annual fee within thirty days from the end of each financial year

**Attachments:**

- Certified true copy of Board resolution showing authorization given for filing this declaration. (Mandatory)
- Duly audited statement of financial position by a chartered accountant in practice.(Mandatory)

**(54) E-Form MGT-6- Persons not holding beneficial interest in shares**

eForm MGT-6 is required to be filed pursuant to section 89(6) of the Companies Act, 2013.

Time limit (days) for filing – Within 30 days from the date of receipt of declaration.

**Purpose of the eForm**

A company makes a declaration to the Registrar regarding persons whose name is in the register of members as a shareholder but they do not hold any beneficial interest in such shares. This form of return is filed within 30 days of receipt of declaration by the company by filing eForm MGT-6.

**Attachments:**

- Declaration by person who does not hold the beneficiary interest as per section 89 (1) is to be attached.
- Declaration by the person who holds the beneficiary interest 89 (2) is to be attached.
- Declaration by beneficial owner on any change in beneficial interest 89(3).

**(55) E-Form MGT-3- Notice of situation or change of situation or discontinuation of situation, of place where foreign register shall be kept.**

eForm MGT-3 is required to be filed pursuant to section 88(4) of the Companies Act, 2013 and rule 7(2) of the Companies (Management and Administration) Rules, 2014.

Time limit (days) for filing – 30 days from the date of such change or discontinuance of situation.

**Purpose of the eForm**

A company may, if so authorized by its articles, keep in any country outside India a part of the register of members/of debenture holders/of any other security holders/of beneficial owners, resident in that country. The company shall, within thirty days from the date of the opening of any foreign register, file with the Registrar notice of the situation of such place in Form No.MGT-3 where the register is kept. In the event of any change in the situation of such place or of its discontinuance, the same should be communicated within thirty days from the date of such change or discontinuance, as the case may be, in Form No.MGT-3 with the Registrar.

**(56) E-Form MGT-15-** Form for filing Report on Annual General Meeting

eForm MGT-15 is required to be filed pursuant to section 121(1) of the Companies Act,2013 and Rule 31(2) of Companies (Management and Administration) Rules, 2014.

Time limit (days) for filing - Within 30 days from the date of the Annual General Meeting.

**Purpose of the eForm**

Every listed public company shall prepare a report on each annual general meeting including the confirmation to the effect that the meeting was convened, held and conducted and file the same in eForm MGT-15 with ROC.

**(57) E-Form AOC-5-** Notice of address at which books of account are maintained

eForm AOC-5 is required to be filed pursuant to Section 128 of the Companies Act 2013.

Time limit (days) for filing - 7 days from the date of passing the board resolution.

**Purpose of the eForm**

Every company must keep proper books of account with respect to:

- all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure take place;
- all sales and purchases of goods by the company;
- the assets and liabilities of the company; and
- in the case of a company engaged in production, processing, manufacturing or mining activities, such particulars relating to utilization of material or labor or other items of cost as may be prescribed by the Central Government, provided the Central Government so directs to any such class of companies or any particular company. If the Board of Directors decides by passing the resolution to keep all or any of the books of account at any other place in India besides the registered office then, the company shall, within seven days of passing the Board Resolution, file this form giving full address of that other place in form AOC-5.

**Attachments:**

- Copy of Board resolution wherein a decision regarding address at which books of account are to be maintained has been taken is to be attached.

**(58) E-Form INC-20-** Intimation to Registrar of revocation/surrender of license issued under section 8

eForm INC-20 is required to be filed pursuant to section 8 (4) & 8 (6) of the Companies Act,2013 and rule 23 of Companies (Incorporation) Rules, 2014

### **Purpose of the eForm**

License granted to a company under section 8 may be revoked by the Central Government and on such revocation or the company itself wants to surrender the license granted, an intimation of such revocation or surrender of license shall be filed with the Registrar by the company in eForm INC-20. Registrar shall enter the word(s) "Limited" or "Private Limited" as the case may be at the end of the name of the company and the company shall cease to enjoy the exemptions/privileges granted to it under section 8 of the Act.

### **Attachments:**

- Copy of Order of Central Government
- Certified true copy of altered memorandum and articles of association
- It is mandatory to attach declaration of directors for compliance of conditions in case of surrender of license

### **(59) E-Form INC-28-** Notice of Order of the Court or any other competent authority

eForm INC-28 is required to be filed pursuant to Section 12(6), 13(7), 58(5), 87 & 111(5) of the Companies Act, 2013 and section 81(4), 102(1), 107(3), 167, 186, 391, 394, 396, 397,398, 445, 481, 466, 518, 559 & 621A of the Companies Act, 1956.

Time limit (days) for filing - within a period of sixty days of the date of confirmation who shall register the same.

### **Purpose of the eForm**

Registrar needs to be informed about the order of Court or Tribunal or any other competent authority for which the company or liquidator has to file eForm INC-28 with ROC informing about the order, which may take the form of approval or extension of time or condonation of non-compliance.

### **Attachments:**

- Copy of court order or NCLT or CLB or order by any other competent authority is a mandatory attachment.

### **(60) E-Form ICP-** Investor Complaint Form

### **Purpose of the eForm**

Any investor, shareholder, creditor, employee, deposit holder can file complaint related to shares, debentures, bonds, fixed deposits etc. against a company by filling Investor Complaints form. There is no fee for filing an Investor Complaint Form. Alternatively the investor, shareholder, creditor, employee, deposit holder can also lodge an investor complaint by handing over a written complaint directly to an MCA official in the office of Registrar of Companies. One Investor Compliant Form should be filed against only one company/ LLP and for one type of complaint. If there are multiple complaints against one company or LLP, file a different Investor Compliant Form for each type of Compliant. This will help in effective tracking and closure of complaint.

### **Attachments:**

- Identity proof of the complainant

### **(61) E-Form SCP-** Serious Complaint Form

A complainant can file a Serious Complaint eForm in the following cases by uploading a Serious Complain eForm:

- Cessation of Director
- Removal of Director
- Management Dispute
- Financial Mismanagement
- Corporate Fraud
- Accounting Fraud
- Oppression of Minority Shareholders
- Others

#### **Purpose of the eForm**

To register Serious Complaint against a company by filing E-Form with MCA Alternatively complainant can also lodge Serious Complaint by handing over a written complaint directly to MCA official in the office of Registrar of Companies.

#### **Attachments:**

- Attach identity proof of the complainant.
- In cases complaint is in respect of non-filing of Form No. 32/DIR-12 for cessation of a Director, correspondence with the company with respect to the cessation, attach the necessary proof of such correspondence

#### **(62) E-Form MR-2**

E-Form MR-2 is required to be filed pursuant to Section 196, 197, 200, 201(1) and 203(1) of the Companies Act, 2013 and rule 7 of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014.

Time Limit (days) for filing: E Form MR-2 is required to be filed within 90 days of appointment or reappointment.

#### **Purpose of the eForm**

In order to seek approval from Central Government for appointment, reappointment, payment of remuneration including increase in remuneration, waiver of excess remuneration to the managerial personnel (managing director or whole time director or manager) and payment of commission or remuneration to directors or modification in terms and conditions of appointment, company needs to file eForm MR-2.

#### **Attachments:**

- Copy of the calculation sheet of effective capital .....is mandatory in case Option 4 selected in field 4(a)
- Certified true copy of the resolution of Board of directors is mandatory in all cases.
- Copy of the resolution of nomination and remuneration committee..... is mandatory in case date entered in 10(b) or 14(b).
- Certified true copy of resolution of shareholder(s) along with notice ..... is mandatory in case date entered in 10(c) or 14(c).
- Certificate from the auditor or company secretary .....is mandatory in all cases.

- Certificate of no-default in repayment of debts..... if no selected in field 15.
- No objection certificate from the financial institutions(s) or bank(s) ..... if not selected in field 15.
- Copy of the order of BIFR or NCLT together with the copy of a scheme of revival or rehabilitation.
- Copy of draft agreement between the company and the proposed..... is mandatory incase option 1 selected in 4(a).
- Newspaper clipping in which notices ..... is mandatory in all cases.
- Copy of employment visa/ passport, in case the proposed appointee is a foreign citizen.
- Copies of educational or professional qualification certificate.
- Statement as per item (IV) of third proviso ..... is mandatory in case option 4 selected in 4(a).
- Projections of the Turnover and net profits for next three years.
- Calculation of estimated profit under section 198 of the Act is mandatory in all cases except option 1 of 4(a).
- Auditors Certificate pursuant to Section 164 of the Companies..... is mandatory in case option 1 selected in 4(a).
- An application under Section 460 of the Act for condonation of delay..... is mandatory in case no selected in field 4(b).
- Full and proper justification in favor of the proposal.....is mandatory in all cases.
- Documentary proof regarding compliance of the provisions ..... is mandatory in case option 1 selected in 4(a).
- Certificate by the secretary of the company or CA/CS in whole time practice to be notified erstwhile.
- Details, if Applicant Company is a subsidiary of listed company.
- Certificate from CA/CS in whole time practice along..... is mandatory in case option 3 selected in 4(a).

**(63) E-Form MR-1-** Return of appointment of MD/WTD/Manager

eForm MR-1 is filed in pursuant to Section 196, 197, and Schedule V of the Companies Act, 2013 and Rule 3 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules 2014.

Time limit (days) for filing - 60 days from the date of passing the board resolution.

**Purpose of the eForm**

In case the appointment of an key managerial personnel is made within the specified parameters (in accordance of schedule V of the Companies Act, 2013) then a return has to be filed in eForm MR-1 with RoC within 60 days from the date of such appointment. The provisions of section 196 are applicable to all the companies whether public or private and no company can appoint at the same time managing director and a manager. While the maximum term of Managing Director/ Whole Time Director & Manager has been fixed for 5 years at a time, it has been provided that no reappointment shall be made earlier than 1 year before the expiry of his term.

**Attachments:**

- Certified true copy of Board Resolution

- Certified true copy of shareholders resolution along with explanatory statement is mandatory in case passed for such appointment
- Copy of central government approval is mandatory in case appointee is convicted or detained as per Schedule V.
- Copy of letter of consent to act as a managing director, whole time director, or manager
- Copy of certificate by the Nomination and Remuneration Committee of the company, if any

**(64) AOC- 4 XBRL-** Form for filing XBRL document in respect of financial statement and other documents with the Registrar

AOC- 4 XBRL is required to be filed pursuant to section 137 of the Companies Act, 2013 and rule 12(2) of the Companies (Accounts) Rules, 2014 read with Companies (Filing of documents and forms in Extensible Business Reporting Language) Rules, 2015

Time limit (days) for filing:

1. Filing of Adopted financial statement by a OPC - 180 days from financial year end date
2. Provisional Un-adopted financial statement - 30 days from the actual date of AGM. In case date of AGM is not entered then due date of AGM (shall be extended due date if entered)
3. Filing of Adopted financial statement by a company other than OPC - 30 days from the date of Adjourned AGM. If not entered then actual date of AGM.
4. Revised financial statement u/s 130 or 131 - 30 days from the date of order of competent authority

### **Purpose of the eForm**

Every company needs to file its financial statements, including consolidated financial statement and mandatory attachments, within the prescribed time limit as per section 137. In case financial statements are not adopted in AGM then un-adopted financial statements need to be filed within 30 days of date of AGM (due date of AGM if AGM not held or extended due date, if any). Once financial statements are adopted then company shall file the adopted financial statements within 30 days of the AGM (actual or adjourned whichever is applicable). In case company revise the financial statement, then revised financial statements are required to be filed.

Certain classes of companies as notified under Companies (Filing of documents and forms in Extensible Business Reporting Language) Rules, 2015 by the Central Government are required to mandatorily file their financial statement in Extensible Business Reporting Language (XBRL) format. Other companies can also file their financial statement in XBRL format voluntarily. However, once, filed in XBRL format, they would be required to file subsequent financial statements only in XBRL format. Companies can file this eform for financial year commencing on or after 1st April 2014, for the following reasons:

- (i) Provisional unadopted financial statements
- (ii) Adopted financial statements
- (iii) Revised financial statements u/s 130
- (iv) Revised financial statements u/s 131

### **Attachments:**

1. XBRL financial statements duly authenticated as per section 134 (including Board's report, auditors' report and other documents) – This is a mandatory attachment
2. XBRL document in respect of Consolidated financial statement (Note- This is mandatory if company is having Subsidiary and Yes is

selected for consolidated Financial Statements)

3. Statement of subsidiaries as per section 129-Form AOC-1 (Note-To be attached in respect of Foreign subsidiaries)
4. Statement of the fact and reasons for not adopting balance sheet in the annual general meeting (AGM) (Note- This attachment is mandatory if nature of financial statements was selected as 'Provisional Un-adopted financial statements')
5. Statement of the fact and reasons for not holding the AGM. (Note- This attachment is mandatory if AGM was not held)
6. Approval letter of extension of financial year or AGM (Note- This attachment is mandatory if extension was granted for AGM or financial year)
7. Supplementary or test audit report under section 143 (Note- This attachment is mandatory if CAG of India had conducted supplementary or test audit under section 143)
8. Details of comments of CAG of India (Note-This attachment is mandatory if CAG of India had conducted supplementary or test audit under section 143)

**(65) E-Form MGT-7-** Form for filing annual return by a company.

eForm MGT-7 is required to be filed pursuant to Section 92(1) of the Companies Act, 2013 and rule 11(1) of the Companies (Management and Administration) Rules, 2014

Time limit (days) filing –

- (1) In case of company other than OPC – Within 60 days from AGM date or calculated due date of AGM whichever is earlier.
- (2) In case of One Person Company – Within 60 days from financial year end date plus 6 months.

#### **Purpose of the eForm**

Every company shall prepare an annual return in the form MGT-7 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) its members and debenture-holders along with changes therein since the close of the previous financial year
- (d) its promoters, directors, key managerial personnel along with changes therein since the close of the previous financial year;
- (e) meetings of members or a class thereof, Board and its various committees along with attendance details;
- (f) remuneration of directors and key managerial personnel;
- (g) 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;
- (h) matters relating to certification of compliances, disclosures as may be prescribed;
- (i) Shareholding pattern of the company; and such other matters as required in the form.

#### **Attachments:**

- List of shareholders, debenture holders shall be mandatory in case of company having share

capital and it has selected 'Yes' in field XIII 'Whether complete list of shareholders, debenture holders has been enclosed as an attachment'

- Approval letter for extension of AGM; Shall be enabled and mandatory in case 'Yes' selected in field I.(viii)(c)
- Copy of MGT-8; shall be enabled and mandatory in case anything entered in field XIV.
- Optional Attachment(s), if any shall be mandatory in case 'Yes' selected in field 4(iii)
- 'Separate sheet attached for details of transfers'.

**(66) E-Form AOC- 4-** Form for filing financial statement and other documents with the Registrar

eForm AOC-4 is required to be filed pursuant to Section 129(3), 137 of the Companies Act, 2013 and Rule 12(1) of the Companies (Accounts) Rules, 2014.

**Purpose of the eForm**

Every company needs to file its financial statements and mandatory attachments, via e-Form AOC-4 within the prescribed time limit as per section 137. In case financial statements are not adopted in AGM then un-adopted financial statements shall be filed within 30 days of date of AGM (due date of AGM if AGM not held or extended due date if any). Once financial statements are adopted then company shall file the adopted financial statements via e-form AOC-4 within 30 days of the AGM (actual or adjourned whichever is applicable).

In case company needs to revise the financial statement or Board's report under provisions of section 130 or section 131 then revised financial statements shall be filed via e-Form AOC-4.

Time limit (days) for filing –

- Adopted financial statements (in case of OPC) – Within 180 days from financial year end date.
- Provisional Unadopted financial statements (in case of other than OPC) – Within 30 days from actual date of AGM. In case date of AGM is not entered then due date of AGM (shall be extended due date, if extended)
- Adopted financial statements (in case of other than OPC) – Within 30 days from the date of Adjourned AGM. If not entered then actual date of AGM.
- Revised financial statements u/s 130 – Within 30 days from the date of order of competent authority
- Revised financial statements u/s 131 – Within 30 days from the date of order of competent authority

**Attachments:**

- Financial statements duly authenticated as per section 134 (including Board's report, auditors' report and other documents) – This is a mandatory attachment.
- Statement of subsidiaries as required under section 129 in the format of Form AOC-1 prescribed under the Companies (Accounts) Rules, 2014.
- Statement of the fact and reasons for not adopting balance sheet in the annual general meeting (AGM) – This attachment is mandatory if provisional unadopted financial statements are being filed.
- Statement of the fact and reasons for not holding the AGM - This attachment is mandatory if

AGM was not held.

- Approval letter of extension of financial year or AGM - This attachment is mandatory if any extension has been granted for AGM or financial year.
- Supplementary or test audit report under section 143 - This attachment is mandatory if CAG of India had conducted supplementary or test audit under section 143.
- Company CSR policy as per sub-section (4) of section 135.
- Details of other entity (ies): This attachment is mandatory in case any amount of CSR is spent not directly by company. Details of all such implementing agencies should be attached in that case.
- Details of salient features and justification for entering into contracts/arrangements/transactions with related parties as per sub-section (1) of section 188 - Form AOC-2.
- Details of comments of CAG of India - It is mandatory if C&AG of India had conducted supplementary or test audit under section 143.
- Secretarial Audit Report - This attachment is mandatory if Secretarial Audit was applicable
- Directors' report as per sub-section (3) of section 134 - This attachment is mandatory if the same was mentioned in the Segment VI of the eform.
- Details of remaining CSR activities: Details of CSR programmes/projects/activities not mentioned in e-form is mandatory to attach in excel sheet. Optional attachments (s)- if any.

**(67) E-Form AOC- 4 CFS-** Form for filing consolidated financial statements and other documents with the Registrar

eForm AOC-4 CFS is required to be filed pursuant to Section 129(3), 137 of the Companies Act, 2013 and Rule 6, 12(1) of the Companies (Accounts) Rules, 2014.

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### **Purpose of the eForm**

Every company needs to file its financial statements, including consolidated financial statement and mandatory attachments, within the prescribed time limit as per section 137.

For the purpose of filing, form AOC-4 is prescribed for standalone financial statement (if XBRL is not applicable for the company) and form AOC-4 CFS for consolidated financial statements.

In case financial statements (including CFS) are not adopted in AGM then un-adopted financial statements shall be filed within 30 days of date of AGM (due date of AGM if AGM not held or extended due date if any). Once financial statements are adopted then company shall file the adopted consolidated financial statements via e-form AOC-4 CFS within 30 days of the AGM (actual or adjourned whichever is applicable). In case company needs to revise the financial statement or Board's report under provisions of section 130 or section 131 then revised consolidated financial statements shall be filed via e-Form AOC-4 CFS.

Time limit (days) for filing –

1. Adopted consolidated financial statements (in case of OPC) - 180 days from financial year end date.
2. Provisional Un-adopted consolidated financial statements (in case of other than OPC) – 30 days from Actual date of AGM. In case date of AGM is not entered then due date of AGM (shall be

extended due date, if extended).

3. Adopted consolidated financial statements (in case of other than OPC) – 30 days from the date of Adjourned AGM. If not entered then actual date of AGM.
4. Revised consolidated financial statements u/s 130 – 30 days from the date of order of competent authority
5. Revised consolidated financial statements u/s 131 - 30 days from the date of order of competent authority

**Attachments:**

- Consolidated financial statements duly authenticated as per section 134 (including Board's report, auditors' report and other documents) – This is a mandatory attachment
- Statement of subsidiaries/associate companies/joint ventures as required under section 129 in the format of Form AOC-1 prescribed under the Companies (Accounts) Rules, 2014 – This is a mandatory attachment
- Supplementary or test audit report under section 143 - This attachment is mandatory if CAG of India had conducted supplementary or test audit under section 143
- Details of other entity(s) – This is an optional attachment
- Details of comments of CAG of India - This is mandatory if CAG of India had conducted supplementary or test audit under section 143
- Secretarial Audit Report - This attachment is mandatory if Secretarial Audit was applicable
- Directors' report as per sub-section (3) of section 134 - This attachment is mandatory if the same was mentioned in the Segment IV of the eform Professional Training Module for ICLS Probationary Officers 119

**(68) E-Form GNL-4-Addendum for rectification of defects or incompleteness.**

eForm GNL-4 (Form for filing Addendum for rectification of defects or incompleteness) is required to be filed pursuant to Rule 10 of the Companies (Registration offices and Fees) Rules, 2014.

**Purpose of the eForm**

User may require the applicant to provide some clarifications or additional document(s) in support of the form and details filed by the applicant which shall be submitted via form GNL-4. This functionality shall not be available for forms filed through STP mode. There may be cases where the amount of stamp duty paid through MCA21 system by the user in respect of any document is not correct and differential payment of stamp duty is required. In such cases, the user will have to pay the additional (differential) stamp duty through the MCA21 system and then file eForm GNL-4 (Addendum) mentioning the SRN of such payment.

**(69) E-Form Refund- Application for requesting refund of fees paid.**

**Purpose of the eForm**

The user is required to make various payments to avail MCA21 services. A number of instances have been observed where the users make multiple payments or incorrect payment or excess payment while using these services. In order to allow the stakeholders to claim refund of such payments, refund process has been introduced by MCA for both Companies and LLPs.

**Attachments:**

- Copy of challan duly acknowledged by bank in respect of SRN for which refund is sought

(Mandatory in case payment mode of SRN for which refund is sought is 'Offline')

- Copy of challan duly acknowledged by bank in respect of other SRN, if applicable (Mandatory in case payment mode of SRN of other transaction entered in field 10(a) is 'Offline')
- Scanned copy of cancelled cheque

**(70) E-Form DIR-5-** Application for surrender of Director Identification Number

eForm DIR-5 is required to be filed Pursuant to section 153 & rule 11(f) of Companies (Appointment and Qualification of Directors) Rules, 2014.

**Attachments:**

- Proof of Identity

For Indian Nationals: (Any one of the following):

- Income tax Permanent Account Number Card
- Voter's identity card
- Passport
- Driving licence 5
- Unique Identity Number (UIN)

For Foreign Nationals and Non Resident Indians:

- Passport
- Others
- Proof of residence

**(71) E-Form DIR-9-** A Report by a company to ROC for intimating the disqualification of the director

eForm DIR-9 is required to be filed pursuant to Section 164(2) read with rule 14(2) of the Companies (Appointment and Qualification of Directors) Rules, 2014.

**(72) E-Form DIR-10-** Form of application for removal of disqualification of directors eForm DIR-10 is required to be filed pursuant to Section 164(2) read with rule 14(5) of Companies (Appointment and Qualification of Directors) Rules, 2014.

**(73) FORM DPT-1-** Circular or circular in the form of advertisement inviting deposits

FORM DPT-1 is required to be filed pursuant to section 73 (2)(a) and section 76 and rule 4(1) and 4(2) of the Companies (Acceptance of Deposits) Rules, 2014.

**(74) Form NDH-1-** Return of Statutory Compliances

Form NDH-1 is required to be filed pursuant to sub rule (2) of rule 5 of Nidhi Rules, 2014.

**(75) Form NDH-2-** Application for extension of Time

Form NDH-2 is required to be filed pursuant to sub rule (3) of rule 5 of Nidhi Rules, 2014.

**Attachments:**

- Board resolution
- Detailed application
- Reasons and justification for the application

**(76) Form NDH-3-** Half Yearly Return

Form NDH-3 is required to be filed pursuant to rule 21 of Nidhi Rules, 2014.

(All information shall be furnished for the half year ended 30th September and 31st March

of every year; wherever space is not sufficient, separate sheet containing the required details shall be attached)

**(77) Form PAS-2-** Information Memorandum

Form PAS-2 is required to be filed pursuant to section 31(2) of the Companies Act, 2013 and rule 10 of Companies (Prospectus and Allotment of Securities) Rules, 2014.

**(78) Form PAS-4-** Private Placement Offer Letter

Form No PAS-4 pursuant to section 42 and rule 14(1) of Companies (Prospectus and Allotment of Securities) Rules, 2014.

**Attachments:**

- Copy of board resolution
- Copy of shareholders resolution

**(79) E-Form STK-2-** Application by company to ROC for removing its name from register of Companies eForm STK-2 is required to be filed pursuant to Section 248(2) of the Companies Act, 2013 and rule 4, 5, 6 & 8 of the Companies (Removal of Names of Companies from the Register of Companies) Rules, 2016.

Purpose of the eForm: A company may, after extinguishing all its liabilities, by a special resolution or consent of seventy five per cent members in terms of paid-up share capital, file an application in STK-2 to the Registrar for removing the name of the company from the register of companies.

**Attachments:**

- A statement of accounts showing the assets and liabilities of the Company made up to a day, not more than thirty days before the date of application and certified by a Chartered Accountant
- Copy of Board resolution authorizing the filing of this application Copy of special resolution passed or copies of consent obtained under sub-section (2) of section 248, as applicable;
- Indemnity bonds [to be given individually or collectively by the director(s)] in Form No. STK-3;
- Affidavit in Form No. STK-4 by every director of the company
- Copy of order of the concerned regulatory authority, if any, approving the filing of this application;
- Copy of relevant order for delisting, if any, from the concerned Stock Exchange

**Penalty for Filing False Documents/Statements with the Registrar**

According to Section 448 of the Companies Act 2013, 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 this Act or the rules made there under, any person makes a statement,—

- (i) which is false in any material particulars, knowing it to be false; or
- (ii) which omits any material fact, knowing it to be material, he shall be liable under section 447.

Further Section 447, without prejudice to any liability including repayment of any debt under this Act or any other law for the time being in force, any person who is found to be guilty of fraud, shall be

punishable with imprisonment for a term which shall not be less than six months but which may extend to ten years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud:

Provided that where the fraud in question involves public interest, the term of imprisonment shall not be less than three years.

### **MODE OF PAYMENT OF FEES**

MCA-21 system provides for the facility of payment of statutory fees through multiple modes i.e.

- (i) Off-line payment through a challan generated by the system and payment of fees at the counter of the notified bank branches through DDs/Cash;
- (ii) On-line payments through Internet Banking, Credit Cards [Master Card/ VISA], Debit Card and NEFT.
- (iii) Ministry has introduced 'Pay Later' facility through which user can upload the eForm/ generate SRN for MCA21 services in one step and make the payment at a later point in time using the online payment mode (Credit card or Internet banking). An eChallan shall be generated by the system at the time of eForm upload/ SRN generation. User shall be required to make the payment within the validity date as per the eChallan.
- (iv) User can make the payment through online payment mode i.e. Credit card or Internet banking through Pay Later.

### **XBRL**

XBRL stands for eXtensible Business Reporting Language. XBRL is a language for the electronic communication of business and financial data which has revolutionized business reporting around the world. It provides major benefits in the preparation, analysis and communication of business information. It offers cost savings, greater efficiency and improved accuracy and reliability to all those involved in supplying or using financial data.

XBRL is a data-rich dialect of XML (Extensible Markup Language), the universally preferred language for transmitting information via the Internet. It was developed specifically to communicate information between businesses and other users of financial information, such as analysts, investors and regulators. XBRL provides a common, electronic format for business reporting. It does not change what is being reported. It only changes how it is reported.

XBRL is a world-wide standard, developed by an international, non-profit-making consortium - XBRL International Inc. (XII). XII is made up of many hundred members, including government agencies, accounting firms, software companies, large and small corporations, academics and business reporting experts. XII has agreed the basic specifications which define how XBRL works.

### **XBRL tags**

In XBRL, information is not treated as a static block of text or set of numbers.

Instead, information is broken down into unique items of data (e.g. total liabilities = 100). These data items are then assigned mark-up tags that make them computer-readable. For example, the tag <Liabilities>100</Liabilities> enables a computer to understand that the item is liabilities, and it has a value of 100.

Computers can treat information that has been tagged using XBRL 'intelligently'; they can recognize,

process, store, exchange and analyse it automatically using software.

Because XBRL tags are formed in a universally-accepted way, they can be read and processed by any computer that has XBRL software. XBRL tags are defined and organized using categorization schemes called taxonomies.

### **XBRL taxonomies**

Different countries use different accounting standards. Reporting under each standard reflects differing definitions. The XBRL language uses different dictionaries, known as 'taxonomies', to define the specific tags used for each standard. Different dictionaries may be defined for different purposes and types of reporting. Taxonomies are the computer-readable 'dictionaries' of XBRL. Taxonomies provide definitions for XBRL tags, they provide information about the tags, and they organize the tags so that they have a meaningful structure.

As a result, taxonomies enable computers with XBRL software to:

- understand what the tag is (e.g. whether it is a monetary item, a percentage or text);

In tagging section, "N" refers to navigation, "A" refers to attaching the disclosures " T" refers to text entry etc

- what characteristics the tag has (e.g. if it has a negative value);
- its relationship to other items (e.g. if it is part of a calculation).

This additional information is called meta-data. When information that has been tagged with XBRL is transmitted, the meta-data contained within the tags is also transmitted.

Taxonomies differ according to reporting purposes, the type of information being reported and reporting presentation requirements. Consequently, a company may use one taxonomy when reporting to a stock exchange, but use a different taxonomy when reporting to a securities regulator. Taxonomies are available for most of the major national accounting standards around the world.

### **BENEFITS OF XBRL**

XBRL offers major benefits at all stages of business reporting and analysis. The benefits are seen in automation, cost saving, faster, more reliable and more accurate handling of data, improved analysis and in better quality of information and decision-making. All types of organisations can use XBRL to save costs and improve efficiency in handling business and financial information. Because XBRL is extensible and flexible, it can be adapted to a wide variety of different requirements. All participants in the financial information supply chain can benefit, whether they are preparers, transmitters or users of business data.

XBRL enables producers and consumers of financial data to switch resources away from costly manual processes, typically involving time-consuming comparison, assembly and re-entry of data. They are able to concentrate effort on analysis, aided by software which can validate and manipulate XBRL information. However, big the size of balance sheet is, .XML will be in a capsule form to project such details ,thus consuming lesser file size in comparison to normal .pdf attachments.

### **Data Collection and Reporting**

By using XBRL, companies and other producers of financial data and business reports can automate the processes of data collection. For example, data from different company divisions with different accounting systems can be assembled quickly, cheaply and efficiently if the sources of information have been upgraded to using XBRL. Once data is gathered in XBRL, different types of reports using varying subsets of the data can be produced with minimum effort. A company finance division, for example, could quickly and reliably generate internal management reports, financial statements for publication, tax and

other regulatory filings, as well as credit reports for lenders. Not only can data handling be automated, removing time-consuming, error-prone processes, but the data can be checked by software for accuracy.

An .XML document is more accurate and reliable. As the name suggest, an extensible reading of the financial statement and the board report is possible. The major changes in the financial structure or other changes in the nature of business or such other implications are given thrust so as to make the regulators and stakeholders have clarity on the company.

### **Data Consumption and Analysis**

Users of data which is received electronically in XBRL can automate its handling, cutting out time-consuming and costly collation and re-entry of information. Software can also immediately validate the data, highlighting errors and gaps which can immediately be addressed. It can also help in analysing, selecting, and processing the data for re-use. Human effort can switch to higher, more value-added aspects of analysis, review, reporting and decision-making. In this way, investment analysts can save effort, greatly simplify the selection and comparison of data, and deepen their company analysis. Lenders can save costs and speed up their dealings with borrowers. Regulators and government departments can assemble, validate and review data much more efficiently and usefully than they have hitherto been able to do.

### **Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015**

Rule 3 of the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015 provides that the following class of companies shall file their financial statement and other documents under section 137 of the Act, with the Registrar in e-form AOC-4 XBRL. The stand alone and the consolidated financial statements, if any, shall be filed in In AOC4-XBRL only. This is in contrary to the general AOC4 for standalone and AOC4 (CFS) for consolidated accounts. The following class of companies are:

- (i) all companies listed with any Stock Exchange(s) in India and their Indian subsidiaries; or
- (ii) all companies having paid up capital of rupees five crore or above;
- (iii) all companies having turnover of rupees hundred crore or above; or
- (iv) all companies which were hitherto covered under the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2011:

Provided that the companies in banking, insurance, power sector, non-banking financial companies and housing finance companies need not file financial statements under this rule.

Rule 4 of the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015 provides that a company required to furnish cost audit report and other documents to the Central Government under sub-section (6) of section 148 of the Act and rules made there under, shall file such report and other documents using the XBRL taxonomy given in Annexure-III for the financial years commencing on or after 1st April, 2014 in e-Form CRA-4 specified under the Companies (Cost Records and Audit) Rules, 2002.

W.E.F 01.04.2016, There is a separate taxonomy for IND-AS companies and these companies shall give their financials in IND-AS taxonomy only.

### **LESSON ROUND-UP**

- Filing and filing of forms is an important part of the secretarial function of a company secretary. Normally, where company appoints a company secretary, he is designated as the officer responsible for compliance under the Companies Act and other allied legislations. Therefore, for any lapse in complying with the various provisions of the Companies Act or such other legislations, for the compliance of which

the company secretary has been made responsible, he becomes liable as “officer in default”.

- Professionals are responsible for submitting/certifying documents (to be signed digitally by them) and system would accept most of these documents online without approval by Registrar of Companies or other officers of the Ministry. If a professional gives a false certificate or omits any material information knowingly, he is liable to punishment under section 447 and 448 of the Companies Act, 2013 besides disciplinary action by the Institute which issued the Certificate of Practice.
- An existing company registered under section 8 seeks to convert itself into a company of any other kind shall make an application to the Regional Director for conversion of its status. Once the approval is given by the Regional Director, the company shall cease to enjoy all the privileges/ concessions obtained by it on account of being a Section 8 company.
- Whenever a company makes any allotment of shares or securities, it is required to file a return of allotment in e Form PAS-3 to Registrar within thirty days of such allotment including the complete list of allottees to whom the securities have been issued.
- In case the appointment of a key managerial personnel is made within the specified parameters (in accordance of schedule V of the Companies Act, 2013) then a return has to be filed in e Form MR-1 with RoC within 60 days from the date of such appointment.
- Any partnership firm, limited liability partnership, cooperative society, society or any other business entity formed under any other law for the time being in force consisting of seven or more members, may at any time register itself under Companies Act, 2013 as a Part I Company. For this purpose, e Form URC-1 shall be filed along with.
- A foreign company file the particulars of the principal place of business in eform FC-1 within 30 days of establishment of place of business in India along with the required documents to RoC, Delhi. The Registrar of the corresponding state shall have access to these documents filed with the RoC, Delhi.

### SELF TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

1. Discuss E-Governance and MCA-21.
2. State the check points with reference to Form-7.
3. What are the modes of payment under filing of forms under Companies Act, 2013?
4. State the check points with reference to Form No. PAS-3.
5. State the check points with reference to Form No. FC-4

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# Lesson 14

## Global Developments

### LESSON OUTLINE

- Distinguishing features of Company Law in various countries
- Lesson Round up
- Self-Test Questions

### LEARNING OBJECTIVES

The governments the world over recognized the importance of companies as an engine for economic growth. It is widely acknowledged that companies have become the centre of or even the driving force behind the emergence and growth of modern global economy. Therefore, to ensure that companies continue to play their role as an engine for economic growth, there is an international drive to review, reconstruct and recognize the law governing companies. Several countries are also aiming to ensure that corporate activities function within a modern, and forward looking regulatory framework that supports and sustains their economic growth. This lesson covers salient features of company law emerged/ emerging in the following countries:

- United Kingdom
- The United States of America
- Australia
- Canada
- Hong Kong
- Singapore

## MODERNIZATION OF COMPANY LAW FOR GLOBAL COMPETITIVENESS

Most of the countries in the world today including UK, Hong Kong, Singapore, Australia and Canada are in the various stages of modernizing their company law. A fair modern and effective framework of company law is crucial to the performance of any economy and society. To achieve competitiveness, it is essential that while the law must balance the needs of many interests, for example, shareholders, directors, employees, creditors and customers, it must also avoid unnecessary burdens.

In the current national and international scenario of complex business operations, there is a need for simplifying corporate laws so that they are amenable to clear interpretation and provide a framework that would facilitate faster economic growth. It is also being recognised that the framework for regulation of corporate entities has not only to be in tune with the emerging economic scenario, it must also encourage good corporate governance and enable protection of the interests of investors and other stakeholders.

Growing emphasis on good corporate governance, corporate social responsibility and good corporate citizenship is predominantly influencing company law reforms the world over. Modernization of company law has in fact become a part of the drive to facilitate enterprise, enhance the attractiveness of the country as a preferred destination to do business and foster business competitiveness. The overall objective is to achieve a simple, consolidated and accessible company law. Simultaneously, worldwide the Company Law reforms are focusing on transparency through enhanced disclosures and increased accountability on the part of corporate owners while at the same time providing a flexible regime for small and medium businesses. Additionally, the reforms aim at cutting back on overly regulatory intervention, thus, providing companies operating flexibility to tune in conformity with changing environment.

The litmus test lies in the harmonization of company law with that of global standards, the process which has been started about a decade ago in most countries, so as to achieve global competitiveness.

## DISTINGUISHING FEATURES OF COMPANY LAW IN VARIOUS COUNTRIES

### United Kingdom (UK)

Company Law in UK has undergone major reforms under the Company Law Review (CLR), the objective of which was to modernize the legal framework in which companies operate. In 1998, the Government commissioned an independent Company Law Review Group, comprising experts, practitioners and business people to take a long-term fundamental look at core company law and to see how it could be brought up to date. The CLR conducted a thorough review and assessment and provided the essential blue print in the form of a Report in 2001. As a response to the final Report of the Company Law Review, the Government brought out White Paper on Company Law 2002, introducing which the then Competition Minister, Melanie Johnson stated "Our current company law is creaking with age and needs to modernize and reform. A thorough overhaul is needed to make the law clear and accessible".

The White Paper 2002 evoked huge response. Considering the suggestions received, the Department of Trade and Industry again released the UK White Paper on Company Law, 2005 which contained draft of the Companies Bill, and invited views. Consequently, New Company Law Reform Bill was introduced in Parliament in May, 2006 for discussion and approval.

The UK Companies Act, 2006 received Royal Assent on 8th November 2006. The Act has effectively replaced the previous companies' legislation with the exception of provisions relating to company investigations and community interest companies.

## Salient features of Company Law in United Kingdom (Companies Act, 2006)

### ***Mode of forming incorporated company (Section 7)***

Any one or more persons associated for a lawful purpose may, by subscribing their names to the memorandum of association and otherwise complying with the requirement of the Act in respect of registration, form an incorporated company, with or without limited liability. A company may not be so formed for an unlawful purpose.

### ***Minimum Authorized capital (public companies) (Section 763)***

The amount of share capital with which the public company is proposed to be registered, must not be less than the authorized minimum (£50,000 or the prescribed euro equivalent or such other sum as the Secretary of State may by order specify).

### ***Minimum membership (for carrying on business)***

If a company, other than a private company limited by shares or by guarantee, carries on business without having at least two members and does so for more than 6 months, a person who, for the whole or any part of the period that it so carries on business after those 6 months (a) is a member of the company and (b) knows that it is carrying on business with only one member, is liable (jointly and severally with the company) for the payment of the company's debts contracted during the period or, as the case may, that part of it. For the purpose of the said provision, references to a member of a company do not include the company itself where it is such a member only by virtue of its holding shares as treasury shares.

### ***Power of directors to bind the company***

In favour of a person dealing with a company in good faith, the power of the board of directors to bind the company, or authorize others to do so, shall be deemed to be free of any limitation under the company's constitution. For this purpose, a person deals with a company if he is a party to any transaction or other act to which the company is a party; a person shall not be regarded as acting in bad faith by reason only of his knowing that an act is beyond the powers of the directors under the company's constitution; and a person shall be presumed to have acted in good faith unless contrary to be proved.

The references above to limitations on the directors' powers under the company's constitution include limitations deriving from a resolution of the company in general meeting or a meeting of any class of shareholders, or from any agreement between the members of the company or of any class of shareholders.

### ***Treasury Shares (Section 724)***

Where qualifying shares are purchased by a company out of distributable profits, the company may (a) hold shares (or any of them) or (b) deal with any of them, at any time, in accordance with section 727 or 729 for disposal and cancellation of treasury shares. When shares are held under (a) above, then the name of the company must be entered in the register as the member holding those shares. For the purpose of the Act, references to a company holding shares as treasury shares are references to the company holding shares which (a) were (or are treated as having been) purchased by it in circumstances in which this section applies, and (b) have been held by the company continuously since they were so purchased. (or treated as purchase).

Where a company has shares of only one class, the aggregate nominal value of shares held as treasury shares must not at any time exceed 10 per cent of the nominal value of the issued share capital of the company at that time.

***Directors (Section 154)***

Every public company shall have at least two directors and every private company is required to have at least one director.

***Minimum age for appointment as director (Section 157)***

A person may not be appointed a director of a company unless he has attained the age of 16 years.

***Appointment of directors of public company to be voted on individually (Section 160)***

A motion for the appointment of two or more persons as directors of the company by a single resolution at a general meeting of a public company can not be made. It can be done, if a resolution in this regard has first been agreed to by the meeting without any vote being given against it.

***Validity of acts of directors (Section 161)***

The acts of a person acting as a director are valid even if it is afterwards discovered—

- (1) that there was a defect in his appointment;
  - (a) that he was disqualified from holding office;
  - (b) that he had ceased to hold office;
  - (c) that he was not entitled to vote on the matter in question.
- (2) This applies even if the resolution for this appointment is void under section 160.

***Register of directors (Section 162, 163, 164, 165)***

Every company must keep a register of its directors. The register must contain the following particulars of each person who is a director of the company:

- in the case of an individual—

name and any former name; a service address; the country or state (or part of the United Kingdom) in which he is usually resident; nationality; business occupation (if any); date of birth.
- in the case of a body corporate, or a firm that is a legal person under the law by which it is governed— corporate or firm name; registered or principal office;
- in the case of an EEA company to which the First Company Law Directive (68/151/EEC) applies, particulars of—
  - (i) the register in which the company file mentioned in Article 3 of that Directive is kept (including details of the relevant state), and (ii) the registration number in that register;
- in any other case, particulars of—

the legal form of the company or firm and the law by which it is governed, and if applicable, the register in which it is entered (including details of the state) and its registration number in that register.

The register must be kept available for inspection –

- (a) at the company's registered office, or
- (b) at a place specified in regulations

The company must give notice to the Registrar of the place at which the register is kept available for inspection, and of any change in that place, unless it has at all times been kept at the company's registered office.

The register must be open to the inspection of any member of the company without charge, and of any other person on payment of such fee as may be prescribed.

***Resolution to remove director (Section 168)***

A company may by ordinary resolution at a meeting remove a director before the expiration of his period of office, notwithstanding anything in any agreement between it and him.

Special notice is required of a resolution to remove a director or to appoint somebody instead of a director so removed at the meeting at which he is removed.

A vacancy created by the removal of a director under this section, if not filled at the meeting at which he is removed, may be filled as a casual vacancy.

***Duty of directors (Section 171)***

A director of a company must—

- (a) act in accordance with the company's constitution, and
- (b) only exercise powers for the purposes for which they are conferred.

***General Duties***

- Duty to promote the success of the company. (Section 172)
- Duty to exercise independent judgment. (Section 173)
- Duty to exercise reasonable care, skill and diligence. (Section 174)
- Duty to avoid conflicts of interest. (Section 175)
- Duty not to accept benefits from third parties. (Section 176)
- Duty to declare interest in proposed transaction or arrangement. (Section 177)
- Duty to declare interest in existing transaction or arrangement. (Section 182)
- A General notice in accordance with section 185 is a sufficient declaration of interest in relation to the matters to which it relates.

***Duty to prepare directors' remuneration report (Section 420 & 422)***

The directors of a quoted company shall for each financial year prepare a directors' remuneration report which shall contain the information specified in the Schedule to Act and comply with any requirement of that Schedule as to how the information is to be set out in the report. The directors' remuneration report shall be approved by the Board of directors and signed on behalf of the Board by a director or the secretary of the company. Every copy of the said report which is laid before the company in general meeting or which is otherwise circulated, published or issued, shall state the name of the person who signed it on behalf of the Board. The copy of the directors' remuneration report which is delivered to the registrar shall be signed on behalf of the Board by a director or the secretary of the company.

***Members' approval of directors' remuneration report (Section 439)***

The company must, prior to the meeting, give to the members of the company notice of the resolution to be

moved at the meeting, as an ordinary resolution for approving the directors' remuneration report for the financial year. Notice shall be given to each such member in any manner permitted for the service on him of notice of the meeting. The business that may be dealt with at the meetings shall include the resolution. The existing directors must ensure that the resolution is put to vote at the meeting. No entitlement of a person to remuneration is made conditional on the resolution being passed by reason only of the provision made. If there solution is not put to vote at the meeting, each existing director is guilty of an offence and liable to a fine.

**Secretary (Section 270, 271, 273)**

A Private Company is not required to have a Secretary. A public company must have a secretary. It is the duty of the directors of a public company to take all reasonable steps to secure that the secretary (or each joint secretary) of the company –

- (a) is a person who appears to them to have the requisite knowledge and experience to discharge the functions of secretary of the company, and
- (b) has one or more of the following qualifications.

The qualifications are–

- (a) That he has held the office of secretary of a public company for atleast three of the five years immediately preceding his appointment as secretary;
- (b) that he is a member of any of the bodies specified as below–
  - a. the Institute of Chartered Accountants in England and Wales;
  - b. the Institute of Chartered Accountants of Scotland;
  - c. the Association of Chartered Certified Accountants;
  - d. the Institute of Chartered Accountants in Ireland;
  - e. the Institute of Chartered Secretaries and Administrators;
  - f. the Chartered Institute of Management Accountants;
  - g. the Chartered Institute of Public Finance and Accountancy.
- (c) that he is a barrister, advocate or solicitor called or admitted in any part of the United Kingdom;
- (d) that he is a person who, by virtue of his holding or having held any other position or his being a member of any other body, appears to the directors to be capable of discharging the functions of secretary of the company.

**Duty to keep register of secretaries (Section 275)**

- (1) A company must keep a register of its secretaries.
- (2) The register must contain the required particulars of the person who is, or persons who are, the secretary or joint secretaries of the company.
- (3) The register must be kept available for inspection–
  - (a) at the company's registered office, or
  - (b) at a place specified in regulations
- (4) The company must give notice to the registrar–

- (a) of the place at which the register is kept available for inspection, and
- (b) of any change in that place,  
  - unless it has at all times been kept at the company's registered office.
- (5) The register must be open to the inspection–
  - (a) of any member of the company without charge, and
  - (b) of any other person on payment of such fee as may be prescribed.

***Duty to notify registrar of changes (Section 276)***

- (1) A company must, within the period of 14 days from–
  - a. a person becoming or ceasing to be its secretary or one of its joint secretaries, or
  - b. the occurrence of any change in the particulars contained in its register of secretaries,
 give notice to the registrar of the change and of the date on which it occurred.
- (2) Notice of a person having become secretary, or one of joint secretaries, of the company must be accompanied by consent by that person to act in the relevant capacity.
- (3) If default is made in complying with this section, an offence is committed by every officer of the company who is in default.  
 For this purpose a shadow director is treated as an officer of the company.
- (4) A person guilty of an offence under this section is liable on summary conviction to a fine not exceeding level 5 on the standard scale &, for continued contravention, a daily default fine not exceeding one-tenth of level 5 on the standard scale.

***Duty to keep accounting records (Section 386)***

- (1) Every company must keep adequate accounting records.
- (2) Adequate accounting records means records that are sufficient–
  - (a) to show and explain the company's transactions,
  - (b) to disclose with reasonable accuracy, at any time, the financial position of the company at that time, and
  - (c) to enable the directors to ensure that any accounts required to be prepared comply with the requirements of this Act (and, where applicable, of Article 4 of the IAS Regulation).
- (3) Accounting records must, in particular, contain–
  - (a) Entries from day to day of all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure takes place, and
  - (b) a record of the assets and liabilities of the company.
- (4) If the company's business involves dealing in goods, the accounting records must contain–
  - (a) statements of stock held by the company at the end of each financial year of the company,
  - (b) all statements of stock takings from which any statement of stock as is mentioned in paragraph (a) has been or is to be prepared, and

- (c) except in the case of goods sold by way of ordinary retail trade, statements of all goods sold and purchased, showing the goods and the buyers and sellers in sufficient detail to enable all these to be identified.

***Where and for how long records to be kept (Section 388)***

- (1) A company's accounting records–
  - (a) must be kept at its registered office or such other place as the directors think fit, and
  - (b) must at all times be open to inspection by the company's officers.
- (2) If accounting records are kept at a place outside the United Kingdom, accounts and returns with respect to the business dealt with in the accounting records so kept must be sent to, and kept at, a place in the United Kingdom, and must at all times be open to such inspection.
- (3) The accounts and returns to be sent to the United Kingdom must be such as to–
  - (a) disclose with reasonable accuracy the financial position of the business in question at intervals of not more than six months, and
  - (b) enable the directors to ensure that the accounts required to be prepared under this Part comply with the requirements of this Act (and, where applicable, of Article 4 of the IAS Regulation).
- (4) Accounting records that a company is required by section 386 to keep must be preserved by it–
  - (a) in the case of a private company, for three years from the date on which they are made;
  - (b) in the case of a public company, for six years from the date on which they are made.

***A company's financial year (Section 390)***

A company's financial year is determined as follows. Its first financial year–

- (a) begins with the first day of its first accounting reference period, and
- (b) ends with the last day of that period or such other date, not more than seven days before or after the end of that period, as the directors may determine.

Subsequent financial years–

- (a) begin with the day immediately following the end of the company's previous financial year, and
- (b) end with the last day of its next accounting reference period or such other date, not more than seven days before or after the end of that period, as the directors may determine.

In relation to an undertaking that is not a company, references in this Act to its financial year are to any period in respect of which a profit and loss account of the undertaking is required to be made up (by its constitution or by the law under which it is established), whether that period is a year or not.

The directors of a parent company must secure that, except where in their opinion there are good reasons against it, the financial year of each of its subsidiary undertakings coincides with the company's own financial year. The directors of a parent company must secure that, except where in their opinion there are good reasons against it, the financial year of each of its subsidiary undertakings coincides with the company's own financial year.

***Accounts to give true and fair view (Section 393)***

The directors of a company must not approve accounts for the purposes of this Chapter unless they are

satisfied that they give a true and fair view of the assets, liabilities, financial position and profit or loss—

- (a) in the case of the company's individual accounts, of the company;
- (b) in the case of the company's group accounts, of the undertakings included in the consolidation as a whole, so far as concerns members of the company.

The auditor of a company in carrying out his functions under this Act in relation to the company's annual accounts must have regard to the directors' duty under sub-section (1).

***Duty to prepare individual accounts (Section 394)***

The directors of every company must prepare accounts for the company for each of its financial years. (unless the company is exempt from the requirement under section 394A). Those accounts are referred to as the company's "individual accounts".

***Approval and signing of accounts (Section 414)***

- (1) A company's annual accounts must be approved by the board of directors and signed on behalf of the board by a director of the company.
- (2) The signature must be on the company's balance sheet.
- (3) If the accounts are prepared in accordance with the provisions applicable to companies subject to the small companies regime, the balance sheet must contain a statement to that effect in a prominent position above the signature.

Every copy of the balance sheet which is laid before the company in general meeting or which otherwise circulated, published or issued, shall state the name of the person who signed the balance sheet on behalf of the Board. The copy of the company's balance sheet which is delivered to the Registrar shall be signed on behalf of the Board by a director of the company.

If annual accounts are approved that do not comply with the requirements of this Act, every director of the company who—

- (a) knew that they did not comply, or was reckless as to whether they complied, and
- (b) failed to take reasonable steps to secure compliance with those requirements or, as the case may be, to prevent the accounts from being approved, commits an offence.

A person guilty of an offence under this section is liable—

- (a) on conviction on indictment, to a fine;
- (b) on summary conviction, to a fine not exceeding the statutory maximum.

***Approval and signing of directors' report (Section 419)***

- (1) The directors' report must be approved by the board of directors and signed on behalf of the board by a director or the secretary of the company.
- (2) If in preparing the report, advantage is taken of the small companies exemption, it must contain a statement to that effect in a prominent position above the signature.
- (3) If a directors' report is approved that does not comply with the requirements of this Act, every director of the company who—
  - a. knew that it did not comply, or was reckless as to whether it complied, and
  - b. failed to take reasonable steps to secure compliance with those requirements or, as the case

may be, to prevent the report from being approved, commits an offence.

- (4) A person guilty of an offence under this section is liable—
- a. on conviction on indictment, to a fine;
  - b. on summary conviction, to a fine not exceeding the statutory maximum.

***Duty to file accounts and reports with the registrar (Section 441)***

The directors of a company must deliver to the registrar for each financial year the accounts and reports required by—

- section 444 (filing obligations of companies subject to small companies regime),
- section 445 (filing obligations of medium-sized companies),
- section 446 (filing obligations of unquoted companies), or
- section 447 (filing obligations of quoted companies).

This is subject to section 448 (unlimited companies exempt from filing obligations) and section 448A (dormant subsidiaries exempt from filing obligations).

***Period allowed for laying and delivering accounts and reports (Section 442)***

This section specifies the period allowed for directors of a company to comply with their obligation under Section 441 to deliver accounts and reports for a financial year to the Registrar. This is referred to in the Companies Acts as the “period for filing” those accounts and reports.

The period allowed for laying and delivering accounts and reports is for a private company, 9 months after the end of the relevant accounting reference period, and for a public company, 6 months after the end of that period. If the relevant accounting reference period is the company’s first and is a period of more than 12 months, the period allowed is (a) 9 months or 6 months, as the case may be, from the first anniversary of the incorporation of the company, or (b) 3 months after the end of the accounting reference period, whichever last expires.

The ‘relevant accounting reference period’ means the accounting reference period by reference to which the financial year for the accounts in question was determined.

***Requirement for audited accounts (Section 475)***

A company’s annual accounts for a financial year must be audited in accordance with this Part (Part 16) unless the company—

- (a) is exempt from audit under section 477 (small companies), section 479A (subsidiary companies), or section 480 (dormant companies); or
- (b) is exempt from the requirements of this Part under section 482 (non profit-making companies subject to public sector audit).

A company is not entitled to any such exemption unless its balance sheet contains a statement by the directors to that effect.

A company is not entitled to exemption under any of the provisions mentioned in sub-section (1)(a) unless its balance sheet contains a statement by the directors to the effect that—

- (a) the members have not required the company to obtain an audit of its accounts for the year in

question in accordance with section 476, and

- (b) the directors acknowledge their responsibilities for complying with the requirements of this Act with respect to accounting records and the preparation of accounts.

The statement required by sub-section (2) or (3) must appear on the balance sheet above the signature required by section 414.

***Right of members to require audit (Section 476)***

The members of a company that would otherwise be entitled to exemption from audit under any of the provisions mentioned in section 475(1)(a) may by notice under this section require it to obtain an audit of its accounts for a financial year.

The notice must be given by—

- (a) Members representing not less in total than 10% in nominal value of the company's issued share capital, or any class of it, or
- (b) if the company does not have a share capital, not less than 10% in number of the members of the company.

The notice may not be given before the financial year to which it relates and must be given not later than one month before the end of that year.

***Duties of auditor (Section 498)***

- (1) A company's auditor, in preparing his report, must carry out such investigations as will enable him to form an opinion as to—
  - a. whether adequate accounting records have been kept by the company and returns adequate for their audit have been received from branches not visited by him, and
  - b. whether the company's individual accounts are in agreement with the accounting records and returns, and
  - c. in the case of a quoted company, whether the auditable part of the company's directors' remuneration report is in agreement with the accounting records and returns.
- (2) If the auditor is of the opinion—
  - a. That adequate accounting records have not been kept, or that returns adequate for their audit have not been received from branches not visited by him, or
  - b. That the company's individual accounts are not in agreement with the accounting records and returns, or
  - c. in the case of a quoted company, that the auditable part of its directors' remuneration report is not in agreement with the accounting records and returns,

the auditor shall state that fact in his report.
- (3) If the auditor fails to obtain all the information and explanations which, to the best of his knowledge and belief, are necessary for the purposes of his audit, he shall state that fact in his report.
- (4) If—
  - a. the requirements of regulations under section 412 (disclosure of directors' benefits:

remuneration, pensions and compensation for loss of office) are not complied with in the annual accounts, or

- b. in the case of a quoted company, the requirements of regulations under section 421 as to information forming the auditable part of the directors' remuneration report are not complied within that report,

the auditor must include in his report, so far as he is reasonably able to do so, a statement giving the required particulars.

- (5) If the directors of the company (a) have prepared accounts and reports in accordance with the small companies regime or (b) have taken advantage of small companies exemption in preparing the director's report, and in the auditor's opinion they were not entitled so to do, the auditor shall state that fact in his report.

### ***Resolution removing auditor from office (Section 510)***

- (1) The members of a company may remove an auditor from office at anytime.
- (2) This power is exercisable only—
  - a. by ordinary resolution at a meeting, and
  - b. in accordance with section 511 (special notice of resolution to remove auditor).
- (3) Nothing in this section is to be taken as depriving the person removed of compensation or damages payable to him in respect of the termination—
  - c. of his appointment as auditor, or
  - d. of any appointment terminating with that as auditor.
- (4) An auditor may not be removed from office before the expiration of his term of office except by resolution under this section.

### ***Annual Return***

Part 24 of the Companies Act 2006 of UK relates to a Company's Annual Return.

### ***Duty to deliver Annual Return (Section 854)***

Every company must deliver to the registrar successive annual return each of which is made up to a date not later than the date that is the Company's return date.

The Company's return date is the anniversary of the Company's incorporation or if the Company's last return delivered in accordance with this part was made up to a different date, then the anniversary of that date.

### ***Contents of Annual Return (Section 855-857)***

- General – address of the registered office, type of company and its principal business activities, particulars of Directors, Secretary, etc.
- Information about share capital
- Information about shareholders, etc.

## B. The United States of America (USA)

The United States is undoubtedly one of the richest sources of legislation, case laws and debate about corporations. There is no federal corporations' statute as such. Each state has its own corporate law regime which resulted in competition among states to attract incorporations. State incorporation has produced a wide diversity of legislation and experimentation in the corporate form. The situation is, however not as chaotic as might be implied by the existence of nearly fifty different corporate laws operating in the same country. There are several mitigating factors promoting harmonization, cooperation and, in some cases, uniformity across the United States.

The first is the federal Constitution. Although there is no express federal jurisdiction to govern incorporations, the various clauses of interstate commerce provides a myriad of federal legislative provisions which apply to state in corporate entities. In this way, uniformity of standards and treatment in certain cases are as is assured i.e., anti- trust, bankruptcy, securities, among others. In addition, the court structure is such that the so-called “diversity jurisdiction” of the federal court system may catch commercial litigation, thus developing a body of federal case law applicable to corporations.

The most significant of these federal laws applicable to corporations is the federal securities regime. The United States has a long tradition of individual ownership of securities. It began with the bonds of railroads and other enterprises as they developed early in the history of the country and particularly during the post-civil war period. This wide dispersion of ownership resulted in the separation of ownership and control; the predominance of individual ownership is reflected in the federal securities laws adopted in 1933 and 1934 (in reaction to the stock market crash of 1929) in the interests of public investor protection. The agency created to administer this legislation, the Securities and Exchange Commission (SEC), has grown to be one of the most powerful administrative agencies in the world. Although there have been jurisdictional battles between the SEC and state legislatures over where the lines are drawn between corporate law matters and securities law matters (in the realm of takeovers, for example, during the 1980s), it remains the case that many areas of overlap respecting shareholders have been pre-empted by SEC action. Thus many matters characterized as “company law” elsewhere have been characterized in the United States as securities law and taken out of the orbit of the state legislatures.

A second harmonizing factor has been the existence of model statutes. These serve variously as uniform acts or as drafting guides which may be customized by each individual state. A Uniform Business Corporation Act was sponsored in 1928 and adopted by a few states. It was renamed the Model Business Corporation Act in 1943 and then withdrawn in 1958. It was supplanted in 1946 by the American Bar Association Model Business Corporations Act (MBCA) which was revised almost annually after that. During the 1960s, the “march of American state corporation law became a march toward uniformity”. By 1977, 34 of the 50 states had adopted MBCA statutes. In 1984, the Model Business Corporation Act was itself supplanted by the Revised Model Business Corporation Act (RMBCA) (the “revised” was recently dropped but is retained here to distinguish it from its predecessor). A large number of states adhere to one or the other Model Acts, with the RMBCA gaining adherents.

### Salient features of MBCA of US Corporations

A Business Corporation Act is the collection of laws in each state that governs corporations.

A model corporation statute compiled by the American Bar Association has been adopted in whole or in part by, or has influenced the statutes of many states.

#### **Secretary (1.40)**

“Secretary” means the corporate officer to whom the board of directors has delegated responsibility under

section 8.40(c) for custody of the minutes of the meetings of the board of directors and of the share holders and for authenticating records of the corporation.

***Required Officers (Section 8.40)***

- (a) A corporation has the officers described in its by laws or appointed by the board of directors in accordance with the by laws.
- (b) The board of directors may elect individuals to fill one or more offices of the corporation. An officer may appoint one or more officers or assistant officers if authorized by the bylaws or the board of directors.
- (c) The bylaws or the board of directors shall assign to one of the officers responsibility for preparing minutes of the directors' and shareholders' meetings and for authenticating records of the corporation.
- (d) Unless the byelaws provided otherwise, the same individual may simultaneously hold more than one office in a corporation.

***Duties of Officers (Section 8.41)***

Each officer has the authority and shall perform the duties set forth in the by laws or, to the extent consistent with the bylaws, the duties prescribed by the board of directors or by direction of an officer authorized by the board of directors to prescribe the duties of other officers.

***Standards of Conduct for Officers (Section 8.42)***

- (a) An officer, when performing in such capacity, shall act:
  - (1) in good faith;
  - (2) with the care that a person in a like position would reasonably exercise under similar circumstances; and
  - (3) in a manner the officer reasonably believes to be in the best interests of the corporation.
- (b) The duty of an officer includes the obligation:
  - (1) to inform the superior officer to whom, or the board of directors or the committee thereof to which, the officer reports of information about the affairs of the corporation known to the officer, within the scope of the officer's functions, and known to the officer to be material to such superior officer, board or committee; and
  - (2) to inform his or her superior officer, or another appropriate person within the corporation, or the board of directors, or a committee thereof, of any actual or probable material violation of law involving the corporation or material breach of duty to the corporation by an officer, employee, or agent of the corporation, that the officer believes has occurred or is about to occur.
- (c) In discharging those duties an officer, who does not have knowledge that makes reliance unwarranted, is entitled to rely on:
  - (1) The performance of properly delegated responsibilities by one or more employees of the corporation whom the officer reasonably believes to be reliable and competent in performing the responsibilities delegated; or
  - (2) information, opinions, reports or statements, including financial statements and other financial data, prepared or presented by one or more employees of the corporation whom the officer

reasonably believes to be reliable and competent in the matters presented or by legal counsel, public accountants, certified public accountants or other persons retained by the corporation as to matters involving skills or expertise the officer reasonably believes are matters (i) within the particular person's professional or expert competence or (ii) as to which the particular person merits confidence.

- (d) An officer shall not be liable to the corporation or its shareholders for any decision to take or not to take action, or any failure to take any action, as an officer, if the duties of the office are performed in compliance with this section. Whether an officer who does not comply with this section shall have liability will depend in such instance on applicable law, including those principles of Section 8.31 that have relevance.

### ***Resignation and Removal of Officers (Section 8.43)***

An officer may resign at any time by giving notice to the corporation. A resignation is effective when the notice is given unless the notice specifies a later effective date. If a resignation is made effective at a later time and the board or the appointing officer accepts the future effective time, the board or the appointing officer may fill the pending vacancy before the effective time if the board or the appointing officer provides that the successor does not take office until the effective date.

An officer may be removed at any time with or without cause by: (i) the board of directors; (ii) the officer who appointed such officer, unless the bylaws or the board of directors provide otherwise; or (iii) any other officer if authorized by the bylaws or the board of directors.

In this section, "appointing officer" means the officer (including any successor to that officer) who appointed the officer resigning or being removed.

### ***Incorporators (Section 2.01)***

One or more persons may act as the incorporator or incorporators of a corporation by signing & delivering articles of incorporation to the judge of probate of the country in which the corporation is to have its initial registered office for filing.

### ***Incorporation (Section 2.03)***

- (a) Upon the effectiveness of filing of the articles, corporate existence begins.

### ***Purposes (Section 3.01)***

- (a) Every corporation incorporated under this Act has the purpose of engaging in any lawful business unless a more limited purpose is set forth in the articles of incorporation.
- (b) A corporation engaging in a business that is subject to regulation under another statute of this state may incorporate under this Act only if permitted by, and subject to all limitations of, the other statute.

### ***Corporate Name (Section 4.01)***

- (a) A corporatename:
- (1) must contain the word "corporation", "incorporated", "company", or "limited", or the abbreviation "corp.", "inc.", "co.", or "Ltd.", or words or abbreviations of like import in another language; and
  - (2) may not contain language stating or implying that the corporation is organized for a purpose other than that permitted by relevant section and its articles of incorporation.

- (b) Except as authorized by sub-sections (c) and (d), a corporate name must be distinguishable upon the records of the secretary of state from:
  - (1) the corporate name of a corporation incorporated or authorized to transact business in this state;
  - (2) a corporate name reserved or registered under the Act;
  - (3) the fictitious name adopted by a foreign corporation authorized to transact business in this state because its real name is unavailable; and
  - (4) the corporate name of a not-for-profit corporation incorporated or authorized to transact business in this state.
- (c) A corporation may apply to the secretary of state for authorization to use a name that is not distinguishable upon his records from one or more of the names described in sub-section (b). The secretary of state shall authorize use of the name applied for if:
  - (1) The other corporation consents to the use in writing and submits an undertaking in form satisfactory to the secretary of state to change its name to a name that is distinguishable upon the records of the secretary of state from the name of the applying corporation; or
  - (2) the applicant delivers to the secretary of state a certified copy of the final judgment of a court of competent jurisdiction establishing the applicant's right to use the name applied for in this state.
- (d) A corporation may use the name (including the fictitious name) of another domestic or foreign corporation that is used in this state if the other corporation is incorporated or authorized to transact business in this state and the proposed user corporation:
  - (1) has merged with the other corporation;
  - (2) has been formed by reorganization of the other corporation; or
  - (3) has acquired all or substantially all of the assets, including the corporate name, of the other corporation.
- (e) This Act does not control the use of fictitious names.

***Annual Meeting (Section 7.01)***

- (a) A corporation shall hold a meeting of shareholders annually at a time stated in or fixed in accordance with the by laws.
- (b) Annual shareholders' meetings may be held in or out of this state at the place stated in or fixed in accordance with the bylaws. If no place is stated in or fixed in accordance with the bylaws, annual meetings shall be held at the corporation's principal office.
- (c) The failure to hold an annual meeting at the time stated in or fixed in accordance with a corporation's by laws doesn't affect the validity of any corporate action.

***Special Meeting (Section 7.02)***

- (a) A corporation shall hold a special meeting of shareholders:
  - (1) on call of its board of directors or the person or persons authorized to do so by the articles of incorporation or bylaws; or
  - (2) if the holders of at least 10 percent of all the votes entitled to be cast on an issue proposed to

be considered at the proposed special meeting sign, date, and deliver to the corporation one or more written demands for the meeting describing the purpose or purposes for which it is to be held, provided that the articles of incorporation may fix a lower percentage or a higher percentage not exceeding 25 percent of all the votes entitled to be cast on any issue proposed to be considered. Unless otherwise provided in the articles of incorporation, a written demand for a special meeting may be revoked by a writing to that effect received by the corporation prior to the receipt by the corporation of demands sufficient in number to require the holding of a special meeting.

***Court-Ordered Meeting (Section 7.03)***

- (a) The [name or describe] court of the county where a corporation's principal office (or, if none in this state, its registered office) is located may summarily order a meeting to be held:
  - (1) On application of any share holder of the corporation entitled to participate in an annual meeting if an annual meeting was not held within the earlier of 6 months after the end of the corporation's fiscal year or 15 months after its last annual meeting; or
  - (2) on application of a shareholder who signed a demand for a special meeting valid, if:
    - a. notice of the special meeting was not given within 30 days after the date the demand was delivered to the corporation's secretary; or
    - b. the special meeting was not held in accordance with the notice.
- (b) The court may fix the time and place of the meeting, determine the shares entitled to participate in the meeting, specify a record date for determining shareholders entitled to notice of and to vote at the meeting, prescribe the form and content of the meeting notice, fix the quorum required for specific matters to be considered at the meeting (or direct that the votes represented at the meeting constitute a quorum for action on those matters), and enter other orders necessary to accomplish the purpose or purposes of the meeting.

***Quorum and Voting Requirements for Voting Groups (Section 7.25)***

- (a) Shares entitled to vote as a separate voting group may take action on a matter at a meeting only if a quorum of those shares exists with respect to that matter. Unless the articles of incorporation or this Act provide otherwise, a majority of the votes entitled to be cast on the matter by the voting group constitutes a quorum of that voting group for action on that matter.
- (b) Once a share is represented for any purpose at a meeting, it is, unless established the contrary, presumed present for quorum purposes for the remainder of the meeting.
- (c) If a quorum exists, action on a matter (other than the election of directors) by a voting group is approved if the votes cast within the voting group favoring the action exceed the votes cast opposing the action, unless the articles of incorporation or this Act require a greater number of affirmative votes.

***Voting Trusts (Section 7.30)***

- (a) One or more share holders may create a voting trust, conferring on a trustee the right to vote or otherwise act for them, by signing an agreement setting out the provisions of the trust (which may include anything consistent with its purpose) and transferring their shares to the trustee. When a voting trust agreement is signed, the trustee shall prepare a list of the names and addresses of all owners of beneficial interests in the trust, together with the number and class of shares each

transferred to the trust, and deliver copies of the list and agreement to the corporation's principal office.

- (b) A voting trust becomes effective on the date the first shares subject to the trust are registered in the trustee's name. A voting trust is valid for not more than 10 years after its effective date unless extended under sub-section (c).
- (c) All or some of the parties to a voting trust may extend it for additional terms of not more than 10 years each by signing an extension agreement and obtaining the voting trustee's written consent to the extension. An extension is valid for 10 years from the date the first shareholder signs the extension agreement. The voting trustee must deliver copies of the extension agreement and list of beneficial owners to the corporation's principal office. An extension agreement binds only those parties signing it.

***Requirement for and Duties of Board of Directors (Section 8.01)***

- (a) Except as provided in section 7.32, each corporation must have a board of directors.
- (b) All corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed by or under the direction of, its board of directors, subject to any limitation set forth in the articles of incorporation or in an agreement authorized under section 7.32.

***Qualifications of Directors (Section 8.02)***

The articles of incorporation or bylaws may prescribe qualifications for directors. A director shall be a natural person of the age of at least nineteen (19) years but need not be a resident of this state or a shareholder of the corporation unless the articles of incorporation or bylaws so prescribe.

***Number and Election of Directors (Section 8.03)***

- (a) A board of directors must consist of one or more individuals, with the number specified in or fixed in accordance with the articles of incorporation or by laws.
- (b) If a board of directors has power to fix or change the number of directors, the board may increase or decrease by 30 percent or less the number of directors last approved by the shareholders, but only the shareholders may increase or decrease by more than 30 percent the number of directors last approved by the shareholders.
- (c) Directors are elected at the first annual shareholders' meeting and at each annual meeting thereafter unless their terms are staggered under section 8.06.

***Resignation of Directors (Section 8.07)***

- (a) A director may resign at any time by delivering written notice to the board of directors, its chairman, or to the corporation.
- (b) A resignation is effective when the notice is delivered unless the notice specifies a later effective date.

***Meetings (Section 8.20)***

The board of directors may hold regular or special meetings in or out of this state.

Unless the articles of incorporation or bylaws provide otherwise, the board of directors may permit any or all directors to participate in a regular or special meeting by, or conduct the meeting through the use of, any means of communication by which all directors participating may simultaneously hear each other during the meeting.

A direct or participating in a meeting by this means is deemed to be present in person at the meeting.

***Dissolution by Incorporators or Initial Directors (Section 14.01)***

A majority of the incorporators or initial directors of a corporation that has not issued shares or has not commenced business may dissolve the corporation by delivering to the secretary of state for filing articles of dissolution that set forth:

- (1) the name of the corporation;
- (2) the date of its incorporation;
- (3) either (i) that none of the corporation's shares has been issued or (ii) that the corporation has not commenced business;
- (4) that no debt of the corporation remains unpaid;
- (5) that the net assets of the corporation remaining after winding up have been distributed to the shareholders, if shares were issued; and
- (6) that a majority of the incorporators or initial directors authorized the dissolution.

***Dissolution by Board of Directors and Shareholders (Section 14.02)***

- (a) A corporation's board of directors may propose dissolution for submission to the shareholders.
- (b) For a proposal to dissolve to be adopted:
  - (1) The board of directors must recommend dissolution to the shareholders unless the board of directors determines that because of conflict of interest or other special circumstances, it should make no recommendation and communicates the basis for its determination to the shareholders; and
  - (2) The shareholders entitled to vote must approve the proposal to dissolve as provided in sub-section(e).
- (c) The board of directors may condition its submission of the proposal for dissolution on any basis.
- (d) The corporation shall notify each shareholder, whether or not entitled to vote, of the proposed shareholders' meeting. The notice must also state that the purpose, or one of the purposes, of the meeting is to consider dissolving the corporation.
- (e) Unless the articles of incorporation, or the board of directors, [acting pursuant to sub-section (c)], require a greater vote or a vote by voting groups, adoption of the proposal to dissolve shall require the approval of the shareholders at a meeting at which a quorum consisting of at least a majority of the votes entitled to be cast exists.

***Corporate Records (Section 16.01)***

- (a) A corporation shall keep as permanent records minutes of all meetings of its share holders and board of directors, and records of all actions taken by the share holders or board of directors without a meeting, and records of all actions taken by a committee of the board of directors in place of the board of directors on behalf of the corporation.
- (b) A corporation shall maintain appropriate accounting records.
- (c) A corporation or its agent shall maintain a record of its shareholders, in a form that permits preparation of a list of the names and addresses of all shareholders, in alphabetical order by class

of shares showing the number and class of shares held by each.

- (d) A corporation shall maintain its records in written form or in another form capable of conversion into written form within a reasonable time.
- (e) A corporation shall keep a copy of the following records at its principal office:
  - (1) its articles or restated articles of incorporation and all amendments to them currently in effect;
  - (2) its bylaws or restated bylaws and all amendments to them currently ineffect;
  - (3) resolutions adopted by its board of directors creating one or more classes or series of shares, and fixing their relative rights, preferences, and limitations, if shares issued pursuant to those resolutions are outstanding;
  - (4) the minutes of all shareholders' meetings, and records of all action taken by shareholders without a meeting, for the past three years
  - (5) all written communications to share holders generally within the past three years, including the financial statements furnished for the past three years under section 16.20;
  - (6) a list of the names and business addresses of its current directors and officers; and
  - (7) its most recent annual report delivered to the secretary of state.

## Australia

### Legislative history

In Australia, prior to the adoption of the U.K. Joint Stock Companies Act, 1844, by the various colonies, private companies generally operated as unincorporated deed-of-settlement joint-stock companies.

Public utility companies were either incorporated by Royal Charter, or were conferred with powers to sue and be sued in the name of an officer by private act. Most of the colonies passed legislation based on the British Companies Act, 1862, which was subsequently modified over the years.

The "no liability" mining company was developed in 1871, while compulsory auditing and financial information provisions were enacted as early as 1896. However, these provisions applied only to publicly traded companies; private companies, to which the new requirements did not apply, were defined as proprietary companies, which are still a viable form of business organization today.

The no liability company was developed in the speculative area of mining investment. It was first provided for in the Mining Companies Act, 1871. At the time, mining concerns, which formed companies limited by shares, sometimes found it difficult to recover unpaid calls of share capital. Shareholders often bought their stakes under fictitious names and would simply abandon their holdings if the venture proved less fruitful. The noteworthy aspect of the no liability company is that a member who does not pay calls is liable to the forfeiture of his shares.

Although the memorandum of association of a no liability company had to state that acceptance of shares did not constitute a contract to pay calls or contribute towards the payment of the company's debts, a no liability company could nevertheless contract around this.

### Corporations Law

In Australia, corporations are registered and regulated by the Commonwealth Government. Corporations law has been largely codified in the Corporations Act 2001. The Act is the result of a successful High Court of

Australia challenge in *New South Wales v. Commonwealth* (1990) 169 CLR 482 ('The Corporations Act Case'). The Commonwealth was found to have insufficient power to legislate in relation to the formation of companies. Section 51(xx) of the Australian Constitution was found to provide sufficient power for legislation applicable to foreign corporations and corporations already formed within the Commonwealth. To some extent, the Act was an outcome of the resolve of the Federal Parliament to establish modern national laws to govern corporations and the securities market so as to establish the governing rules and to provide a pyramid of graduated responses where the law was shown to have been broken.

The Corporations Act, 2001, sometimes referred to just as the Corporations Act is presently the largest corporations' statute in the world. It is an act of the Commonwealth of Australia. This Act sets out the laws dealing with business entities in Australia at federal and interstate level. Although the focus of the Act is primarily on companies, it also covers some laws relating to other entities such as partnerships and managed investment schemes. All states have adopted the Act.

The Corporations Act is the principal legislation regulating companies in Australia. It regulates matters such as the formation and operation of companies (in conjunction with a constitution that may be adopted by a company), duties of officers, takeovers and fundraising.

The Act gives statutory force to many common law principles and imposes a number of additional fiduciary duties on directors of incorporated bodies. Breach of statutory duties draws penalties under the Act which range up to \$220,000. Under both the common law and the Corporations Act, 2001, officers may also be required to pay compensation or to account for profits. In some cases, directors may also be disqualified from office.

The Corporation Regulations, 2001 contains all the regulations made under the Corporations Act, 2001.

## Salient features of Australian Corporations Act

### Structure and functions of the Board

Under the Corporations Act, a proprietary company must have at least one director. That director must ordinarily reside in Australia. For this purpose, a proprietary company is a company that is registered as, or converts to, a proprietary company under this Act.

A proprietary company must:

- be limited by shares or be an unlimited company with a share capital;
- have no more than 50 non-employee shareholders;
- not do anything that would require disclosure to investors under the Chapter of the Act (except in limited circumstances).

Further, a public company must have at least 3 directors (not counting alternate directors). At least 2 directors must ordinarily reside in Australia. Only an individual who is at least 18 may be appointed as a director of a company. A person who is disqualified from managing corporations may only be appointed as director of a company if the appointment is made with permission granted by Australian Securities and Investments Commission under the leave granted by the Court.

The business of a company is to be managed by or under the direction of the directors. The directors may exercise all the powers of the company except any powers that this Act or the company's constitution (if any) requires the company to exercise in general meeting. For example, the directors may issue shares, borrow money and issue debentures. The directors of a company may confer on a managing director any of the

powers that the directors can exercise. The directors may revoke or vary a conferral of powers on the managing director.

The director of a proprietary company who is its only director and only shareholder may exercise all the powers of the company except any powers that this Act or the company's constitution (if any) requires the company to exercise in general meeting. The business of the company is to be managed by or under the direction of the director. For example, the director may issue shares, borrow money and issue debentures. The director of a proprietary company who is its only director and only shareholder may sign, draw, accept, endorse or otherwise execute a negotiable instrument. The director may determine that a negotiable instrument may be signed, drawn, accepted, endorsed or otherwise executed in a different way.

### ***Appointment of Directors***

#### *Special Rules for the appointment of public company directors*

There are special rules for appointment of directors of public company and the appointment of directors for single director/single shareholder proprietary companies. A resolution passed at a general meeting of a public company appointing or confirming the appointment of 2 or more directors is void unless:

- (a) the meeting has resolved that the appointments or confirmations may be voted on together; and
- (b) no votes were cast against there solution.

Therefore, said requirement does not affect (a) a resolution to appoint directors by an amendment to the company's constitution (if any); or (b) a ballot or poll to elect two or more directors if the ballot or poll does not require members voting for one candidate to vote for another candidate.

For aforesaid purposes, a ballot or poll does not require a member to vote for a candidate merely because the member is required to express a preference among individual candidates in order to cast a valid vote.

#### *Special Rules for the appointment of directors for single director/single shareholder proprietary companies.*

The director of a proprietary company who is its only director and only shareholder may appoint another director by recording the appointment and signing the record. If a person who is the only director and the only shareholder of a proprietary company dies; or cannot manage the company because of the person's mental incapacity; and a personal representative or trustee is appointed to administer the person's estate or property, the personal representative or trustee may appoint a person as the director of the company.

If the office of the director of a proprietary company is vacated because of the bankruptcy of the director; and the person is the only director and the only shareholder of the company; and a trustee in bankruptcy is appointed to the person's property; the trustee may appoint a person as the director of the company. A person who has a power of appointment as aforesaid may appoint themselves as director. A person appointed as a director of a company as aforesaid holds office as if they had been appointed in the usual way.

### ***Remuneration of Directors***

The directors of a company are to be paid the remuneration that the company determines by resolution. The company may also pay the directors' travelling and other expenses that they properly incur: (a) in attending directors' meetings or any meetings of committees of directors; and (b) in attending any general meetings of the company; and (c) in connection with the company's business.

#### ***Members may obtain information about director's remuneration.***

A company must disclose the remuneration paid to each director of the company or a subsidiary (if any) by

the company or by an entity controlled by the company if the company is directed to disclose the information by: (a) members with at least 5% of the votes that may be cast at a general meeting of the company; or (b) at least 100 members who are entitled to vote at a general meeting of the company. The company must disclose all remuneration paid to the director, regardless of whether it is paid to the director in relation to their capacity as director or another capacity.

The company must comply with the direction as soon as practicable by: (a) preparing a statement of the remuneration of each director of the company or subsidiary for the last financial year before the direction was given; and (b) having the statement audited; and (c) sending a copy of the audited statement to each person entitled to receive notice of general meetings of the company.

*Special Rules for single director/single shareholder proprietary companies.*

A person who is the only director and the only shareholder of a proprietary company is to be paid any remuneration for being a director that the company determines by resolution. The company may also pay the director's travelling and other expenses properly incurred by the director in connection with the company's business.

### **Company Secretaries**

A company other than a proprietary company must have a company secretary. However, a proprietary company may choose to have a company secretary. The directors appoint the company secretary. A company secretary must be at least eighteen years old. If a company has only one company secretary, they must ordinarily reside in Australia. If a company has more than one company secretary, at least 1 of them must ordinarily reside in Australia.

A company secretary must consent in writing to holding the position of company secretary. The company must keep the consent and must notify ASIC of the appointment.

The same person may be both a director of a company and the company secretary.

Generally, a company secretary may resign by giving written notice of resignation to the company. A company secretary who resigns may notify ASIC of the resignation. If the company secretary does not do so, the company must notify ASIC of the company secretary's resignation.

The company secretary is an officer of the company and, in that capacity, may be subject to the requirements imposed by the Corporations Act on company officers.

The Company Secretary has specific responsibilities under the Corporations Act, including responsibility for ensuring that the company:

- notifies ASIC about changes to the identities, names and addresses of the company's directors and company secretaries; and
- notifies ASIC about changes to the register of members; and
- notifies ASIC about changes to any ultimate holding company; and
- responds, if necessary, to an extract of particulars that it receives and that it responds to any return of particulars that it receives.

A company secretary's obligations may continue even after the company has been deregistered.

### **Auditors**

The following may be appointed as auditor of a company for the purposes of the Act:

- (a) An individual;

- (b) A firm;
- (c) A company.

In case of Proprietary Company, the directors may appoint an auditor for the company if an auditor has not been appointed by the company in general meeting.

The company may have more than one auditor. The appointment of a firm as auditor of a company is taken to be an appointment of all persons who, at the date of the appointment, are (a) members of the firm; and (b) registered company auditors. This is so whether or not those persons are resident in Australia.

The appointment of the members of a firm as auditors of a company or registered scheme, that is taken to have been made because of the appointment of the firm as auditor of the company or scheme, is not affected by the dissolution of the firm.

A report or notice that purports to be made or given by a firm appointed as auditor of a company is not taken to be duly made or given unless it is signed by a member of the firm who is a registered company auditor, both:

- (a) in the firm name; and
- (b) in his or her own name.

A notice required or permitted to be given to an audit firm under the Corporations legislation may be given to the firm by giving the notice to a member of the firm.

For the purposes of criminal proceedings under this Act against a member of an audit firm, an act or omission by:

- (a) a member of the firm; or
- (b) an employee or agent of the audit firm;

acting within the actual or apparent scope of his or her employment, or within his or her actual or apparent authority, is also to be attributed to the audit firm.

The directors of a public company must appoint an auditor of the company within one month after the day on which a company is registered as a company unless the company at a general meeting has appointed an auditor.

A public company must appoint an auditor of the company at its first AGM and appoint an auditor of the company to fill any vacancy in the office of auditor at each subsequent AGM.

An auditor holds office until the auditor dies; or is removed, or resigns, from office; or ceases to be capable of acting as auditor; or ceases to be auditor.

## Canada

Like the United States and Australia, Canada is a federal state with a multiplicity of corporate statutes. Unlike the United States, there is a federal corporation's statute, the Canada Business Corporations Act (CBCA), as well as corporate legislation in each of the 10 provinces. Upon implementation of the CBCA in 1975, a deliberate and fairly successful effort was made to harmonize the provincial statutes to the new federal regime in Canada.

Again, unlike the United States, there is no federal securities regulator in Canada. Although Canada has adopted securities regimes which are very much American in concept and approach, each province has its own securities law regime.

Over the last two decades, regional variations have crept back into the harmonized provincial corporate statutes but overall they remain similar to the CBCA in general structure and detail. Some provincial legislatures have been more responsive to change than others and have renewed their corporate statutes with greater regularity than the federal government. This has resulted in some divergence in detail.

The CBCA, and the Dickerson Report which preceded it, continue to influence reforms in jurisdictions as diverse as South Africa, Singapore, Australia and New Zealand where concepts introduced by the CBCA and time-tested in Canada are now making their appearance. The CBCA has been complemented over the last twenty years by a broad range of judicial decisions.

### ***About the Act***

The CBCA sets out the legal and regulatory framework for nearly 235,000 federally incorporated corporations. Most CBCA corporations are small or medium-sized privately held companies. However, many large businesses have chosen to incorporate under the provisions of the CBCA, including almost half of Canada's largest publicly traded companies. As an important market place framework law, the CBCA is designed to enhance the efficiency and competitiveness of the Canadian marketplace.

As a framework statute, the CBCA provides the basic structure and standards for the direction and control of a corporation, but it does not prescribe how a corporation is to be run. The Act sets out the rules and provides the mechanisms to facilitate the interaction among shareholders, directors, management and other interested parties that determines corporate decision making. With respect to publicly traded corporations, some of the corporate governance provisions contained in the CBCA overlap with parallel provisions in provincial securities laws, such as the process for selecting directors and the rights of shareholders to participate in key corporate decisions.

When the CBCA came into force in 1975, it was considered a leading-edge corporate law statute. The evolution of the corporate market place since its enactment led to comprehensive amendments to the Act in 2001. Among other things, these amendments enhanced shareholder participation in corporate decision making, increased transparency and accountability, and further harmonized the Act with provincial securities laws. The overall effect was to facilitate entrepreneurship and assist corporations in meeting the challenges of an increasingly competitive global market place.

Today, Canada's corporate governance framework is well recognized internationally for its efficiency. In 2013, the World Bank ranked Canada third among 185 economies for a regulatory environment that is conducive to starting and operating a business and fourth in protecting investors. The efficacy of corporate boards of directors and the protection of minority shareholders' interests have also been identified by the World Economic Forum as factors that give Canada a competitive advantage over other countries.

The CBCA remains a well-functioning statute. Nevertheless, continuous changes and developments in the marketplace require constant monitoring to ensure that Canada's corporate regulatory structure meets the challenges of the future. To grow and thrive in the global knowledge-based economy, Canada needs a strong corporate governance framework that both reflects and facilitates the best practices of Canadian corporations.

### ***Structure and functions of the Board***

Under the CBCA, the articles of incorporation are to set out the number of directors or the minimum and maximum number of directors of the incorporation. A corporation may have one or more directors but if any of its issued securities are or were part of a distribution to the public and remain outstanding and are held by more than one person, the corporation is to have at least three directors, at least two of whom are not to be officers or employees of the corporation or its affiliates.

### ***About the Consultation***

Industry Canada is undertaking this consultation to ensure that the governance framework for CBCA corporations remains effective, fosters competitiveness, supports investment and entrepreneurial activity, and instills investor and business confidence.

### ***Issues under Review***

The House of Commons Standing Committee on Industry, Science and Technology (the “Committee”) conducted a statutory review of the CBCA in 2009–10. In June 2010, the Committee published a report that recommended that the Government consult on four issues: (1) rules relating to disclosure of executive compensation, (2) rules applicable to shareholder voting and participation rights, (3) rules regarding the holding and transfer of shares and insider trading, and (4) rules applicable to the incorporation of socially responsible enterprises.

In addition to these issues, other issues were identified for review and consultation. The topics include greater transparency of the ownership of corporations, the role of corporate governance legislation in preventing bribery and corruption, the diversity of the members composing corporate boards and management teams, takeover bid rules, the use of the arrangement provisions of the CBCA to restructure insolvent businesses, the role of corporate social responsibility, and administrative and technical reforms to the Act.

## **Salient features of Canadian Business Corporations Act**

### ***INCORPORATION***

#### ***Incorporators***

- (1) One or more individuals not one of whom
  - (a) is less than eighteen years of age,
  - (b) is of unsound mind and has been so found by a court in Canada or elsewhere, or
  - (c) has the status of bankrupt,
 may incorporate a corporation by signing articles of incorporation and complying with section 7.

#### ***Bodies Corporate***

- (2) One or more bodies corporate may incorporate a corporation by signing articles of incorporation and complying with section 7.

#### ***Articles of incorporation***

- (1) Articles of incorporation shall follow the form that the Director fixes and shall set out, in respect of the proposed corporation,
  - (a) the name of the corporation;
  - (b) the province in Canada where the registered office is to be situated;
  - (c) the classes and any maximum number of shares that the corporation is authorized to issue, and
    - (i) if there will be two or more classes of shares, the rights, privileges, restrictions and conditions attaching to each class of shares, and
    - (ii) if a class of shares may be issued in series, the authority given to the directors to fix the

number of shares in, and to determine the designation of, and the rights, privileges, restrictions and conditions attaching to, the shares of each series;

- (d) if the issue, transfer or ownership of shares of the corporation is to be restricted, a statement to that effect and a statement as to the nature of such restrictions;
- (e) the number of directors or, subject to paragraph 107(a), the minimum and maximum number of directors of the corporation; and
- (f) any restrictions on the businesses that the corporation may carry on.

#### ***Additional provision on articles***

- (2) The articles may set out any provisions permitted by this Act or by law to be set out in the by-laws of the corporation.
  - (i) Subject to sub-section (4), if the articles or a unanimous shareholder agreement require a greater number of votes of directors or shareholders than that required by this Act to effect any action, the provisions of the articles or of the unanimous shareholder agreement prevail.
  - (ii) The articles may not require a greater number of votes of shareholders to remove a director than the number required by section 109.

An incorporator shall send to the Director articles of incorporation and the documents required by sections 19 and 106.

On receipt of articles of incorporation, the Director shall issue a certificate of incorporation in accordance with section 262.

The Director may refuse to issue the certificate if a notice that is required to be sent under sub-section 19(2) or 106(1) indicates that the corporation, if it came into existence, would not be in compliance with this Act.

## **DIRECTORS AND OFFICERS**

**102.** (1) Subject to any unanimous shareholder agreement, the directors shall manage, or supervise the management of, the business and affairs of a corporation.

- (2) A corporation shall have one or more directors but a distributing corporation, any of the issued securities of which remain outstanding and are held by more than one person, shall have not fewer than three directors, at least two of whom are not officers or employees of the corporation or its affiliates.

**105.**(1) The following persons are disqualified from being a director of a corporation:

- (a) anyone who is less than eighteen years of age;
  - (b) anyone who is of unsound mind and has been so found by a court in Canada or elsewhere;
  - (c) a person who is not an individual; or
  - (d) a person who has the status of bankrupt.
- (2) Unless the articles otherwise provide, a director of a corporation is not required to hold shares issued by the corporation.
  - (3) Subject to subsection (3.1), at least twenty-five per cent of the directors of a corporation must be resident Canadians. However, if a corporation has less than four directors, at least one director must be a resident Canadian.

- (3.1) If a corporation engages in an activity in Canada in a prescribed business sector or if a corporation, by an Act of Parliament or by a regulation made under an Act of Parliament, is required, either individually or in order to engage in an activity in Canada in a particular business sector, to attain or maintain a specified level of Canadian ownership or control, or to restrict, or to comply with a restriction in relation to, the number of voting shares that any one shareholder may hold, own or control, then a majority of the directors of the corporation must be resident Canadians.
- (3.2) Nothing in subsection (3.1) shall be construed as reducing any requirement for a specified number or percentage of resident Canadian directors that otherwise applies to a corporation referred to in that sub-section.
- (3.3) If a corporation referred to in sub-section (3.1) has only one or two directors, that director or one of the two directors, as the case may be, must be a resident Canadian.
- (4) Despite sub-section(3.1),not more than one-third of the directors of a holding corporation referred to in that sub-section need be resident Canadians if the holding corporation earns in Canada directly or through its subsidiaries less than five per cent of the gross revenues of the holding corporation and all of its subsidiary bodies corporate together as shown in:
- (a) the most recent consolidated financial statements of the holding corporation referred to in section157; or
- (b) the most recent financial statements of the holding corporation and its subsidiary bodies corporate as at the end of the last completed financial year of the holding corporation.
- 109.** (1) Subject to paragraph 107(g), the shareholders of a corporation may by ordinary resolution at a special meeting remove any director or directors from office.
- (2) Where the holders of any class or series of shares of a corporation have an exclusive right to elect one or more directors, a director so elected may only be removed by an ordinary resolution at a meeting of the shareholders of that class or series.
- (3) Subject to paragraphs 107(b) to (e), a vacancy created by the removal of a director may be filled at the meeting of the shareholders at which the director is removed or, if not so filled, may be filled under section 111.
- (4) If all of the directors have resigned or have been removed without replacement, a person who manages or supervises the management of the business and affairs of the corporation is deemed to be a director for the purposes of this Act.
- (5) Subsection (4) does not apply to:
- (a) an officer who manages the business or affairs of the corporation under the direction or control of a shareholder or other person;
- (b) a lawyer, notary, accountant or other professional who participates in the management of the corporation solely for the purpose of providing professional services; or
- (c) a trustee in bankruptcy, receiver, receiver-manager, sequestrator or secured creditor who participates in the management of the corporation or exercises control over its property solely for the purpose of the realization of security or the administration of a bankrupt's estate, in the case of a trustee in bankruptcy.
- 112.**(1) The shareholders of a corporation may amend the articles to increase or, subject to paragraph 107(h), to decrease the number of directors, or the minimum or maximum number of directors, but no

decrease shall shorten the term of an incumbent director.

- (2) Where the shareholders at a meeting adopt an amendment to the articles of a corporation to increase or, subject to paragraph 107(h) and to subsection (1), decrease the number or minimum or maximum number of directors, the shareholders may, at the meeting, elect the number of directors authorized by the amendment, and for that purpose, notwithstanding sub-sections 179(1) and 262(3), on the issue of a certificate of amendment the articles are deemed to be amended as of the date the shareholders adopt the amendment.

**114.** (1) Unless the articles or by-laws otherwise provide, the directors may meet at any place and on such notice as the by-laws require.

- (2) Subject to the articles or by-laws, a majority of the number of directors or minimum number of directors required by the articles constitutes a quorum at any meeting of directors, and, notwithstanding any vacancy among the directors, a quorum of directors may exercise all the powers of the directors.
- (3) Directors, other than directors of a corporation referred to in sub-section 105(4), shall not transact business at a meeting of directors unless,
  - (a) if the corporation is subject to subsection 105(3), at least twenty-five per cent of the directors present are resident Canadians or, if the corporation has less than four directors, at least one of the directors present is a resident Canadian; or
  - (b) if the corporation is subject to sub-section 105(3.1), a majority of directors present are resident Canadians or if the corporation has only two directors, at least one of the directors present is a resident Canadian.
- (4) Despite subsection (3), directors may transact business at a meeting of directors where the number of resident Canadian directors, required under that subsection, is not present if
  - (a) a resident Canadian director who is unable to be present approves in writing, or by telephonic, electronic or other communication facility, the business transacted at the meeting; and
  - (b) the required number of resident Canadian directors would have been present had that director been present at the meeting.
- (5) A notice of a meeting of directors shall specify any matter referred to in sub-section 115(3) that is to be dealt with at the meeting but, unless the by-laws otherwise provide, need not specify the purpose of or the business to be transacted at the meeting.
- (6) A director may in any manner waive a notice of a meeting of directors; and attendance of a director at a meeting of directors is a waiver of notice of the meeting, except where a director attends a meeting for the express purpose of objecting to the transaction of any business on the grounds that the meeting is not lawfully called.
- (7) Notice of an adjourned meeting of directors is not required to be given if the time and place of the adjourned meeting is announced at the original meeting.
- (8) Where a corporation has only one director, that director may constitute a meeting.
- (9) Subject to the by-laws, a director may, in accordance with the regulations, if any, and if all the directors of the corporation consent, participate in a meeting of directors or of a committee of directors by means of a telephonic, electronic or other communication facility that permits all participants to communicate adequately with each other during the meeting. A director participating

in such a meeting by such means is deemed for the purposes of this Act to be present at that meeting.

**118.** (1) Directors of a corporation who vote for or consent to a resolution authorizing the issue of a share under section 25 for a consideration other than money are jointly and severally, or solidarily, liable to the corporation to make good any amount by which the consideration received is less than the fair equivalent of the money that the corporation would have received if the share had been issued for money on the date of the resolution.

- (2) Directors of a corporation who vote for or consent to a resolution authorizing any of the following are jointly and severally, or solidarily, liable to restore to the corporation any amounts so distributed or paid and not otherwise recovered by the corporation:
- (a) a purchase, redemption or other acquisition of shares contrary to section 34, 35 or 36;
  - (b) a commission contrary to section 41;
  - (c) a payment of a dividend contrary to section 42;
  - (d) a payment of an indemnity contrary to section 124; or
  - (e) a payment to a shareholder contrary to section 190 or 241.
- (3) A director who has satisfied a judgment rendered under this section is entitled to contribution from the other directors who voted for or consented to the unlawful act on which the judgment was founded.
- (4) A director liable under subsection (2) is entitled to apply to a court for an order compelling a shareholder or other recipient to pay or deliver to the director any money or property that was paid or distributed to the shareholder or other recipient contrary to section 34, 35, 36, 41, 42, 124, 190 or 241.
- (5) In connection with an application under subsection (4) a court may, if it is satisfied that it is equitable to do so,
- (a) Order a shareholder or other recipient to pay or deliver to a director any money or property that was paid or distributed to the shareholder or other recipient contrary to section 34, 35, 36, 41, 42, 124, 190 or 241;
  - (b) order a corporation to return or issue shares to a person from whom the corporation has purchased, redeemed or otherwise acquired shares; or
  - (c) make any further order it thinks fit.
- (6) A director who proves that the director did not know and could not reasonably have known that the share was issued for a consideration less than the fair equivalent of the money that the corporation would have received if the share had been issued for money is not liable under subsection (1).
- (7) An action to enforce a liability imposed by this section may not be commenced after two years from the date of the resolution authorizing the action complained of.

## SHAREHOLDERS

**132.** (1) Meetings of shareholders of a corporation shall be held at the place within Canada provided in the by-laws or, in the absence of such provision, at the place within Canada that the directors determine.

- (2) Despite subsection (1), a meeting of shareholders of a corporation may be held at a place outside

Canada if the place is specified in the articles or all the shareholders entitled to vote at the meeting agree that the meeting is to be held at that place.

- (3) A shareholder who attends a meeting of shareholders held outside Canada is deemed to have agreed to it being held outside Canada except when the shareholder attends the meeting for the express purpose of objecting to the transaction of any business on the grounds that the meeting is not lawfully held.
- (4) Unless the by-laws otherwise provide, any person entitled to attend a meeting of shareholders may participate in the meeting, in accordance with the regulations, if any, by means of a telephonic, electronic or other communication facility that permits all participants to communicate adequately with each other during the meeting, if the corporation makes available such a communication facility. A person participating in a meeting by such means is deemed for the purposes of this Act to be present at the meeting.
- (5) If the directors or the shareholders of a corporation call a meeting of shareholders pursuant to this Act, those directors or shareholders, as the case may be, may determine that the meeting shall be held, in accordance with the regulations, if any, entirely by means of a telephonic, electronic or other communication facility that permits all participants to communicate adequately with each other during the meeting, if the by-laws so provide.

**133.** (1) The directors of a corporation shall call an annual meeting of shareholders

- (a) not later than eighteen months after the corporation comes into existence; and
  - (b) subsequently, not later than fifteen months after holding the last preceding annual meeting but not later than six months after the end of the corporation's preceding financial year.
- (2) The directors of a corporation may at any time call a special meeting of share holders.
- (3) Despite subsection (1), the corporation may apply to the court for an order extending the time for calling an annual meeting.

**135.**(1) Notice of the time and place of a meeting of shareholders shall be sent within the prescribed period to —

- (a) each shareholder entitled to vote at the meeting;
  - (b) each director; and
  - (c) the auditor of the corporation.
- (1.1) In the case of a corporation that is not a distributing corporation, the notice may be sent within a shorter period if so specified in the articles or by-laws.
- (2) A notice of a meeting is not required to be sent to shareholders who were not registered on the records of the corporation or its transfer agent on the record date determined under paragraph 134(1)(c) or subsection 134(2), but failure to receive a notice does not deprive a shareholder of the right to vote at the meeting.
  - (3) If a meeting of shareholders is adjourned for less than thirty days it is not necessary, unless the by-laws otherwise provide, to give notice of the adjourned meeting, other than by announcement at the earliest meeting that is adjourned.
  - (4) If a meeting of shareholders is adjourned by one or more adjournments for an aggregate of thirty days or more, notice of the adjourned meeting shall be given as for an original meeting but, unless

the meeting is adjourned by one or more adjournments for an aggregate of more than ninety days, subsection 149(1) does not apply.

- (5) All business transacted at a special meeting of shareholders and all business transacted at an annual meeting of shareholders, except consideration of the financial statements, auditor's report, election of directors and re-appointment of the incumbent auditor, is deemed to be special business.
- (6) Notice of a meeting of shareholders at which special business is to be transacted shall state the nature of that business in sufficient detail to permit the shareholder to form a reasoned judgment thereon; and the text of any special resolution to be submitted to the meeting.

**137.** (1) Subject to sub-sections (1.1) and (1.2), a registered holder or beneficial owner of shares that are entitled to be voted at an annual meeting of shareholders may

- (a) submit to the corporation notice of any matter that the person proposes to raise at the meeting (a "proposal"); and
- (b) discuss at the meeting any matter in respect of which the person would have been entitled to submit a proposal.

1.1 To be eligible to submit a proposal, a person

- (a) must be, for at least the prescribed period, the registered holder or the beneficial owner of at least the prescribed number of outstanding shares of the corporation; or
- (b) must have the support of persons who, in the aggregate, and including or not including the person that submits the proposal, have been, for at least the prescribed period, the registered holders, or the beneficial owners of, at least the prescribed number of outstanding shares of the corporation.

1.2 A proposal submitted under paragraph (1)(a) must be accompanied by the following information:

- (a) the name and address of the person and of the person's supporters, if applicable; and
- (b) the number of shares held or owned by the person and the person's supporters, if applicable, and the date the shares were acquired.

1.3 The information provided under subsection (1.2) does not form part of the proposal or of the supporting statement referred to in subsection (3) and is not included for the purposes of the prescribed maximum word limit set out in subsection (3).

1.4 If requested by the corporation within the prescribed period, a person who submits a proposal must provide proof, within the prescribed period, that the person meets the requirements of subsection (1.1).

- (2) A corporation that solicits proxies shall set out the proposal in the management proxy circular required by section 150 or attach the proposal thereto.
- (3) If so requested by the person who submits a proposal, the corporation shall include in the management proxy circular or attach to it a statement in support of the proposal by the person and then a name and address of the person. The statement and the proposal must together not exceed the prescribed maximum number of words.
- (4) A proposal may include nominations for the election of directors if the proposal is signed by one or more holders of shares representing in the aggregate not less than five per cent of the shares or five per cent of the shares of a class of shares of the corporation entitled to vote at the meeting to

which the proposal is to be presented, but this subsection does not preclude nominations made at a meeting of shareholders.

- (5) A corporation is not required to comply with subsections (2) and (3) if
    - (a) the proposal is not submitted to the corporation at least the prescribed number of days before the anniversary date of the notice of meeting that was sent to shareholders in connection with the previous annual meeting of shareholders;
    - (b) it clearly appears that the primary purpose of the proposal is to enforce a personal claim or redress a personal grievance against the corporation or its directors, officers or security holders;
    - (b.1) it clearly appears that the proposal does not relate in a significant way to the business or affairs of the corporation;
    - (c) not more than the prescribed period before the receipt of a proposal, a person failed to present, in person or by proxy, at a meeting of shareholders, a proposal that at the person's request, had been included in a management proxy circular relating to the meeting;
    - (d) substantially the same proposal was submitted to shareholders in a management proxy circular or a dissident's proxy circular relating to a meeting of shareholders held not more than the prescribed period before the receipt of the proposal and did not receive the prescribed minimum amount of support at the meeting; or
    - (e) the rights conferred by this section are being abused to secure publicity.
  - (5.1) If a person who submits a proposal fails to continue to hold or own the number of shares referred to in subsection (1.1) up to and including the day of the meeting, the corporation is not required to set out in the management proxy circular, or attach to it, any proposal submitted by that person for any meeting held within the prescribed period following the date of the meeting.
  - (6) No corporation or person acting on its behalf incurs any liability by reason only of circulating a proposal or statement in compliance with this section.
  - (7) If a corporation refuses to include a proposal in a management proxy circular, the corporation shall, within the prescribed period after the day on which it receives the proposal or the day on which it receives the proof of ownership under subsection (1.4), as the case may be, notify in writing the person submitting the proposal of its intention to omit the proposal from the management proxy circular and of the reasons for the refusal.
  - (8) On the application of a person submitting a proposal who claims to be aggrieved by a corporation's refusal under subsection (7), a court may restrain the holding of the meeting to which the proposal is sought to be presented and make any further order it thinks fit.
  - (9) The corporation or any person claiming to be aggrieved by a proposal may apply to a court for an order permitting the corporation to omit the proposal from the management proxy circular, and the court, if it is satisfied that subsection (5) applies, may make such order as it thinks fit.
  - (10) An applicant under sub-section (8) or (9) shall give the Director notice of the application and the Director is entitled to appear and be heard in person or by counsel.
- 138.** (1) A corporation shall prepare an alphabetical list of its shareholders entitled to receive notice of a meeting, showing the number of shares held by each share holder,
- (a) if a record date is fixed under paragraph 134(1)(c), not later than ten days after that date; or

(b) if no record date is fixed, on the record date established under paragraph 134(2)(a).

(2) If a record date for voting is fixed under paragraph 134(1)(d), the corporation shall prepare, no later than ten days after the record date, an alphabetical list of shareholders entitled to vote as of the record date at a meeting of shareholders that shows the number of shares held by each shareholder.

(3) If a record date for voting is not fixed under paragraph 134(1)(d), the corporation shall prepare, no later than ten days after a record date is fixed under paragraph 134(1)(c) or no later than the record date established under paragraph 134(2)(a), as the case may be, an alphabetical list of shareholders who are entitled to vote as of the record date that shows the number of shares held by each shareholder.

(3.1) A shareholder whose name appears on a list prepared under subsection (2) or (3) is entitled to vote the shares shown opposite their name at the meeting to which the list relates.

(4) A shareholder may examine the list of share holders during usual business hours at the registered office of the corporation or at the place where its central securities register is maintained; and at the meeting of shareholders for which the list was prepared.

**139.**(1) Unless the by-laws otherwise provide, a quorum of share holders is present at a meeting of shareholders, irrespective of the number of persons actually present at the meeting, if the holders of a majority of the shares entitled to vote at the meeting are present in person or represented by proxy.

(2) If a quorum is present at the opening of a meeting of shareholders, the shareholders present may, unless the by-laws otherwise provide, proceed with the business of the meeting, notwithstanding that a quorum is not present throughout the meeting.

(3) If a quorum is not present at the opening of a meeting of shareholders, the shareholders present may adjourn the meeting to a fixed time and place but may not transact any other business.

(4) If a corporation has only one shareholder, or only one holder of any class or series of shares, the shareholder present in person or by proxy constitutes a meeting.

## **INSIDER TRADING**

**126.**(1) In this Part,

“business combination” means an acquisition of all or substantially all the property of one body corporate by another, or an amalgamation of two or more bodies corporate, or any similar reorganization between or among two or more bodies corporate;

“insider” means, except in section 131,

(a) a director or officer of a distributing corporation;

(b) a director or officer of a subsidiary of a distributing corporation;

(c) a director or officer of a body corporate that enters into a business combination with a distributing corporation; and

(d) a person employed or retained by a distributing corporation;

“officer” means the chairperson of the board of directors, the president, a vice-president, the secretary, the treasurer, the comptroller, the general counsel, the general manager, a managing director, of an entity, or any other individual who performs functions for an entity similar to those normally performed by an individual

occupying any of those offices;

“share” means a share carrying voting rights under all circumstances or by reason of the occurrence of an event that has occurred and that is continuing, and includes

- (a) a security currently convertible into such a share, and
- (b) currently exercisable options and rights to acquire such a share or such a convertible security.

(2) For the purposes of this Part,

- (a) a director or an officer of a body corporate that beneficially owns, directly or indirectly, shares of a distributing corporation, or that exercises control or direction over shares of the distributing corporation, or that has a combination of any such ownership, control and direction, carrying more than the prescribed percentage of voting rights attached to all of the outstanding shares of the distributing corporation not including shares held by the body corporate as underwriter while those shares are in the course of a distribution to the public is deemed to be an insider of the distributing corporation;
- (b) a director or an officer of a body corporate that is a subsidiary is deemed to be an insider of its holding distributing corporation;
- (c) a person is deemed to beneficially own shares that are beneficially owned by a body corporate controlled directly or indirectly by the person;
- (d) a body corporate is deemed to own beneficially shares beneficially owned by its affiliates; and
- (e) the acquisition or disposition by an insider of an option or right to acquire a share is deemed to be a change in the beneficial ownership of the share to which the option or right to acquire relates.

**130.**(1) An insider shall not knowingly sell, directly or indirectly, a security of a distributing corporation or any of its affiliates if the insider selling the security does not own or has not fully paid for the security to be sold.

- (2) An insider shall not knowingly, directly or indirectly, sell a call or buy a put in respect of a security of the corporation or any of its affiliates.
- (3) Despite sub section (1), an insider may sell a security they do not own if they own another security convertible into the security sold or an option or right to acquire the security sold and, within ten days after the sale, they
  - (a) exercise the conversion privilege, option or right and deliver the security so acquired to the purchaser; or
  - (b) transfer the convertible security, option or right to the purchaser.
- (4) An insider who contravenes sub section (1) or (2) is guilty of an offence and liable on summary conviction to a fine not exceeding the greater of one million dollars and three times the profit made, or to imprisonment for a term not exceeding six months or to both.

## Hong Kong

Hong Kong has a significant trading economy and is a center for both multinational and local companies operating in Asia. Hong Kong companies can easily carrying out business in the Peoples Republic of China and throughout Asia. Hong Kong incorporated companies are increasingly becoming the chosen entities for conducting trading activities in Asia as they benefit from a tax friendly environment and business friendly legal system. Hong Kong Companies are guided by the Hong Kong Companies Ordinance.

Hong Kong Companies Ordinance is enforced by the Company Registry of Hong Kong. The primary functions of the Hong Kong Company Registry include the incorporation of local companies; the registration of overseas companies; the registration of documents required to be submitted by registered companies; the deregistration of defunct, solvent private companies; the prosecution of companies and their officers for breaches of the various regulatory provisions of the Hong Kong Companies Ordinance; the provision of facilities to inspect and obtain company information; and advising the Government on policy and legislative issues regarding company law and related legislation, including the Overall Review of the Hong Kong Companies Ordinance.

## **Salient features of Hong Kong Companies Ordinance**

### **Short Title and Commencement (Section 1)**

- (1) This Ordinance may be cited as the Companies Ordinance.
- (2) This Ordinance comes into operation on a day to be appointed by the Secretary for Financial Services and the Treasury by notice published in the Gazette.

### ***Company Formation and Related Matters***

#### ***Types of companies (Section 66)***

- (a) Only the following companies may be formed under this Ordinance –
  - (b) a public company limited by shares;
  - (c) a private company limited by shares;
  - (d) a public unlimited company with a share capital;
  - (e) a private unlimited company with a share capital;
  - (f) a company limited by guarantee without a share capital.

#### ***Formation of company (Section 67)***

- (1) Any one or more persons may form a company by–
  - (a) signing the articles of the company intended to be formed; and
  - (b) delivering to the Registrar for registration–
    - (i) an incorporation form in the specified form; and
    - (ii) a copy of the articles.
- (2) A company may only be formed for a lawful purpose.

#### ***Content of incorporation form (Section 68)***

- (1) An incorporation form must–
  - (a) in relation to the company intended to be formed, contain the particulars and statements specified in section 1 of Schedule 2;
  - (b) in relation to each founder member of the company, contain the particulars specified in section 2 of Schedule 2;
  - (c) in relation to each person who is to be a director of the company on the company's formation, contain–

- (i) the particulars specified in section 3 of Schedule 2; and
- (ii) the statement specified in section 4 of Schedule 2;
- (d) in relation to each person who is to be the company secretary, or one of the joint company secretaries, of the company on that formation, contain the particulars specified in section 5 of Schedule 2;
- (e) contain the statements specified in section 7 of Schedule 2; and
- (f) contain the statement of compliance specified in section 70(1).

If the company intended to be formed is a company limited by shares or an unlimited company, the incorporation form must also contain the statement specified in section 8 of Schedule 2.

***Signing of incorporation form (Section 69)***

An incorporation form must be signed by the founder member named in the form or, if 2 or more founder members are named, by any one of those members.

***Issue of certificate of incorporation on registration (Section 71)***

1. On registering an incorporation form and a copy of the articles delivered under section 67(1)(b), the Registrar must issue a certificate of incorporation certifying that the company—

- (a) is incorporated under this Ordinance; and (b) is a limited company or an unlimited company.

2. A certificate of incorporation must be signed by the Registrar.

***Conclusiveness of certificate of incorporation (Section 72)***

A certificate of incorporation is conclusive evidence that-

- (a) all the requirements of this Ordinance in respect of the registration of the company have been complied with; and
- (b) the company is registered under this Ordinance.

***Effect of incorporation (Section 73)***

- (1) On and after the date of incorporation stated in the certificate of incorporation, the founder members, and any other persons who may from time to time become the company's members, are a body corporate with the name stated in the certificate or, if a change of name has effect under section 107, 110, 770 or 772, with the new name.
- (2) On and after the date of incorporation, the body corporate is capable of exercising all the functions of an incorporated company, and has perpetual succession.
- (3) On and after the date of incorporation, the founder members, and any other persons who may from time to time become the company's members, are liable to contribute to the assets of the company in the event of the company being wound up as is mentioned in the Companies (Winding Up and Miscellaneous Provisions) Ordinance.

***Share Capital – Nature of Shares***

***Nature and transferability of shares (Section 134)***

A share or other interest of a member in a company is personal property.

A share or other interest of a member in a company is transferable in accordance with the company's articles.

***No nominal value (Section 135)***

1. Shares in a company have no nominal value.
2. This section applies to shares issued before the commencement date of this section as well as shares issued on or after that date.

***Allotment and Issue of shares***

***Exercise by directors of power to allot shares or grant rights (Section 140)***

- (1) Except in accordance with section 141, the directors of a company must not exercise any power—
  - (a) to allot shares in the company; or
  - (b) to grant rights to subscribe for, or to convert any security into, shares in the company.
- (2) Subsection (1) does not apply to—
  - (a) an allotment of shares, or grant of rights, under an offer made to the members of the company in proportion to their share holdings;
  - (b) an allotment of shares, or grant of rights, on a bonus issue of shares to the members of the company in proportion to their shareholdings;
  - (c) an allotment to a founder member of a company of shares that the member, by signing the company's articles, has agreed to take; or
  - (d) an allotment of shares made in accordance with a grant of a right to subscribe for, or to convert any security into, shares if the right was granted in accordance with an approval under section 141.
- (3) For the purposes of subsection (2)(a), the offer is not required to be made to any member whose address is in a place where the offer is not permitted under the law of that place.
- (4) A director commits an offence if the director knowingly contravenes, or authorizes or permits a contravention of, this section.
- (5) A director who commits an offence under sub-section (4) is liable to a fine at level 5 and to imprisonment for 6 months.
- (6) Nothing in this section or section 141 affects the validity of an allotment or other transaction.

***Registration of allotment (Section 143)***

- (1) A company must register an allotment of shares as soon as practicable and in any event within 2 months after the date of the allotment, by entering in the register of its members the information referred to in section 627(2) and(3).
- (2) If a company fails to register an allotment of shares within 2 months after the date of the allotment, the company, and every responsible person of the company, commit an offence, and each is liable to a fine at level 4 and, in the case of a continuing offence, to a further fine of \$700 for each day during which the offence continues.

***Transfer and Transmission of Shares – Transfer of Shares***

***Requirement for instrument of transfer (Section 150)***

- (1) A company must not register a transfer of shares in the company unless a proper instrument of

transfer has been delivered to the company.

- (2) Sub-section (1) does not affect any power of a company to register as a member a person to whom the right to shares has been transmitted by operation of law.

***Registration of transfer or refusal of registration (Section 151)***

- (1) The transferee or transferor of shares in a company may lodge the transfer with the company.
- (2) Within 2 months after the transfer is lodged, the company must either—
- (a) register the transfer; or
  - (b) send the transferee and the transferor notice of refusal to register the transfer.
- (3) If a company refuses registration, the transferee or transferor may request a statement of the reasons for the refusal.
- (4) If a request is made under sub-section (3), the company must, within 28 days after receiving the request—
- (a) send the person who made the request a statement of the reasons; or
  - (b) register the transfer.
- (5) If a company contravenes sub-section (2) or (4), the company and every responsible person of the company, commit an offence, and each is liable to a fine at level 4 and, in the case of a continuing offence, to a further fine of \$700 for each day during which the offence continues.

***Permitted alteration of share capital (Section 170)***

- (1) A limited company may alter its share capital in any one or more of the ways set out in sub-section (2).
- (2) The company may—
- (a) increase its share capital by allotting and issuing new shares in accordance with this Part;
  - (b) increase its share capital without allotting and issuing new shares, if the funds or other assets for the increase are provided by the members of the company;
  - (c) capitalize its profits, with or without allotting and issuing new shares;
  - (d) allot and issue bonus shares with or without increasing its share capital;
  - (e) convert all or any of its shares into a larger or smaller number of shares;
  - (f) cancel shares—
    - (i) that, at the date the resolution for cancellation is passed, have not been taken or agreed to be taken by any person; or
    - (ii) that have been forfeited.
- (3) A limited company may alter its share capital as referred to in sub-section (2)(e) or (f) only by resolution of the company.
- (4) A resolution referred to in subsection (3) may authorize the company to exercise the power—
- (a) on more than one occasion;
  - (b) at a specified time or in specified circumstances.

(5) Any amount remaining unpaid on shares being converted under subsection (2)(e) is to be divided equally among the replacement shares.

(6) If shares are cancelled under sub-section (2)(f), the company must reduce its share capital by the amount of the shares cancelled.

(7) For the purposes of Part 5, a cancellation of shares under this section is not a reduction of share capital.

(8) A limited company's articles may exclude or restrict the exercise of a power conferred by this section.

***Directors and Company Secretaries – Requirement to have Directors***

***Public company and company limited by guarantee required to have at least 2 directors (Section 453)***

(1) This section applies to –

- (a) a public company; and
- (b) a company limited by guarantee.

(2) The company must have at least 2 directors.

(3) With effect from the date of incorporation of the company, the first directors of the company are the persons named as the directors in the incorporation form delivered to the Registrar under section 67(1).

(4) A person who is deemed to be a director of the company under section 153(2) of the pre-amended predecessor Ordinance immediately before the commencement date of this section continues to be deemed to be a director of the company as if section 19 (1) of Schedule 2 to the Companies (Amendment) Ordinance 2004 had not been enacted, until a notice of appointment of a director is delivered to the Registrar in accordance with section 645(1).

(5) If a power specified in subsection (6) is exercisable by a director under the company's articles where the number of directors is reduced below the number fixed as the necessary quorum of directors, the power is exercisable also where the number of directors is reduced below the number required by subsection(2).

(6) The power specified for the purposes of sub-section (5) is a power to act for the purpose of—

- (a) increasing the number of directors; or
- (b) calling a general meeting of the company,

but not for any other purpose.

***Private company required to have at least one director (Section 454)***

(1) A private company must have at least one director.

(2) With effect from the date of incorporation of a private company, the first directors of the company are the persons named as the directors in the incorporation form delivered to the Registrar under section 67(1).

(3) A person who is deemed to be a director of a private company under section 153A(2) of the pre-amended predecessor Ordinance immediately before the commencement date of this section continues to be deemed to be a director of the company as if section 20 (1) of Schedule 2 to the Companies (Amendment) Ordinance 2004 (30 of 2004) had not been enacted, until a notice of appointment of a director is delivered to the Registrar in accordance with section 645(1).

### ***Appointment of Directors***

#### ***Minimum age for appointment as director (Section 459)***

- (1) A person must not be appointed a director of a company unless at the time of appointment the person has attained the age of 18 years.
- (2) An appointment made in contravention of subsection (1) is void.
- (3) Nothing in this section affects any liability of a person under any provision of this Ordinance or the Companies (Winding-Up and Miscellaneous Provisions) Ordinance if the person—
  - (a) purports to act as a director; or
  - (b) acts as a shadow director,

although the person could not, by virtue of this section, be appointed as a director.

#### ***Appointment of directors to be voted on individually (Section 460)***

- (1) This section applies to –
  - (a) a public company; and
  - (b) a company limited by guarantee.
- (2) At a general meeting of the company, a motion for the appointment of 2 or more persons as directors of the company by a single resolution must not be made, unless a resolution that it may be so made has first been passed at the meeting without any vote against it.
- (3) A resolution moved in contravention of subsection (2) is void, whether or not its being so moved was objected to at the time.
- (4) Despite the fact that the resolution is void, no provision (whether contained in a company's articles or in any contract with the company or otherwise) for the automatic reappointment of retiring directors in default of another appointment applies.
- (5) For the purposes of this section, a motion for approving a person's appointment, or for nominating a person for appointment, is to be regarded as a motion for the appointment of the person.

### ***Removal and Resignation of Directors***

#### ***Resolution to remove director (Section 462)***

- (1) A company may by an ordinary resolution passed at a general meeting remove a director before the end of the director's term of office, despite anything in its articles or in any agreement between it and the director.
- (2) Subsection (1) does not, if the company is a private company, authorize the removal of a director who has held office for life since 31 August, 1984.
- (3) Subsections (4), (5), (6), (7) and (8) apply in relation to a removal of a director by resolution, irrespective of whether the removal by resolution is under subsection (1) or otherwise.
- (4) Special notice is required of a resolution—
  - (a) to remove a director; or
  - (b) to appoint some body in place of a director so removed at the meeting at which the director is removed.

- (5) A vacancy created by the removal of a director, if not filled at the meeting at which the director is removed, may be filled as a casual vacancy.
- (6) A person appointed director in place of a removed director is to be regarded, for the purpose of determining the time at which that person or any other director is to retire, as if that person had become director on the day on which the person removed was last appointed a director.
- (7) In relation to a resolution to remove a director before the end of the director's term of office, no share may, on a poll, carry a greater number of votes than it would carry in relation to the generality of matters to be voted on at a general meeting of the company.
- (8) If a share carries special voting rights (that is to say, rights different from those carried by other shares) in relation to some matters but not others, the reference in subsection (7) to the generality of matters to be voted on at a general meeting of the company is to be construed as a reference to the matters in relation to which the share carries no special voting right.
- (9) This section is not to be regarded as depriving a person of compensation or damages payable to the person in respect of the termination of –
- (a) the person's appointment as director; or
  - (b) any appointment terminating with that as director.

***Resignation of director (Section 464)***

- (1) A director of a company may, unless it is otherwise provided in the articles of the company or by any agreement with the company, resign as director at anytime.
- (2) If a director of a company resigns, the company must deliver a notice of the resignation to the Registrar in the manner required by section 645(4).
- (3) Despite subsection (2), if the director resigning has reasonable grounds for believing that the company will not deliver the notice, the director resigning must deliver to the Registrar for registration a notice of the resignation in the specified form.
- (4) The notice required to be delivered under subsection (3) must state –
- (a) whether the director resigning is required by the articles of the company or by any agreement with the company to give notice of resignation to the company; and
  - (b) if notice is so required, whether the notice has been given in accordance with the requirement.
- (5) If notice of the resignation of a director of a company is required to be given by the articles of the company or by any agreement with the company, the resignation does not have effect unless the director gives notice in writing of the resignation–
- (a) in accordance with the requirement;
  - (b) by leaving it at the registered office of the company; or
  - (c) by sending it to the company in hard copy form or in electronic form.

***Appointment of Auditor***

***Eligibility for appointment (Section 393)***

- (1) Only a practice unit is eligible for appointment as auditor of a company under this Sub-division.

(2) The following are disqualified for appointment as auditor of a company under this Sub-division—

- (a) a person who is an officer or employee of the company;
- (b) a person who is a partner or employee of a person mentioned in paragraph(a);
- (c) a person who –
  - (i) is, by virtue of paragraph (a) or (b), disqualified for appointment as auditor of any other undertaking that is a subsidiary undertaking, or a parent undertaking, of the company or is a subsidiary undertaking of that parent undertaking; or
  - (ii) would be so disqualified if the undertaking were a company.

(3) In this section, a reference to an officer or employee of a company excludes an auditor of the company

***Auditor must be appointed for each financial year (Section 394)***

- (1) An auditor must be appointed for each financial year of a company.
- (2) An auditor may be appointed only under this Sub-division.

***Termination of Auditor’s Appointment***

***When appointment is terminated (Section 416)***

(1) A person’s appointment as auditor of a company is terminated if—

- (a) the term of office expires;
- (b) the person resigns from office under section 417(1);
- (c) the person ceases to be auditor under section 418;
- (d) the person is removed from office under section 419(1); or
- (e) a winding up order is made in respect of the company.

(2) Where a firm is appointed, by the firm name, as auditor of a company, the appointment is also terminated if every person who is regarded as being appointed as auditor by virtue of section 399—

- (a) ceases to be a partner in the firm before the term of office expires; or
- (b) ceases to be eligible, or becomes disqualified, for appointment as auditor of the company under Subdivision 2 before the term of office expires.

(3) Where a body corporate is appointed as auditor of a company, the appointment is also terminated if the body corporate is dissolved.

(4) If 2 or more persons are appointed as auditor of a company, and the appointment of any of the persons is terminated, the termination does not affect the appointment of the other person.

***Resignation of auditor (Section 417)***

(1) A person may resign from the office of auditor by giving the company a notice in writing that is accompanied by a statement required to be given under section 424.

(2) Such a person’s term of office expires—

- (a) at the end of the day on which notice is given to the company under sub-section (1); or

(b) if the notice specifies a time on a later day for the purpose, at that time.

(3) Within 15 days beginning on the date on which a company receives a notice of resignation, the company must deliver a notification in the specified form of that fact to the Registrar for registration.

(4) If a company contravenes subsection (3), the company and every responsible person of the company, commit an offence, and each is liable to a fine at level 5 and to imprisonment for 6 months and, in the case of a continuing offence, to a further fine of \$1,000 for each day during which the offence continues.

## **SINGAPORE**

The Companies Act of Singapore was first enacted in 1967. It has been subjected to numerous piecemeal amending legislations effected from time to time. In view of technological advancements, globalization and the regional economies undergoing massive changes, the Government saw that a major revamp of the Companies Act was due.

Hence, the Company Legislation and Regulatory Framework Committee (CLRFC) was formed in December 1999. It was asked to modernize Singapore's company and business regulatory framework and to recommend one which will promote a competitive economy.

The Committee delivered its final report in early October 2002 and all its 77 recommendations were accepted by the Government. Since then the Singapore Companies Act has been amended three times to give effect to the recommendations of the CLRFC, the major being Amendment Acts of 2004 and 2005.

## **Salient features of Singapore Companies Act**

### ***Formation of companies (Section 17)***

(1) Any person may, whether alone or together with another person, by subscribing his name or their names to a constitution and complying with the requirements as to registration, form an incorporated company.

(2) A company may be –

- (a) a company limited by shares;
- (b) a company limited by guarantee; or
- (c) an unlimited company.

(3) No company, association or partnership consisting of more than 20 persons can be formed for the purpose of carrying on any business that has for its object the acquisition of gain by the company, association or partnership, or by the individual members thereof, unless it is registered as a company under this Act, or is formed in pursuance of some other written law in Singapore or letters patent.

### ***Minimum of one member***

A company must have at least one member.

### ***No par value shares (Section 62A)***

All shares, whether issued before, on or after 30th January 2006 have no par value.

### ***Treasury Shares (Section 76H)***

Where ordinary shares or stocks are purchased or otherwise acquired by a company in accordance with the provisions of the Act, the company may –

- (a) hold the shares or stocks (or any of them); or

- (b) deal with any of them, at any time, as provided hereunder.

***Treasury Shares: Disposal and cancellation (Section 76K)***

Where shares are held as treasury shares, the company may at any time—

- (a) sell the shares (or any of them) for cash;
- (b) transfer the shares (or any of them) for the purposes of or pursuant to an employees' sharescheme;
- (c) transfer the shares (or any of them) as consideration for the acquisition of shares in or assets of another company or assets of a person;
- (d) cancel the shares (or any of them);or
- (e) sell, transfer or otherwise use the treasury shares for such other purposes as the Minister may by order prescribe.

***Treasury Shares: Maximum Holdings (Section 76I)***

Where a company has shares of only one class, the aggregate number of shares held as treasury shares shall not at any time exceed 10% of the total number of shares of the company at that time.

Where the share capital of a company is divided into shares of different classes, the aggregate number of the shares of any class held as treasury shares shall not at any time exceed 10% of the total number of the shares in that class at that time.

***Treasury Shares: Voting and Other Rights (Section 76J)***

- (1) This section shall apply to shares which are held by a company as treasury shares.
- (2) The company shall not exercise any right in respect of the treasury shares and any purported exercise of such a right is void.
- (3) The above said right include any right to attend or vote at meetings and for the purposes of this Act, the company shall be treated as having no right to vote and the treasury shares shall be treated as having no voting rights.
- (4) No dividend may be paid, and no other distribution (whether in cash or otherwise) of the company's assets (including any distribution of assets to members on a winding up) may be made, to the company in respect of the treasury shares.
- (5) Nothing in this section is to be taken as preventing –
  - (a) an allotment of shares as fully paid bonus shares in respect of the treasury shares; or
  - (b) the subdivision or consolidation of any treasury share into treasury shares of a greater or smaller amount, if the total value of the treasury shares after the sub-division or consolidation is the same as the total value of the treasury share before the subdivision or consolidation, as the case may be.
- (6) Any shares allotted as fully paid bonus shares in respect of the treasury shares shall be treated for the purpose of this Act as if they were purchased by the company at the time they were allotted, in circumstances in which section 76H applied.

***Company may have duplicate common seal (Section 124)***

A company may, if authorized by its constitution, have a duplicate common seal which shall be a facsimile of

the common seal of the company with the addition on its face of the words "Share Seal" and a certificate under such duplicate seal shall be deemed to be sealed with the common seal of the company for the purposes of this Act.

***Power to entrench provisions of memorandum and articles of company (Section 26 A)***

- (1) An entrenching provision may—
  - (a) be included in the constitution with which a company is formed; and
  - (b) at any time be inserted in the constitution of a company only if all the members of the company agree.
- (2) An entrenching provision may be removed or altered only if all the members of the company agree.
- (3) The provisions of this Act relating to the alteration of the constitution of a company are subject to any entrenching provision in the constitution of a company.
- (4) In this section, "entrenching provision" means a provision of the constitution of a company to the effect that other specified provisions of the constitution —
  - (a) may not be altered in the manner provided by this Act; or
  - (b) may not be so altered except—
    - (i) by a resolution passed by a specified majority greater than 75% (the minimum majority required by this Act for a special resolution); or
    - (ii) where other specified conditions are met.

***Company auditors (Section 10)***

- (1) No person other than an accounting entity shall —
  - (a) knowingly consent to be appointed as auditor for a company; or
  - (b) knowingly act as an auditor for a company
- (2) Without prejudice to the generality of subsection (1)(b), a person acts as an auditor for a company if the person prepares any report required by this Act to be prepared by an auditor of the company.
- (3) No company or person shall appoint an accounting entity as an auditor of a company without obtaining the accounting entity's prior consent.
- (4) For the purposes of subsection (3), the consent —
  - (a) of a public accountant shall be in writing signed by the public accountant;
  - (b) of an accounting firm, or an accounting limited liability partnership, shall be in writing signed by at least one partner of the firm or limited liability partnership; and
  - (c) of an accounting corporation shall be in writing signed by at least one director of the corporation.
- (5) Where an accounting firm is appointed as auditor of the company in the name of the accounting firm, the appointment shall take effect and operate as if the partners of the firm at the time of the appointment, who are public accountants at that time, are appointed as auditors of the company.
- (6) Where an accounting corporation is appointed as auditor of the company in the name of the corporation, the appointment shall take effect and operate as if —

- (a) the directors of the corporation who are practicing as public accountants in the corporation (whether directors at the time the accounting corporation was appointed as auditor or later); and
- (b) the employees of the corporation who are practicing as public accountants in the corporation (whether employed at the time the accounting corporation was appointed as auditor or later),

are appointed as auditors of the company.

***Directors (Section 145)***

- (1) Every company must have at least one director who is ordinarily resident in Singapore and, where the company has only one member, that sole director may also be the sole member of the company.
- (2) No person other than a natural person who has attained the age of 18 years & who is otherwise of full legal capacity shall be a director of a company.

***As to the duty and liability of officers (Section 157)***

- (1) A director shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office.
- (2) An officer or agent of a company shall not make improper use of any information acquired by virtue of his position as an officer or agent of the company to gain, directly or indirectly, an advantage for himself or for any other person or to cause detriment to the company.

***Powers of directors (Section 157A)***

- (1) The business of a company shall be managed by or under the direction of the directors.
- (2) The directors may exercise all the powers of a company except any power that this Act or the constitution of the company requires the company to exercise in general meeting.

***Secretary (Section 171)***

- (1) Every company shall have one or more secretaries each of whom shall be a natural person who has his principal or only place of residence in Singapore.
  - (1A) It shall be the duty of the directors of a company to take all reasonable steps to secure that each secretary of the company is a person who appears to them to have the requisite knowledge and experience to discharge the functions of secretary of the company.
  - (1AA) In addition, it shall be the duty of the directors of a public company to take all reasonable steps to secure that each secretary of the company is a person who –
    - (a) On 15 May, 1987 held the office of secretary in that company and continued to hold that office on 15 May, 2003; or
    - (b) Satisfies such requirements relating to experience, professional and academic requirements and membership of professional associations, as may be prescribed.
  - (1AB) The Registrar may require a private company to appoint a person who satisfies either of above as its secretary if he is satisfied that the company has failed to comply with any provision of this Act with respect to the keeping of any register or other record.
  - (1B) Any person who is appointed by the directors of a company as a secretary shall, at the time of his appointment, by himself or through a prescribed person authorized by him, file with the Registrar a

declaration in the prescribed form that he consents to act as secretary and providing the prescribed particulars.

- (1E) Where a director is the sole director of a company, he shall not act or be appointed as the secretary of the company.

***Annual general meeting (Section 175)***

(1) A general meeting of every company to be called the “annual general meeting” shall in addition to any other meeting be held once in every calendar year and not more than 15 months after the holding of the last preceding annual general meeting, but so long as a company holds its first annual general meeting within 18 months of its incorporation, it need not hold it in the year of its incorporation or in the following year.

(2) Notwithstanding sub section (1), the Registrar may extend the period of 15 months or 18 months referred to in that subsection, notwithstanding that the period is so extended beyond the calendar year–

- (a) upon an application by the company, if the registrar thinks there are special reasons to do so; or
- (b) in respect of any class of companies.

A private company may, by resolution passed by all of such members as, being entitled to do so, vote in person or, where proxies are allowed, by proxy present at the meeting, dispense with the holding of annual general meetings. (Section 175A)

***Audit Committees (Section 201B)***

(1) Every listed company shall have an audit committee.

(2) An audit committee shall be appointed by the directors from among their number (pursuant to a resolution of the board of directors) and shall be composed of 3 or more members of whom a majority shall not be –

- (a) executive directors of the company or any related corporation;
- (b) a spouse, parent, brother, sister, son or adopted son or daughter or adopted daughter of an executive director of the company or of any related corporation; or
- (c) any person having a relationship which, in the opinion of the board of directors, would interfere with the exercise of independent judgment in carrying out the functions of an audit committee.

(3) The members of an audit committee shall elect a chairman from among their number who is not an executive director or employee of the company or any related corporation.

(4) The functions of an audit committee shall be –

- (a) to review –
  - (i) with the auditor, the audit plan;
  - (ii) with the auditor, his evaluation of the system of internal accounting controls;
  - (iii) with the auditor, his audit report;
  - (iv) the assistance given by the company’s officers to the auditor;
  - (v) the scope and results of the internal audit procedures; and
  - (vi) the financial statements of the company and, if it is a parent company, the consolidated financial

statements, submitted to it by the company or the parent company, and thereafter to submit them to the directors of the company or parent company; and

(b) to nominate a person or persons as auditor, together with such other functions as may be agreed to by the audit committee and the board of directors.

(5) Upon the request of the auditor, the chairman of the audit committee shall convene a meeting of the committee to consider any matters the auditor believes should be brought to the attention of the directors or shareholders.

(6) Where the directors of the company or of a parent company are required to make a statement and the company is a listed company, the directors shall describe in the statement the nature and extent of the functions performed by the audit committee.

**LESSON ROUND UP**

- It is increasingly being recognized that the framework for regulation of corporate entities must facilitate companies to operate in a national and global context, encourage good corporate governance and enable protection of interests of investors, employees, creditors as well as boost economy as a whole. In the competitive and technology driven business environment, while corporates require greater autonomy of operation and opportunity for self-regulation with optimum compliance costs, there also is a need to bring about transparency through better disclosures and greater responsibility on the part of corporates and managements for improved compliance.
- In recognition of the fact that the primary purpose of any law is to facilitate the public and bearing in mind the current international style of legal drafting, an ideal law for the corporate sector should be clear, concise and comprehensible. It is desirable that the law is a “core company law” i.e. regulating the “entity” (irrespective of its corporate structure and size) rather than its “activity” and providing the basic principles governing all aspects of the operation of corporate entities within a single, comprehensive framework.
- It is in this context that countries across the world are modernizing and harmonizing their company law with global standards

**SELF TEST QUESTIONS**

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

1. The extension of corporate activity beyond the frontiers of the country has given rise to complex problems. Discuss.
2. Discuss the essential ingredients of a good system of company law.
3. The ultimate control of the company lies with the majority of shareholders. Discuss.
4. Discuss, in brief, distinguishing features of company law in United Kingdom.
5. Discuss the requirements relating to audit of financial statements in United States of America.
6. Enumerate brief provisions regarding formation of companies under the Singapore Companies Act.

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# Lesson 15

## Board Constitution and its Powers

### LESSON OUTLINE

- Board Composition
- Restriction and Powers of Board
- Board Committees- Audit Committee, Nomination and Remuneration Committee, Stakeholders and Relationship Committee and other Committees
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

The company is an artificial person and is managed by the human beings. The people who run it are known as Board of Directors. Directors acting collectively are known as Board. The directors play a very important role in the day to day functioning of the company. It is the board, who is responsible for the company's overall performance.

To attain the objectives prescribed in Memorandum of Association of the company, the company depends on Board of Directors (collectively) and directors (individually).

Committees as constituted by the Board are essential for effective functioning of the company.

As future company secretaries this chapter will guide you to understand the powers of Board and restrictions to the Board powers, and formation of committees and their roles.

## Introduction

The Board of directors of a company is a nucleus, selected according to the procedure prescribed in the Act and the Articles of Association. Members of the Board of directors are known as directors, who unless especially authorised by the Board of directors of the Company, do not possess any power of management of the affairs of the company. The Board of Directors oversees how the management serves and protects the long term interests of all the stakeholders of the company. The institution of Board of Directors is based on the premise that a group of trustworthy people look after the interests of the large number of shareholders who are not directly involved in the management of the company. The position of board of directors is that of trust as the board is entrusted with the responsibility to act in the best interests of the company. Acting collectively as a Board of directors, they can exercise all the powers of the company except those, which are prescribed by the Act to be specifically exercised by the company in general meeting.

The Board formulate policies and establish organisational set up for implementing those policies and to achieve the objectives contained in the Memorandum, muster resources for achieving the company objectives and control, guide, direct and manage the affairs of the company.

Section 2(10) of the Companies Act, 2013 defines that “Board of Directors” or “Board”, in relation to a company, means the collective body of the directors of the company.

The term ‘Board of Directors’ means a body duly constituted to direct, control and supervise the affairs of a company.

As per Section 149 of the Companies Act, 2013, the Board of Directors of every company shall consist of individual only. Thus, no body corporate, association or firm shall be appointed as director.

## Board Composition

### Minimum/Maximum Number of Directors in a Company [Section 149(1)]

Section 149(1) of the Companies Act, 2013 requires that every company shall have a minimum number of 3 directors in the case of a public company, two directors in the case of a private company, and one director in the case of a One Person Company. A company can appoint maximum 15 fifteen directors without any specific compliance. A company may appoint more than fifteen directors after passing a special resolution in general meeting.

The restriction of maximum number of directors shall not apply to section 8 companies.

#### Minimum number of directors

Public Company	-	3 Directors
Private Company	-	2 directors
One Person Company (OPC)	-	1 Director

Maximum Number of Director is 15, which can be increased by passing a special resolution. Section 8 companies can have more than 15 directors.

Section 149(3) provides that every company shall have at least one director who has stayed in India for a total period of not less than one hundred and eighty-two days in the previous calendar year.

Further, Second proviso to Section 149(1) read Rule 3 of Companies (Appointment and Qualification of Directors) Rules, 2014 following class of companies must have at least one Women Director.

All Listed Companies	
Public companies	<ul style="list-style-type: none"> <li>with paid up capital of ₹100 crore or more or</li> <li>with turnover of ₹300 crore or more</li> </ul>

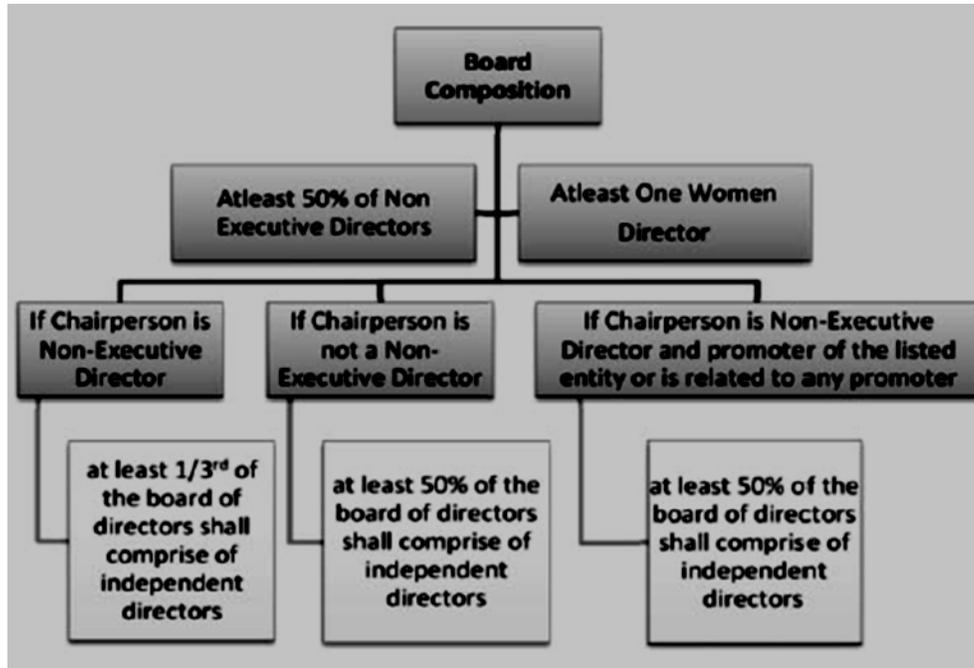


Figure 1: A typical Board composition of a listed company.

### Number of directorships [Section 165]

Maximum number of directorships, including any alternate directorship, a person can hold is 20. Same time, a person cannot be a director of more than 10 public companies. For the purpose of counting such directorship in public company, directorship in private companies that are either holding or subsidiary of a public company shall be included. Alternate directorship shall also be included while calculating the directorship of 20 companies. Section 8 company will not be counted for the purpose of maximum number of Directorship. Further the members of a company may restrict abovementioned limit by passing a special resolution for its own directors.

For reckoning the limit of directorships of twenty companies, the directorship in a dormant company shall not be included.

If a person accepts an appointment as a director in contravention of above mentioned provisions, he shall be punishable with fine which shall not be less than five thousand rupees but which may extend to twenty five thousand rupees for every day after the first day during which the contravention continues.

Additionally for listed entities SEBI vide recent notification provides that the board of directors of the top 1000 listed entities (with effect from April 1, 2019) and the top 2000 listed entities (with effect from April 1, 2020) shall comprise of not less than six directors.

Explanation: The top 1000 and 2000 entities shall be determined on the basis of market capitalisation as at the end of the immediate previous financial year.

No listed entity shall appoint a person or continue the directorship of any person as a non-executive director who has attained the age of seventy five years unless a special resolution is passed to that effect, in which case the explanatory statement annexed to the notice for such motion shall indicate the justification for appointing such a person.

With effect from April 1, 2020, the top 500 listed entities shall ensure that the Chairperson of the board of such listed entity shall - (a) be a non-executive director; (b) not be related to the Managing Director or the Chief Executive Officer as per the definition of the term "relative" defined under the Companies Act, 2013: Further it is provided that this sub-regulation shall not be applicable to the listed entities which do not have any identifiable promoters as per the shareholding pattern filed with stock exchanges. Explanation - The top 500 entities shall be determined on the basis of market capitalisation, as at the end of the immediate previous financial year.

It is also provided that the Board of directors of the top 500 listed entities shall have at least one independent woman director by April 1, 2019 and the Board of directors of the top 1000 listed entities shall have at least one independent woman director by April 1, 2020. The top 500 and 1000 entities shall be determined on the basis of market capitalisation, as at the end of the immediate previous financial year.

- *Maximum limit on total number of directorship has been fixed at 20 companies and the maximum number of public companies in which a person can be appointed as a director shall not exceed ten.*
- *The members of a company may, by special resolution, specify any lesser number of companies in which a director of the company may act as director.*

#### **Power of Board [Section 179]**

Section 179 of the Act deals with the powers of the board; all powers to do such acts and things for which the company is authorised is vested with board of directors. But the board can act or do the things for which powers are vested with them and not with general meeting.

The following [Section 179(3) read with Rule 8 of Companies (Management & Administration) Rules, 2014] powers of the Board of directors shall be exercised only by means of resolutions passed at meetings of the Board, namely :-

- (1) to make calls on shareholders in respect of money unpaid on their shares;
- (2) to authorise buy-back of securities under section 68;
- (3) to issue securities, including debentures, whether in or outside India;
- (4) to borrow monies;
- (5) to invest the funds of the company;
- (6) to grant loans or give guarantee or provide security in respect of loans;
- (7) to approve financial statement and the Board's report;
- (8) to diversify the business of the company;
- (9) to approve amalgamation, merger or reconstruction;
- (10) to take over a company or acquire a controlling or substantial stake in another company;
- (11) to make political contributions;
- (12) to appoint or remove key managerial personnel (KMP);
- (13) to appoint internal auditors and secretarial auditor;

The Board may, by a resolution passed at a meeting, delegate to any committee of directors, the managing director, the manager or any other principal officer of the company or in the case of a branch office of the company, the principal officer of the branch office, the powers specified in (4) to (6) above on such conditions as it may specify.

The banking company is not covered under the purview of this section. The company may impose restriction and conditions on the powers of the Board.

*Note: in case of Section 8 companies resolutions related to clauses (d), (e) and (f) of sub-section (3) of Section 179 of the Act i.e. borrow monies, to invest funds of the company and to grant loans or give guarantee or provide security in respect of loans by section 8 companies may be decided by the Board by circulation. (Refer to exemption notification dt. 5.6.2015)*

### **Restriction on Powers of Board [Section 180]**

The board can exercise the following powers only with the consent of the company by special resolution, namely –

- (a) to sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company or where the company owns more than one undertaking, of the whole or substantially the whole of any of such undertakings.
- (b) to invest otherwise in trust securities the amount of compensation received by it as a result of any merger or amalgamation;
- (c) to 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, free reserves and securities premium apart from temporary loans obtained from the company's bankers in the ordinary course of business;
- (d) to remit, or give time for the repayment of, any debt due from a director.

The special resolution relating to borrowing money exceeding paid up capital, free reserves and securities premium shall specify the total amount up to which the money may be borrowed by Board.

The title of buyer or the person who takes on leases any property, investment or undertaking on good faith cannot be affected and also in case if such sale or lease covered in the ordinary business of such company.

The resolution may also stipulate the conditions of such sale and lease, but this doesn't authorise the company to reduce its capital except the provisions contained in this Act.

The debt incurred by the company exceeding the paid up capital and free reserves is not valid and effectual, unless the lender proves that the loan was advanced on good faith and also having no knowledge of limit imposed had been exceeded.

After exemption notification dated 05.06.2015, in case of Private Companies provisions of Section 180 shall not apply.

### **Contributions to Charitable Funds and Political Parties [Section 181]**

The power of making contribution to 'bona fide' charitable and other funds is available to the board subject to certain limits.

Further, the prior permission of company in general meeting is required if such contribution exceeds five percent of its average net profits for the three immediately preceding previous years.

### **Prohibitions and Restrictions Regarding Political Contributions [Section 182]**

According to Section 182 of the Act, a company, other than a government company which has been in existence for less than three financial years, may contribute any amount directly to any political party. Further the contribution under this section shall not be made except by an account payee cheque drawn on a bank or an account payee bank draft or use of electronic clearing system through a bank account.

Further, the limit of contribution to political parties is 7.5% of the average net profits during the three immediately preceding financial years. The Finance Act, 2017 amended section 182 of the Companies Act, 2013, accordingly the limit on the maximum amount that can be contributed by a company to a political party has been removed. Hence a company now can contribute any percentage without any limit.

The contribution must be authorised by board in its meeting by resolution and such resolution deemed to be the justification in law for such contribution.

The donation may be directly or indirectly. The contribution so made if or likely to affect the public support for a political party deemed to be the contribution for political purpose.

If the expenditure incurred on advertisement in any publication souvenir, brochure, tract, pamphlet or the like is deemed as political contribution if such publication is by or on behalf of political party or if not, then for the advantage to such political party for a political purpose.

Every company is required to disclose in its profit and loss account the total amount contributed by it under this section during the financial year to which the account relates.

### **Penalty for Contravention**

The contribution in contravention of the provisions of this section, the company shall be punishable for an amount of which may extend to five times of the amount so contributed and every officer who is in default shall be punishable with imprisonment for a term which may extend to six months and with fine which may extend to five times of the amount so contributed.

### **Power of Board and other Persons to make Contributions to National Defence Fund, etc. [Section 183]**

The Board is authorised to contribute such amount as it thinks fit to the National Defence Fund or any other fund approved by the Government for the purpose of national defence.

The company is required to disclose in its profit and loss account the total amount or amounts contributed by it during the financial year.

## **BOARD COMMITTEES**

A board committee is a small working group identified by the board, consisting of board members, for the purpose of supporting the board's work. Committees are generally formed to perform some expertise work. Members of the committee are expected to have expertise in the specified field.

Committees are usually formed as a means of improving board effectiveness and efficiency, in areas where more focused, specialized and technical discussions are required. These committees prepare the groundwork for decision-making and report at the subsequent board meeting. Committees enable better management of full board's time and allow in-depth scrutiny and focused attention.

For a Board of Directors to do its work effectively, it is necessary that members understand their individual

responsibilities and that the board organizes itself to perform the necessary tasks effectively. Committees are so appointed by the Board to focus on specific areas and take informed decisions within the framework of delegated authority, and make specific recommendations to the Board on matters in their areas or purview. All decisions and recommendations of the committees are placed before the Board for information or for approval.

Through committees, work can be divided so that far more can be accomplished than if the entire board acted on all matters. Committees provide organizational structure, and at the same time allow enough flexibility so the board can adapt quickly to the changing demands of the environment.

The functions of board committees can be divided as under:

- Divide and expediting the work of the organization by removing routine tasks from monthly board consideration
- Utilize the specific talents and knowledge of board members
- Permit broader participation by all board members

For a committee to operate effectively, it needs:

- A specific terms of reference so that it is aware of its responsibility, timeline, and the limits of its authority
- A capable staff for assistance when needed
- An effective committee chairperson who:
  - Understands the decision-making process
  - Knows how to lead a group through that process
  - Enables the committee to arrive at appropriate decisions
- Responsible committee members who:
  - Spend the time and effort as may be necessary
  - Understand how to contribute and evaluate the adequacy of available data and its limits
  - Brain storm for alternative course of actions

However, the Board of Directors is ultimately responsible for the acts of the committee. Board is responsible for defining the committee role and structure.

Mandatory Committees of the Board are prescribed under Companies Act, 2013 (for certain class of companies) and SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 for listed companies.

Mandatory Committees under the Companies Act 2013 are:

- Audit Committee
- Nomination and Remuneration Committee
- Stakeholders Relationship Committee
- Corporate Social Responsibility Committee

## **AUDIT COMMITTEE**

Audit Committee is one of the main pillars of the corporate governance mechanism in any company. The

Committee is charged with the principal oversight of financial reporting and disclosure and aims to enhance the confidence in the integrity of the company's financial reporting, the internal control processes and procedures and the risk management systems.

The constitution of Audit Committee is mandated under the Companies Act, 2013 and SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

### **Constitution of Audit Committee**

Section 177(1) of the Companies Act, 2013 read with Rule 6 of the Companies (Meetings of the Board and its Powers) Rules, 2014, provides that the Board of directors of following companies are required to constitute a Audit Committee of the Board-

- (i) Every listed Public companies;
- (ii) All public companies with a paid up capital of 10 crore rupees or more;
- (iii) All public companies having turnover of 100 crore rupees or more;
- (iv) All public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding 50 crore rupees 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 for the purposes of this rule.

The following classes of unlisted public company shall not be covered for above purpose:-

- (a) a joint venture;
- (b) a wholly owned subsidiary; and
- (c) a dormant company as defined under section 455 of the Act.

### **Composition of the Audit Committee Section [177(2)]**

There shall be minimum of three directors, with majority being independent. The majority including the Chairperson should be persons with ability to read and understand the financial statement.

The requirement of Independent directors forming a majority is not applicable to Section 8 companies (*vide* exemption notification dt. 5-6-2015)

### ***For the listed entities, according to SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015***

Every listed entity shall constitute a qualified and independent audit committee in accordance with the terms of reference, subject to the following:

- (a) The audit committee shall have minimum three directors as members.
- (b) Two-thirds of the members of audit committee shall be independent directors.
- (c) All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise.

The word "financially literate" shall mean the ability to read and understand basic financial statements i.e. balance sheet, profit and loss account, and statement of cash flows.

Further it has been explained that a member shall be considered to have accounting or related financial management expertise if he or she possesses experience in finance or accounting, or requisite professional certification in accounting, or any other comparable experience or background which results in the individual's financial sophistication, including being or having been a chief executive officer, chief financial officer or other senior officer with financial oversight responsibilities.

The regulation further provides that the chairperson of the audit committee shall be an independent director and he shall be present at Annual general meeting to answer shareholder queries. The Company Secretary shall act as the secretary to the audit committee.

The audit committee at its discretion shall invite the finance director or head of the finance function, head of internal audit and a representative of the statutory auditor and any other such executives to be present at the meetings of the committee:

Provided that occasionally the audit committee may meet without the presence of any executives of the listed entity.

### **Number of Meetings and Quorum**

In case of unlisted public companies, audit committee may meet number of times as desirable to serve its purpose. In such companies quorum, minimum number of meetings and quorum may be decide by the Board of Directors.

For listed companies, SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 provides for the minimum number of meetings and quorum of the audit committee.

- (i) The Audit Committee of a listed entity shall meet at least four (4) times in a year and not more than 120 days shall elapse between two meetings.
- (ii) The quorum for audit committee meeting shall either be
  - 2 members, or 1/3rd of the members of the audit committee, whichever is greater; with at least 2 independent directors.

The requirement of minimum 2 independent directors in the meeting of Audit Committee is new provision which must be complied by all the listed entities.

### **Functions/Role of the Audit Committee [Section 177(4)]**

Every Audit Committee shall act in accordance with the terms of reference specified in writing by the Board. Terms of reference as prescribed by the board shall *inter alia*, include, –

- (a) the recommendation for appointment, remuneration and terms of appointment of auditors of the company;  
*(In case of Government Companies, in Clause (1) of sub-section (4) of section 177, for the words "recommendation for appointment, remuneration and terms of appointment" the words "recommendation for remuneration" shall be substituted – Exemption Notification dated 05-06-2015)*
- (b) review and monitor the auditor's independence and performance, and effectiveness of audit process;
- (c) examination of the financial statements and the auditors' report thereon;
- (d) approval or any subsequent modification of transactions of the company with related parties;

The Audit Committee may make omnibus approval for related party transactions proposed to be entered into by the company subject to such conditions as prescribed under rule 6A of the Companies (Meetings of Board and its Powers) Rules, 2014.

Further in case of transaction, other than transactions referred to in section 188 (Related Party Transactions), and where Audit Committee does not approve the transaction, it shall make its recommendations to the Board.

In case any transaction involving any amount not exceeding one crore rupees 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 three 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 authorised by any other director, the director concerned shall indemnify the company against any loss incurred by it:

The provisions of this clause 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.

- (e) scrutiny of inter-corporate loans and investments;
- (f) valuation of undertakings or assets of the company, wherever it is necessary;
- (g) evaluation of internal financial controls and risk management systems;
- (h) monitoring the end use of funds raised through public offers and related matters.

### **Powers of the Audit Committee [Section 177(5) and (6)]**

The Audit Committee has the power to call for the comments of the auditors about internal control systems, the scope of audit, including the observations of the auditors and review of financial statements 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.

The Audit Committee has authority to investigate into any matter in relation to the items specified in terms of reference or referred to it by the Board and for this purpose the Committee has power to obtain professional advice from external sources. The Committee for this purpose shall have full access to information contained in the records of the company.

SEBI (LODR) Regulations in addition empowers the Audit committee to seek any information from any employee, obtain outside legal or other professional advice and secure attendance of outsiders with relevant expertise, if it considers necessary.

The auditors of a company and the key managerial personnel 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) of the Act provides that the board's report shall disclose the following –

- Composition of an Audit Committee
- Where the Board had not accepted any recommendation of the Audit Committee, the same shall be disclosed in the report along with the reasons therefore.

**Audit Committee and Vigil Mechanism [Section 177(9) to (14)]**

Section 177 read with Rule 7 of the Companies (Meetings of Board and its powers Rules, 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 fifty crore rupees.

The vigil mechanism set up as above, shall provide for adequate safeguards against victimisation of persons who use such mechanism and make provision for direct access to the chairperson of the Audit Committee in appropriate or exceptional cases:

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 conflicted of interest in a given case, they should recuse themselves and the others on the committee would deal with the matter on hand.

In case of other companies (not required to constitute audit committee), 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. This 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, as the case may be, in exceptional cases.

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.

The details of establishment of the Vigil Mechanism is required to be disclosed by the company on its website, if any, and in the Board's report.

**Additional role of the Audit Committee under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015****A. The role of the audit committee shall include the following:**

- (1) oversight of the listed entity's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible;
- (2) recommendation for appointment, remuneration and terms of appointment of auditors of the listed entity;
- (3) approval of payment to statutory auditors for any other services rendered by the statutory auditors;
- (4) reviewing, with the management, the annual financial statements and auditor's report thereon before submission to the board for approval, with particular reference to:
  - (a) matters required to be included in the director's responsibility statement to be included in the board's report in terms of clause (c) of sub-section (3) of Section 134 of the Companies Act, 2013;
  - (b) changes, if any, in accounting policies and practices and reasons for the same;
  - (c) major accounting entries involving estimates based on the exercise of judgment by

- management;
- (d) significant adjustments made in the financial statements arising out of audit findings;
  - (e) compliance with listing and other legal requirements relating to financial statements;
  - (f) disclosure of any related party transactions;
  - (g) modified opinion(s) in the draft audit report;
- (5) reviewing, with the management, the quarterly financial statements before submission to the board for approval;
  - (6) reviewing, with the management, the statement of uses / application of funds raised through an issue (public issue, rights issue, preferential issue, etc.), the statement of funds utilized for purposes other than those stated in the offer document / prospectus / notice and the report submitted by the monitoring agency monitoring the utilisation of proceeds of a public or rights issue, and making appropriate recommendations to the board to take up steps in this matter;
  - (7) reviewing and monitoring the auditor's independence and performance, and effectiveness of audit process;
  - (8) approval or any subsequent modification of transactions of the listed entity with related parties;
  - (9) scrutiny of inter-corporate loans and investments;
  - (10) valuation of undertakings or assets of the listed entity, wherever it is necessary;
  - (11) evaluation of internal financial controls and risk management systems;
  - (12) reviewing, with the management, performance of statutory and internal auditors, adequacy of the internal control systems;
  - (13) reviewing the adequacy of internal audit function, if any, including the structure of the internal audit department, staffing and seniority of the official heading the department, reporting structure coverage and frequency of internal audit;
  - (14) discussion with internal auditors of any significant findings and follow up there on;
  - (15) reviewing the findings of any internal investigations by the internal auditors into matters where there is suspected fraud or irregularity or a failure of internal control systems of a material nature and reporting the matter to the board;
  - (16) discussion with statutory auditors before the audit commences, about the nature and scope of audit as well as post-audit discussion to ascertain any area of concern;
  - (17) to look into the reasons for substantial defaults in the payment to the depositors, debenture holders, shareholders (in case of non-payment of declared dividends) and creditors;
  - (18) to review the functioning of the whistle blower mechanism;
  - (19) approval of appointment of chief financial officer after assessing the qualifications, experience and background, etc. of the candidate;
  - (20) Carrying out any other function as is mentioned in the terms of reference of the audit committee.
  - (21) reviewing the utilization of loans and/ or advances from/investment by the holding company in the subsidiary exceeding rupees 100 crore or 10% of the asset size of the subsidiary, whichever is lower including existing loans / advances / investments existing as on the date of coming into force of this provision.(Notified on 9<sup>th</sup> May, 2018 effective from April 1, 2019)

**B. The audit committee shall mandatorily review the following information:**

- (1) management discussion and analysis of financial condition and results of operations;
- (2) statement of significant related party transactions (as defined by the audit committee), submitted by management;
- (3) management letters / letters of internal control weaknesses issued by the statutory auditors;
- (4) internal audit reports relating to internal control weaknesses; and
- (5) the appointment, removal and terms of remuneration of the chief internal auditor shall be subject to review by the audit committee.
- (6) statement of deviations:
  - (a) quarterly statement of deviation(s) including report of monitoring agency, if applicable, submitted to stock exchange(s) in terms of Regulation 32(1).
  - (b) annual statement of funds utilized for purposes other than those stated in the offer document/prospectus/notice in terms of Regulation 32(7).

**Comparison table of Audit Committee under Companies Act 2013 and SEBI (LODR) Regulations, 2015**

SEBI (LODR) Regulations, 2015	<p><b>Regulation 18</b></p> <p>(1) Every listed entity shall constitute a qualified and independent audit committee in accordance with the terms of reference, subject to the following:</p> <ul style="list-style-type: none"> <li>a) The audit committee shall have minimum three directors as members.</li> <li>b) Two-thirds of the members of audit committee shall be independent directors.</li> <li>c) All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise. Explanation (1). – For the purpose of this regulation, “financially literate” shall mean the ability to read and understand basic financial statements i.e. balance sheet, profit and loss account, and statement of cash flows. Explanation (2). – For the purpose of this regulation , a member shall be considered to have accounting or related financial management expertise if he or she possesses experience in finance or accounting, or requisite professional certification in accounting, or any other comparable experience or background which results in the individual’s financial sophistication, including being or having been a chief executive officer, chief financial officer or other senior officer with financial oversight responsibilities.</li> <li>d) The chairperson of the audit committee shall be an Independent Director and he shall be present at Annual general meeting to answer Shareholder queries.</li> <li>e) The Company Secretary shall act as the Secretary to the Audit Committee.</li> <li>f) The Audit Committee at its discretion shall invite the finance director or head of the finance function, head of internal audit and a representative of the statutory auditor and any other such executives to be present at the</li> </ul>
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	<p>meetings of the committee:</p> <p>Provided that occasionally the audit committee may meet without the presence of any executives of the listed entity.</p> <p>(2) The listed entity shall conduct the meetings of the audit committee in the following manner:</p> <ol style="list-style-type: none"> <li>a) The audit committee shall meet at least four times in a year and not more than one hundred and twenty days shall elapse between two meetings.</li> <li>b) The quorum for audit committee meeting shall either be two members or one third of the members of the audit committee, whichever is greater, with at least two independent directors.</li> <li>c) The audit committee shall have powers to investigate any activity within its terms of reference, seek information from any employee, obtain outside legal or other professional advice and secure attendance of outsiders with relevant expertise, if it considers necessary.</li> </ol> <p>(3) The role of the audit committee and the information to be reviewed by the audit committee shall be as specified in Part C of Schedule II.</p>
Companies Act, 2013	<p><b>Section 177</b></p> <p>(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.</p> <p>(2) The Audit Committee shall consist of a minimum of three directors with independent directors forming a majority: Provided that majority of members of Audit Committee including its Chairperson shall be persons with ability to read and understand the financial statement.</p> <p>(3) Every Audit Committee of a company existing immediately before the commencement of this Act shall, within one year of such commencement, be reconstituted in accordance with sub-section (2).</p> <p>(4) Every Audit Committee shall act in accordance with the terms of reference specified in writing by the Board which shall, inter alia, include, –</p> <ol style="list-style-type: none"> <li>i. the recommendation for appointment, remuneration and terms of appointment of auditors of the company;</li> <li>ii. review and monitor the auditor's independence and performance, and effectiveness of audit process;</li> <li>iii. examination of the financial statement and the auditors' report thereon;</li> <li>iv. approval or any subsequent modification of transactions of the company with related parties;</li> <li>v. scrutiny of inter-corporate loans and investments;</li> <li>vi. valuation of undertakings or assets of the company, wherever it is necessary;</li> <li>vii. Evaluation of internal financial controls and risk management systems;</li> <li>viii. monitoring the end use of funds raised through public offers and related matters.</li> </ol> <p>(5) The Audit Committee may call for the comments of the auditors about internal control systems, the scope of audit, including the observations of the auditors and</p>

	<p>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.</p> <p>(6) The Audit Committee shall have authority to investigate into any matter in relation to the items specified in sub-section (4) or referred to it by the Board and for this purpose shall have power to obtain professional advice from external sources and have full access to information contained in the records of the company.</p> <p>(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.</p> <p>(8) The Board's report under sub-section (3) of section 134 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 therefor.</p>
<p>Comments</p>	<ol style="list-style-type: none"> <li>1. The listing Regulations and the Companies Act provides standalone provision with regard to the audit committee. Accordingly, it requires that the compliance conditions under Companies Act along with the Listing Regulations shall be complied.</li> <li>2. The Regulations requires all members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise whereas the Companies Act, 2013 provides for majority of members of Audit Committee including its Chairperson shall be persons with ability to read and understand, the financial statement.</li> <li>3. The Role of Audit Committee and the mandatory review of information by audit committee is prescribed under Regulations whereas the Companies Act, 2013 prescribe the terms of Reference of the Committee. The role of Audit Committee under the Regulations is wider.</li> <li>4. The Companies Act 2013 does not prescribe that the chairman shall be an independent Director</li> <li>5. The Companies Act 2013 does not provide for frequency of meeting of the audit Committee.</li> <li>6. The Companies Act 2013 does not provide for quorum for Audit committee meeting.</li> <li>7. The Regulations requires 2/3rd of members of the Audit Committee to be independent whereas Companies Act 2013 requires majority of members to Audit Committee to be Independent.</li> </ol>

**SECTION 178: Nomination and Remuneration Committee**

**Constitution**

The Nomination and Remuneration Committee helps the Board of Directors in the preparations relating to the election of members of the Board of Directors, and in handling matters within its scope of responsibility that relate to the conditions of employment and remuneration of senior management, and to management's and personnel's remuneration and incentive schemes. The responsibilities of the Nomination

and Remuneration Committee are defined in Nomination and remuneration policy or terms of reference of the Nomination and Remuneration document.

The Board of directors of following companies shall constitute Nomination and Remuneration Committee of the Board:

- (a) Every listed Public Companies; or
- (b) The following class of companies –
  - (i) all public companies with a paid up capital of ten crore rupees or more;
  - (ii) all public companies having turnover of one hundred crore rupees or more;
  - (iii) all public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding fifty crore rupees or more.

The following classes of unlisted public company shall not be covered for above purpose:-

- (a) a joint venture;
- (b) a wholly owned subsidiary; and
- (c) a dormant company as defined under section 455 of the Act.

***After exemption notification dated 05.06.2015 the provisions of Section 178 of the Act are not applicable to the Section 8 Companies.***

The committee shall consist of three 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 member, but shall not chair such committee.

Additionally, for listed Companies, SEBI (LODR) Reg, 2015 provides that the nomination and remuneration committee shall comprise of at least three directors. All directors of the committee shall be non-executive directors; and at least fifty percent of the directors shall be independent directors.

The Chairperson of the nomination and remuneration committee shall be an independent director. The chairperson of the listed entity, whether executive or non-executive, may be appointed as a member of the Nomination and Remuneration Committee but shall not chair such Committee.

The Chairperson of the nomination and remuneration committee may be present at the annual general meeting, to answer the shareholders' queries; however, it shall be up to the chairperson to decide who shall answer the queries.

## **Functions**

As per section 178(2) of the Act, the Committee shall identify the person qualified to become directors and may be appointed in senior management and recommend their appointment and removal and shall specify the manner for effective evaluation of performance of Board, its committees and individual directors to be carried out either by the Board, by the Nomination and Remuneration Committee or by an independent external agency and review its implementation and compliance.

As per section 178(3) of the Act, the Committee shall formulate the criteria, for determining qualifications, positive attributes and independence of a director and recommend to the Board the policy relating to remuneration for directors, KMPs and other employees.

As per section 178(4) of the Act, while formulating its policy, the Nomination and Remuneration Committee shall ensure that

- (a) the level and composition of remuneration is reasonable and sufficient to attract, retain and motivate the directors
- (b) relationship of remuneration to performance is clear and meets appropriate performance benchmarks and
- (c) remuneration to directors, key managerial personnel 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:

Provided that such policy shall be placed on the website of the company, if any, and the salient features of the policy and changes therein, if any, along with the web address of the policy, if any, shall be disclosed in the Board's report.

***After exemption notification dated 05.06.2015, in case of the Government Company provisions of Section 178(2), (3) and (4) shall apply for the appointment of Senior management and other employees only.***

Additionally, in case of listed companies SEBI(LODR) Reg, 2015 provides that the committee shall devise a policy on diversity of board of directors.

The quorum for a meeting of the nomination and remuneration committee shall be either two members or one third of the members of the committee, whichever is greater, including at least one independent director in attendance. The nomination and remuneration committee shall meet at least once in a year.(Notified on 9th May, 2018 effective from April 1, 2019)

The committee shall recommend to the board, all remuneration, in whatever form, payable to senior management. (Notified on 9th May, 2018 effective from April 1, 2019)

**Comparison table of Nomination and Remuneration Committee under Companies act 2013 and SEBI (LODR) Regulations, 2015**

<b>SEBI (LODR) Regulations, 2015</b>	<p><b>Regulation 19</b></p> <p>(1) The board of directors shall constitute the nomination and remuneration committee as follows:</p> <ul style="list-style-type: none"> <li>(a) the committee shall comprise of at least three directors ;</li> <li>(b) all directors of the committee shall be non-executive directors; and</li> <li>(c) at least fifty percent of the directors shall be independent directors.</li> </ul> <p>(2) The Chairperson of the nomination and remuneration committee shall be an independent director:</p> <p>Provided that the chairperson of the listed entity, whether executive or non-executive, may be appointed as a member of the nomination and remuneration committee and shall not chair such committee.</p> <p>The quorum for a meeting of the nomination and remuneration committee shall be either two members or one third of the members of the committee, whichever is greater, including at least one independent director in attendance. The nomination and</p>
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	<p>remuneration committee shall meet at least once in a year.(Notified on 9<sup>th</sup> May, 2018 effective from April 1, 2019)</p> <p>(3) The chairperson of the nomination and remuneration committee may be present at the annual general meeting, to answer the shareholders' queries; however, it shall be up to the chairperson to decide who shall answer the queries.</p> <p>(3A) The nominations and remunerations Committee shall meet at least once in a year (notified 9th May 2018, effective from April 1, 2019).</p> <p>(4) The role of the nomination and remuneration committee shall be as specified as in Part D of the Schedule II.</p>
<p><b>Companies Act, 2013</b></p>	<p><b>Section 178</b></p> <p>(1) The Board of Directors of every listed company and such other class or classes of companies, as may be prescribed shall constitute the nomination and remuneration committee consisting of three or more non-executive directors out of which not less than one-half shall be independent directors:</p> <p>Provided that the chairperson of the company (whether executive or non-executive) may be appointed as a member of the nomination and remuneration committee but shall not chair such Committee.</p> <p>(2) The nomination and 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 carry out evaluation of every director's performance.</p> <p>(3) The nomination and 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, key managerial personnel and other employees.</p> <p>(4) The nomination and remuneration committee shall, while formulating the policy under sub-section (3) ensure that –</p> <p>(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;</p> <p>(b) relationship of remuneration to performance is clear and meets appropriate performance benchmarks; and</p> <p>(c) remuneration to directors, key managerial personnel 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:</p> <p>Provided that such policy shall be disclosed in the Board's report.</p>
<p><b>Comments</b></p>	<p>1. The regulation prescribes that the chairperson of the committee shall be an Independent Director.</p> <p>2. The regulation requires all the members of the committee to be non-executive directors.</p> <p>3. The regulation prescribes that the chairperson of committee may be present at the</p>

	<p>annual General Meeting.</p> <p>4. The regulation prescribes the following key additions to the role of the committee :</p> <ul style="list-style-type: none"> <li>• formulation of criteria for evolution of performance of Independent director and the Board of Director</li> <li>• devising a policy on diversity of Board of Directors</li> <li>• To extent or continue the terms of appointment of Independent Director</li> </ul>
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### THE STAKEHOLDERS RELATIONSHIP COMMITTEE

Section 178(5) of the Companies Act, 2013 provides for constitution of the stakeholders relationship committee.

The Board of a company that has more than one thousand shareholders, debenture-holders, deposit-holders and any other security holders at any time during a financial year is required to 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.

The stakeholders relationship committee shall consider and resolve the grievances of security holders of the company. The Committee shall consider and resolve the grievances of the security holders of the listed entity including complaints related to transfer of shares, non-receipt of annual report and non-receipt of declared dividends.

The chairperson of each of the committees constituted under this section or, in his absence, any other member of the committee authorised by him in this behalf shall attend the general meetings of the company.

The role of the committee shall *inter-alia* include the following:

1. Resolving the grievances of the security holders of the listed entity including complaints related to transfer/transmission of shares, non-receipt of annual report, non-receipt of declared dividends, issue of new/duplicate certificates, general meetings etc.
2. Review of measures taken for effective exercise of voting rights by shareholders.
3. Review of adherence to the service standards adopted by the listed entity in respect of various services being rendered by the Registrar & Share Transfer Agent.
4. Review of the various measures and initiatives taken by the listed entity for reducing the quantum of unclaimed dividends and ensuring timely receipt of dividend warrants/annual reports/statutory notices by the shareholders of the company. (Notified on 9<sup>th</sup> May, 2018 effective from April 1, 2019)

### Comparison table of Stakeholders and Relationship Committee under Companies act 2013 and SEBI (LODR) Regulations, 2015

<b>SEBI (LODR) Regulations, 2015</b>	<b>Regulation 20</b>
	<p>(1) The listed entity shall constitute a Stakeholders Relationship Committee to specifically look into various aspects of interests of shareholders, debenture holders and other security holders.</p> <p>(2) The chairperson of this committee shall be a non-executive director.</p>

	<p>(2A) At least three directors, with at least one being an independent director, shall be members of the Committee.</p> <p>(3) The Chairperson of the Stakeholders Relationship Committee shall be present at the annual general meetings to answer queries of the security holders.</p> <p>(3A) The stakeholders relationship committee shall meet at least once in a year. (Notified on 9th May, 2018 effective from April 1, 2019)</p> <p>(4) The role of the Stakeholders Relationship Committee is discussed above.</p>
<b>Companies Act, 2013</b>	<b>Section 178</b>
	<p>(5) The Board of Directors of a company which consists of more than one thousand 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.</p> <p>(6) The Stakeholders Relationship Committee shall consider and resolve the grievances of security holders of the company</p>
<b>Comments</b>	<p>The Regulations specifically prescribe role of the committee in Schedule II, Part D of the Regulations, that the Committee will also resolve the complaint related to transfer of Shares, non receipt of Annual report and non receipt of declared dividends.</p> <p>Further a listed entity even if having less than 1000 debenture holders/security holders is required to constitute a stakeholder relationship committee, though for such a company, if it were not listed then it is not required under Companies Act, 2013.</p>

### Penalty for Contravention of Section 177 and 178

Section 178(8) provides that the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees for contravention of provisions of Section 177 and 178. Every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine not less than rupees twenty five thousand but which may extend to one lakh rupees or with both.

However, the non inability to resolve or consider any grievance by the Stakeholders Relationship Committee in good faith shall not constitute a contravention of this section.

Schedule IV under Section 149(7) of the Act contains the Code for Independent Directors. Under Sl. No. II (5) of the Code, Independent Directors are mandated to safeguard the interest of all stakeholders, especially the Minority Shareholders and balance the conflicting interests of the stakeholders.

The requirement for a Stakeholders Relationship Committee is an interesting one. Relationships with stakeholders can be critical, and balancing the contending interests of different stakeholder groups and building mutually beneficial relationships with stakeholders are hallmarks of the effective board.

Again minimum compliance would be to establish a committee and hope it does not get in the way or prove a distraction. More benefit might be derived from using such a provision as a catalyst to identify and/or

reassess the nature, interests and priorities of different stakeholder groups, the current state of relationships with them and how these might be improved.

Direction should be seen as a separate but complementary activity to management, rather than as a route to elevated status and higher earnings. Directors need to look beyond functional considerations and work for the best interests of the company and its stakeholders. Their perspective should be strategic rather than departmental.

Directors must reconcile the concerns of various stakeholder groups, and respect views of colleagues who may have a different perspective. Non-financial considerations need to be taken into account.

**Risk Management Committee under SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015**

As per regulations 21 of the SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015, the board of directors of the top 100 (500 notified 9th May, 2018, effective from 1st April, 2019) listed entities, determined on the basis of market capitalisation, as at the end of the immediate previous financial year shall constitute a Risk Management Committee. The board of directors shall constitute a Risk Management Committee, the majority of members of Risk Management Committee shall consist of members of the board of directors. The Chairperson of the Risk management committee shall be a member of the board of directors and senior executives of the listed entity may be members of the committee. The Committee shall meet at least once in a year.

The majority of members of Risk Management Committee shall consist of members of the board of directors.

The Chairperson of the Risk management committee shall be a member of the board of directors and senior executives of the listed entity may be members of the committee.

The board of directors shall define the role and responsibility of the Risk Management Committee and may delegate monitoring and reviewing of the risk management plan to the committee and such other functions as it may deem fit. (Such functions shall specifically cover cyber security)(Notified 9th May, 2018, effective from 1st April, 2019)

**Comparison table of Risk Management Committee under Companies act 2013 and SEBI (LODR) Regulations, 2015**

SEBI (LODR) Regulations, 2015	Regulation 21
	(1) The board of directors shall constitute a Risk Management Committee (2) The majority of members of Risk Management Committee shall consist of members of the board of directors. (3) The Chairperson of the Risk management committee shall be a member of the board of directors and senior executives of the listed entity may be members of the committee. (4) The board of directors shall define the role and responsibility of the Risk Management Committee and may delegate monitoring and reviewing of the risk management plan to the committee and such other functions as it may deem fit. Notified 9th May, 2018, effective from 1st April, 2019) (5) The provisions of this regulation shall be applicable to top 100 listed entities, determined on the basis of market capitalization, as at the end of the immediate previous financial year

<b>Companies Act, 2013</b>	<b>Section 134(3)(n)</b>
	Companies Act, 2013 provides that a disclosure to be made in the board report with a statement indicating development and implementation of a risk management policy for the company
<b>Comments</b>	There is no requirement for constitution of risk management committee under the Companies Act 2013.

**ROUND UP:**

	<b>Listed Company</b>	<b>Public Company</b>			<b>Company</b>
		<b>Paid up capital</b>	<b>Turnover</b>	<b>Loans or borrowings</b>	<b>No. of Shareholders or debenture holders</b>
		<b>10 Crore or more</b>	<b>100 crore or more</b>	<b>Exceeding 50 crore</b>	<b>1000 or more</b>
Nomination and Remuneration Committee (3 or more Non-Executive Directors with majority Independent)	Yes	Yes	Yes	Yes	No
Audit Committee (Minimum of 3 directors with majority Independent)	Yes	Yes	Yes	Yes	No
Stakeholders Relationship Committee (Chairman shall be Non-executive Director)	Yes	No	No	No	Yes

**Corporate Social Responsibility Committee**

India has one of the richest traditions of CSR. Much has been done in recent years to make Indian entrepreneurs aware of social responsibility as an important segment of their business activity but CSR in India has yet to receive widespread recognition. If this goal has to be realised then the CSR approach of corporates has to be in line with their attitudes towards mainstream business- companies setting clear objectives, undertaking potential investments, measuring and reporting performance publicly.

One of the key changes in the Companies Act, 2013 is the introduction of a Corporate Social Responsibility section making India the first country to mandate CSR through a statutory provision. While CSR is not mandatory for companies, the rules are in line with the 'Comply or Explain' principle with penalties applicable only if an explanation is not offered. The provisions of the Section 135 of the Act may be summarized as under:

1. The Section applies to the following classes of companies during immediately preceding financial year:
  - (i) Companies having Net Worth of rupees five hundred crore or more;

- (ii) Companies having turnover of rupees one thousand crore or more;
  - (iii) Companies having Net Profit of rupees five crore or more
2. The companies specified above shall constitute a Corporate Social Responsibility Committee (CSR Committee) of the Board.

A Company which ceases to be a company covered under the above three threshold requirement to constitute CSR Committee for three consecutive financial years shall not be required to constitute CSR Committee till such time it meets the threshold as specified above. [Rule 3(2)]

3. The CSR Committee shall consist of three or more Directors, out of which at least one Director shall be an Independent Director.

Where a company is not required to appoint an independent director under sub-section (4) of section 149, it shall have in its Corporate Social Responsibility Committee two or more directors.

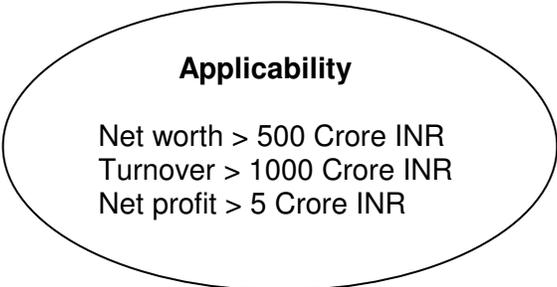
4. After taking into account the recommendations of the CSR Committee, the Board shall approve the CSR Policy for the company.
5. The contents of the Policy shall be disclosed in the Board's report.
6. It shall also be placed on the Company's website, if any, in a manner to be prescribed by the Central Government.
7. The Board shall ensure that the activities as are included in the CSR Policy (from the activities as specified in Schedule VII) are undertaken by the Company.

The following additional features of the Section are relevant:

1. While spending the amount earmarked for CSR activities, the company shall give preference to the local area and areas around it where it operates;
2. If the Company fails to spend the amount, the Board shall specify the reasons for not spending the amount in the Board's Report.
3. The eligible companies are required to spend in every financial year, at least two per cent of the Average Net Profits of the Company made during the three immediately preceding financial years in pursuance of its CSR Policy. For this purpose, "Average Net Profit" shall be calculated in accordance with the provisions of Section 198 of the Companies Act, 2013.

( Note: CSR Committee has been dealt in detail in chapter "Corporate Social Responsibility")

### **Corporate Social Responsibility Committee**



#### **Applicability**

Net worth > 500 Crore INR  
Turnover > 1000 Crore INR  
Net profit > 5 Crore INR

Role of the Board	Role of Corporate Social Responsibility Committee
Form a CSR Committee	Three or more directors with at least one independent director
Approve the CSR policy	Formulate and recommend a CSR policy to the board
Ensure implementation of the Activities under CSR	Recommend activities and the amount of expenditure to be incurred
Ensure 2% spend	Monitor the CSR policy from time to time
Disclose reasons for not the amount (if applicable)	

### Other Board Committees

In addition to the Committees of the Board mandated by the Companies Act, 2013 viz, Audit Committee, Nomination and Remuneration Committee, Stakeholders Relationship Committee and the CSR Committee, Board of Directors may also constitute other Committees to oversee a specific objective or project. The nomenclature, composition and role of such Committees will vary, depending upon the specific objectives of the company.

A few examples of such Committees prevalent in the corporate sector in India and abroad are given below:

1. Corporate Governance Committee
2. Science, Technology & Sustainability Committee
3. Regulatory, Compliance & Government Affairs Committee
4. Investment Committee
5. Ethics Committee.

### Composition of board and its Committees as per SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015

Particulars	Board	Audit Committee	Nomination and Remuneration Committee	Stakeholders Committee	Risk Management Committee
<i>Applicability</i>	All Listed Entities	All Listed Entities	All Listed Entities	All Listed Entities	Top 100 Listed Entities
<i>Min. No. Of Members</i>	Atleast 3	Atleast 3	Atleast 3	Atleast 3	Atleast 3
<i>Kind of Directors (Executive [E] or Non</i>	Both [E & NE]	Both[E & NE]	3 or more NE	Both [E & NE]	Both [E & NE] + Senior executives

<i>Executive (NE)</i>					
<i>No. of Independent Directors Required</i>	If Chairperson. is executive or non-executive but related to promoter then atleast 50% of Members shall be Independent otherwise atleast 1/3rd of Directors shall be Independent.	Atleast 2/3rd of Members shall be Independent Directors.	Atleast 50% of Members shall be Independent Directors.	No such criteria and condition is essential.	No such criteria and condition is essential
<i>Chairperson</i>	Chairperson may be Independent and may not be Independent	Chairperson shall be independent	Chairperson Shall be Independent and also that Chairperson of Company shall not chair the Committee.	Chairperson shall be a non-executive director and may or may not be Independent Director.	Chairperson shall be a member of the board of directors and senior executives of the listed entity may be members of the committee
<i>Presence at Annual General Meeting (AGM)</i>	All directors shall be present at AGM, if any Director is absent the Chairman shall explain the absence of directors.	Chairperson of AGM shall be present at AGM.	Chairperson may be present at the Annual General meeting	Chairperson of AGM shall be present at AGM.	No Such criteria or essential condition.
<i>Other members</i>				The Board shall decide composition of other members of the Committee	The Board shall decide composition of other members of the Committee But majority shall be members of the Board

### LESSON ROUND-UP

- Every Listed Company and such other company as may be prescribed shall form Audit Committee comprised of minimum 3 directors with majority of the Independent Directors and majority of members of committee shall be person with ability to read and understand financial statement
- Vigil mechanism to be established in the prescribed manner by every listed company or such class or classes of companies, as may be prescribed.
- Every listed company and prescribed class or classes of companies, shall constitute the Nomination and Remuneration Committee consisting of three or more non-executive directors out of which not less than one half shall be independent directors
- Applicability of Corporate Social Responsibility Net worth > 500 Crore INR or Turnover > 1000 Crore INR or Net profit > 5 Crore INR.

### GLOSSARY

Dormant company

Where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed, for obtaining the status of a dormant company.(Sec 455 of Companies Act, 2013)

Vigil mechanism

A Vigil Mechanism or a Whistle Blower Policy provides a channel to the employees and Directors to report to the management concerns about unethical behavior, actual or suspected fraud.

### SELF-TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

1. Which Companies are required to Constitute Audit Committee, Nomination Remuneration Committee and Stakeholder Relationship Committee?
2. Explain the provisions relating to constitution of Corporate Social Responsibility Committee?
3. Explain the provisions relating to constitution of Nomination & Remuneration Committee?
4. Explain the provisions relating to constitution of Stakeholders and Relationship Committee?
5. Analyse the powers of the Board and the restrictions on Board Powers under the Act?

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# Lesson 16

## Directors

### LESSON OUTLINE

- Procedure for Obtaining DIN
- Types of Directors
- Procedure of Appointment of Each Kind of Director
- Disqualifications
- Vacation of office
- Retirement
- Removal of Directors
- Duties of Directors
- Rights of Directors
- Loans to Directors
- Disclosure of Interest
- Lesson Round up
- Self-Test Questions

### LEARNING OBJECTIVES

Appointment of a Director is not only a crucial administrative requirement, but is also a procedural requirement that has to be fulfilled by every company. Under the Companies Act, 2013 only an individual can be appointed as a Director; a corporate, association, firm or other body with artificial legal personality cannot be appointed as a Director.

Directors of a company are individuals that are elected as, or elected to act as, representatives of the stockholders to establish corporate management related policies and to make decisions on major company issues. The success of the company depends, to a very large extent, upon the competence and integrity of its directors.

This chapter explains the procedural and legal requirements for the appointment of directors, removal, and vacation of directors. This chapter shall enable you to understand the legal technicalities involved.

## INTRODUCTION

The Companies Act 2013 does not contain an exhaustive definition of the term “director”. Section 2(34) of the Act prescribed that “director” means a director appointed to the Board of a company.

Section 2(10) of the Companies Act, 2013 defined that “Board of Directors” or “Board”, in relation to a company, means the collective body of the directors of the company.

The term ‘Board of Directors’ means a body duly constituted to direct, control and supervise the affairs of a company.

As per Section 149 of the Companies Act, 2013, the Board of Directors of every company shall consist of individual only. Thus, no body corporate, association or firm shall be appointed as director.

Again Section 166 (6) of Companies Act, 2013, prohibits assignment of office of director to any other person. Any assignment of office made by a director shall be void.

## DIRECTOR IDENTIFICATION NUMBER (DIN)

As per Section 153 of the Act, every individual intending to be appointed as director of a company shall make an application electronically in Form DIR-3 for allotment of Director Identification Number to the Central Government along with the prescribed fees. Further, DINs to the proposed first Directors in respect of new companies would be mandatorily required to be applied for in SPICe forms (subject to a ceiling of 3 new DINs) only.

Within one month of application the Central government shall allot a Director Identification Number (DIN) to the applicant. A person appointed as a director shall on or before the appointment give his consent to hold the office of director in physical form DIR-2 i.e. consent to act as a director of a company. Company shall file Form DIR-12 (particulars of appointment of directors and KMP along with the form DIR-2 as an attachment within 30 days of the appointment of a director, necessary fee. In case of any appointment of director by Central Government or State Government consent of director is not required.

Companies Amendment Act, 2017 provides that the Central Government may prescribe any identification number which shall be treated as Director Identification Number for the purposes of this Act and in case any individual holds or acquires such identification number, the requirement of this section shall not apply or apply in such manner as may be prescribed.

No person shall continue or be appointed as director without obtaining DIN. Section 153 read with the Companies (Appointment and Qualification of Directors) Rules, 2014, provides for the procedure for making application for allotment of DIN.

## Procedure for application for allotment of DIN - Section 153 & Rule 9

- (1) Every individual, who is to be appointed as director of a company shall make an application electronically in Form DIR-3 (Application for allotment of Director Identification Number) to the Central Government for the allotment of a Director Identification Number (DIN) along with such fees as may be prescribed.
- (2) MCA 21 portal facilitates submission of application for the allotment of DIN.
- (3) (a) The applicant shall download Form DIR-3 from the portal, fill in the required particulars and attaching photograph; proof of identity; proof of residence; board resolution proposing his appointment as director in an existing company and specimen signature duly verified and sign

the form digitally.

- (b) Form DIR-3 shall be signed and submitted electronically by the applicant using his or her own Digital Signature Certificate and shall be verified digitally by - :
  - (i) a chartered accountant in practice or a company secretary in practice or a cost accountant in practice; or
  - (ii) a company secretary in full time employment of the company or by the managing director or by director of the company in which the applicant is to be appointed a director;
- (4) Rule 9(4) provides that in case the name of a person does not have a last name, then his or her father's or grandfather's surname shall be mentioned in the last name along with declaration in Form-DIR-3A. This declaration will be submitted along with Form DIN-3.

### **Procedure for Allotment of DIN- Section 154 and Rule 10**

The Central Government shall, within one month from the receipt of the application under section 153, allot a Director Identification Number to an applicant in such manner as mentioned below:

- (1) On the submission of the Form DIR-3 on the portal and payment of the requisite amount of fees through online mode an application number shall be generated by the system automatically.
- (2) After generation of the application number, the Central Government shall process the application received for allotment of DIN under Sub-rule (2) of Rule 9 decide on the approval or rejection thereof and communicate the same to the applicant along with DIN allotted. In case of approval by way of a letter by post or electronically or in any other mode within a period of one month from the receipt of such application.
- (3) If the Central Government, on examination, finds such application to be defective or incomplete in any respect, it shall give intimation of such defect or incompleteness, by placing it on the website and by email to the applicant who has filed such application, directing the applicant to rectify such defects or incompleteness by resubmitting the application within a period of fifteen days of such placing on the website and email.

The Central Government may on application:

- (a) reject the application and direct the applicant to file fresh application with complete and correct information, where the defect has been rectified partially or the information given is still found to be defective;
- (b) treat and label such application as invalid in the electronic record in case the defects are not removed within the given time; and
- (c) inform the applicant either by way of letter by post or electronically or in any other mode.
- (4) In case of rejection or invalidation of application, the fee so paid with the application shall neither be refunded nor adjusted with any other application.
- (5) All Director Identification Numbers allotted to individual(s) by the Central Government before the commencement of Companies (Appointment and Qualification of Directors) Rules, 2014 shall be deemed to have been allotted to them under these rules.
- (6) The Director Identification Number so allotted under these rules is valid for the life-time of the applicant and shall not be allotted to any other person.
- (7) The intimation by the company of Director Identification Number of its directors under section 157

of the Act shall be furnished in Form DIR-3C (New Form) within fifteen days of receipt of intimation under section 156 (Sub rule 10A).

#### **Intimation of changes in particulars of Director [Rule 12]**

- (1) Every individual having DIN in the event of any change in his particulars as stated in Form DIR-3, intimate such change(s) to the Central Government within a period of 30 days of such change(s) in Form DIR-6 (Intimation of change in particulars of Director to be given to the Central Government). The applicant shall fill in the relevant changes in DIR-6, verify the form and attach duly scanned copy of the proof of the changed particulars and submit electronically. Form requires pre-certification by the professional CA/CS/CMA in practice.
- (2) The changes shall be incorporated in the electronic database after due verification from the enclosed proofs and confirm the applicant by post/email/any other mode.
- (3) The DIN cell of the MCA shall also intimate the change(s) in the particulars of the director submitted to it in Form DIR-6 to the concerned Registrar(s) under whose jurisdiction the registered office of the company(s) in which such individual is a director is situated.
- (4) The concerned individual shall also intimate the change(s) in his particulars to the company or companies in which he is a director within fifteen days of such change.

#### **Cancellation/Surrender/Deactivation of DIN [ Rule 11]**

The Competent Authority (Central Government/RD (North), Noida/ Authorised Officer by the RD) may, upon being satisfied on verification of particulars or documentary proof attached with the application along with specified fee received from any person, cancel or deactivate the DIN in case –

- (a) the DIN is found to be duplicated in respect of the same person provided the data related to both the DIN shall be merged with the validly retained number;
- (b) the DIN was obtained in a wrongful manner or by fraudulent means;
- (c) of the death of the concerned individual;
- (d) the concerned individual has been declared as a lunatic or of unsound mind by a competent Court;
- (e) if the concerned individual has been adjudicated an insolvent.

Provided that before cancellation or deactivation of DIN pursuant to clause (b), an opportunity of being heard shall be given to the concerned individual;

- (f) on an application made in Form DIR-5 by the DIN holder to surrender his or her DIN along with declaration that he has never been appointed as director in any company and the said DIN has never been used for filing of any document with any authority, the Central Government may deactivate such DIN but after verification of e-records.

#### **General Provisions regarding DIN**

##### **Prohibition to obtain more than one DIN:**

According to Section 155, No individual shall apply for/obtain/ possess another Director Identification Number who has already been allotted a Director Identification Number under section 154.

**Director to intimate DIN:**

Section 156 stipulated that every existing director shall intimate his DIN to the company or all companies wherein he is a director within one month of the receipt of DIN from the Central Government.

**Company to inform DIN to Registrar:**

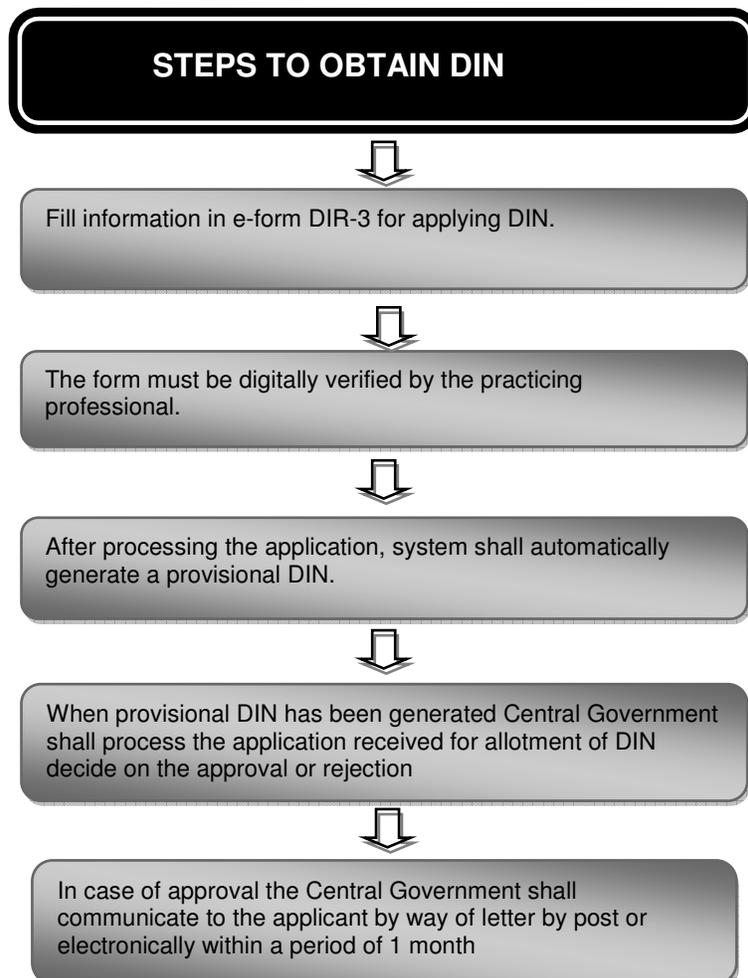
Every company shall, within fifteen days of the receipt of intimation of DIN from director, furnish the DIN to the Registrar/authorised office by the Central Government in e-form DIR-3C. The e-form is to be digitally signed by Company Secretary of the company or Company Secretary in Practice.

If a company fails to furnish Director Identification Number under section 157 (1), with additional fee, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

**Obligation to obtain DIN:**

Section 158 specified that every person or company shall mention the DIN in return, information or particulars as required to be furnished under this Act, in case such return etc. relate to the director or contain any reference of any director.

Steps to obtain DIN





If Central Government, on examination, finds any defects or incompleteness then it may intimate such defects by placing it on website and by e-mail to the applicant.



Resubmit the application after rectify the defects within 15 days

## TYPES OF DIRECTORS

**A director so appointed may either be executive director or non-executive director.**

An Executive Director can be either a Whole-time Director of the company (i.e., one who devotes his whole time of working hours to the company and has a significant personal interest in the company as his source of income), or a Managing Director (i.e., one who is employed by the company as such and has substantial powers of management over the affairs of the company subject to the superintendence, direction and control of the Board). They are generally responsible for overseeing the administration, programs and strategic plan of the organization. Other key duties include fund raising, marketing, and community out reach. The position reports directly to the Board of Directors.

**In contrast, a non-executive Director is a Director who is neither a Whole-time Director nor a Managing Director.**

A director to the Board may be appointed as

- First Director
- Resident Director
- Women Director
- Independent Director
- Alternate Director
- Additional Director
- Small Shareholder Director
- Nominee Director
- Casual Vacancy

### First Director

Section 152 of the Act provides for the appointment of first directors, accordingly, where there is no provision made in Articles of Association of the company for appointment of first directors then the subscribers to the memorandum who are individuals shall be deemed to be the first directors of the company until the directors are duly appointed.

### Resident Director

Section 149(3) provides that every company shall have at least one director who has stayed in India for a

total period of not less than one hundred and eighty-two days during the financial year:

Provided that in case of a newly incorporated company the requirement under this sub-section shall apply proportionately at the end of the financial year in which it is incorporated.

### Women Director

Second proviso to Section 149(1) read Rule 3 of Companies (Appointment and Qualification of Directors) Rules, 2014 following class of companies must have at least one Women Director.

All Listed Companies	
Public companies	with paid up capital of ₹100 crore or more or with turnover of ₹300 crore or more

Additionally for listed entities SEBI vide recent notification provides that the Board of directors of the top 500 listed entities shall have at least one independent woman director by April 1, 2019 and the Board of directors of the top 1000 listed entities shall have at least one independent woman director by April 1, 2020. The top 500 and 1000 entities shall be determined on the basis of market capitalisation, as at the end of the immediate previous financial year.

### Director elected by Small Shareholders [Section 151]

According to section 151 of the Act every listed company may have one director elected by such small shareholders in such manner and on such terms and conditions as may be prescribed.

“Small shareholder” means a shareholder holding shares of nominal value of not more than twenty thousand rupees or such other sum as may be prescribed.

Here, the ‘nominal value’ of shares is relevant. It does not matter how much is the ‘paid up value’ or ‘market value’ of shares. However, a small shareholder may be a holder of equity shares or preference shares or both.

For example: Mr. A holds 5000 equity shares of ₹10 each (₹5 paid up) in XYZ Ltd. However, Mr. A cannot be considered as small shareholder since the nominal value of shares held by him (i.e. ₹50,000) exceeds ₹20,000.

### Terms & Conditions for Small Shareholders’ Director

Rule 7 of Companies (Appointment and Qualification of Directors) Rules, 2014 laid down the following terms and conditions for appointment of small shareholder’s director, which are as under:

#### (i) Election of small shareholders’ director:

A listed company, may upon notice of not less than

- (a) One thousand small shareholders; or
- (b) one-tenth of the total number of such shareholders,

whichever is lower; have a small shareholder’s director elected by the small shareholder.

A ‘Small Shareholders’ Director’ may be elected voluntarily by any listed company. Thus, a listed company, may, on its own, act to appoint a Small Shareholders’ Director. In such a case, no notice from small shareholder(s) is required.

***(ii) Notice of intention to propose a candidate:***

The small shareholders intending to propose a person as a candidate for the post of small shareholder's director shall leave a signed notice of their intention with the company at least 14 days before the meeting specifying their details and proposed director's details. The details include name, address, shares held and folio number etc. If the proposer does not hold any shares in the company, the details of shares held and folio number need not be specified in the notice.

**Shareholders eligible to give notice:**

The notice shall be given by at least-

- (a) 1000 small shareholders; or
- (b) 1/10th of the total number of small shareholders, whichever ever is lower.

***(iii) Statement by the proposed small shareholders' director:***

The notice shall be accompanied by a statement signed by the proposed director for the post of small shareholders' director stating

- (a) his Director Identification Number;
- (b) that he is not disqualified to become a director under the Act; and
- (c) his consent to act as a director of the company.

***(iv) Small shareholders' director to be an independent director:***

Small shareholders' director shall be considered as an independent director, if-

- (a) he is eligible for appointment as an independent director as per sub-section (6) of section 149; and
- (b) he gives a declaration of his independence as per sub-section (7) of section 149.

***(v) Tenure of office and no retirement by rotation:***

The tenure of small shareholders' director shall not exceed a period of 3 consecutive years and he shall not be liable to retire by rotation. Further he shall not be eligible for re-appointment after the expiry of his tenure.

***(vi) Grounds of disqualification:***

Disqualifications of a small shareholders' director are the same as that of any other director specified under section 164 of the Act.

***(vii) Grounds of vacation of office: A Small shareholders' director shall vacate the office if -***

- (a) he ceases to be a small shareholder, on and from the date of cessation;
- (b) he incurs any of the disqualifications specified in section 164;
- (c) the office of the director becomes vacant in pursuance of section 167;
- (d) he ceases to meet the criteria of independence as provided section 149 (6).

***(viii) Number of small shareholders' directorship:***

A person shall not hold the office of small shareholders' director in more than two companies. If second company is in competitive business or is in conflict with business of the first company, he shall not be appointed in second company.

***(ix) No association with the company for next 3 years:***

He shall directly or indirectly not be appointed or associated in any other capacity with the company either

directly or indirectly for a period of 3 years from the date of cessation as a small shareholder's director.

**Important points to note:**

- a) A small shareholders' director may be removed by passing an ordinary resolution in the general meeting in accordance with the provisions of section 169 of the Act. At the time of voting on such resolution, every equity shareholders shall have a right to vote irrespective of the fact as to whether he is a small shareholder or not.
- b) A small shareholders' director shall be included in the 'total number of directors' as prescribed under section 152 (6) of the Act.

### Independent Directors

Section 149(4) read with Rule 4 of Companies (Appointment and Qualification of Directors) Rules, 2014 provides following companies to have specified number of independent directors.

All listed public companies	At least 1/3rd of total number of independent Directors
Other public companies with paid up capital of ₹10 crore or more or with turnover of ₹100 crore or more or with outstanding loans, debentures and deposits of ₹50 crore or more	At least 2 independent Directors

However, the following classes of unlisted public company shall not be covered under sub-rule as above

- (a) a joint venture;
- (b) a wholly owned subsidiary; and
- (c) a dormant company as defined under section 455 of the Act.

In case a company covered under this rule is required appoint higher number of independents directors due to composition of its audit committee and then they shall appoint such higher number of independent directors.

Further if there is any intermittent vacancy of an independent director then it shall be filled up by the board of directors within 3 months from the date of such vacancy or not later than immediate next board meeting, whichever is later.

Once the company covered under above sub-rule (i) to (iii) of Rule 4, ceases to fulfil any of three conditions for three consecutive years then it shall not be required to comply these provisions until such time as it meets any of such conditions.

### Definition of an Independent Director – Section 149 (6)

An independent director means a director other than a managing director or a whole-time director or a nominee director who does not have any material or pecuniary relationship with the company/ directors. Basically an independent director is a non-executive director. Section 149(6) of the Act prescribes the criteria

for independent directors which are as follows:

- (a) Who in the opinion of the Board (Ministry or Department of the Central Government which is administratively in charge of the company, in case of Government company), or as the case may be, the State Government, is a person of integrity and possesses relevant industrial expertise and experience;
- (b) Such individual shall not be a promoter or related to promoter of the company or its holding, subsidiary or associate company;
- (c) Such individuals must not have any material or pecuniary relationship during the two immediately preceding financial years or during the current financial year with the company or its promoters/directors/holding/ subsidiary/ associate company; (this does not apply to government company);
- (d) The relatives of such person should not have had any pecuniary relationship with the company or its subsidiaries, amounting to 2% or more of its gross turnover or total income or Rs. 50 lacs or such higher amount as may be prescribed, whichever is less, during the two immediately preceding financial years or in the current financial year;
- (e) He must not either directly or any of his relatives
  - (i) hold or has held the position of a key managerial personnel or is or has been employee of the company or its holding, subsidiary or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed.
  - (ii) is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of—
    - (A) firm of auditors or company secretaries in practice or cost auditors of the company or its holding, subsidiary or associate company; or
    - (B) any legal or a consulting firm that has or had any transaction with the company, its holding, subsidiary or associate company amounting to ten per cent. or more of the gross turnover of such firm;
  - (iii) holds together with his relatives two per cent or more of the total voting power of the company; or
  - (iv) is a Chief Executive or director, by whatever name called, of any non-profit organisation that receives 25% or more of its receipts from the company, any of its promoters, directors or its holding, subsidiary or associate company or that holds 2% or more of the total voting power of the company, then also he is not eligible for office of independent director; or
- (f) who possesses such other qualifications as prescribed in Rule 5 as an independent director shall possess appropriate skills, experience and knowledge in one or more fields of finance, law, management, sales, marketing, administration, research, corporate governance, technical operations or other disciplines related to the company's business.
  1. None of the relatives of an independent director, for the purposes of sub-clauses (ii) and (iii) of clause (d) of sub-section (6) of section 149:
    - (i) is indebted to the company, its holding, subsidiary or associate company or their promoters, or directors ; or
    - (ii) has given a guarantee or provided any security in connection with the indebtedness of any third

person to the company, its holding, subsidiary or associate company or their promoters, or directors of such holding company, for an amount of fifty lakhs rupees, at any time during the two immediately preceding financial years or during the current financial year.”

As per sub section 4 of Section 149 of the Companies Act 2013, every listed public company is mandatorily required to have at least one-third of the total number of directors as independent directors.

Unlisted public companies must appoint at least two independent directors in the following circumstances:

- i. if the paid up share capital exceeds ₹10 crores;
- ii. if the turnover exceeds ₹100 crores;
- iii. if the aggregate of all the outstanding loans, debentures and deposits exceeds ₹ 50 crores.

### **Declaration by an Independent Director- Section 149 (7)**

Section 149 (7) of the Act, prescribed that every independent director shall give a declaration that he meets the criteria of independence when:

- (a) he attends the first meeting of the Board as a director;
- (b) thereafter at the first meeting of the Board in every financial year and
- (c) whenever there is any change in the circumstances which may affect his status as an independent director.

Additionally for listed entities SEBI vide recent notification provides that every independent director shall, at the first meeting of the board in which he participates as a director and thereafter at the first meeting of the board in every financial year or whenever there is any change in the circumstances which may affect his status as an independent director, submit a declaration that he meets the criteria of independence and that he is not aware of any circumstance or situation, which exist or may be reasonably anticipated, that could impair or impact his ability to discharge his duties with an objective independent judgment and without any external influence.

The board of directors of the listed entity shall take on record the declaration and confirmation submitted by the independent director after undertaking due assessment of the veracity of the same. (Notified on 9th May, 2018 effective from April 1, 2019)

With effect from October 1, 2018, the top 500 listed entities by market capitalization calculated as on March 31 of the preceding financial year, shall undertake Directors and Officers insurance ('D and O insurance') for all their independent directors of such quantum and for such risks as may be determined by its board of directors.”

Further “nominee director” means a director nominated by any financial institution in pursuance of the provisions of any law for the time being in force, or of any agreement, or appointed by any Government or any other person to represent its interests.

### **Remuneration of an Independent Director- Section 149(9)**

As per section 149(9) of the Act an independent director shall not be entitled to any stock option. He may receive remuneration by way of sitting fee, reimbursement of expenses incurred for participation in the Board and other committee meetings and profit related commission as may be approved by the members as provided under section 197(5) of the Act.

### Term of an Independent Director- Section 149(10)

Subject to the provisions of Section 152, an independent director can be appointed for a term of up to five consecutive years on the Board. However, in case of his reappointment for further five year then special resolution passed in general meeting and disclosure of such appointment is made in the Board's report shall be required. {Section 149 (10)} .

Further independent director can be considered for re-appointment after expiration of three years of ceasing to become an independent director but he must not be appointed/associated with the company directly or indirectly in any other capacity during the said period of three years. Any tenure of an independent director on the date of commencement of this Act is not considered for the above term. {Section 149 (11)}.

It has been clarified that as such while appointment of an ID for a term of less than 5 years would be permissible, appointment for any term (whether for 5 years or less) is to be treated as a one term under section 149(10) of the Act. Further, under section 149(11) of the Act, no person can hold office of ID for more than two consecutive term's such a person shall have to demit office after two consecutive terms, even if the total number of years of his appointment in such two consecutive terms is less than 10 years. In such a case the person completing 'consecutive terms of less than 10 years' shall be eligible for appointment only after the expiry of the requisite cooling –off period of 3 years.

The provisions of retirement of directors by rotation are not applicable on Independent director. [Section 149 (13)].

Further, in case of independent directors, the explanatory statement relating to their appointment should contain a declaration from the Board that in their opinion, the independent directors satisfy the conditions provided in the Act for such appointment. [Proviso to Section 152 (5)].

#### Requirement for Independent Director

1. Is Applicable on Listed Companies: 1/3<sup>rd</sup> of total directors be the Independent Director
2. Public companies having capital more than 10 crore: At least 2 directors as Independent Directors

**1. Appointment Term of Independent Director:** Term shall be of maximum 5 years. And term shall not be more than 2 consecutive terms. And shall be re-appointed only by Special Resolution by the company.

**2. Remuneration of Independent Director:** may receive remuneration by way of fee provided under sub-section (5) of section 197, reimbursement of expenses for participation in the Board and other meetings and profit related commission as may be approved by the members.

**3. Retirement by Rotation of Independent Director in AGM:** shall not be applicable to appointment of independent directors.

**4. Vacancy of Independent Director:** To be filled in the very next Board Meeting or within 3 months of such vacancy, whichever is later

**5. Separate Meeting of Independent Director:** The independent directors of the company shall hold at least one meeting in a year, without the attendance of non-independent directors and members of management;

<b>Presence of Independent Director in Committees</b>	
Name of the Committees	Composition
Audit committee	The Audit Committee shall consist of a minimum of three directors with independent directors forming a majority.
Nomination and Remuneration Committee	The Nomination and Remuneration Committee shall consist of three or more non-executive directors out of which not less than one-half shall be independent directors.
Corporate Social Responsibility	Corporate Social Responsibility Committee shall consist of three or more non-executive directors out of which at least one should be an independent director.

### **PAYMENT OF SITTING FEE/COMMISSION**

According to Section 149(9), the independent director is entitled to receive

- (a) sitting fee for Board/Committee meetings as may be prescribed under second proviso under Section 197(5)
- (b) reimbursement of expenses for attending the board/committee meetings (c) commission related to profits of the company subject to the provisions of Section 197 and 198 ( one percent of the net profits if there is a Managing Director or Whole-Time Director or Manager and three percent of the net profits in any other case). The net profits shall be computed in accordance with Section 198. The independent director, however, shall not be entitled to receive any “stock option”.

MCA has exempted section 8 companies vide notification dated June 05, 2015 and Specified IFSC public company vide notification dated 4th January 2017 from the provisions of section 149(4) to (11), 12(i) and (13). This means all the provisions relating to requirement of independent directors, definition of independent directors and other provisions shall not be applicable to section 8 companies.

### **Obligations with respect to independent directors as per SEBI (LODR) 2015.**

- (1) A person shall not serve as an independent director in more than seven listed entities:  
Provided that any person who is serving as a whole time director in any listed entity shall serve as an independent director in not more than three listed entities.
- (2) The maximum tenure of independent directors shall be in accordance with the Companies Act, 2013 and rules made thereunder, in this regard, from time to time.
- (3) The independent directors of the listed entity shall hold at least one meeting in a year, without the presence of non-independent directors and members of the management and all the independent directors shall strive to be present at such meeting.
- (4) The independent directors in the meeting referred in sub-regulation (3) shall, inter alia review the performance of non-independent directors and the board of directors as a whole; review the performance of the chairperson of the listed entity, taking into account the views of executive directors and non-executive directors; assess the quality, quantity and timeliness of flow of information between the management of the listed entity and the board of directors that is necessary for the board of directors to effectively and reasonably perform their duties.
- (5) An independent director shall be held liable, only in respect of such acts of omission or commission

by the listed entity which had occurred with his knowledge, attributable through processes of board of directors, and with his consent or connivance or where he had not acted diligently with respect to the provisions contained in these regulations.

- (6) An independent director who resigns or is removed from the board of directors of the listed entity shall be replaced by a new independent director by listed entity at the earliest but not later than the immediate next meeting of the board of directors or three months from the date of such vacancy, whichever is later. Where the listed entity fulfils the requirement of independent directors in its board of directors without filling the vacancy created by such resignation or removal, the requirement of replacement by a new independent director shall not apply.
- (7) The listed entity shall familiarise the independent directors through various programmes about the listed entity, including the following:
  - a. nature of the industry in which the listed entity operates;
  - b. business model of the listed entity;
  - c. roles, rights, responsibilities of independent directors; and
  - d. any other relevant information.

## **ROLE OF INDEPENDENT DIRECTOR**

Independent directors are required because they perform the following important role:

- (i) Balance the often conflicting interests of the stakeholders.
- (ii) Facilitate withstanding and countering pressures from owners.
- (iii) Fulfill a useful role in succession planning.
- (iv) Act as a coach, mentor and sounding Board for their full time colleagues.
- (v) Provide independent judgment and wider perspectives.

As per Schedule IV of the Companies Act, 2013, the Independent Director shall –

- 1) uphold ethical standards of integrity and probity;
- 2) act objectively and constructively while exercising his duties;
- 3) exercise his responsibilities in a bonafide manner in the interest of the company;
- 4) devote sufficient time and attention to his professional obligations for informed and balanced decision making;
- 5) Not allow any extraneous considerations that will vitiate his exercise of objective independent judgment in the paramount interest of the company as a whole, while concurring in or dissenting from the collective judgment of the Board in its decision making;
- 6) Avoid abusing his position to the detriment of the company or its shareholders or for the purpose of gaining direct or indirect personal advantage or advantage for any associated person;
- 7) Refrain from any action that would lead to the loss of his independence;
- 8) Inform the Board immediately whose circumstances arise which makes an Independent Director lose his independence;

- 9) Assist the company in ensuring best corporate governance practices.

### **Additional director**

Section 161(1) of the Companies Act, 2013, provides that the articles of a company may confer on its Board of Directors the power to appoint any person, other than a person who fails to get appointed as a director in a general meeting, as an additional director at any time who shall hold office up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier.

In case of default in holding annual general meeting, the additional director shall vacate his office on the last day on which the annual general meeting ought to be held. A person who fails to get appointed as a director in a general meeting cannot be appointed as Additional Director. Section 161(1) of the Act applies to all companies, whether public or private.

### **Alternate Director**

Section 161(2) of the Act empowers the Board, if so authorized by its articles or by a resolution passed by the company in general meeting, to appoint a director (termed as 'alternate director') to act in the absence of an original director during his absence for a period of not less than three months from India.

The provisions applicable to an alternate director are as follows.

#### ***(i) Applicability:***

Section 161(2) of the Act applies to all companies, whether public or private.

#### ***(ii) Conditions for appointment of an alternate director:***

- (a) The Board of Directors of a company must be authorised by its articles or by a resolution passed by the company in general meeting for appointment of the alternate director.
- (b) The person in whose place the Alternate Director is being appointed should be absent for a period of not less than 3 months from India.
- (c) The person to be appointed as the Alternate Director shall be the person other than the person holding any alternate directorship for any other Director in the company or holding directorship in the same company.
- (d) If it is proposed to appoint an Alternate Director to an Independent Director, it must be ensured that the proposed appointee also satisfies the criteria of Independence as per section 149(6) of the Act.

#### ***(iii) Power to appoint:***

The Board may appoint an alternate director only if it is authorized by the articles or by an ordinary resolution passed at a general meeting. The right to appoint an alternate director vests in the Board. The original director has no right to appoint an alternate director. The members have no right to appoint an alternate director, the members can only empower to appoint alternate director as and when board thinks fit.

#### ***(iv) Method of appointment:***

There is no condition that an alternate director shall be appointed only by passing a resolution at a Board meeting. Therefore, an alternate director can be appointed by passing a resolution by circulation.

**(v) Terms of office of an alternate director:**

- (a) Not exceeding the term permissible to original director: An alternate director shall not hold office for a period longer than that permissible to the director in whose place he has been appointed. If the original director ceases to be a director by reason of death or vacation of office under section 167, the alternate director shall immediately cease to hold his office.
- (b) On the return of original director: The alternate director shall vacate his office when the original director in whose place he has been appointed returns to India.

**(vi) Automatic reappointment applies to the original director:** If the term of office of an original director expires before he returns back to India, the provision for automatic reappointment of a director as envisaged under section 152(7)(b) shall be applicable to the original director, and not to the alternate director.

Additionally for listed entities SEBI vide recent notification provides that no person shall be appointed or continue as an alternate director for an independent director of a listed entity with effect from October 1, 2018.

As per section 165, an alternate directorship in a company shall also be included while counting the number of directorship held by a director.

**Nominee director**

Section 161(3) of the Companies Act, 2013, provides that subject to the articles of a company, the Board may appoint any person as a director nominated by any institution in pursuance of the provisions of any law for the time being in force or of any agreement or by the Central Government or the State Government by virtue of its shareholding in a Government company.

**Appointment of Directors in casual vacancy**

Section 161(4) provides that If any vacancy is caused by death or resignation of a director appointed by the shareholders in General meeting, before expiry of his term, the Board of directors can appoint a director to fill up such vacancy. The appointed director shall hold office only up to the term of the director in whose place he is appointed. Section 161(4) in the case of a public company, if the office of any director appointed by the company in general meeting is vacated before his term of office expires in the normal course, the resulting casual vacancy may, in default of and subject to any regulations in the articles of the company, be filled by the Board of Directors at a meeting of the Board which shall subsequently approved by the members in the immediate next general meeting. The person so appointed shall hold office only upto the day upto which the director in whose place he has been appointed, would have held office if he had not vacated as aforesaid. Where a person appointed by the Board vacates his office it is not a case of casual vacancy and cannot be filled by the Board in the place.

**Appointment/ Reappointment, Disqualifications, Vacation of Office, Retirement, Resignation and Removal, and Duties of Directors****Appointment of directors to be voted individually- Section 162(1)**

A single resolution shall not be moved for the appointment of two or more persons as directors of the company unless a proposal to move such a motion has first been agreed to at the meeting without any vote being cast against it. A resolution moved in contravention of aforesaid provision shall be void, whether or not any objection was taken when it was moved. A motion for approving a person for appointment, or for nominating a person for appointment as a director, shall be treated as a motion for his appointment.

This provision is not applicable to a private company and Specified IFSC public company.

This provision shall not apply to (a) a Government Company in which the entire paid up share capital is held by the Central Government, or by any State Government or Governments or by the Central Government and one or more State Governments: (b) a subsidiary of a Government company, referred to in (a) above, in which the entire paid up share capital is held by that Government company.

### **Number of Directorships [Section 165]**

According to Section 165 of the Companies Act, 2013, no person shall hold office as a director, including any alternate directorship, in more than twenty companies at the same time. The maximum number of public companies in which a person can be appointed as a director shall not exceed ten. For reckoning the limit of public companies in which a person can be appointed as director, directorship in private companies that are either holding or subsidiary company of a public company shall be included. For reckoning the limit of directorships of twenty companies, the directorship in a dormant company shall not be included.

Additionally for listed entities SEBI vide recent notification provides that the directors of listed entities shall comply with the following conditions with respect to the maximum number of directorships, including any alternate directorships that can be held by them at any point of time -

(1) A person shall not be a director in more than eight listed entities with effect from April 1, 2019 and in not more than seven listed entities with effect from April 1, 2020:

Further it has been provided that a person shall not serve as an independent director in more than seven listed entities.

(2) Notwithstanding the above, any person who is serving as a whole time director / managing director in any listed entity shall serve as an independent director in not more than three listed entities.

For the purpose of this sub-regulation, the count for the number of listed entities on which a person is a director / independent director shall be only those whose equity shares are listed on a stock exchange.

### **Appointment of First Director**

The first directors of most of the companies are named in their articles. Regulation 60 of Table F provides that the number of the directors and the names of the first directors shall be determined in writing by the subscribers of the memorandum or a majority of them. If they are not so named in the articles of a company, then subscribers to the memorandum who are individuals shall be deemed to be the first directors of the company until the directors are duly appointed.

In the case of a One Person Company, an individual being a member shall be deemed to be its first director until the director(s) are duly appointed by the member in accordance with the provisions of Section 152. Section 152(1) of the Act is applicable to all companies, whether public or private.

### **Appointment of Directors by Members at General Meeting**

A person appointed as director shall not act as director unless he gives his consent to hold office of director and such consent in Form DIR - 2 has been filed with the registrar within thirty days of his appointment. The company shall within thirty days of appointment of a director, file such consent with the Registrar in form DIR-12. However, a specified IFSC public company shall file such consent in sixty days. According to Section 152, every director shall be appointed by the company in general meeting.

Separate motion should move for the appointment of each director as per section 162. A motion for

approving a person for appointment or for nomination a person for appointment shall also be treated as motion for his appointment.

Under section 152(6), articles of a company may provide that all directors of the company shall be retiring by rotation. Where article does not provide for retirement by rotation for all directors, not less than two – thirds of total number of directors of a public company shall be liable to be retired by rotation and be appointed by company in general meeting. At the first annual general meeting of a public company held next after the date of the general meeting at which the first directors are appointed and at every subsequent annual general meeting, one-third of such of the directors for the time being as are liable to retire by rotation, or if their number is neither three nor a multiple of three, then, the number nearest to one-third, shall retire from office. The directors to retire by rotation at every annual general meeting shall be those who have been longest in office since their last appointment, but as between persons who became directors on the same day, those who are to retire shall, in default of and subject to any agreement among themselves, be determined by lot.

As per Section 152(7) (a) if the vacancy of the retiring director is not filled-up and the meeting has not expressly resolved not to fill the vacancy, the meeting shall stand adjourned till the same day in the next week, at the same time and place, or if that day is a national holiday, till the next succeeding day which is not a holiday, at the same time and place.

(b) If at the adjourned meeting also, the vacancy of the retiring director is not filled up and that meeting also has not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been re-appointed at the adjourned meeting, unless –

- i. at that meeting or at the previous meeting a resolution for the re-appointment of such director has been put to the meeting and lost;
- ii. the retiring director has, by a notice in writing addressed to the company or its Board of directors, expressed his unwillingness to be so re-appointed;
- iii. he is not qualified or is disqualified for appointment;
- iv. a resolution, whether special or ordinary, is required for his appointment or re-appointment by virtue of any provisions of this Act; or
- v. section 162 is applicable to the case.

For the purposes of this section and section 160, the expression “retiring director” means a director retiring by rotation.

In case of Government companies, section 152(6) and (7) shall not apply to –

- (a) a Government Companies in which the entire paid up share capital is held by the Central Government , or by any State Government or Governments or by the Central Government and one or more State Governments
- (b) a subsidiary of a Government company referred to in (a) above , in which the entire paid up share capital is held by that Government company- Notification No. [ F.No.1/2/2014-CL.V], dated 5-6-2015. MCA has exempted a Specified IFSC public company vide notification dated 4th January 2017 from the provisions of section 152(6) and (7).

### **Procedure for re-appointment of the retiring director at the Annual General Meeting**

1. Ascertain which directors are due to retire by rotation. As a general principle, the directors to retire shall be those who have been longest in office since their last appointment.

2. Ensure that the retiring director is not subject to any disqualification for re-appointment as director of the company under sections 164 and 165 of the Companies Act, 2013.
3. Ensure that the consent of the director as well as the declaration from the director has been obtained.
4. Convene a Board meeting after giving notice to all directors of the company in accordance with Section 173 of the Act, to consider the re-appointment of retiring director.
5. Fix the time, place and agenda of the annual general meeting to pass an ordinary resolution for the reappointment of retiring director.
6. Send the notice in writing at least 21 clear days before the date of annual general meeting to the members such notice is required to be sent to the Stock Exchanges where the shares of company are listed.
7. Hold the annual general meeting and pass an ordinary resolution for re-appointment of the retiring director.
8. In case of listed companies, forward a copy of the proceedings of the annual general meeting to the stock exchanges where the company's shares are listed. [Regulation 3 of sub-regulation (4) of schedule III of SEBI (Listing Obligation and Disclosure) Regulations 2015]

### **Right of persons other than retiring directors to stand for directorship [Section 160]**

1. A person who is not a retiring director shall be eligible for appointment to the office of a director at any general meeting, if he, or some member intending to propose him as a director, has, not less than fourteen days before the meeting, left at the registered office of the company, a notice in writing under his hand signifying his candidature as a director or, as the case may be, the intention of such member to propose him as a candidate for that office. Such a person may be a member or a non-member, an additional director or a director to fill a casual vacancy or an alternate director or a nominee director.
2. Such notice must come along with the deposit of one lakh rupees or such higher amount as may be prescribed which shall be refunded to such person or, as the case may be, to the member, if the person proposed gets elected as a director or gets more than twenty five of total valid votes cast either on show of hands or on poll on such resolution.

In case of Nidhi company, instead of Rupees One Lakh, the deposit of Rupees ten thousand is required with the notice.

The requirements of deposit of amount shall not apply in case of appointment of an independent director or a director recommended by the Nomination and Remuneration Committee, if any, constituted under sub-section (1) of section 178 or a director recommended by the Board of Directors of the Company, in the case of a company not required to constitute Nomination and Remuneration Committee

3. Section 160 is not applicable to Government Company where the entire paid up share capital is held by Central Government jointly or severally or in case of subsidiary of Government Company in which the entire paid up capital is held by that Government Company.

Further, Section 160 is not applicable to Private Companies, Section 8 Companies whose article provide for election of directors by Ballot.

### **Procedure for appointment of a director other than a retiring director at the Annual General Meeting**

In case of a public company, the following procedure is to be adopted:

- The candidate for directorship or any member proposing other person for appointment to office of director, is required to give a notice in writing not less than fourteen days before the meeting at the office of the company, signifying candidature for the office of director or intention to propose other person as a candidate for that office, as the case may be, along with a deposit of one lakh rupees which shall be refunded to such person, or as the case may be, to such member, if the person succeeds in getting elected as a director.

The requirements of deposit of amount shall not apply in case of appointment of an independent director or a director recommended by the Nomination and Remuneration Committee, if any, constituted under sub-section (1) of section 178 or a director recommended by the Board of Directors of the Company, in the case of a company not required to constitute Nomination and Remuneration Committee

- On receipt of notice, the company will inform its members of the candidature of a person for the office of director or intention of the member to propose such person as candidate for that office by serving individual notice on the members, not less than seven days before the meeting.
- Where individual notice is not practicable, publish notice not less than seven days before the meeting, in at least two newspapers (one in English and the other in regional language) circulating in the place where the registered office of the company is situated.
- In case of listed company, forward copies of this notice also to the stock exchange, where the shares of the company are listed.
- Check whether the director to be appointed in the general meeting has obtained Director Identification Number (DIN). If not then ask such person to make application to Central Government for obtaining DIN and ensure that the Director has intimated his DIN to the Company.
- Ensure that the consent of the director as well as the declaration from the director has been obtained in Form DIR – 2.
- At the general meeting, the motion to appoint a person other than the retiring director will be taken up.

Where more than one such proposals are to be decided, they are to be discussed one by one and the decision of the meeting to be arrived at in respect of each proposal separately.

- In case of listed company, send the notice and a copy of the proceedings of the general meeting to the stock exchange with which the company is listed.
- In case the person is appointed as a director, the company shall refund the deposit of one lakh rupees to such person or to such other member, who had proposed his name for directorship.
- The company has to file particulars of director in Form DIR – 12 with the Registrar of Companies within thirty days of the appointment after paying the requisite fee electronically.

Ensure that said Form is digitally signed by managing director or manager or secretary of the company and also certified by a Company Secretary or Chartered accountant or Cost accountant in Whole time practice by digitally signing it.

For the purpose of filing Form DIR – 12, the following attachments are required:

- (a) Letter of appointment
- (b) Declaration by the first director

- (c) Declaration of the appointee Director in Form DIR-2;
- (e) Interest in other entities;

In case of a private company, any additional requirement in its Articles of Association will also have to be followed.

- In case of listed company, particulars of appointment of director should also be given to the stock exchange if the shares of the company are listed.
- The particulars of the director and other aspects of the director have to be entered by the company in the registers maintained under Sections 170 and 189
- After appointment the director concerned has to inform other companies in which he is director about his appointment.

### **Appointment of Independent directors**

(1) Appointment process of independent directors shall be independent of the company management; while selecting independent directors the Board shall ensure that there is appropriate balance of skills, experience and knowledge in the Board so as to enable the Board to discharge its functions and duties effectively. Independent director may be selected from Databank.

(2) The appointment of independent director(s) of the company shall be approved by the company at the meeting of the shareholders.

(3) The explanatory statement attached to the notice of the meeting for approving the appointment of independent director shall include a statement that in the opinion of the Board, the independent director proposed to be appointed fulfils the conditions specified in the Act and the rules made thereunder and that the proposed director is independent of the management. It shall also indicate the justification for choosing the appointee for appointment as Independent Director.

(4) The appointment of independent directors shall be formalized through a letter of appointment, which shall set out:

- (a) The term of appointment;
- (b) The expectation of the Board from the appointed director; the Board-level committee(s) in which the director is expected to serve and its tasks;
- (c) The fiduciary duties that come with such an appointment along with accompanying liabilities;
- (d) Provision for Directors and Officers (D and O) insurance, if any;
- (e) The Code of Business Ethics that the company expects its directors and employees to follow;
- (f) The list of actions that a director should not do while functioning as such in the company; and
- (g) The remuneration, mentioning periodic fees, reimbursement of expenses for participation in the Boards and other meetings and profit related commission, if any.

(5) The terms and conditions of appointment of independent directors shall be open for inspection at the registered office of the company by any member during normal business hours.

(6) The terms and conditions of appointment of independent directors shall also be posted on the company's website.

(7) He shall be hold office for a term of upto 5 consecutive years of a company. [Section 149(10)]

### **Re-appointment of Independent directors**

The re-appointment of independent director shall be on the basis of report of performance evaluation. (Schedule IV – Code for Independent Directors)

Section 149(11) provides that the Independent Director shall be eligible for re-appointment on passing of special resolution. He shall not hold office for more than 2 consecutive terms, but such independent director shall be eligible for appointment after the expiration of 3 years of ceasing to become an independent director.

However, he shall not, during the said period of 3 years, be appointed in or be associated with the company in any other capacity, either directly or indirectly.

### **APPOINTMENT OF DIRECTORS BY BOARD**

#### **Procedure for appointment of Additional Director**

- Ensure that the Articles of the company authorise the Board to appoint an additional director and such appointment is within the maximum limit of directors mentioned in the Articles.
- Ensure that individual proposed to be appointed as an additional director, does not suffer from any disqualification mentioned.
- The Board may, if so authorised by articles otherwise, Additional Director may be appointed by passing a resolution at general meeting.
- Before appointing a person as an additional director, his consent to act as director should be obtained. – Check whether the additional director to be appointed in the board meeting has obtained Director Identification Number (DIN). If not then ask such director to make application to Central Government for obtaining DIN and ensure that the Director has intimated his Directors Identification Number to the Company.
- Rest the procedure for appointment remains the same.

#### **Appointment of Directors to fill casual vacancy**

In case of a private company, the procedure for appointment will be governed by its Articles.

#### **Procedure for appointing Directors in casual vacancy**

- Where it is proposed by the Board to appoint a person to fill a casual vacancy, his written consent to act as a director has to be obtained before appointment.
- Check whether the director to be appointed in the casual vacancy in the board meeting has obtained Director Identification Number (DIN). If not then ask such director to make application to Central Government for obtaining DIN and ensure that the Director has intimated his Directors Identification Number to the Company.
- Rest of the procedure remains the same.

#### **Procedure for Appointment of an Alternate Director**

- Consult the Articles of Association of the company to see whether they authorize the Board to appoint an alternate director. Otherwise, either alter them accordingly or pass a resolution in

company's general meeting authorizing the Board to make such appointment

- Where it is proposed to appoint a person as an alternate director his written consent to act as director shall be obtained. – Check whether alternate director to be appointed in board meeting has obtained Director Identification Number (DIN). If not then ask such director to make application to Central Government for obtaining DIN and ensure that the Director has intimated his Directors Identification Number to the Company.
- Rest of the procedure remains the same.

### **Appointment of Directors by Tribunal**

While giving order on an application made under section 241, i.e., for relief in cases of oppression the Tribunal may provide order for appointment of such numbers of persons as directors of the company and ask them to report to the Tribunal on matters as the Tribunal may direct. [Section 242(2)(k)].

The directors, so appointed, may or may not be the members of the company. For the purpose of reckoning two thirds or any other proportion of the total number of directors of the company, any director or directors appointed by the Tribunal shall not be taken into account. Such director or directors shall not liable to determination by retirement of directors by rotation. But they can be removed by the Tribunal at any time and other persons can be appointed by it in their place. Where the directors have been appointed by the Tribunal, it may also issue such directions to the company, as it may consider necessary or appropriate in regard to their affairs.

### **Appointment of Director by system of Proportional Representation**

According to section 163 the articles of a company may provide for the appointment of not less than two-thirds of the total number of the directors of a company in accordance with the principle of proportional representation, whether by the single transferable vote or by a system of cumulative voting or otherwise and such appointments may be made once in every three years and casual vacancies of such directors shall be filled as provided in subsection (4) of section 161.

In case of Government Companies, section 163 shall not apply to –

- (a) a Government Companies in which the entire paid up share capital is held by the Central Government , or by any State Government or Governments or by the Central Government and one or more state Governments;
- (b) a subsidiary of a Government Company, referred to in (a) above , in which the entire paid up share capital is held by that Government company.

### **Appointment of Nominee Directors**

Explanation to Section 149(7) defines, “nominee director” means a director nominated by any financial institution in pursuance of the provisions of any law for the time being in force, or of any agreement, or appointed by any Government, or any other person to represent its interests. Nominee Director shall not be deemed to be independent director as per Section 149(6). [Section 149(7) is not applicable to a Specified IFSC public company as per notification dated 4th January 2017]

Companies, which secure financial assistance from financial institutions, banks, major shareholders, debenture holders, etc. usually confer on their lenders, power to appoint and terminate the appointments of their nominees on their Boards. Such power is conferred by incorporating appropriate provisions in the financial assistance agreements.

These institutions/banks etc. also insist on borrowing companies to alter their articles of association so as to empower them to appoint and terminate the services of their nominee directors on the Board of the company as and when they like. These directors are known as nominee directors. They are not liable to retire by rotation and hold office at the pleasure of their nominating agencies. They cannot be removed by the company.

Procedure to appoint a nominee director is same as appointment as additional director by the Board or appointment of director other than retiring director by the company in general meeting. Depending upon the term and condition of agreement with the appointing bank/institution/Government, the company may choose any of these two methods.

### **Procedure for Appointment of Directors to be elected by Small Shareholders**

A listed company may have one director elected by small shareholders. Small shareholders means a shareholder holding shares of nominal value of not more than twenty thousand rupees or such other sum prescribed. [Section 151]

Rule 7 of the Companies (Appointment and Qualification of Directors) Rules, 2014

1. A listed company having a paid-up capital of five crore rupees or more and having one thousand or more small shareholders (holding shares of nominal value of Rs. 20,000 or less may have a director elected by such small shareholders.

2. Small shareholders intending to propose a person as a candidate for the post of small shareholders' director shall leave a notice of their intention with the company at least fourteen days before the meeting under their signature specifying the name, address, shares held and folio number of the person whose name is being proposed for the post of director and of the small shareholders who are proposing such person for the office of director.

If the person being proposed does not hold any shares in the company, the details of shares held and folio number need not be specified in the notice.

3. The notice shall be accompanied by statement of proposed director stating his DIN, that he is not disqualified and his consent to act as director of the company.

4. Such director shall be considered as an independent director subject to being eligible and giving a declaration of his independence in accordance with sub-section (6) and (7) of section 149 of the Act.

5. The small shareholder director shall be elected through postal ballot.

6. Ensure that the proposed director shall not hold the position of small shareholder director in more than 2 companies at the same time. Provided that the second company in which he has been appointed shall not be in a business which is competing or is in conflict with the business of the first company.

7. Such director shall not be retire by rotation and shall have tenure of continuous three years.

8. After completion of tenure small shareholders director shall not be eligible for reappoint.

9. When small shareholders directors cease to be a small shareholder, he cease to be a small shareholders director.

10. The company has to file particulars of director in Form DIR – 12 with the Registrar of Companies within thirty days of the appointment after paying the requisite fee electronically.

11. Ensure that said Form is digitally signed by managing director or manager or secretary of the company and also certified by a Company Secretary or Chartered accountant or Cost accountant in Whole time practice by digitally signing it.

12. For the purpose of filing Form DIR – 12, the following attachments are required:

- (a) Letter of appointment
- (b) Declaration by the first director
- (c) Declaration of the appointee Director, in Form DIR-2;
- (d) Interest in other entities;

13. In case of listed company, the particulars of appointment of director should also be given to the stock exchange if the shares of the company are listed.

14. The particulars of the director and other aspects of the director have to be entered by the company in the registers maintained under Sections 170 and 189

15. After appointment the director concerned has to inform other companies in which he is director about his appointment

### **Disqualifications for Appointment of Director**

Section 164(1) Provides that a person shall not be eligible for appointment as a director of a company, if –

- (a) He is of unsound mind and stands so declared by a competent court;
- (b) He is an undischarged insolvent;
- (c) He has applied to be adjudicated as an insolvent and his application is pending;
- (d) He has been convicted by a court of any offence, whether involving moral turpitude or otherwise, and sentenced in respect thereof to imprisonment for not less than six months and a period of five years has not elapsed from the date of expiry of the sentence. Provided that if a person has been convicted of any offence and sentenced in respect thereof to imprisonment for a period of seven years or more, he shall not be eligible to be appointed as a director in any company.
- (e) An order disqualifying him for appointment as a director has been passed by a court or Tribunal and the order is in force;
- (f) He has not paid any calls in respect of any shares of the company held by him, whether alone or jointly with others, and six months have elapsed from the last day fixed for the payment of the call;
- (g) He has been convicted of the offence dealing with related party transactions under section 188 at any time during the last preceding five years; or
- (h) He has not complied with sub-section (3) of section 152.

Section 164(2) also provides that no person who is or has been a director of a company which –

- (a) Has not filed financial statements or annual returns for any continuous period of three financial years; or
- (b) Has failed to repay the deposits accepted by it or pay interest thereon or to redeem any debentures on the due date or pay interest due thereon or pay any dividend declared and such failure to pay or redeem continues for one year or more,

shall be eligible to be re-appointed as a director of that company or appointed in other company for a period of five years from the date on which the said company fails to do so.

Provided that where a person is appointed as a director of a company which is in default of clause (a) or clause (b), he shall not incur the disqualification for a period of six months from the date of his appointment.

In case of Government Companies, section 164(2) shall not apply – Notification No. [F.No. 1/2/2014- CL.V], dated 5-06-2015.

Every director shall inform to the company concerned about his disqualification under sub-section (2) of section 164, if any, in Form DIR-8 before he is appointed or re-appointed.

Whenever a company fails to file the financial statements or annual returns, or fails to repay any deposit, interest, dividend, or fails to redeem its debentures, as specified in sub-section (2) of section 164, the company shall immediately file Form DIR-9, to the Registrar furnishing therein the names and addresses of all the directors of the company during the relevant financial years.

When a company fails to file the Form DIR-9 within a period of thirty days of the failure that would attract the disqualification under sub-section (2) of section 164, officers of the company specified in clause (60) of section 2 of the Act shall be the officers in default.

Upon receipt of the Form DIR-9 under sub-rule (2), the Registrar shall immediately register the document and place it in the document file for public inspection. Any application for removal of disqualification of directors shall be made in Form DIR-10.

However, a private company may by its articles provide for any disqualifications for appointment as a director in addition to those specified in sub-sections (1) and (2). The disqualifications referred to in clauses (d), (e) and (g) of sub-section (1) shall continue to apply even if the appeal or petition has been filed against the order of conviction or disqualification.

### **Removal of Directors**

Under section 169 of the Act, a company may, by ordinary resolution remove a director before the expiry of the period of his office. The provisions of section 169 shall apply regardless of the way in which the director concerned was appointed and notwithstanding anything contained in the articles of the company or any agreement with the director concerned.

### **Removal of Director by Shareholders**

According to Section 169, a company may, by ordinary resolution, remove a director, not being a director appointed by the Tribunal under section 242, before the expiry of the period of his office after giving him a reasonable opportunity of being heard. The provision relating to removal shall not apply where the company has availed itself of the option to appoint not less than two – thirds of the total number of directors according to the principle of proportional representation.

### **Procedure for Removal of Director**

The following procedure is required to be adopted for removal of a director:

1. A special notice from a member of the company proposing an ordinary resolution for removing the director is necessary.
2. Send forthwith a copy of the special notice to the director proposed to be removed.

3. Decide to call a general meeting through the Board resolution.
4. Issue notice of the general meeting in writing at least twenty-one clear days before the date of the meeting informing about the special notice and proposing the ordinary resolution for removal.
5. In the notice of the meeting, state the facts of the representation made by the director concerned and also 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 representations by the company).
6. If the representation is received too late and it could not be sent to the members, the director concerned may require that the representation shall be read out at the meeting. The director concerned has also the right of being heard at the meeting.
7. However, the National Company Law Tribunal on an application of the company or any other person who claims to be aggrieved, on having satisfied, may dispense with the procedure of sending a copy of representation and reading thereof at the meeting if it is being used to secure needless publicity for defamatory matter.
8. In case of listed company, send notice of the general meeting to the stock exchange(s) within 24 hours of the occurrence of the event where the company is listed [Refer regulation 30(6) of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015].
9. Hold the general meeting and pass the proposed resolution by ordinary resolution.
10. In case of listed company, forward a copy of the proceedings of the meeting within 24 hours of the occurrence of the event to the stock exchange(s) where the company is listed.
11. Ensure that said Form is digitally signed by managing director or manager or secretary of the company and also certified by a Company Secretary or Chartered accountant or Cost accountant in Whole time practice by digitally signing it.
12. The company has to file particulars of director in Form DIR – 12 with the Registrar of Companies within thirty days of the removal after paying the requisite fee electronically.

For the purpose of filing Form DIR – 12, the following attachments are required:

- (a) Notice of resignation;
- (b) Evidence of Cessation;
- (c) Interest in other entities;

13. The particulars of the director and other aspects of the director have accordingly be modified in the registers maintained under Sections 170 and 189.
14. Give a general public notice in newspaper regarding removal of the director if it is so warranted for the protection of the company and benefit of the general public.

### **Removal of Director by the National Company Law Tribunal**

Where an application has been made to the National Company Law Tribunal under Section 241 of the Companies Act 2013 for prevention of oppression or mismanagement and the Tribunal has conducted its proceedings on the application, it has the power under Section 242(2)(h) of the Act, to remove any director.

### **Vacation of Office by Director**

According to Section 167 of the Companies Act, 2013, the office of a director shall become vacant in case –

- (a) he incurs any of the disqualifications specified in section 164;  
where he incurs disqualification under sub-section (2) of section 164, the office of the director shall become vacant in all the companies, other than the company which is in default under that sub-section.
- (b) he absents himself from all the meetings of the Board of Directors held during a period of twelve months with or without seeking leave of absence of the Board;
- (c) he acts in contravention of the provisions of section 184 relating to entering into contracts or arrangements in which he is directly or indirectly interested;
- (d) he fails to disclose his interest in any contract or arrangement in which he is directly or indirectly interested, in contravention of the provisions of section 184;
- (e) he becomes disqualified by an order of a court or the Tribunal;
- (f) he is convicted by a court of any offence, whether involving moral turpitude or otherwise and sentenced in respect thereof to imprisonment for not less than six months. Provided that the office shall not be vacated by the director in case of orders referred to in clauses (e) and (f)-
  - (i) for thirty days from the date of conviction or order of disqualification;
  - (ii) where an appeal or petition is preferred within thirty days as aforesaid against the conviction resulting in sentence or order, until expiry of seven days from the date on which such appeal or petition is disposed of; or
  - (iii) where any further appeal or petition is preferred against order or sentence within seven days, until such further appeal or petition is disposed of
- (g) he is removed in pursuance of the provisions of this Act;
- (h) he, having been appointed a director by virtue of his holding any office or other employment in the holding, subsidiary or associate company, ceases to hold such office or other employment in that company.

A private company, which is not a subsidiary of a public company, may, by its articles, provide additional grounds for vacation of office of director.

On vacation of office of director, the company is required to file Form DIR – 12 to the Registrar of Companies.

If the office held by any director has become vacant on the ground of disqualification provided above and the concerned director continues to function, he shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees, or with both.

### **Resignation of Directors**

According to section 168 –

1. A director may resign from its office by giving a notice with the reasons of resignation in writing to the company.
2. The Board shall on receipt of such a notice from a director shall take note of the same.

3. The company shall within 30 days from the date of receipt of notice of resignation from a director, intimate the registrar in Form DIR-12 and post the information on its website if any as provided in Rule 15 of the companies (Appointment and Qualification of Directors) Rules, 2014.
4. The board shall place the facts of such resignation by the director in the Report of Directors laid in immediately following general meeting by the company.
5. The Director may within 30 days from his resignation, forward to the registrar a copy of his resignation along with reasons for resignation with reasons provided therein in Form DIR-11 along with the fee provided. In case of Specified IFSC public and private company, a director may file Form DIR-11 to the Registrar.
6. The resignation shall be effective from the date on which the notice is received by the company or the date specified by the Director in the notice whichever is later.
7. When all the Directors resign at the same time under section 167, in such case the required number of directors are to be appointed by the promoter or, the Central Government. The Directors so appointed shall hold office till the Directors are appointed by the company in general meeting.

The proviso to sub section (2) of section 168 of Companies Act, 2013 clarifies that the Director who shall be liable even after his resignation for the offences which occurred during his tenure.

### **Rights and Duties of directors [Section 166]**

The duties of directors as contained in section 166 of the Companies Act, 2013 are described as follows

#### **1. Duty to act as per the articles of the company**

The director of a company shall act in accordance with the articles of the company.

#### **2. Duty to act in good faith**

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. Duty to exercise due care**

A director of a company shall exercise his duties with due and reasonable care, skill and diligence and shall exercise independent judgment.

#### **4. Duty to avoid conflict of interest**

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. Duty not to make any undue gain**

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. Duty not to assign his office**

A director of a company shall not assign his office and any assignment so made shall be void.

### **Punishment for contravention**

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 one lakh rupees but which may extend to five lakh rupees.

### **Loans to Directors**

A company may give loan to director in the form of book debt or guarantee or security subject to certain conditions. According to section 185(1) No company shall, directly or indirectly, advance any loan, including any loan represented by a book debt to, or give any guarantee or provide any security in connection with any loan taken by,—

- (a) any director of company, or of a company which is its holding company or any partner or relative of any such director; or
- (b) any firm in which any such director or relative is a partner.

(2) A company may advance any loan including any loan represented by a book debt, or give any guarantee or provide any security in connection with any loan taken by any person in whom any of the director of the company is interested, subject to the condition that—

- (a) A special resolution is passed by the company in general meeting:

Provided that the explanatory statement to the notice for the relevant general meeting shall disclose the full particulars of the loans given, or guarantee given or security provided and the purpose for which the loan or guarantee or security is proposed to be utilised by the recipient of the loan or guarantee or security and any other relevant fact; and

- (b) the loans are utilised by the borrowing company for its principal business activities.

Explanation.—For the purposes of this sub-section, the expression "any person in whom any of the director of the company is interested" means—

- (a) any private company of which any such director is a director or member;
- (b) any body corporate at a general meeting of which not less than twenty-five per cent. of the total voting power may be exercised or controlled by any such director, or by two or more such directors, together; or
- (c) any body corporate, the Board of directors, managing director or manager, whereof is accustomed to act in accordance with the directions or instructions of the Board, or of any director or directors, of the lending company.

(3) Nothing contained in sub-sections (1) and (2) shall apply to—

- (a) the giving of any loan to a managing or whole-time director—
  - (i) as a part of the conditions of service extended by the company to all its employees; or
  - (ii) pursuant to any scheme approved by the members by a special resolution; or
- (b) a company which in the ordinary course of its business provides loans or gives guarantees or securities for the due repayment of any loan and in respect of such loans an interest is charged at a rate not less than the rate of prevailing yield of one year, three years, five years or ten years Government security closest to the tenor of the loan; or
- (c) any loan made by a holding company to its wholly owned subsidiary company or any guarantee

given or security provided by a holding company in respect of any loan made to its wholly owned subsidiary company; or

- (d) any guarantee given or security provided by a holding company in respect of loan made by any bank or financial institution to its subsidiary company:

Provided that the loans made under clauses (c) and (d) are utilised by the subsidiary company for its principal business activities.

(4) If any loan is advanced or a guarantee or security is given or provided or utilised in contravention of the provisions of this section,—

- (i) the company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees;
- (ii) every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees; and
- (iii) the director or the other person to whom any loan is advanced or guarantee or security is given or provided in connection with any loan taken by him or the other person, shall be punishable with imprisonment which may extend to six months or with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees, or with both.

#### **Exemption for applicability of section 185**

Section 185 shall not apply to Private Company subject to the following conditions:

- (a) In whose share capital no other body corporate has invested any money
- (b) If the borrowings of such company from banks or financial institutions or any body corporate is less than twice of its paid up share capital or fifty crore rupees, whichever is lower and
- (c) Such a company has not defaulted in repayment of such borrowings subsisting at the time of making transactions under this section.

Section 185 shall not apply to Nidhi Company if the loan is given to a director or his relative in their capacity as member and such transaction is disclosed in the annual accounts by a note.

Section 185 shall not apply to Government Company in case such company obtains approval of the Ministry or Department of the Central Government which is administratively in charge of the company or, as the case may be, the State Government before making any loan or giving any guarantee or providing any security under the section.

#### **Disclosures by a director of his interest**

Section 184 (1) states that every director shall at the first meeting of the Board in which he participates as a director and thereafter at the first meeting of the Board in every financial year or whenever there is any change in the disclosures already made, then at the first Board meeting held after such change, disclose his concern or interest in any company or companies or bodies corporate, firms, or other association of individuals which shall include the shareholding, in such manner as may be prescribed in Rule 9 .

#### **Rule 9 of Companies (Meetings of Board and its Powers) Rules, 2014**

(1) Every director shall disclose his concern or interest in any company or companies or bodies corporate

(including shareholding interest), firms or other association of individuals, by giving a notice in writing in Form MBP 1.

(2) It shall be the duty of the director giving notice of interest to cause it to be disclosed at the meeting held immediately after the date of the notice.

(3) All notices shall be kept at the registered office and such notices shall be preserved for a period of eight years from the end of the financial year to which it relates and shall be kept in the custody of the company secretary of the company or any other person authorised by the Board for the purpose.

### **Register of Directors and Key Managerial Personnel and their shareholding**

Section 170 makes it obligatory for every company to maintain a register containing the prescribed particulars of all its directors and Key Managerial Personnel and their shareholding.

The provisions of section 170 read with Rule 17 and Rule 18 of the Companies (Appointment and Qualification of Directors) Rules, 2014 are as follows:

- (i) Every company shall keep at its registered office a register containing such particulars of its directors and key managerial personnel as may be prescribed and which shall include details of securities held by each of them in the company or its holding, subsidiary, subsidiary of its holding companies or associate companies. [Section 170(1)]
- (ii) A return containing such particulars and documents as may be prescribed, of the directors and the key managerial personnel shall be filed with the Registrar in e-form DIR-12 within 30 days from the appointment of every director and key managerial personnel, as the case may be, and within 30 days of any change taking place.

In case of Government Company - Section 170 shall not apply to Government Company in which the entire share capital is held by the Central Government, or by any State Government or Governments or by the Central Government or by one or more State Governments. - Notification dated 5th June, 2015.

In case of Specified IFSC Public Company- InSub-section (2) of section 170 For the words "thirty days" at both places read as "sixty days". - Notification Dated 4th January 2017.

### **Members right to inspect (Section 171)**

- (i) The register of directors and Key Managerial Personnel kept under section 170(1) shall be open for inspection during business hours and the members shall have the right to take extracts there from and copies thereof, on request and will be provided within 30 days free of cost. [Section 171(1)(a)]
- (ii) Such register shall also be kept open for inspection at every annual general meeting of the company and shall be made accessible to any person attending the meeting. [Section 171(1)(b)]
- (iii) If any inspection during business hours is refused, or if any copy required as above is not sent within thirty days from the date of receipt of such request, the Registrar shall on an application made to him order immediate inspection and supply of copies required there under. [Section 171(2)]

In case of Government Company - Section 171 shall not apply to Government Company in which the entire share capital is held by the Central Government, or by any State Government or Governments or by the Central Government or by one or more State Governments.

## LESSON ROUND-UP

- To attain the objectives prescribed in Memorandum of Association of the company, company depends on Board of Directors. Directors of a company are its eyes, ears, brain, hands and other essential limbs.
- Every public company shall have at least 3 directors and every private company shall have at least 2 directors and every one person company shall have atleast 1 director as per section 149.
- Directors are trustees for the company i.e. the directors are persons selected to manage the affairs of the company for the benefit of the shareholders.
- Section 164 lays down disqualifications of directors. Also individually only can be a director under section 152 of the Act.
- Maximum Number of Director is 15, which can be increased by passing a special Resolution.
- Certain prescribed class or classes of companies is required to have at least one woman director. This is a mandatory provision.
- Every company including one person company shall have at least on director who stays in India for a period of not less than 180 days in the previous calendar year.
- Maximum limit on total number of directorship has been fixed at 20 companies including sub limit of 10 for public companies.
- The members of a company may, by special resolution, specify any lesser number of companies in which a director of the company may act as director.
- A director may be removed from the office by giving a special notice.
- A director may resign his office in the manner provided by the articles.
- Any officer or employee of a company shall be punishable with the fine on the complaint of the company or any creditor or contributory thereof, if he wrongfully obtains, possess or withholds any property of the company.

## SELF-TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

1. Explain the concept appointment of small shareholder directors?
2. What are the qualifications of a director? When is a person disqualified for appointment as a director of the company?
3. Mr. 'A' is to be appointed as independent director. Explain the law relating to number of directors.
4. Mr. 'A' an independent director of ABC Ltd. Has Mr. B as alternate director. Mr. B is also the Vice president and director of the company. Explain the nature of working and legal interpretation?
5. How can the directors be removed from the office before the expiry of their term?
6. Under what circumstances is a director deemed to have vacated the office of directorship?



# Lesson 17

## Key Managerial Personnel

### LESSON OUTLINE

- Key Managerial Personnel
- Managing Director
- Company Secretary
- Role and duties of Company Secretary
- Managerial Remuneration
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

The Companies Act 2013 has introduced a new concept for appointment of the Key Managerial Personnel at top level of the organizational structure. In the new Act the position of company secretary has been enhanced multifold, from record keeper to key managerial personnel. A present day company secretary is expected to do statutory, administrative, managerial and strategic functions.

After reading this lesson, you will be able to understand the legal and procedural aspects as regards appointment, conditions for appointment, how to fill the vacancies in office of Key Managerial Personnel, role of a Company Secretary as a Key Managerial personnel, powers and duties.

## INTRODUCTION

The executive management of a company is responsible for the day to day management of a company. The Companies Act, 2013, has used the term key management personnel to define the executive management. The key management personnel are the point of first contact between the company and its stakeholders. While the Board is responsible for providing the oversight, it is the key management personnel who are responsible for not just laying down the strategies as well as its implementation.

Chapter XIII of the Companies Act, 2013 read with Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 deal with the legal and procedural aspects of appointment of key managerial personnel including managing director, whole-time director or manager, managerial remuneration, secretarial audit etc.

Let us understand certain definitions.

According to section 2(51) "**key managerial personnel**", in relation to a company, 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; and
- (vi) such other officer as may be prescribed.

**Chief Executive Officer** has been defined under section 2(18) so as to mean an officer of a company, who has been designated as such by it.

**Chief Financial Officer** has been defined under section 2(19) so as means a person appointed as the Chief Financial Officer of a company.

**Company Secretary**-According to section 2(24) "company secretary" or "secretary" means a company secretary as defined in clause (c) of sub-section (1) of section 2 of the Company Secretaries Act, 1980 (56 of 1980) who is appointed by a company to perform the functions of a company secretary under this Act.

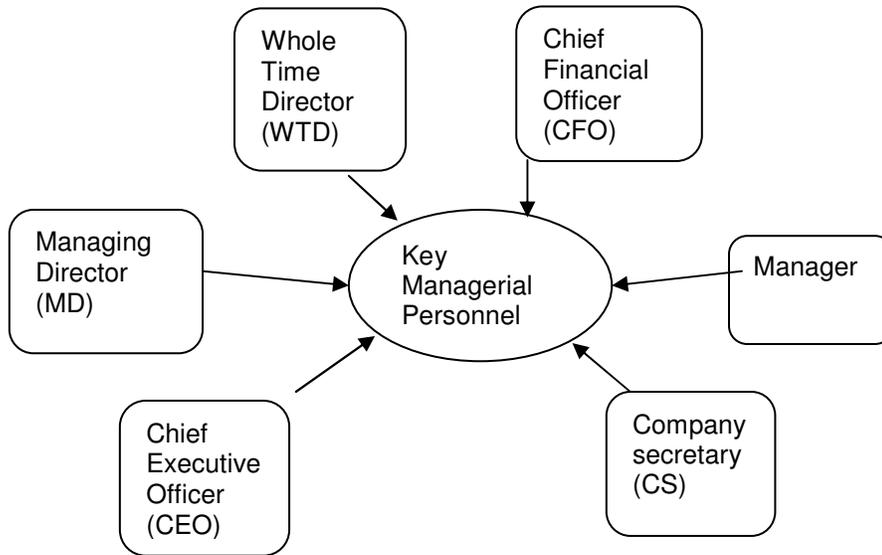
**Manager** as defined under section 2(53) means an individual who, subject to the superintendence, control and direction of the Board of Directors, has the management of the whole, or substantially the whole, of the affairs of a company, and includes a director or any other person occupying the position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

**Managing Director** as defined under section 2(54) 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.*—For the purposes of this clause, the power to do administrative acts of a routine nature when so authorised by the Board such as the power to affix the common seal (if any) 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;

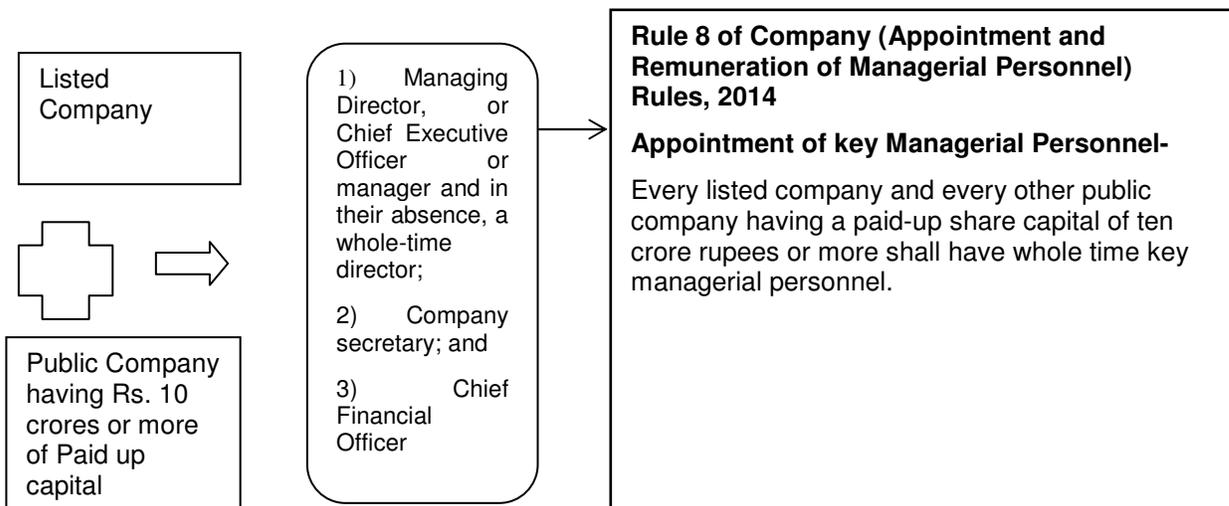
According to section 2(94) whole-time director includes a director in the whole-time employment of the company.



### Appointment of Key Managerial Personnel

Section 203 of the Companies Act, 2013 read with Rule 8 mandates the appointment of Key Managerial Personnel and makes it obligatory for a listed company and every other public company having a paid-up share capital of rupees ten crores or more, to appoint following whole-time key managerial personnel:

- (i) managing director, or Chief Executive Officer or manager and in their absence, a whole-time director;
- (ii) company secretary; and
- (iii) chief financial officer



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.

Rule 8 of the Companies (Meetings of Board and its powers) Rules, 2014, requires such appointment by the Board of Directors only by means of Resolution passed at meeting of the Board.

An individual shall not be appointed or reappointed as the chairperson of the company, as well as the managing director or chief executive officer 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, such class of companies engaged in multiple businesses and which has appointed one or more chief executive officers for each such business as may be notified by the Central Government are exempted from the above.

**MCA vide its notification S.O. 1913(E) dated 25-7-2014 notified that public companies having paid up Share capital of Rs. 100 Cr or more and annual turnover of ₹1000 Cr or more which are engaged in multiple businesses and have appointed Chief Executive Officer for each such business can appoint an individual as Chairperson and Managing Director.**

A Whole-time key managerial personnel shall not hold office in more than one company except in its subsidiary company at the same time. However, he can hold directorship in other companies with the permission of the Board.

A company may appoint or employ a person as its managing director, if he is the managing director or manager of one, and of not more than one, other company and such appointment or employment is made or approved by a resolution passed at a meeting of the Board with the consent of all the directors present at the meeting and of which meeting, and of the resolution to be moved thereat, specific notice has been given to all the directors then in India.

If the office of any whole-time key managerial personnel is vacated, the resulting vacancy shall be filled-up by the Board at a meeting of the Board within a period of six months from the date of such vacancy.

#### **Vide Exemption notification dated 05.06.2015 for Government Company**

A new sub-section 4A has been inserted thereby providing that sub-sections (1), (2), (3) and (4) of section 203 shall not apply to a managing director or chief executive officer or manager and in their absence, a whole-time director of the government company.

**Note:** The Provisions of section 203 relating to appointment of KMP shall not apply to MD/CEO/Manager or in their absence a whole time director of the Government Company.

#### **Procedure to appoint Key Managerial Personnel**

1. Hold the Board meeting and pass the Board resolution containing the terms and conditions of the appointment of key managerial personnel.
2. A whole time key managerial personnel shall not hold office in more than one company except in its subsidiary at the same time.
3. A company may appoint or employ a person as its managing director, if he is the managing director or manager of one, and of not more than one, other company and such appointment or employment is made or approved by a resolution passed at a meeting of the Board with the consent of all the directors present at the meeting and of which meeting, and of the resolution to be moved thereat, specific notice has been given to

all the directors then in India.

4. On vacation of the office of a whole time Key Managerial Personnel, the resulting vacancy shall be filled-up by the Board at a meeting of the Board within a period of 6 months.

5. File with the Registrar the Form MGT-14 and a return of appointment of a managing director, whole time director or manager in Form MR-1 (Return of appointment of Managing Director, Whole Time Director and Manager).

6. File DIR-12 (Particulars of appointment of Directors and the Key Managerial Personnel and changes among them) along with the fee prescribed in Companies (Registration of Offices and Fees) Rules, 2014.

### **Appointment of Managing Director, Whole-Time Director or Manager**

Section 196 of the Companies Act, 2013 provides that no company shall appoint or employ at the same time a Managing Director and a Manager. Further, a company shall not appoint or reappoint any person as its Managing Director, Whole Time Director or manager for a term exceeding five years at a time and no reappointment shall be made earlier than one year before the expiry of his term.

No company shall appoint or employ at the same time a Managing Director and a Manager.

No company shall appoint or continue the employment of any person as managing director, whole-time director or manager who —

- (a) is below the age of twenty-one years or has attained the age of seventy years:
- (b) is an undischarged insolvent or has at any time been adjudged as an insolvent;
- (c) has at any time suspended payment to his creditors or makes, or has at any time made, a composition with them; or
- (d) has at any time been convicted by a court of an offence and sentenced for a period of more than six months.

Appointment of a person who has attained the age of seventy 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;

Where no such special resolution is passed but votes cast in favour of the motion exceed the votes, if any, cast against the motion and the Central Government is satisfied, on an application made by the Board, that such appointment is most beneficial to the company, the appointment of the person who has attained the age of seventy years may be made.

Section 196(4) of the Companies Act, 2013 provides that subject to the provisions of section 197 and Schedule V, a managing director, whole-time director or manager shall be appointed and the terms and conditions of such appointment and remuneration payable be approved by the Board of Directors at a meeting which shall be subject to approval by a resolution at the next general meeting of the company and by the Central Government in case such appointment is at variance to the conditions specified in Schedule V. Approval of the Central Government is not necessary if the appointment is made in accordance with the conditions specified in specified in Part I of Schedule V to the Act.

The appointment of a managing director or whole-time director or manager and the terms and conditions of such appointment and remuneration payable thereon must be first approved by the Board of directors at a meeting and then by an ordinary resolution passed at a general meeting of the company.

**Exemption to private company for section 196(4) & (5) vide notification dated 05.06.2015**

*Section 196(4) and Section 196(5) is not applicable to Private Company*

**Note:** Exemption is given to the private companies for Section 196(4) which deals with appointment of Managing Director/Whole time director /manager /approval of Central Government as the case may be and Section 196(5) deals with validating actions of Managing/Whole time Director/manager, if the appointment is not approved by a company in general meeting.

Therefore a private company may appoint managing director, Whole time Director or Manager in the manner prescribed in its Articles of Association.

**Exemption to government company for section 196 (2), (4) & (5) vide notification dated 05.06.2015**

**Section 196 (2), (4) & (5) shall not apply to Government Company**

**Note:** Section 196(2) relates to term of managing director not to exceed five years. Section 196(4) relates to approval of the members/central government as the case may be for appointment of managing director and section 196(5) relates to validity of actions of Managing Director if his appointment is not approved at the General Meeting. These provisions are not applicable to a government company.

Therefore a government company may appoint managing director, Whole time Director or Manager in the manner prescribed in its Articles of Association. The term of appointment of managing director, Whole time Director or Manager may exceed five years.

**Exemption to Specified International Financial Services Centres (IFSC) public company for section 196 (4) vide notification dated 05.01.2017**

Section 196 (4) shall not apply to Specified IFSC public company

**Note:** Section 196(4) relates to approval of the members/central government as the case may be for appointment of managing director.

Therefore a private company may appoint managing director, Whole time Director or Manager in the manner prescribed in its Articles of Association.

*Notice convening Board and General Meeting to contain particulars of appointment*

A notice convening Board or general meeting for considering such appointment 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.

**Rule 3 of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014**

A company shall file a return of appointment of a Managing Director, Whole Time Director or Manager within sixty days of the appointment, with the Registrar in Form No. MR.1 along with such fee as may be specified for this purpose.

Section 196(5) provides that subject to the provisions of this Act, 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.

***No approval of appointment not to invalidate act done by managing director/ whole-time director or manager during his provisional before general meeting.***

### Appointment with the Approval of Central Government

In case the provisions of Schedule V of the Companies Act, 2013 are not fulfilled by company, an application seeking approval to the appointment of a managing director (Whole-time director or manager) shall be made to the Central Government, in e-Form No. MR.2.

#### Issue of General Notice before making Application to Central Government

As per Section 201, before such application is made, there shall be issued by a company a general notice to the members indicating nature of application. The general notice shall be published in at least once in a newspaper in the principal language of the district in which registered office is situated and at least once in English in an English newspaper circulating in that district indicating the nature of application proposed to be made to the Central Government.

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

### Procedure for appointment of Managing Director

Appointment of Managing Director is to be made according to Section 196 and its remuneration should be in accordance with Section 197 and Schedule V of the Companies Act, 2013. Provisions relating to managerial remuneration are not applicable to a private company, government company and Specified IFSC public company.

1. Convene and hold a Board meeting after giving to all the directors due notice as required under Section 173 of the Companies Act, for transacting, *inter alia*, the following business:-
  - (a) take a decision on the person to be appointed as managing director after fully ensuring that he does not suffer from any disqualification in Sections 164, 196, 203, Schedule V and any other provision of the Companies Act;
  - (b) approve the draft agreement to be signed and executed by and between the company and the proposed managing director (it is not mandatory);
  - (c) fix time, date and venue for holding a general meeting of the company;
  - (d) approve notice of the general meeting along with the explanatory statement as required by Sections 101 and 102 of the Act after keeping in mind the requirements of Section 190 of the Act and
  - (e) to authorise company secretary to issue notice of the general meeting on behalf of the Board.
2. Hold the general meeting and get the resolution passed approving appointment of the managing director.
3. In case the appointment of the managing director is not in accordance with the provisions of Schedule V of the Act, the company is required to obtain approval of the Central Government as per Section 201 of the Act.
4. For getting the approval of the Central Government under Section 201 certain formalities are to be complied with:
  - (a) As required by Section 201 of the Act, the Company shall give a general notice to the members of the company indicating the nature of the application proposed to be made, and
  - (b) this notice has to be published at least once in the principal language of the district in which the registered office of the company is situate and circulating in that district and also once in English in an English newspaper also circulating in that district,
  - (c) the company shall attach a copy of this notice with the application together with certificate as to the

due publication thereof.

- (d) The application should be filed electronically in MR – 2 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 accompanied by the prescribed fees.
- (e) The application should be made within 90 days from the date of such appointment.

Details of proposal need to be entered along with certain attachments as given below:

- i. Copy of the calculation sheet of effective capital;
  - ii. Copy(ies) of Board Resolutions;
  - iii. Copy of resolution of Nomination and Remuneration Committee along with its composition and certificate by the nomination committee that the remuneration is as per remuneration policy of the company;
  - iv. Copy of shareholders resolution;
  - v. certificate from auditor or company secretary of the company or company secretary in practice with regard to compliance of Section 196;
  - vi. Certificate of no default in repayment of debts for continuous period of thirty days in the preceding financial year from a director or company secretary of the company;
  - vii. No objection certificate from the financial institutions or banks to whom the company has defaulted;
  - viii. copy of order of NCLT with scheme of revival of the company;
  - ix. Copy of Draft agreement between the company and the proposed appointee;
  - x. Newspaper clipping of notices published under section 201
  - xi. Copy of visa or passport in case the proposed appointee is foreign national;
  - xii. Copies of education or professional qualification certificate;
  - xiii. Statement as per item (iv) of third proviso of section II of Part II of Schedule V to the Companies Act, 2013
  - xiv. Projections of the Turnover and net profits for next three years;
  - xv. Calculation of estimated profit under section 198 of the Act;
  - xvi. An application under Section 460 of the Act for condonation of delay;
  - xvii. Full and proper justification in favour of the proposal along with bio-data of the appointee;
  - xviii. Documentary proof regarding compliance of the provisions of Section 196 of the Companies Act, 2013 at the time of appointment/ re-appointment of the proposed appointee;
  - xx. Certificate by the secretary of the company or CA/CS in whole time practice to be notified erstwhile;
  - xxi. Details, if Applicant Company is a subsidiary of listed company;
  - xxii. Certificate from CA/CS in whole time practice along with calculation of excess remuneration paid to the appointee;
5. Execute the agreement, as approved by the Board, with the managing director.

6. Make necessary entries in the register of directors etc. and other records and registers of the company.

7. File the following documents with the ROC:

- (a) The company should file with the ROC return of appointment of the managing director in Form MR - 1, within sixty days as per Section 196(4) of the appointment and the return must be certified by the auditors of the company or the company secretary or a secretary in whole-time practice. The Mandatory attachments for Form MR – 1:
  - i. Copy of Board Resolution,
  - ii. Copy of Shareholders Resolution
  - iii. Copy of letter of consent to act as managing director
  - iv. Copy of Central Government Approval
  - v. Copy of certificate by nomination and remuneration committee
- (b) Form DIR – 12 is to be filed with registrar for particular of appointment of a key managerial personnel, within thirty days of the appointment.
- (c) Form MGT – 14 for special resolution is to be filed with registrar within thirty days of the appointment.

8. Inform all concerned about the appointment of the managing director. It is advisable to issue a general notice in newspapers about the appointment of the managing director.

#### **Appointment of a Person as Managing Director, who is Managing Director of Another Company**

According to Section 203(3) of the Companies Act, 2013, Whole-time key managerial personnel shall not hold office in more than one company except in its subsidiary company at the same time.

A company may appoint or employ a person as its managing director, if he is the managing director or manager of one, and of not more than one, other company and such appointment or employment is made or approved by a resolution passed at a meeting of the Board with the consent of all the directors present at the meeting and of which meeting, and of the resolution to be moved thereat, specific notice has been given to all the directors then in India.

The procedure shall remain same as discussed earlier but notice for the board meeting shall be a special notice to all the directors then in India.

#### **OFFICER WHO IS IN DEFAULT**

##### **Officer [Section 2(59)]**

“officer includes any director, manager or key managerial personnel 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.”

##### **Who is an “Officer who is in Default” [Section 2(60)]**

As per Section 2(60), “officer who is in default”, for the purpose of any provision in this 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;
- (iii) where there is no key managerial personnel, such director or directors as specified by the Board in this behalf and who has or have given his or their consent in writing to the Board to such specification, or all the directors, if no director is so specified;
- (iv) any person who, under the immediate authority of the Board or any key managerial personnel, is charged with any responsibility including maintenance, filing or distribution of accounts or records, authorises, 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, other than a person who gives advice to the Board in a professional capacity;
- (vi) every director, in respect of a contravention of any of the provisions of this Act, who is aware of such contravention by virtue of the receipt by him of any proceedings of the Board or participation in such proceedings without objecting to the same, 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.

## COMPANY SECRETARY APPOINTMENT, ROLE AND RESPONSIBILITIES

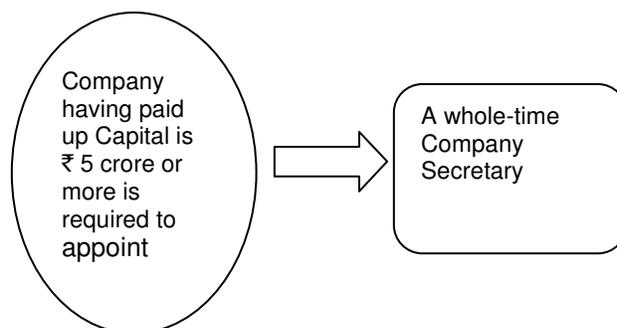
### Who can be a Company Secretary?

Section 2(24) of the Companies Act, 2013 defines “company secretary” or “secretary” means a company secretary as defined in clause (c) of sub-section (1) of section 2 of the Company Secretaries Act, 1980 who is appointed by a company to perform the functions of a company secretary under this Act.

According to clause (c) of Sub-section (1) of Section 2 of the Company Secretaries Act, 1980, a company secretary means a person who is a member of the Institute of Company Secretaries of India.

Therefore, ‘Company Secretary’ means a person who is a member of the Institute of Company Secretaries of India (ICSI) and who is appointed by a company to perform the functions of a company secretary. The functions of company secretary have been detailed in section 205 of the Act.

**Rule 8A of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 provides for mandatory appointment of whole time company secretary** in companies having a paid up share capital of five crore rupees or more.



## Role & Responsibilities of Company Secretary

A company secretary is an officer of the company responsible for compliance by the company with the provisions of the Companies Act, 2013 and various other corporate, taxation, industrial and economic laws applicable to companies in general.

Under the Companies Act, the role of a secretary is three-fold, viz., as a statutory officer, as a co-ordinator and as an administrative officer if so authorized. Similarly, the responsibility of company secretaries extends not only to a company, but also to its shareholders, depositors, creditors, employees, consumers, society and government.

The role of a company secretary may conveniently be studied from three different angles:

- (a) as a statutory officer,
- (b) as a co-ordinator,
- (c) as an administrative officer.

**(a) Statutory Officer:** The company secretary is an officer responsible for compliance with numerous legal requirements under different Acts including the Companies Act, 2013 as applicable to companies. The responsibilities of company secretary has also increased as he has been included in the definition of Key Managerial Personnel as defined in section 2(51) of the Act, who are also liable to punishment by way of imprisonment, fine or otherwise for violation of the provisions of the Companies Act which hold the “officers in default” under Section 2(60).

Company Secretary is one of the key managerial personnel of a company. All companies (including Private Companies) are required to appoint Company Secretary in whole time employment whose paid up Share Capital is five crore rupees or more. However, Company Secretary is not a ‘managerial personnel’ for purpose of restriction on remuneration under section 197 of Companies Act, 2013. His salary is not considered for purpose of computation of ‘managerial remuneration’ under section 197 of the Companies Act, 2013, unless he is also a director of the company.

The various provisions and rules framed under the Companies Act make it obligatory for the secretary to sign the annual return filed with the Registrar [Section 92], to sign financial statements [Section 134(1)] duty to report fraud [Section 143(12)] and to make declaration under Section 7(1) of the Act before incorporation of a company confirming that all the requirements of Act and the Rules there under have been complied with in respect of registration of a company and the Registrar may accept such a declaration as sufficient evidence of such compliance.

Under Regulation 18(1)(e) of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 the Company Secretary shall act as the secretary to the Audit Committee in case of a listed company.

Under the Indian Stamp Act it is the duty of a secretary to see that the documents such as letter of allotment, share certificate, debentures, and mortgages are issued duly stamped. He is the principal officer under Section 2(35) of the Income Tax Act, 1961.

The most important task of the company pertaining to statutory and legal obligations comes upon the secretary. Under the Companies Act, he has either to comply with the various provisions of the Act or is liable to be fined or imprisoned for non-compliance of his obligations.

Thus the responsibility of a secretary as a statutory officer has been greatly expanded by enactment of various economic statutes, like Competition Act, Foreign Exchange Management Act, SEBI Act, Security

Contracts (Regulation) Act, 1956 and Depositories Act. Accordingly, the numerous provisions which a Company is obliged to comply with, makes the secretary's job onerous and difficult. The duties imposed upon a secretary by various statutes clearly indicate the important place he occupies in the corporate administrative hierarchy.

**(b) Co-ordinator:** On dealing with the Board functions, Peter Ferdinand Drucker<sup>1</sup> say — “But there are real functions which only a Board of directors can discharge”.

The Board cannot function without proper coordination amongst various department of the company and communication of their proposals and project which deserve consideration of the board.

In India, most companies have an increasing dependence on the financial institutions for assistance. Every big sized project involves assistance from the financial institutions. These institutions expect the Board of directors to oversee the overall management and performance of the assisted companies and for this purpose, would insist on all basic policy issues to be discussed at the Board meetings and decisions reached. For this purpose, it would be necessary for the company's management to place all the salient features and information before the Board in order that they can arrive at a proper decision.

This is evidenced by the various conditions imposed in the loan agreements entered into between the financial institutions and the assisted companies. Company managements look to the company secretary for implementation of the conditions in the loan agreements.

The financial institutions stipulate that in the case of companies assisted by them financially, compliance certificate as per their format duly certified by the company secretary should be furnished periodically at the Board meetings.

Furnishing of the certificate requires skill of coordination between the company secretary and the functional heads and the factory manager.

The Company Secretary as a co-coordinator has an important role to play in administration of the company's business and affairs. It is for the secretary to ensure effective execution and implementation of the management policies laid out by the Board. The position that the company secretary occupies in the administrative set-up of the company makes his function as one of co-coordinator and link between the top management and other levels. He is not only the communicating channel between the Board and the executives but he also co-ordinates the actions of other executives *vis-a-vis* the Board. The ambit of his role as a co-coordinator also extends beyond the Company and he is the link between the Company and its shareholders, the society and the Government. Thus, the role of a company secretary as a co-coordinator has two aspects, namely internal and external. The internal role of a co-coordinator extends to the Board including the Chairman and Managing Director, various line and staff personnel, the trade unions and the auditors of the company. His role as an external co-ordinator extends to the relationship of the company with shareholders, Regulators, Government and Society.

## GUIDANCE AND ASSISTANCE TO BOARD

Rule 10 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, provide that a company secretary shall provide to the directors of the company, collectively and individually, such guidance as they may require with regard to their duties, responsibilities and process.

Whilst the Directors discuss and decide policy matters as a body, the Secretary is responsible for

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<sup>1</sup> The Practice of Management, Peter F. Drucker, Page 154, Classic Drucker Collection edition, 2007 Routledge Publication, New York

transmitting the policies and decisions of the Board, to all levels in the company and outsiders. His duties in relation to the Board include amongst others

- (i) Facilitating the convening of meetings, Board, General and committee meetings, drafting out the minutes and reports.
- (ii) Keeping the Board informed as an advisor on matters regarding legal, financial and other laws and problems as far as they relate to the company. This will include advising the Board of the various obligations imposed on the directors by various statutes, including changes in laws which will have a bearing on the activities of the company.
- (iii) He must ensure that all decisions taken by the Board are in consonance with legal requirements, and the powers they exercise do not require approval of the shareholders, Central Government or any other authority.
- (iv) Since meetings of the Board are confidential in nature, he should ensure secrecy regarding matters discussed at such meetings.

According to Section 205(1)(b) the company secretary shall ensure the compliance with secretarial standards issued by the Institute of Company Secretaries of India constituted under section 3 of the Company Secretaries Act, 1980 and approved by the Central Government.

Whilst the Board decides on policy matters, the day-to-day administration of companies is vested in the managing director, if there is one. In other cases, where the company is a board managed company, i.e. where none of the directors is a managing director or a whole-time director, the Secretary has to seek guidance and instructions from the Chairman on all important matters. He must, however, ensure that a Chairman who is not a managing director does not exercise substantial powers of management as he will be deemed to be a managing director within the meaning of the Act and, therefore, his appointment and remuneration will require the approval of the shareholders and the Central Government, if necessary. Where, however, the company has a managing director, he must seek his guidance and instructions regarding implementation of the policies laid down by the Board and also on matters arising out of the implementation of the decisions. He is also required to keep the chairman and managing director apprised of changes in policies of the Government, obligations under various statutes and to give balanced advice on matters which have legal ramifications.

As per Rule 10, he has to assist and advise the Board in ensuring good corporate governance and in complying with Corporate Governance requirements and best practices.

## **RELATIONSHIP WITH OTHER FUNCTIONARIES**

We have seen that the Secretary is responsible for conveying the Board's decisions on various aspects of the company's policies to the person in-charge of such functions. He is, in addition, responsible to ensure that the returns and reports received from various operational executives are submitted in time, complete in all respects, and do not conflict with the corporate objectives.

Even where different persons are in-charge of other functions, e.g., sales, personnel, etc., it is usually the Secretary who communicates with outside agencies, particularly with government and semi-government bodies to ensure that the information given to various agencies do not conflict with each other and are in accordance with the corporate objectives of the organisation.

## **TRADE UNION(S)**

Where the Secretary is responsible either directly or through his assistants with industrial relations, he must

exercise extreme caution while dealing with Trade Union officials whether they belong to recognised unions or not. He must ensure that proper notes are kept of the discussions and negotiations and all decisions arrived at during such negotiations. Whenever long-term settlement with recognised unions are finalised he should see that the agreement embodying these settlements are in accordance with the relevant statutes applicable.

It is the responsibility of the Secretary through the Human Relations/Industrial Relations to ensure compliance with the provisions of various labour legislations such as Industrial Disputes Act, 1947, Employees' Provident Funds and Miscellaneous Provisions Act, 1952, Payment of Bonus Act, 1965, Payment of Gratuity Act, 1972, Payment of Wages Act, 1936, etc.

In many companies, there is a system whereby a compliance report is submitted to the Board at every meeting confirming that there has been no delay in the compliance with the statutory formalities like deposit of Provident Fund Money, E.S.I. Contribution etc.

Whilst he must ensure that the employees guilty of misconduct are charge-sheeted and punished, he must simultaneously ensure that all formalities, e.g., holding of enquiries etc., must also be scrupulously followed. He should ensure that industrial labor relations are always cordial and he should take steps to further ensure that various creative activities of the employees are encouraged wherever possible by grants and subsidies from the company.

## **AUDITORS**

Apart from the statutory audit, services of the company's auditors are required for certifications required under various statutes and, therefore, the Secretary must liaise very closely with the auditors. It may be pointed out that copies of minutes of Board meetings and general meetings should be made available for the inspection of the auditors during the statutory annual audit. He is to ensure that before their appointment, proper certificate is obtained under Section 141(3)(g) of the Companies Act, 2013. The company secretary, on behalf of the company is required to file a notice with the Registrar about appointment within 15 days of the annual general meeting.

Further, with regard to Secretarial audit, section 204(2) provides that it shall be the duty of company to give all assistance and facilities to Company Secretaries in practice for auditing the secretarial and related records

## **SHAREHOLDERS**

The relationship with the shareholders is an important sphere of his co-ordinating role and, therefore, the Secretary will have to maintain proper relationships with the shareholders of the company.

He should ensure that there is no delay in the inspection of books and registers required by a shareholder provided all formalities are complied with. He must ensure that extracts of registers demanded by shareholders are furnished to them within the prescribed time.

However, the most important thing for a Secretary is to ensure that all correspondence from shareholders is dealt with promptly and their queries are answered as far as possible keeping the statutory provisions in mind. As part of public relations, he should be able to give time without prior notice to shareholders who personally come for information, to furnish documents or any other matter. He must also ensure that requests for issues of duplicate certificates/dividend warrants and intimation of address are dealt with properly and promptly. This is important as the image of the company will, to a great extent, depend on the relationship of the Secretary with the shareholders.

**Bridge between IEPF and members:**

The company secretary acts as nodal officer of the company for the purpose of reclaiming shares by members from the Investor Education and Protection Fund. The company secretary shall verify with the record claim of an applicant to reclaim his shares from IEPF.

**GOVERNMENT**

All the information and correspondence with the government are normally co-ordinated or routed through the Secretary to ensure uniform reporting. The Secretary has a very important role vis-a-vis the government. He should endeavour to have information on government policies and programmes in advance wherever possible to ensure effective implementation. Good relationship with the Government can be developed where the company sincerely tries to implement various statutes in letter as well as in spirit.

**COMMUNITY**

Section 135 of the Act provides for spending of specified amount for Corporate Social Responsibility. Corporate Social Responsibility of a company has become very important since the company is expected to fulfill certain obligations to the society in which it functions. With this in view, a number of companies have undertaken rural development initiatives including adoption of villages and have built schools, colleges and hospitals to cater to the needs of society. In respect of companies in consumer goods industry, it is necessary to project that the products and their prices are in consonance with the standards expected by the consumers.

Arising out of such social responsibility, many companies have also allowed small sectors to manufacture ancillaries and raw materials required by the organisation for promotion of employment opportunities. The provisions of the Consumer Protection Act, 1986, the Pollution Control Laws, Public Liability Insurance Act 1991, etc., are important in the operations of companies and the role of Company Secretaries in these areas is quite important.

The principal duty of a secretary as an administrator is to ensure that the activities of a company are in conformity with the company's policy. In his role as an administrator, the secretary provides the very foundation on which the entire structure of company administration is constructed.

**(C) Administrator**

The role of a company secretary as an administrator can be sub-divided into organisational, financial, office and personnel administration.

**ORGANIZATIONAL ADMINISTRATION**

Since the secretary has an opportunity of looking at the entire organisation, he has the scope to advise the top management including the Board of directors on the need to develop a good structure. Since the secretary collects, interprets and assimilates information relating to all aspects of business to aid and assist the Board in carrying out its function, he, therefore, gets an opportunity to know the strengths and the weaknesses of the functional executives.

In his role as administrator, wherever applicable he has to make a detailed analysis of various activities, decision making machinery, inter-departmental relationship and their functioning. He has, therefore, to ensure that the organisational structure is always under constant study. The making of such examination and study and the consequent advice and recommendation for making changes is a task which the company secretary has to perform.

## **FINANCIAL ADMINISTRATION**

Since various monthly and periodical operating reports and financial statements are routed for consideration of the board through the secretary, he should analytically study these statements. Thus, as a secretary to the board, the Company Secretary in consultation with the Finance Manager has to devise suitable and proper systems of accounting procedure, internal control and internal audit with a view to safeguarding the company's funds. The Company Secretary should have a good knowledge of budgetary control and procedures, accounts and other related matters. He is also expected to be proficient in dealing with matters connected with taxation.

The Company Secretary is generally assisted by the Chief Accountant in the discharge of his functions relating to financial administration. In many companies, the Secretary is also the Chief Accountant. He has to negotiate with banks and financial institutions the terms of finance both for working capital requirements and capital expenditure.

## **TAX ADMINISTRATION**

Company Secretary deals with tax administration of the company. Tax administration does not restrict to accounting transactions only. Tax administration involves in tax planning, utilization of input credits, assessment and appeals. The company secretary with the help of accounts and legal teams ensure proper tax administration for the organization.

## **OFFICE ADMINISTRATION**

In all big companies, the office administration is carried on by a departmental head or an officer who generally reports to the Company Secretary. It is the duty of the Secretary to ensure that different departments of the office are properly staffed, organised, co-ordinated and supervised.

He has to review from time to time the various procedures and systems with a view to making the administration effective. He is also responsible in most organisations for office services including transport. The image of a company depends on the design and office layout from the reception to the records.

The Secretary has not only to ensure that these services are maintained and improved but to also ensure that the cost of such services is reviewed from time to time.

## **PERSONNEL ADMINISTRATION**

Personnel administration includes recruitment, training, remuneration, promotion retirement, discharge and dismissal of staff. This is a very important yet difficult task to administer. Whilst in large organisations there may be a separate personnel or Human Resources Manager or Officer, in smaller companies the Secretary may be called upon to advise and assist the directors on principles and legal points involved in this area of administration.

The Company Secretary should ensure that implication of new rules, orders, in this field of management are advised to all concerned for effective implementation.

## **ADMINISTRATION-COMPANY'S PROPERTIES**

The secretary has an important role to play in safeguarding the company's interest in property matters. He has to ensure that all properties are properly maintained and insured and maintain a suitable register for each property containing relevant information. He should have a good knowledge of relevant rules and bye-laws applicable to property. He should also ensure that registration of trademarks, patents, licenses or other intellectual property rights are done from time to time and take legal action in respect of infringement of such rights.

## MAINTENANCE OF RECORDS OF COMPANY

The Secretary is required to maintain certain other records in addition to those specified under the Companies Act. The volume, method and procedure will vary with the size and nature of the company.

The secretary also has to ensure that the statutory time limits relating to directors' and shareholders' meetings, payment of dividend and interest, filing of returns under the Companies Act, 2013, Income-tax Act and Sales Tax Act, etc., renewals of contracts and leases and the formalities under stock exchange and SEBI regulations and the listing agreements are complied with.

## ENSURING ADEQUACY OF SYSTEMS OF SAFETY AND SECURITY

The secretary has to ensure that adequate systems of safety and security of personnel based on technical advice are available in the factory and office. He is also responsible for devising and maintaining systems to safeguard the valuable company records, or information against loss, theft, fire, etc. He is to review these from time to time to ensure that the properties of the company are adequately insured. The company secretary should have good knowledge of insurance law and practice.

Whilst the above discussion only gives a brief outline, the duties and responsibilities of the company secretary are subject to continuous change and therefore, has to be reviewed from time to time to ensure that he effectively contributes in respect of the above matters. He should, therefore, keep himself abreast with legal changes and practices

## STATUTORY DUTIES AND LIABILITIES OF A COMPANY SECRETARY

Apart from general secretarial duties with regards to organizing Board and general meetings, keeping minutes of meeting, recording approved share transfers, corresponding with directors and shareholders, maintaining statutory records, filing necessary returns with Registrar of Companies etc., the Companies Act, 2013 has also prescribed some duties and authorities, which are as follows—

### 1. *Declaration regarding compliance with requirement of registration*

In terms of section 7(1)(b) of the Companies Act, 2013, a company gets incorporated by submitting memorandum and articles duly signed along with a declaration in a prescribed form that all requirements of Act and rules have been complied with in respect of registration of company. Such declaration in prescribed form can be signed by an Advocate, a chartered accountant, cost accountant or company secretary in practice who is engaged in the formation of the company and by a person named in the articles as a director, manager or secretary of the company.

2. ***Authentication of documents, proceedings and contracts*** Authentication is more than simply attestation. Authentication is attestation made by proper officer by which he certifies that a record is in due form of law and that the person who certifies is the officer appointed to do so. A document or proceeding requiring authentication by a company or contract made by or on behalf of a company may be signed by any key managerial personnel or an officer of the company duly authorized by the Board in this behalf. [Section 21]

However, in case of Specified IFSC public and private company, the document or proceeding requiring authentication by a company or contract made by or on behalf of a company may be signed by any key managerial personnel or an officer or any other person of the company duly authorized by the Board in this behalf.

In case, a company does not have a common seal, the requirement of law would be complied with if the

authorization is done by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary.

### **3. Signing share certificate**

Share certificates of the company should be signed by two directors (out of which one should be Managing Director or whole time director, if appointed) and Secretary or other person authorized by Board.

### **4. Signing annual return**

Annual return to be filed with Registrar of Companies has to be signed by a director and Company Secretary. If Company does not have Company Secretary, the return can be signed by company secretary in practice. [Section 2(1)]

### **5. Signing of financial statements**

The financial statement, including consolidated financial statement is to be signed on behalf of the Board by the chairperson of the company where he is authorised by the Board or by two directors out of which one shall be managing director, if any, and the Chief Executive Officer, the Chief Financial Officer and the company secretary of the company, wherever they are appointed. [Section 134(1)]

### **6. Appear before NCLT**

A Company Secretary can appear before National Company Law Tribunal (NCLT) on behalf of the company. [Section 432]

### **7. Secretary as Compliance Officer of listed company**

As per clause (1) of Regulation 6 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, a listed company is required to appoint the company secretary to act as 'Compliance Officer', who will be responsible for the following –

- (a) ensuring conformity with the regulatory provisions applicable to the listed entity in letter and spirit.
- (b) co-ordination with and reporting to the Board, recognised stock exchange(s) and depositories with respect to compliance with rules, regulations and other directives of these authorities.
- (c) ensuring that the correct procedures have been followed that would result in the correctness, authenticity and comprehensiveness of the information, statements and reports filed by the listed entity.
- (d) monitoring email address of grievance redressal division as designated by the listed entity for the purpose of registering complaints by investors.

### **8. Demat shares**

Secretary has to coordinate between depository and stock exchange in case of demat shares.

### **9. Additional duties**

In addition to statutory duties of company secretary, he is often entrusted with additional duties like looking after legal matters, personnel matters, finance and sometime even general administration.

### **10. Nodal Officer**

Company secretary has to perform duty of nodal officer under IEPF Rules. He shall verify all applications

filed to reclaim shares from IEPF.

### **Liabilities of Company Secretary**

Company Secretary has been defined as 'Officer in default' along with Managing Director, Manager and Wholetime Director etc. Thus, he can be punished in respect of offences under Companies Act. He may be held liable as Key Managerial Personnel also under various provisions of the Act.

### **Summons to company in civil matters can be served on a Secretary**

As per rule 2 of order 9 of Code of Civil Procedure, in case of suit against a corporation, summons can be served on –

- (a) Company Secretary, Director or other principal officer of the corporation or
- (b) By leaving it or by sending by post to registered office of the corporation. However, validity of this provision has been upheld in *Jute & Gunny Brokers v. UOI* (1962) 32 Comp Cas 845 (SC).

### **Procedure for Appointment of a Company Secretary [Section 203 read with Rule 8A of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014]**

Since company secretary is one among the key managerial person, the procedure of appointment of company secretary would be similar to appointment of all other key managerial person.

As per Rule 8A of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, every company having a paid-up share capital of Rupees five crore or more is required to have a whole time company secretary.

Only an individual, who is a Company Secretary within the meaning of clause (c) of sub-section (1) of section 2 of the Company Secretaries Act, 1980 or who possesses the prescribed qualifications, can be appointed as secretary of the company. The Companies (Appointment and Qualification of Secretary Rules), 1988 contain the prescribed qualifications.

#### **The following procedural steps should be taken for appointing a whole-time company secretary:**

1. Advertise the post, collect applications, hold interview, short list the individuals for the position and finalise the terms of appointment.
2. Convene a Board meeting after giving notice to all the directors of the company as per section 173 of the Act. At the board meeting, place the proposal of appointing Company Secretary with the details of the person finalized and pass a resolution appointing the company secretary and approving the terms and conditions of his appointment.
3. File return of appointment of company secretary with the Registrar in Form DIR.12 within thirty days from the date of appointment (date of joining office) and Form MGT.14 is also required to be filed along with such fee as specified in Companies (Registration of Offices and Fees) Rules, 2014. The particulars of Company Secretary, Income-tax PAN, Membership details (will be validated from ICSI records), residential details, date of appointment, e-mail ID of the person for communication purpose are required to be filled in the Form.
4. A Company Secretary shall not hold office in more than one company except in its subsidiary company at the same time.
5. Make entries in the Register of directors and key managerial personnel under Section 170 of the Act.
6. Inform the Stock Exchange(s) where the company is listed.

7. Since key managerial personnel are included in 'related party' as defined in section 2(76) of the Act, Please verify whether the company secretary so appointed involved in any related party transactions within the provisions of Section 188 of the Act. If yes, then comply with the requirements in this regard.

## REMOVAL OF COMPANY SECRETARY

A company secretary can be removed or dismissed like any other employees of the organization. Since he is appointed by Board, the Board of directors of a company has absolute discretion to remove a company secretary or to terminate his services at any time for any reason or without any reason. However, principles of natural justice like show cause notice, hearing, reasoned order etc. must be followed.

### Procedure for removal/resignation of Company Secretary

1. A Company Secretary can be removed in accordance with the terms of appointment and the Board can record the same.
2. Convene a Board meeting after giving notice to all the directors of the company as per section 173, place the matter of removal/resignation of the Company Secretary and pass a resolution to the effect.
3. File Form DIR-12 in electronic mode within thirty days with the Registrar of Companies together with requisite filing fees. Evidence of Cessation (for example Resignation Letter) is an optional attachment.
4. Inform the stock exchange where the company is listed.
5. Make entries in the Register maintained for recording the particulars of Company Secretaries under section 170.
6. Issue a general public notice, if it is so warranted, according to size and nature of the company.
7. The resulting vacancy shall be filled up by the Board at a meeting of the Board within a period of six months from the date of such vacancy

## FUNCTIONS OF COMPANY SECRETARY

### Functions of Company Secretary

According to Section 205 the functions of the company secretary shall include,—

- (a) to report to the Board about compliance with the provisions of this Act, the rules made thereunder and other laws applicable to the company;
- (b) to ensure that the company complies with the applicable secretarial standards;
- (c) to discharge such other duties as may be prescribed.

*Explanation.*—For the purpose of this section, the expression “secretarial standards” means secretarial standards issued by the Institute of Company Secretaries of India constituted under section 3 of the Company Secretaries Act, 1980 and approved by the Central Government.

### Duties of Company Secretary

Clause (c) of sub-section (1) of section 205, the Central Government has prescribed that the duties of Company Secretary shall also include-

- (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 meetings, the Government and such other authorities as required under the provisions of the Act;
- (4) to represent before various regulators, Tribunal and other authorities under the Act in connection with discharge of various functions 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; and
- (7) to discharge such other duties as may be assigned by the Board from time to time;
- (8) such other duties as have been prescribed under the Act and Rules.

Section 205(2) provides that provisions contained in section 204 and section 205 shall not affect the duties and functions of the Board of Directors, chairperson of the company, managing director or whole-time director under this Act, or any other law for the time being in force.

## REMUNERATION OF MANAGERIAL PERSONNEL

### MANAGERIAL REMUNERATION

Just as profits drive business, incentives drive the managers of business. Not surprisingly then, in a fiercely competitive corporate environment, managerial remuneration is an important piece in the management puzzle. While it is important to incentivize the workforce performing the challenging role of managing companies, it is equally important not to go overboard with the perks and the pay. In India, to keep a check on unnecessary profit squandering by companies and, at the same time, to ensure adequate and reasonable compensation to managerial personnel, the law intervenes to do the balancing act.

### OVERALL MAXIMUM MANAGERIAL REMUNERATION

Section 197 of the Companies Act, 2013, lays down the provisions for overall maximum managerial remuneration and managerial remuneration. The overall managerial remuneration to the Directors including managing director, whole time director and manager is summarized as under:

S. No.	Persons entitled for remuneration	Maximum remuneration in any financial year	If remuneration exceeds maximum remuneration in any financial year as provided under column (b)
	(a)	(b)	(c)
(i)	Directors including managing director, whole time director and manager of public companies	11% of the net profits of the company for that financial year	Company in general meeting subject to provisions of Schedule V may pay remuneration in excess of 11% of the net profits of the company.

(ii)	One Managing director/ Whole time director/ manager	5% of the net profits of the company for that year	With the approval of the company in general meeting this limit may be exceeded.
(iii)	More than one Managing director/ Whole time director/ manager	10% of the net profits	With the approval of the company in general meeting this limit may be exceeded.
(iv)	Directors who are neither Managing director nor whole time directors	1% of the net profits of the company if there is a managing director or a whole time director	Approval of the company in general meeting is required.
(v)	Directors who are neither Managing director nor whole time directors	3% of the net profits of the company if there is no managing director or whole time director	Approval of the company in general meeting is required.

Where the company has defaulted in payment of dues to any bank or public financial institution or 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.

After the exemption notification dated 05.06.2015, in case of Nidhi company, Section 197 (1) shall apply with modification which is as under-

Remuneration of a director who is neither managing director nor whole time director or manager for performing special services to the Nidhis specified in the articles of association may be paid by way of monthly payment subject to the approval of the company in general meeting and also to the provisions of section 197:

Provided that no approval of the company in general meeting shall be required where,-

- (a) a Nidhi does not have a managing director or a whole-time director or a manager;
- (b) the remuneration payable during a financial year to all the directors of the Nidhi does not exceed ten per cent of the net profits of such Nidhi or fifteen lakh rupees, whichever is less; and
- (c) a remuneration payable under clause (b) is approved by a special resolution passed in this behalf by the Nidhi.

Second proviso to Section 197(1) limits the remuneration payable to directors who are neither managing directors nor whole-time directors to one percent of the net profits of the company, if there is a managing or whole-time director or manager; three percent of the net profits in any other case. However, Nidhi companies are allowed to pay remuneration to directors who are neither managing directors nor whole-time directors, for performing special services subject to conditions as laid down.

**In case of Government Company**

After the exemption notification dated 05.06.2015 provisions of Section 197 shall not apply to Government Company.

**In case of Specified IFSC Public Company**

After the exemption notification dated 04.01.2017 provisions of Section 197 shall not apply to Specified IFSC Public Company.

Section 197(1) also states that the net profits shall be computed in the manner laid down in section 198 except that the remuneration of the directors shall not be deducted from the gross profits.

**MANAGERIAL REMUNERATION WHEN THERE ARE NO PROFITS OR PROFITS ARE INADEQUATE [SECTION 197(3) & (11)]**

- (a) If in any financial year, a company has no profits or its profits are inadequate, the company shall not pay by way of remuneration any sum exclusive of sitting fees to its directors, including any managing or whole-time director or manager except in accordance with the provisions of Schedule V.
- (b) If the company is not able to comply with such provisions of Schedule V in the above case, then previous approval of the Central Government shall be taken.
- (c) In cases where Schedule V is applicable on grounds of no profits or inadequate profits, any provision relating to the remuneration of any director which purports to increase or has the effect of increasing the amount thereof, whether the provision be contained in the company's memorandum or articles, or in an agreement entered into by it, or in any resolution passed by the company in general meeting or its Board, shall not have any effect unless such increase is in accordance with the conditions specified in that Schedule.

**REMUNERATION PAYABLE BY COMPANIES HAVING NO PROFIT OR INADEQUATE PROFIT WITHOUT CENTRAL GOVERNMENT APPROVAL (SCHEDULE V- PART II -SECTION II)**

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 under (A) and (B) given below:-

(A):

(1)	(2)
<i>Where the effective capital is</i>	<i>Limit of yearly remuneration payable shall not exceed</i>
(i) Negative or less than ₹5 crore	₹60 Lakhs
(ii) ₹5 crore and above but less than ₹100 crore	₹84 Lakhs
(iii) 100 crore and above but less than ₹500 crore	₹120 Lakhs
(iv) ₹500 crore and above	₹120 lakhs plus 0.01% of the effective capital in excess of ₹500 crore

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

*Explanation.*- It is hereby clarified that for a period less than one year, the limits shall be pro-rated.

**(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 specialised knowledge in the field in which the company operates:

Provided that 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;

Provided further that the limits specified under items (A) and (B) of this section shall apply, if-

(i) payment of remuneration is approved by a resolution passed by the Board and, in the case of a company covered under sub-section (1) of section 178 also by the Nomination and Remuneration Committee;

(ii) the company has not committed any default in repayment of any of its debts (including public deposits) or debentures or interest payable thereon for a continuous period of thirty days in the preceding financial year before the date of appointment of such managerial person and in case of a default, the company obtains prior approval from secured creditors for the proposed remuneration and the fact of such prior approval having been obtained is mentioned in the explanatory statement to the notice convening the general meeting;

(iii) an ordinary resolution or a special resolution, as the case may be, has been passed for payment of remuneration as per the limits laid down in item (A) or a special resolution has been passed for payment of remuneration as per item (13), at the general meeting of the company for a period not exceeding three years.

(iv) a statement along with a notice calling the general meeting referred to in clause (iii) is given to the shareholders containing the following information, namely:-

*I. General information:*

- (1) Nature of industry
- (2) Date or expected date of commencement of commercial production
- (3) In case of new companies, expected date of commencement of activities as per project approved by financial institutions appearing in the prospectus
- (4) Financial performance based on given indicators
- (5) Foreign investments or collaborations, if any.

*II. Information about the appointee:*

- (1) Background details
- (2) Past remuneration
- (3) Recognition or awards
- (4) Job profile and his suitability
- (5) Remuneration proposed
- (6) 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)

- (7) Pecuniary relationship directly or indirectly with the company, or relationship with the managerial personnel, if any.

### III. Other information:

- (1) Reasons of loss or inadequate profits
- (2) Steps taken or proposed to be taken for improvement
- (3) 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 statements:

- (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; and
- (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.

### **REMUNERATION PAYABLE BY COMPANIES HAVING NO PROFIT OR INADEQUATE PROFIT WITHOUT CENTRAL GOVERNMENT APPROVAL IN CERTAIN SPECIAL CIRCUMSTANCES: (SCHEDULE V- PART II -SECTION III)**

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 and that other company is either a foreign company or has got the approval of its shareholders in general meeting to make such payment, and treats this amount as managerial remuneration for the purpose of section 197 and 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 seven 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 Board for Industrial and Financial Reconstruction for a period of five years from the date of sanction of scheme of revival, or
  - (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 National Company Law Tribunal:

Provided that the limits under this Section 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 this Section, the managerial person is not receiving remuneration from any other company;
- (ii) the auditor or Company Secretary of the company or where the company has not appointed a Secretary, a Secretary in whole-time practice, 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 sub-section (4) of section 196.
- (iii) the auditor or Company Secretary or where the company has not appointed a secretary, a secretary in whole-time practice 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 Special Economic Zone 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 per annum.

#### **Remuneration to Directors in other Capacity [Section 197(4)]**

The remuneration payable to the directors including managing or whole-time director or manager shall be inclusive of the remuneration payable for the services rendered by him in any other capacity except the following:

- (a) the services rendered are of a professional nature; and
- (b) in the opinion of the Nomination and Remuneration Committee (if applicable) or the Board of Directors in other cases, the director possesses the requisite qualification for the practice of the profession.

#### **Sitting Fees to Directors for Attending the Meetings [Section 197(5)]**

A director may receive remuneration by way of fee for attending the Board/Committee meetings or for any other purpose as may be decided by the Board. Provided that the amount of such fees shall not exceed the amount as may be prescribed.

The Central Government through rules prescribed that the amount of sitting fees payable to a director for attending meetings of the Board or committees thereof may be such as may be decided by the Board of directors or the Remuneration Committee thereof which shall not exceed the sum of rupees 1 lakh per meeting of the Board or committee thereof.

The Board may decide different sitting fee payable to independent and non-independent directors other than whole-time directors.

Rule 4 of the Companies (Appointment & Remuneration of Managerial Personnel) Rules, 2014 requires that sitting fees of Independent and Women Directors shall not be less than the sitting fees payable to other Directors.

## Monthly Remuneration to Director or Manager

### *Permissible forms of Remuneration*

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. [Section 197 (6)]

### *Independent directors are not entitled to stock options*

An independent director shall not be entitled to any stock option and may receive remuneration by way of fees, reimbursement of expenses for participation in the Board and other meetings and profit related commission as may be approved by the members. [Section 197 (7)]

### *Commission or remuneration from holding or subsidiary company*

Any director who is in receipt of any commission from the company and who is a managing or whole-time director of the company shall not be disqualified from receiving any remuneration or commission from any holding company or subsidiary company of such company subject to its disclosure by the company in the Board's report. [Section 197 (14)]

## Remuneration Drawn in Excess of Prescribed Limit

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 two years or such lesser period as may be allowed by the company, and until such sum is refunded, hold it in trust for the company [section 197(9)]

The company shall not waive the recovery of any sum refundable to it under sub-section 9 mentioned above, unless approved by the company by special resolution within two years from the date the sum becomes refundable.

Provided that where the company has defaulted in payment of dues to any bank or public financial institution or 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. [Section 197 (10)]

## Insurance Premium not part of Remuneration

Where any insurance is taken by a company on behalf of its managing director, whole-time director, manager, Chief Executive Officer, Chief Financial Officer or Company Secretary 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 in relation to the company, the premium paid on such insurance shall not be treated as part of the remuneration payable to any such personnel.

However, if such person is proved to be guilty, the premium paid on such insurance shall be treated as part of the remuneration. [Section 197(13)]

## Disclosure of Remuneration in Board Report

Section 197(14) read with Rule 4 of Companies (Appointment and Remuneration of Managerial Personnel) Rules 2014 provides that 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.

### **Calculation of Net Profit For The Purpose Of Managerial Remuneration (Section 198)**

Section 198 of the Companies Act, 2013 lays down the manner of calculations of net profits of a company any financial year for purposes of Section 197. Sub- Section (2) specifies the sums for which credit shall be given and sub-section (3) specifies the sums for which credit shall not be given while calculating the net profit.

Similarly, sub-section (4)/(5) specifies the sums which shall be deducted/not deducted while calculating the net profit.

### **Recovery of Managerial Remuneration In Certain Cases (Section 199)**

Section 199 of the Companies Act, 2013 provides for recovery of remuneration including stock options received by the specified Managerial Personnel, where the benefits given to them are found to be in excess of what is reflected in the restated financial statements.

It states that without prejudice to any liability incurred under the provisions of this Act or any other law for the time being in force, where a company is required to re-state its financial statements due to fraud or non-compliance with any requirement under this Act and the rules made there under, the company shall recover from any past or present managing director or whole-time director or manager or Chief Executive Officer (by whatever name called) who, during the period for which the financial statements are required to be re-stated, received the remuneration (including stock option) in excess of what would have been payable to him as per restatement of financial statements.

### **Central Government or company to fix limit with regard to remuneration (Section 200)**

In respect of cases where the company has inadequate or no profits, a company may fix the remuneration within the limits specified in the Act. While doing so, the company shall have regard to —

- (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.

As per Rule 6 for the purpose of item (e) of section 200, the company shall have regard to the following matters while granting approval:

- (1) Financial and operating performance of the company during the three preceding financial years.
- (2) Relationship between remuneration and performance.
- (3) The principle of proportionality of remuneration within the company, ideally by a rating methodology which compares the remuneration of directors to that of other executive directors on the board and employees or executives of the company.
- (4) Whether remuneration policy for directors differs from remuneration policy for other employees and if so, an explanation for the difference.
- (5) The securities held by the director, including options and details of the shares pledged as at the end of the preceding financial year.

As per Rule 7(2), the companies other than listed companies and subsidiary of a listed company may without Central Government approval pay remuneration to its managerial personnel, in the event of no profit or inadequate profit beyond ceiling limit specified in Section II, Part II of Schedule V, subject to complying with

the following conditions namely:-

- (i) payment of remuneration is approved by a resolution passed by the Board and, in the case of a company covered under sub-section (1) of section 178 also by the Nomination and Remuneration Committee, if any, and while doing so record in writing the clear reason and justification for payment of remuneration beyond the said limit;
- (ii) the company has not made any default in repayment of any of its debts (including public deposits) or debentures or interest payable thereon preference shares and dividend on preference shares for a continuous period of thirty days in the preceding financial year before the date of payment to such managerial personnel;
- (iii) the approval of shareholders by way of a special resolution at a general meeting of the company for payment of remuneration for a period not exceeding three years;
- (iv) a statement along-with a notice calling the general meeting referred to clause (iii) of sub-rule (2) above, shall contain the information as per sub clause (iv) of second proviso to clause (B) of section II of part-II of Schedule V of the Act including reasons and justification for payment of remuneration beyond the said limit
- (v) the company has filed Balance Sheet and Annual Return which are due to be filed with the Registrar of Companies.

#### **Compensation For Loss Of Office Of Managing Or Whole- Time Director Or Manager (Section 202)**

Section 202 provides that a company may make payment to a managing or whole-time director or manager, but not to any other director, by way of compensation for loss of office, or as consideration for retirement from office or in connection with such loss or retirement.

However, No payment shall be made in the following cases:—

- (a) where the director resigns from his office as a result of the reconstruction/amalgamation of the company and is appointed as the managing or whole-time director, manager or other officer of the reconstructed company/of resulting company from the amalgamation;
- (b) where the director resigns from his office otherwise than on the reconstruction/ amalgamation of the company;
- (c) where the office of the director is vacated due to disqualification;
- (d) where the company is being wound up due to the negligence or default of the director;
- (e) where the director has been guilty of fraud or breach of trust or gross negligence or mismanagement of the conduct of the affairs of the company or any subsidiary company or holding company; and
- (f) where the director has instigated, or has taken part directly or indirectly in bringing about, the termination of his office.

Any payment made to a managing or whole-time director or manager shall not exceed the remuneration which he would have earned if he had been in office for the remainder of his term or for three years, whichever is shorter, calculated on the basis of the average remuneration actually earned by him during a period of three years immediately preceding the date on which he ceased to hold office, or where he held the office for a lesser period than three years, during such period. (Sub-section 3)

Provided that no such payment shall be made to the director in the event of the commencement of the winding up of the company, whether before or at any time within twelve months after, the date on which he ceased to

hold office, if the assets of the company on the winding up, after deducting the expenses thereof, are not sufficient to repay to the shareholders the share capital, including the premiums, if any, contributed by them.

However, Section 202 not prohibit the payment to a managing or whole-time director, or manager, of any remuneration for services rendered by him to the company in any other capacity. (Sub-section 4)

## LESSON ROUND-UP

- Under Section 2(51) a Key Managerial Personnel is defined as the Chief executive officer or managing director or the manager or, a company secretary or the whole time director and the chief financial officer in relation to a company
- Every listed Company having a paid up share capital of ₹ 10 crore or more is compulsorily required to have a key managerial personnel.
- The whole time key managerial personnel is to be appointed by the Board and shall not hold office in more than one company however he is permitted to hold such other office with the permission of Board of the company.
- Every director or the key managerial personnel who is in default shall be punishable with a fine which may extend to 50,000 rupees and a further fine which may be extended to 1,000 rupees for every day during which the default continues.
- The Company secretary has been covered under the same section of KMP i.e. section 203
- Every company secretary is expected to adhere not only to the letter of the law but also ensure that the spirit of the law is followed.
- A Company Secretary exercises supervisory and checking role so as to prevent any chance of negligence in implementing various laws applicable to a particular company.
- Companies Act, through its various sections cast upon company secretary various duties and liabilities called statutory duties and statutory liabilities.
- Role of company secretary is three-fold, namely, as a statutory officer, as a coordinator, and as an administrative officer.

## GLOSSARY

Turnover	"turnover" means the gross amount of revenue recognised in the profit and loss account from the sale, supply, or distribution of goods or on account of services rendered, or both, by a company during a financial year.(Sec 2(91) of Companies Act, 2013
Whole-time director	"whole-time director" includes a director in the whole-time employment of the company; (Sec 2(94) of companies Act, 2013)
<i>Vis-a-vis</i>	in relation to; with regard to.





# Lesson 18

## Meetings of Board and its Committees

### LESSON OUTLINE

- Frequency of the meetings of the Board
- Preparation of notices for meetings of Board/committees of Board
- Agenda of Board/Committees Meetings
- Convening a Meeting
- Quorum for Board Meetings
- Attendance Registers
- Passing of Resolution by Circulation
- Duties of Company Secretary
- Lesson Round up
- Self-Test Questions

### LEARNING OBJECTIVES

As a company secretary you need to guide the members on the conduct of affairs of the company and facilitate the convening of meetings and attend Board and Committee meetings and maintain minutes of these meetings. After reading this chapter you shall learn on the legal provisions relating to meetings of the Board and the procedure role and responsibilities of the officers and directors thereunder.

## **INTRODUCTION**

Meetings of the Board are significant in the light of running of the company more efficiently and effectively. Companies Act, 2013, mandates a company to hold minimal number of meetings of the Board for its proper functioning.

Board meetings are crucial for a company's development as the because of the reason that in these formal meetings are held to devise policies, drive the management, strategize and evaluate the expectations of the stakeholders. For board meetings to be effective they need to:

- have a purpose;
- members must be provided with enough notice and appropriate materials in advance;
- chaired effectively;
- follow proper meeting procedures and respect the time of board members;
- have clear supporting documents such as an agenda, minutes and other reports;
- have action taken reports;
- be documented with minutes.

## **Meetings of the Board [Section 173]**

Section 173 of the Act deals with Meetings of the Board and Section 174 deals with quorum.

### **Frequency of the Meetings of the Board**

The Act provides that the first Board meeting should be held within thirty days of the date of incorporation.

Thereafter there shall be minimum of four Board meetings every year and not more one hundred and twenty days shall intervene between two consecutive Board meetings

Further in this context Secretarial Standard on Board Meetings (SS-1) issued by ICSI clarifies that the Board shall meet at least once in every calendar quarter, with a maximum interval of one hundred and twenty days between any two consecutive Meetings of the Board, such that at least four meetings are held in each calendar year.

SS-1 also states that it shall be sufficient that in the year of incorporation if a company, in addition to the first meeting to be held within thirty days of the date of incorporation, holds one meeting in every remaining calendar quarter in the year of incorporation.

In case of One Person Company (OPC), small company, dormant company and private company which is start-up, at least one Board meeting should be conducted in each half of the calendar year and the gap between two meetings should not be less than Ninety days. However, this provision would not apply to a one person company in which there is only one director on its Board.

In case of Section 8 Company, after MCA exemptions Notification Dated 05.06.2015, the provision of Section 173(1) shall apply only to the extent that the Board of Directors, of such companies shall hold at least one meeting within every six calendar months.

## **Meetings of Committees**

If authorised by articles, the directors have power to delegate their authority to a committee and a company may adopt Regulation 71 of Table F to Schedule I which reads as under:

**Regulation 71 states:**

- (1) The Board may, subject to the provisions of the Act, delegate any of its powers to committees consisting of such member or members of its body as it thinks fit;
- (2) Any committee so formed shall in the exercise of the powers so delegated, conform to any regulations that may be imposed on it by the Board." For transacting business of the company, the committee meetings can be conducted in accordance with Regulations 72 to 75 of Table F to Schedule I of the Act or other corresponding provisions of the company's articles. These regulations read as under:

**Regulation 72 provides:** "(1) A committee may elect a chairman of its meetings, (2) if no such chairman is elected, or if at any meeting the chairman is not present within five minutes after the time appointed for holding the meeting, the members present may choose one of their member to be chairman of the meeting."

**Regulation 73 provides:** "(1) A committee may meet and adjourn as it thinks proper (2) Questions arising at any meeting of a committee shall be determined by a majority of votes of the members present and in case of an equality of votes, the chairman shall have a second or casting vote."

**Regulation 74 provides:** "All acts done by any meeting of the Board or of a committee thereof or by any person acting as a director, shall, notwithstanding that it may be afterwards discovered that there was some defect in the appointment of any one or more of such directors or of any person acting as aforesaid, or that they or any of them were disqualified, be as valid as if every such director or such person had been duly appointed and was qualified to be a director."

**Regulation 75 provides:** "Save as otherwise expressly provided in the Act, a resolution in writing by all the members of the Board or of a committee thereof, for the time being entitled to receive notice of a meeting of the Board or Committee, shall be as valid and effectual as if it had been passed at a meeting of the Board or Committee, duly convened and held."

According to SS-1 (Secretarial Standard on Board Meetings) Committees shall meet as often as necessary subject to the minimum number and frequency prescribed by any law or any authority or as stipulated by the Board.

### **Preparation of Notices for meetings of Board/Committees of Board**

1. The Act requires that not less than seven days' notice in writing shall be given to every director at the registered address (whether in India or outside India) as available with the company, unless the Articles prescribe a longer period. Notice of an adjourned Meeting shall be given to all Directors including those who did not attend the Meeting on the originally convened date and unless the date of adjourned Meeting is decided at the Meeting, Notice thereof shall also be given not less than seven days before the Meeting.
2. SS-1 provides exhaustive guide for the meetings of Board/committees. Accordingly, it provides that a notice in writing of every Meeting shall be given to every Director by hand or by speed post or by registered post or by facsimile or by e-mail or by any other electronic means. It will not be given by ordinary post. The notice shall contain contact number or e-mail address(es) of the chairman or the company secretary or any other person authorised by the Board, to whom the Director shall confirm in this regard. In case the company sends the Notice by speed post or by registered post or by courier, an additional two days shall be added for the service of Notice.
3. The Notice shall be sent to the postal address or e-mail address, registered by the Director with the company or in the absence of such details or any change thereto, any of such addresses appearing

in the Director Identification Number (DIN) registration of the Director. Where a Director specifies a particular means of delivery of Notice, the Notice shall be given to him by such means.

4. Proof of sending Notice and its delivery shall be maintained by the company for such period as decided by the Board, which shall not be less than three years from the date of the Meeting.
5. Notice shall be issued by the Company Secretary or where there is no Company Secretary, any Director or any other person authorised by the Board for the purpose.
6. The Notice shall specify the serial number, day, date, time and full address of the venue of the Meeting.
7. The Notice shall inform the Directors about the option available to them to participate through Electronic Mode and provide them all the necessary information.
8. The Notice of a Meeting shall be given even if Meetings are held on pre-determined dates or at pre-determined intervals.

If notice of meeting is not given to one of its directors, meeting of board of directors is invalid and resolution passed at such meeting are inoperative. *Parmeshwari Prasad Gupta v Union of India [1974] 44 Comp Cas 1 (SC)*

Board meeting to transact urgent business, the Notice, Agenda and Notes on Agenda may be given at shorter period of time than stated above, subject to following conditions:

- (A) If the company is required to have independent director:
  - Presence of at least one Independent director is required.
  - In case of absence of independent director, decision taken at such meeting shall be circulated to all the directors, and shall be final only on ratification thereof by at least one Independent director.
- (B) If the company does not require appointing independent director, meeting can be called up at a shorter notice without any conditions to be complied with.

As per SS-1, In case the company does not have an Independent Director, the decisions shall be final only on ratification thereof by a majority of the Directors of the company, unless such decisions were approved at the Meeting itself by a majority of Directors of the company. The fact that the meeting is being held at a shorter notice shall be stated in the notice.

**Sample Notice of the Board/Committee Meeting**

**Notice of the Board Meeting**

To,

Mr./ Ms. ....(Director Name)

.....(Address)

Dear Sir/Madam,

Notice is hereby given that a meeting of the Board of Directors of the Company / (Name of the Committee meeting) of the members will be held on ..... day, the .....(Date), .....(Month), ..... (year) at ..... (time) at the ..... (Registered Office/Corporate Office) of the Company at ..... (Address). The Agenda of the Business to be transacted at the meeting is enclosed herewith.

You are requested to make it convenient to attend the meeting.

For .....(Name of the Company)

Place:

Sd/-

Date:

(Name)

(Designation)

### **Agenda of Board/Committees Meetings**

The Act does not prescribe such requirement to circulate Agenda etc. However Good governance envisage such requirement. Secretarial Standard on Board Meetings provide exhaustively on the Agenda management.

The Agenda, setting out the business to be transacted at the Meeting, and Notes on Agenda shall be given to the Directors at least seven days before the date of the Meeting, unless the Articles prescribe a longer period.

Agenda and Notes on Agenda shall be sent to all Directors by hand or by speed post or by registered post or by e-mail or by any other electronic means. These shall be sent to the postal address or e-mail address or any other electronic address registered by the Director with the company or in the absence of such details or any change thereto, to any of such addresses appearing in the Director Identification Number (DIN) registration of the Directors.

In case the company sends the Agenda and Notes on Agenda by speed post or by registered post, an additional two days shall be added for the service of Agenda and Notes on Agenda.

Where a Director specifies a particular means of delivery of Agenda and Notes on Agenda, these papers shall be sent to him by such means. However, in case of a Meeting conducted at a shorter Notice, the company may choose an expedient mode of sending Agenda and Notes on Agenda.

Proof of sending Agenda and Notes on Agenda and their delivery shall be maintained by the company for such period as decided by the Board, which shall not be less than three years from the date of the Meeting.

The Notice, Agenda and Notes on Agenda shall be sent to the Original Director also at the address registered with the company, even if these have been sent to the Alternate Director. However, the mode of sending Notice, Agenda and Notes on Agenda to the original director shall be decided by the company.

Notes on items of business which are in the nature of Unpublished Price Sensitive Information may be given at a shorter period of time than stated above, with the consent of a majority of the Directors, which shall include at least one Independent Director, if any.

Supplementary Notes on any of the Agenda items may be circulated at or prior to the Meeting but shall be taken up with the permission of the Chairman and with the consent of a majority of the Directors present in the Meeting, which shall include at least one Independent Director, if any.

Each item of business requiring approval at the Meeting shall be supported by a note setting out the details of the proposal, relevant material facts that enable the Directors to understand the meaning, scope and implications of the proposal and the nature of concern or interest, if any, of any Director in the proposal, which the Director had earlier disclosed.

Each item of business to be taken up at the Meeting shall be serially numbered.

Any item not included in the Agenda may be taken up for consideration with the permission of the Chairman and with the consent of a majority of the Directors present in the Meeting.

### Sample Important Agenda Items for Board Meeting

#### Agenda Items of Board Meeting

Item No.	Particulars
1.	To grant leave of absence, if any
2.	Appointment of Chairman of the Meeting
3.	To confirm minutes of last Board/ Committee Meeting held in financial year 2016-17.
4.	To take note of Disclosure of Interest by Directors pursuant to sect 184 (1).
5.	To take note of Declaration given by Independent Director to meets the criteria of Independence under section149(7) of companies Act 2013
6.	To consider and approve policy (Name of the Policy)
7.	To consider the matter of Non-acceptance of Public Deposits
8.	To Take note of Statement containing investor complaint under regulation 13(3) of LODR.
9.	Noting of Compliance Report on corporate governance under regulation 27(2) of LODR.
10.	Appointment Secretarial Auditor of the Company for the financial year 2017-18.
11.	Appointment Internal Auditor of the Company for the financial year 2017-18. (if applicable)
12.	To Approve & consider Audited Financial Statements for the year ended 2016-17.
13.	To Take note of Statutory Auditors Report on the Financial Statements of the Company for the year ended 2016-17.
14.	To take note any other item(s).

### Convening a Meeting

Any Director of a company may, at any time, summon a Meeting of the Board, and the Company Secretary or where there is no Company Secretary, any person authorised by the Board in this behalf, on the requisition of a Director, shall convene a Meeting of the Board, in consultation with the Chairman or in his absence, the Managing Director or in his absence, the Whole-time Director, where there is any, unless otherwise provided in the Articles.

Directors may participate in the meeting either in person or through video conferencing or other audio visual means. (Details are given in chapter 20, i.e., Virtual Meetings).

### Penalty

Every officer of the company who is duty bound to give notice under this section if fails to do so shall be liable to a penalty of twenty five thousand rupees.

### Quorum for Board Meetings : Section 174

One third of total strength or two directors, whichever is higher, shall be the quorum for a meeting. For the purpose of determining the quorum, the participation by a director through Video Conferencing or other audio visual means shall also be counted, unless he is to be excluded for any item of business under any provisions of the Act or the rules - Section 174(1). In the meetings where there is quorum presence in a meeting through physical of directors, any other director may participate conferencing through video or other audio visual means.

Section 174 is not applicable to One Person Company in which there is only one director.

If at any time the number of interested directors exceeds or is equal to two-thirds of the total strength of the Board of directors, the number of directors who are not interested and present at the meeting, being not less than two shall be the quorum during such time. For instance if there are twelve directors and ten of them are interested, remaining two directors would not have normally constituted quorum since four directors is the requisite quorum, but, in such event, remaining two disinterested directors would constitute quorum.

Act lays down only minimum number of to form a quorum, company by its articles can provide for a higher number of quorum - *Amrit Kaur Puri v Kapurthala Flour, Oil & General Mills Co (P) Ltd.* [1984] 56 Comp Cas 194 (P & H)

Where due to removal or resignation or for some other reason, the number of directors is reduced below the quorum, and then the continuing directors may act for the purpose of increasing the number of directors to that fixed for the quorum, or of summoning a general meeting of the company and for no other purpose.

The meeting shall be adjourned due to want of quorum, unless the articles provide shall be held to the same day at the same time and place in the next week or if the day is National Holiday, the next working day at the same time and place.

If the Board meeting is adjourned for want of quorum and at the adjourned Board meeting also no quorum is present, meeting stands dissolved. Adjourned Board meetings are the continuation of the original board meeting.

According to SS-1, the Chairman may, unless dissented to or objected by the majority of Directors present at a Meeting at which a Quorum is present, adjourn the Meeting for any reason, at any stage of the Meeting.

Quorum shall be present not only at the time of commencement of the Meeting but also while transacting business. A director shall not be reckoned for quorum in respect of an item in which he is interested and he shall not be present, whether physically or through electronic mode, during discussions and voting on such item.

Additionally for listed entities SEBI vide recent notification provides that the quorum for every meeting of the board of directors of the top 1000 listed entities with effect from April 1, 2019 and of the top 2000 listed entities with effect from April 1, 2020 shall be one-third of its total strength or three directors, whichever is higher, including at least one independent director ;

The participation of the directors by video conferencing or by other audio-visual means shall also be counted for the purposes of such quorum.

The top 1000 and 2000 entities shall be determined on the basis of market capitalisation, as at the end of the immediate previous financial year.

## Quorum for Board meeting

### Requirement:

- Quorum for Board Meeting =  $1/3^{\text{rd}}$  of its Total strength or two directors, whichever is higher
- A Director participating through video conferencing/audio visual modes will also be counted for quorum
- Any fraction of a member will be rounded off as one
- Total strength shall not include directors whose places are vacant.

### Example:

If a Company has:

- 1) Four Directors: Quorum will be 2 [ $4 \times 1/3 = 1.33$  (rounded off to 2)]
- 2) Six (6) Directors: Quorum will be 2 [ $6 \times 1/3 = 2$ ]
- 3) Eleven (11) Directors: Quorum will be [ $11 \times 1/3 = 3.67$  (rounded off to 4)]

In case of Interested Directors, let us assume Interested Directors are 2:

- 4) Total 10 Directors, so quorum will be  $10 \times 1/3 = 3.33$  (rounded off to 4, but Interested Directors are 2, Then quorum will be  $(10-2) \times 1/3 = 2.67$  (rounded off to 3).

In case Interested Directors are 7, then quorum will be  $(10-7) \times 1/3 = 1$  Director cannot be considered as quorum, as there has to be atleast 2 Directors to form quorum.

## Meetings of Committees

The presence of all the members of any committee constituted by the Board is necessary to form the quorum for meetings of such committee unless otherwise stipulated in the Act or any other law or the Articles or by the Board. Regulation framed under any other law may contain provisions for the quorum of a committee and such stipulations shall be followed.

## Attendance Registers

Every company shall maintain separate attendance registers for the meetings of the Board and meetings of the committee. The pages of the respective attendance registers shall be serially numbered. If an attendance register is maintained in loose leaf form, it shall be bound periodically depending on the size and volume. The attendance register shall be maintained at the Registered Office of the company or such other place as may be approved by the Board. The attendance register may be taken to any place where a Meeting of the Board or Committee is held. The attendance register is open for inspection by the Directors. Even after a person ceases to be a Director, he shall be entitled to inspect the attendance register of the Meetings held during the period of his Directorship.

The attendance register shall contain the following particulars: serial number and date of the Meeting; in case of a Committee Meeting name of the Committee; place of the Meeting; time of the Meeting; names and signatures of the Directors, the Company Secretary and also of persons attending the Meeting by invitation and their mode of presence, if participating through Electronic Mode.

The attendance register shall be deemed to have been signed by the Directors participating through Electronic Mode, if their attendance is recorded in the attendance register and authenticated by the Company Secretary or where there is no Company Secretary, by the Chairman or by any other Director

present at the Meeting, if so authorised by the Chairman and the fact of such participation is also recorded in the Minutes.

The attendance register shall be preserved for a period of at least eight financial years from the date of last entry made therein and may be destroyed thereafter with the approval of the Board. It shall be in the custody of the Company Secretary.

### **Leave of Absence**

Leave of absence shall be granted to a director only when a request for such leave has been received by the company secretary or by the Chairman. The office of a director shall become vacant in case the director absents himself from all the meetings of the Board held during a period of twelve months with or without seeking leave of absence of the Board.

### **Chairman of the meeting of the Board/Committee**

The Chairman of the Company shall be the chairman of the Board. If the company does not have a Chairman, the Directors may elect one of themselves to be the chairman of the Board. In case of committee meeting, a member of the committee appointed by the Board or elected by the Committee as chairman of the Committee, in accordance with the Act or any other law or the Articles, shall conduct the meetings of the committee. If no Chairman has been so elected or if the elected chairman is unable to attend the meeting, the Committee shall elect one of its members present to chair and conduct the meeting of the committee, unless otherwise provided in the articles.

In case of Section 8 companies the quorum for the board meetings shall be either eight members or twenty five per cent of its total strength whichever is less. However, the quorum shall not be less than two members.

In case of private companies section 174(3) shall apply with the exception that the interested director may also be counted towards quorum in such meeting after disclosure of his interest pursuant to section 184. Notification no. GSR464(E), dated 5-06-2015, as amended by notification no. GSR 583(E), dated 13-06-2017.

### **Passing of Resolution by Circulation: Section 175**

A company may pass the resolutions through circulation. The resolution in draft form together with the necessary papers may be circulated to all the directors or members of committee at their address registered with the company in India by hand or by speed post or by courier or through electronic means which may include e-mail or fax.

The said resolution must be passed by majority of directors or members entitled to vote.

If more than one third of directors require that the resolution must be decided at the meeting, the chairperson shall put the resolution to be decided at the meeting.

The resolution passed through circulation be noted at a subsequent meeting and made part of the minutes of such meeting.

Matters covered by section 179(3) and rule 8 of the Companies (Meetings of Board and its powers) Rules, 2014 is required to be passed at a meeting of Board and cannot be passed by circulation.

Further SS-1, requires that each business proposed to be passed by way of resolution by circulation shall be explained by a note setting out details of the proposal, relevant material facts that enable the directors to understand the meaning, scope and implications of the proposal, the nature of concern of interest, if any, of any director in the proposal, which the director had earlier disclosed and the draft of the resolution proposed.

Each resolution shall be separately explained. The decision of the directors shall be sought for each resolution separately. Not more than seven days from the date of circulation of the draft of the resolution shall be given to the directors to respond and the last date shall be computed accordingly.

Passing of resolution by circulation shall be considered valid as if it had been passed at a duly convened meeting of the Board. This shall not dispense with the requirement for the Board to meet at the specified frequency.

The Resolution, if passed, shall be deemed to have been passed on the earlier of:

- (a) the last date specified for signifying assent or dissent by the Directors, or
- (b) the date on which assent has been received from the required majority, provided that on that date the number of Directors, who have not yet responded on the resolution under circulation, along with the Directors who have expressed their desire that the resolution under circulation be decided at a Meeting of the Board, shall not be one third or more of the total number of Directors; and shall be effective from that date, if no other effective date is specified in such Resolution. Resolutions passed by circulation shall be noted at a subsequent Meeting of the Board and the text thereof with dissent or abstention, if any, shall be recorded in the Minutes of such Meeting.

## Minutes

Section 118 provides that every company shall prepare, sign and keep minutes of proceedings of every general meeting, including the meeting called by the requisitionists and all proceedings of meeting of any class of share holders or creditors or Board of Directors or committee of the Board and also resolution passed by postal ballot within thirty days of the conclusion of every such meeting concerned.

In case of meeting of Board of Directors or of a committee of Board, the minutes shall contain name of the directors present and also name of dissenting director or a director who has not concurred the resolution. The Chairman shall exercise his absolute discretion in respect of inclusion or non-inclusion of the matters which is regarded as defamatory of any person, irrelevant or detrimental to company's interest in the minutes. Minutes kept shall be evidence of the proceedings recorded in a meeting.

Rule 25 contains provisions with regards to minutes of meetings. A distinct minute book shall be maintained for each type of meeting namely:

- (i) general meetings of the members;
- (ii) meetings of the creditors;
- (iii) meetings of the Board; and
- (iv) meetings of the committees of the Board.

Detailed of minutes of Board meeting is given in Chapter Register and Records.

## Duties of Company Secretary

### **A. Before the meeting**

1. The Secretary or any other person so authorised shall call give not less than seven days' notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means. [Section 173(3)].
2. Board may be called at shorter notice to transact urgent business subject to the condition that at least one independent director, if any, shall be present at the meeting.

3. Board may be called at shorter notice to transact urgent business subject to the condition that at least one independent director, if any, shall be present at the meeting.
4. According to Regulation 67 of Table – F of Schedule – I of the Act, a director may, or the manager or secretary on the requisition of a director shall, any time summon a meeting of the Board.
5. In case of first board meeting, the notice must also mention that it is the first Board meeting.
6. It is not obligatory to give agenda in the notice, but it is a good secretarial practice to enclose the agenda to the notice of the meeting.
7. Contact and request all the directors to attend the meeting and arrange the facilities required by them in this regard, like conveyance, stay arrangements, location of venue etc.
8. At least half an hour before the meeting, the persons responsible for the conducting the meeting should place the folders containing Agenda, notes to Agenda, draft minutes to Agenda, statement of expenses incurred/to be incurred, Business Plan etc. for ready reference of all directors to enable them to deliberate and discuss on each item of the agenda in detail.
9. Before holding the meeting, welcome the directors and obtain their signatures on the Attendance Register.

**B. At the meeting**

10. If quorum, as required under Section 174, is present, declare the meeting in order and inform the names of the directors who sought leave of absence from attending the meeting. The Quorum of a company shall be one third of the total strength of the Board or two directors whichever is higher. The participation of directors by video conferencing or by other means shall also be complied for the purpose of quorum.
11. In case of section 8 companies, the quorum of co. shall be either eight members or 25% of its total strength whichever is less. Provided that the quorum shall not be less than two members.
12. The directors who are present at the meeting may elect one of them as the Chairman of the meeting and request him to take the Chair.
13. Help the Chairman to conduct the meeting as per the agenda.
14. If any director wants to place any other item for the discussion at the meeting, then such item may be taken up with the permission of the Chairman.
15. Every director shall disclose his concern or interest in any company or companies or bodies corporate, firms or other association of individuals, by giving notice in writing in Form MBP-1 1
16. Decide the date, time and place of the next Board meeting,

**C. After the meeting**

17. After the meeting is over, prepare draft minutes of the meeting; get it reviewed by the chairman of the meeting and/or the Managing Director of the company.
18. Send copy of draft minutes of the meeting to each of the directors of the company for information and comments.
19. Contact and collect draft minutes from each of the directors with their comments. After that, in consultation with the Chairman/Managing Director finalise the minutes and enter them into the

Minutes Book. All pages should be consecutively numbered.

20. Such final minutes may be signed and dated by the Chairman of the meeting or by the Chairman of the succeeding meeting. All pages of the minutes are to be initialed and the last page of the minutes.
20. Minutes is to be signed and dated by the Chairman.
21. Ensure that the minutes are entered within 30 days of the conclusion of meeting.

## LESSON ROUND-UP

- Director can participate in the Board meeting through video conferencing or other audio visual mode as may be prescribed
- Notice of not less than seven days in writing is required to call a board meeting and notice of meeting to all directors shall be given, whether he is in India or outside India by hand delivery or by post or by electronic means.
- The participation of director at Board meeting through video conferencing or by other electronic means shall be counted for the purpose of Quorum
- Section 173 provides the participation of directors in a meeting may be either in person or through video conferencing or other audio visual means, which are capable of recording and recognizing the participation of the directors and of recording and storing the proceedings of such meetings along with date and time.
- The Chairman may adjourn a Meeting with the consent of the Members and shall adjourn a Meeting if so decided by the Members. The Meeting may, however, be adjourned at any time. It may be adjourned after some items of business have been transacted and the remaining items can be transacted at the adjourned Meeting.

## GLOSSARY

One person Company	"One Person Company" means a company which has only one person as a member; (Sec 2(65))
Small Company	<p>"small company" means a company, other than a public company,—</p> <p>(i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees; and</p> <p>(ii) turnover of which as per profit and loss account for the immediately preceding financial year does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than one hundred crore rupees:</p> <p><b>Provided</b> that nothing in this clause shall apply to—</p> <p>(A) a holding company or a subsidiary company;</p> <p>(B) a company registered under section 8; or</p> <p>(C) a company or body corporate governed by any special Act;</p> <p>(Sec 2(85))</p>
Adjournment	Adjournment means to defer or suspend the meeting to a future time, either at an appointed date or indefinitely or as decided by the members present at the scheduled meeting.





# Lesson 19

## General Meetings

### LESSON OUTLINE

- Annual General Meeting
- Extraordinary General Meeting
- Class Meeting
- Types of Resolutions
- Adjourned Meetings
- Voting
- Demand for Poll
- Postal Ballot
- Minutes
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

Members or directors of a company can exercise their powers and can bind the company only when they act as a body at a validly convened and held meeting. An individual member or shareholder, irrespective of his shareholding cannot bind a company by his individual act.

A general meeting is a meeting of the members of the company. In Companies Act, 2013, a new concept of voting *via* electronic means has been introduced. The business undertaken at this meeting may include electing board of directors, adoption of financial statements, declaration of dividend and informing the members of previous and future activities.

It is to be noted that every gathering or assembly does not constitute a meeting. The meetings must be convened and held in perfect compliance with the various provisions of the Companies Act, 2013 and rules framed thereunder. As a prospective company secretary this chapter shall make you aware of all the legal compliances with regard to general meetings.

## INTRODUCTION

A meeting may be generally defined as a gathering or assembly or getting together of a number of persons for transacting any lawful business. There must be atleast two persons to constitute a meeting. Therefore, one shareholder usually cannot constitute a company meeting even if he holds proxies for other shareholders. However, in certain exceptional circumstances, even one person may constitute a meeting.

It is to be noted that every gathering or assembly does not constitute a meeting. Company meetings must be convened and held in perfect compliance with the various provisions of the Companies Act, 2013 and the rules framed thereunder.

A company is composed of members, though it has its own entity distinct from members. The members of a company are the persons who, for the time being, constitute the company, as a corporate entity. However, a company, being an artificial person, cannot act on its own. It, therefore, expresses its will or takes its decisions through resolutions passed at validly held meetings. The primary purpose of a meeting is to ensure that a company gives reasonable and fair opportunity to those entitled to participate in the meeting to take decisions as per the prescribed procedures.

The decision making powers of a company are vested in the members and the directors. They exercise their respective powers through Resolutions passed by them. General meetings of the members provide a platform to express their will in regard to the management of the affairs of the company.

Convening of one such meeting every year is compulsory. Holding of more general meetings is left to the choice of the management or to a given percentage of shareholders to exercise their power to compel the company to convene a meeting. Shareholder democracy, class action suits and protection of interest of investors are the essence and attributes of the Companies Act, 2013.

**Secretarial Standard on General Meetings of companies:** Secretarial Standard on General Meeting (SS-2) issued by the Institute of Company Secretaries of India (ICSI) and approved by central government is to be mandatorily adhered by all companies as per the provision of Section 118(10) of Companies Act, 2013. The objective of secretarial standard is to promote good corporate governance. This Standard is applicable to all types of General Meetings of all companies incorporated under the Act except One Person Company (OPC) and class or classes of companies which are exempted by the Central Government through notification. The revised version of Secretarial Standard is effective 1<sup>st</sup> October 2017.

## Members' Meetings

A company is required to hold meetings of the members to take approval of certain business items, as prescribed in the Act.

The meeting to be held annually for seeking approval to certain ordinary business is called Annual General Meeting. A meeting to be held to transact any business other than ordinary business or special business is called extraordinary general meeting. In certain cases, a company may have to hold a meeting of the members of a particular class of members.

### MEMBER'S MEETINGS

ANNUAL GENERAL  
MEETING

EXTRA ORDINARY  
GENERAL MEETING

CLASS MEETING

## 1. Annual General Meeting (section 96)

Annual general meeting (AGM) is an important annual event where members get an opportunity to discuss the activities of the company. Section 96 provides that every company, other than a one person company is required to hold an annual general meeting every year. SS-2 provides that the Board shall, every year, convene or authorize convening of a meeting of its members called the Annual General Meeting to transact items of ordinary business specifically required to be transacted at an annual general meeting as well as special business, if any. If the Board fails to convene its Annual General Meeting in any year, any Member of the company may approach the prescribed authority, which may then direct the calling of the Annual General Meeting of the company. Following are the key provisions regarding the holding of an Annual General Meeting:

### *Holding of Annual General Meeting*

1. Annual general meeting should be held once **in each calendar year**.
2. **First annual general meeting** of the company should be held within 9 months from the closing of the first financial year. Hence it shall not be necessary for the company to hold any annual general meeting in the year of its incorporation.
3. **Subsequent annual general meeting** of the company should be held within 6 months from the date of closing of the relevant financial year.
4. The gap between two annual general meetings **shall not exceed 15 months**.

Additionally for listed entities SEBI vide recent notification provided that the top 100 listed entities by market capitalization, determined as on March 31st of every financial year, shall hold their annual general meetings within a period of five months from the date of closing of the financial year. The top 100 listed entities shall provide one-way live webcast of the proceedings of the annual general meetings. Explanation: The top 100 entities shall be determined on the basis of market capitalisation, as at the end of the immediate previous financial year. (Notified on 9th May, 2018 effective from April 1, 2019)

### **One person company is exempt from holding an AGM.**

#### **Last date for holding AGM other than the first AGM i.e. subsequent AGM:**

1. AGM is to be held within 6 months of the close of relevant financial year.
2. Not more than 15 months shall elapse between the date of one AGM and that of the next. In other words, AGM is to be held within 15 months of last AGM.
3. AGM is to be held in each calendar year.

The three time limits given above are separate and cumulative. Non-compliance of any of them would constitute an offence. Therefore, the last date for holding AGM shall be the earliest of the above three limits.

### ***Extension of validity period of AGM***

In case, it is not possible for a company to hold an annual general meeting within the prescribed time, the Registrar may, for any special reason, extend the time within which any annual general meeting shall be held. Such extension can be for a period not exceeding 3 months. No such extension of time can be granted by the Registrar for the holding of the first annual general meeting.

#### **Test your knowledge:**

**Question:** The gap between two annual general meetings can never exceed 15 months. Comment

**Answer:** According to section 96(1) of the Companies Act, 2013 gap of not more than 15 months shall elapse between the date of one annual general meeting of the company and that of the next year. According to third proviso to section 96(1), the Registrar may, for any special reason, extend the time within which any annual general meeting, other than the first annual general meeting, shall be held, by a period of not exceeding three months. The company may apply to the Registrar for extension for holding AGM, justifying it as a special reason. The registrar may, after considering it as a special reason, extend the time within which an AGM shall be held which shall be a period not exceeding three months. Accordingly, the gap between the two AGMs shall not elapse a period of 15 months unless the Registrar for special reason has extended the time for holding the AGM. Such extension cannot be more than 3 months.

***Date, Time and place for holding an annual general meeting***

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. It should be held either at the registered office of the company or at some other place within the city, town or village in which the registered office of the company is situated. The Central Government is empowered to exempt any company from these provisions, subject to such conditions as it may impose.

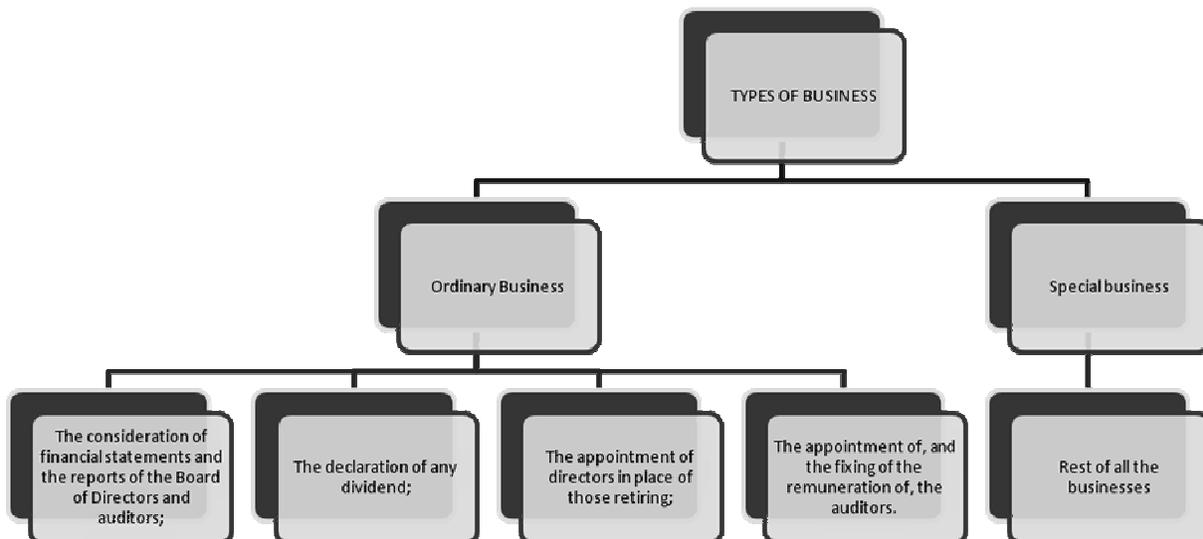
Annual general meeting of an unlisted company may be held at any place in India if consent is given in writing or by electronic mode by all the members in advance.

In case of Government Company, the Central Government may approve such other place for holding AGM, if the place is other than registered office.

In case of Section 8 Company, the time, date and place of each AGM are decided upon before-hand by the Board having regard to the directions, if any, given in this regard by such company in the general meeting

“National Holiday” for this purpose means and includes a day declared as National Holiday by the Central Government. According to SS-2, National Holiday means Republic Day i.e. 26th January, Independence Day i.e. 15th August, Gandhi Jayanti i.e. 2nd October and such other day as may be declared as National Holiday by the Central Government.

***Business to be transacted at annual general meeting:[Section 102]***



Section 102(2)(a) provides that all other businesses transacted at an Annual General Meeting except the following are special business:

- (i) the consideration of financial statements and the reports of the Board of Directors and auditors;
- (ii) the declaration of any dividend;
- (iii) the appointment of directors in place of those retiring;
- (iv) the appointment of, and the fixing of the remuneration of, the auditors.

Accordingly, above mentioned four businesses are ordinary business rest shall be deemed to be special business. Explanatory statement is not required for transacting any item of ordinary business. All business except specified above shall be deemed as special business at an AGM.

In case of meeting other than AGM, all business shall be deemed to be special. Explanatory statement must be annexed to the notice for transacting every items of special business. In case of non-disclosure or insufficient disclosure in Explanatory statement, any benefit accrues to a promoter, director, manager or other key managerial personnel or their relatives, such person shall hold such benefit in trust for the company, and shall compensate the company to the extent of benefit derived by him.

### ***Penalty for default in holding the annual general meeting [Section 99]***

Section 99 provides that if any default is made in complying or holding a meeting of the company, the company and every officer of the company who is in default shall be punishable with fine which may extend to one lakh rupees and in case of continuing default, with a further fine which may extend to five thousand rupees for each day during which such default continues.

If any default is made in holding the annual general meeting of a company, any member of the company may make an application to the Tribunal to call or direct the calling of, an annual general meeting of the company and give such ancillary or consequential directions as the Tribunal thinks expedient. Such directions may include a direction that one member of the company present in person or by proxy shall be deemed to constitute a meeting.

Every listed entities, under Regulation 30 of SEBI (LODR) Regulation, 2015, is required to disclose the proceedings of annual & extraordinary general meeting to the Stock Exchange where its securities are listed within 24 hours of the event.

### **Convening of a valid general meeting**

The business at a meeting is said to have been “validly transacted” if the members of the organisation or body concerned, whether or not they were present, are bound by the decision made there at. They cannot be so bound unless the meeting is validly held. The essentials of a valid meeting are that the meeting should be:

#### **(a) Properly convened:**

- (i) The meeting must be called by proper authority; and
- (ii) Proper notice must be served in the manner specified under Section 101 and 102 of the Act.

#### **(b) Properly constituted:**

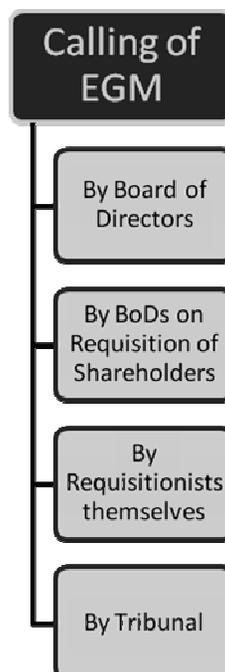
- (i) Proper quorum must be present in the general meeting (Section 103 of the Act)
- (ii) Proper chairman must preside the meeting (Section 104 of the Act)

#### **(c) Properly conducted:**

- (i) The business must be validly transacted at the meeting i.e. resolutions must be properly moved and passed, and voting by show of hands and on poll.
- (ii) Proper minutes of the meeting must be prepared. (Section 118 of the Act)

## 2. Extra-Ordinary General Meeting (Section 100)

There are so many matters relating to the business of a company, which requires approval or consent of members in general meeting. It is always not possible for consideration of such matters to wait until the next annual general meeting. The articles of association of the company of the company make provisions for convening general meeting other than the annual general meeting. All general meetings other than annual general meeting are called extra-ordinary general meetings (EGM). According to SS-2 items of business other than ordinary business may be considered at an EGM or by means of a postal ballot, if thought fit by the Board. This means that all the transactions dealt upon in an EGM shall be special business.



Following are the key provisions, regarding calling and holding of an extraordinary general meeting:

### **(1) By the Board *Suo motu* [Section 100 (1)]**

The Board may, whenever it deems fit, call an EGM of the company. An extraordinary general meeting of the company, shall be held at any place in India. An extraordinary general meeting of a company which is wholly owned subsidiary of a company incorporate outside India, may be held outside India.

### **(2) By Board on requisition of members [Section 100 (2)]**

The Board shall, call an extraordinary general meeting on receipt of the requisition from the following number of members:

- (a) in the case of a **company having a share capital**: members who hold, on the date of the receipt of the requisition, not less than one-tenth of such of the paid-up share capital of the company as on that date carries the right of voting;

- (b) in the case of a **company not having a share capital**: members who have, on the date of receipt of the requisition, not less than one-tenth of the total voting power of all the members having on the said date a right to vote.

**Matter set out for consideration in requisition:** The requisition made as above, shall set out the matters for the consideration of which the meeting is to be called and shall be signed by the requisitionists and sent to the registered office of the company.

**Time period for calling the meeting:** The Board is required to proceed to call a meeting within 21 days from the date of receipt of a valid requisition, to convene a meeting which should be held within 45 days of such deposit of the requisition with the company.

**(3) By requisitionists [Section 100(4)]**

- (1) If the Board does not within 21 days from the date of receipt of a valid requisition in regard to any matter, proceed to call a meeting for the consideration of that matter on a day not later than 45 days from the date of receipt of such requisition, the meeting may be called and held by the requisitionists themselves. However in such case, the meeting should be held within a period of 3 months from the date of the requisition.

Such requisition shall not pertain to any item of business that is required to be transacted mandatorily through postal ballot.

**Requisition for convening of EGM by members:** The members may requisition convening of an extraordinary general meeting, by providing such requisition in writing or through electronic mode at least clear twenty-one days prior to the proposed date of such extraordinary general meeting.

**Reimbursement of expenses in calling a meeting:** Reasonable expenses incurred by the requisitionists in calling such a meeting shall be reimbursed by the company to the requisitionists. The company in turn recovers such expenses from any fee or other remuneration under section 197 payable to such of the directors who were in default in calling the meeting.

In case, the quorum is not present within half-an-hour from the time appointed for holding a meeting called by requisitionists, the meeting shall stand cancelled. [Section 103(2)(b)]

- (2) The notice shall specify the place, date, day and hour of the meeting and shall contain the business to be transacted at the meeting.-

A Meeting called by the requisitionists shall be held either at the registered office of the company or at some other place within the city, town or village in which the registered office of the company is situated. Such meeting shall be held on any working day.

- (3) If the resolution is to be proposed as a special resolution, the notice shall be given as required by sub-section (2) of section 114.
- (4) **Notice to be signed:** The notice shall be signed by all the requisitionists or by a requisitionists duly authorized in writing by all other requisitionists on their behalf or by sending an electronic request attaching therewith a scanned copy of such duly signed requisition.
- (5) **No explanatory statement annexed to the notice:** No explanatory statement as required under section 102 need be annexed to the notice of an extraordinary general meeting convened by the requisitionists and the requisitionists may disclose the reasons for the resolution(s) which they propose to move at the meeting.
- (6) **Serving of notice of the meeting:** The notice of the meeting shall be given to those members

whose names appear in the Register of members of the company within three days on which the requisitionists deposit with the Company a valid requisition for calling an extraordinary general meeting.

- (7) **No meeting convened:** Where the meeting is not convened, the requisitionists shall have a right to receive list of members together with their registered address and number of shares held and the company concerned is bound to give a list of members together with their registered address made as on twenty first day from the date of receipt of valid requisition together with such changes, if any, before the expiry of the forty-five days from the date of receipt of a valid requisition.
- (8) **Mode of giving notice:** The notice of the meeting shall be given by speed post or registered post or through electronic mode. Any accidental omission to give notice to, or the non-receipt of such notice by, any member shall not invalidate the proceedings of the meeting.

#### **(4) By Tribunal [Section 98]**

Section 98 provides that if for any reason it is impracticable to call a meeting of a company or to hold or conduct the meeting of the company, the Tribunal may, either *suomotu* or on the application of any director or member of the company who would be entitled to vote at the meeting:

- (a) order a meeting of the company to be called, held and conducted in such manner as the Tribunal thinks fit; and
- (b) give such ancillary or consequential directions as the Tribunal thinks expedient, including directions modifying or supplementing in relation to the calling, holding and conducting of the meeting, the operation of the provisions of this Act or articles of the company.

Such directions may include a direction that one member of the company present in person or by proxy shall be deemed to constitute a meeting. Meeting held pursuant to such order shall be deemed to be a meeting of the company duly called, held and conducted.

### **3. Class Meetings**

Meetings of members of a company fall into two broad divisions, namely, general meetings and class meetings. Class meetings are meeting of shareholders, holding a particular class of share which is held to pass resolution which will bind only the members of the class concerned. Only members of the class concerned may attend and vote at meeting. Usually the rules to voting apply to class meetings as they govern voting at general meetings. These class meetings must be convened whenever it is necessary to alter or change the rights or privileges of that class as provided by the articles. For effecting such changes, it is necessary that these are approved at a separate meeting of the holders of those shares and supported by a special resolution. Under section 48 of the Companies Act, 2013 (variation of shareholders' rights) class meeting of the holders of different classes of shares shall be held if the rights attaching to these shares are to be varied. Similarly, under Section 232(Merger and Amalgamation of companies), where a scheme of arrangement is proposed, meeting of several classes of shareholders and creditors are required to be held.

Details of meetings of members or class meetings are required to be mentioned in Annual Return as per Section 92(1)(f).

### **TYPES OF RESOLUTIONS**

#### **Ordinary and Special Resolutions**

Section 114 relates to Ordinary and Special Resolution.

**Ordinary Resolution**

A resolution shall be an ordinary resolution if the notice required under this Act has been duly given and it is required to be passed by the votes cast, whether on a show of hands, or electronically or on a poll, as the case may be, in favour of the resolution, including the casting vote, if any, of the Chairman, by members who, being entitled so to do, vote in person, or where proxies are allowed, by proxy or by postal ballot, exceed the votes, if any, cast against the resolution by members, so entitled and voting.

**Special Resolution**

A resolution shall be a special resolution when:

- (a) the intention to propose the resolution as a special resolution has been duly specified in the notice calling the general meeting or other intimation given to the members of the resolution;
- (b) the notice required under this Act has been duly given; and
- (c) the votes cast in favour of the resolution, whether on a show of hands, or electronically or on a poll, as the case may be, by members who, being entitled so to do, vote in person or by proxy or by postal ballot, are required to be **not less than three times** the number of the votes, if any, cast against the resolution by members so entitled and voting.

If the notice convening the meeting (where at special business will be transacted) does not state the nature of the special business, the meeting would be deemed to have been convened irregularly. Consequently, that special business cannot be dealt with at the meeting.

**Test your knowledge:**

**Question:** At a General meeting of a company, a matter was to be passed by a special resolution. Out of 40 members present, 20 voted in favour of the resolution, 5 voted against it and 5 votes were found invalid. The remaining 10 members abstained from voting. The Chairman of the meeting declared the resolution as passed.

With reference to the provisions of the Companies Act, 2013, examine the validity of the Chairman's declaration.

**Hint:** In the given problem, the votes cast in favour (20) being more than 3 times of the votes cast against (5), if other conditions of Section 114 are satisfied, the decision of the Chairman is in order.

**Resolutions requiring Special Notice (Section 115)**

Section 115 provides that where, by any provision contained in this Act or in the articles of a company, special notice is required of any resolution, notice of the intention to move such resolution shall be given to the company by such number of members holding not less than 1% of total voting power or holding shares on which such aggregate sum not exceeding ₹5,00,000/- as may be prescribed has been paid-up and the company shall give its members notice of the resolution in the following manner as prescribed in Rules.

**Provisions contained in the Act requiring special notice:**

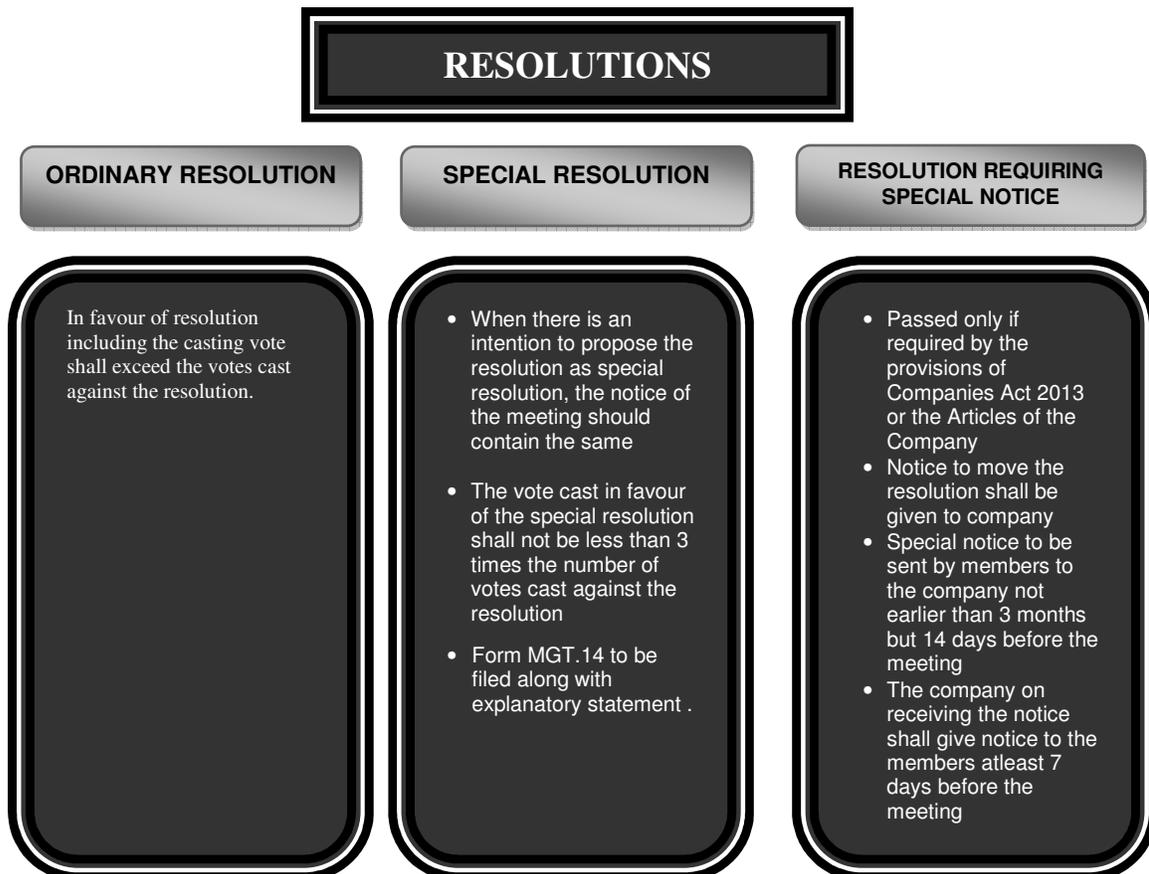
The matters in respect of which special notice is required are:

- (a) A resolution for appointment of a person as auditor at the annual general meeting other than the retiring auditor for providing expressly that the retiring auditor shall not be re-appointed [Section 140(4)];

- (b) A resolution for removing a director before the expiry of the period of his office and appointing someone in the place of the director so removed [Section 169(2)].

**Procedure for special notice:**

- (A) **Signing of special notice:**—A special notice required to be given to the company shall be signed, either individually or collectively by such number of members holding not less than one percent of total voting power or holding shares on which an aggregate sum of not more than five lakh rupees has been paid up on the date of the notice.
- (B) **Sending of notice to the company:**— Such notice shall be sent by members to the company not earlier than three months but at least 14 days before the date of the meeting at which the resolution is to be moved, exclusive of the day on which the notice is given and the day of the meeting.
- (C) **On receipt of notice by the company:**— The company shall immediately after receipt of the notice, give its members notice of the resolution at least seven days before the meeting, exclusive of the day of dispatch of notice and day of the meeting, in the same manner as it gives notice of any general meetings.
- (D) **Publication of notice:**— Where it is not practicable to give the notice in the same manner as it gives notice of any general meetings, the notice shall be published in English language in English newspaper and in vernacular language in a vernacular newspaper, both having wide circulation in the State where the registered office of the Company is situated. Such notice shall also be posted on the website, if any, of the Company. Such notice shall be published at least seven days before the meeting, exclusive of the day of publication of the notice and day of the meeting.



## Resolutions and Agreements to be filed with the Registrar

Section 117 provides that a copy of every resolution and an agreement in respect of matters specified therein together with the explanatory statement shall be filed in Form No. MGT.14 with the Registrar, within thirty days of its passing or making thereof. The Registrar shall register the same, and in case of any default, a company and every officer who is in default including the liquidator shall be punishable with fine which shall not be less than [fifty thousand rupees] but which may extend to five lakh rupees.

*Resolutions and agreements to be filed with the Registrar are as under:*

- (a) special resolutions;
- (b) resolutions which have been agreed to by all the members of a company, but which, if not so agreed to, would not have been effective for their purpose unless they had been passed as special resolutions;
- (c) any resolution of the Board of Directors of a company or agreement executed by a company, relating to the appointment, re-appointment or renewal of the appointment, or variation of the terms of appointment, of a managing director;
- (d) resolutions or agreements which have been agreed to by any class of members but which, if not so agreed to, would not have been effective for their purpose unless they had been passed by a specified majority or otherwise in some particular manner; and all resolutions or agreements which effectively bind such class of members though not agreed to by all those members;
- (e) resolutions requiring a company to be wound up voluntarily passed in pursuance of section 59 of the Insolvency and Bankruptcy Code 2016;
- (f) resolutions passed in pursuance of sub-section (3) of section 179. No person shall be entitled under Section 399 to inspect or obtain copies of such resolutions; This clause shall not apply to a banking company in respect of a resolution passed to grant loans, or give guarantee or provide security in respect of loans under clause (f) of sub-section (3) of section 179 in the ordinary course of its business. This sub-clause is not applicable to private companies vide exemption notification no GSR 464(E) dated 5th June, 2015.
- (g) any other resolution or agreement as may be prescribed and placed in the public domain.

## Notice of Meeting (Section 101)

### ***Length of notice of meeting***

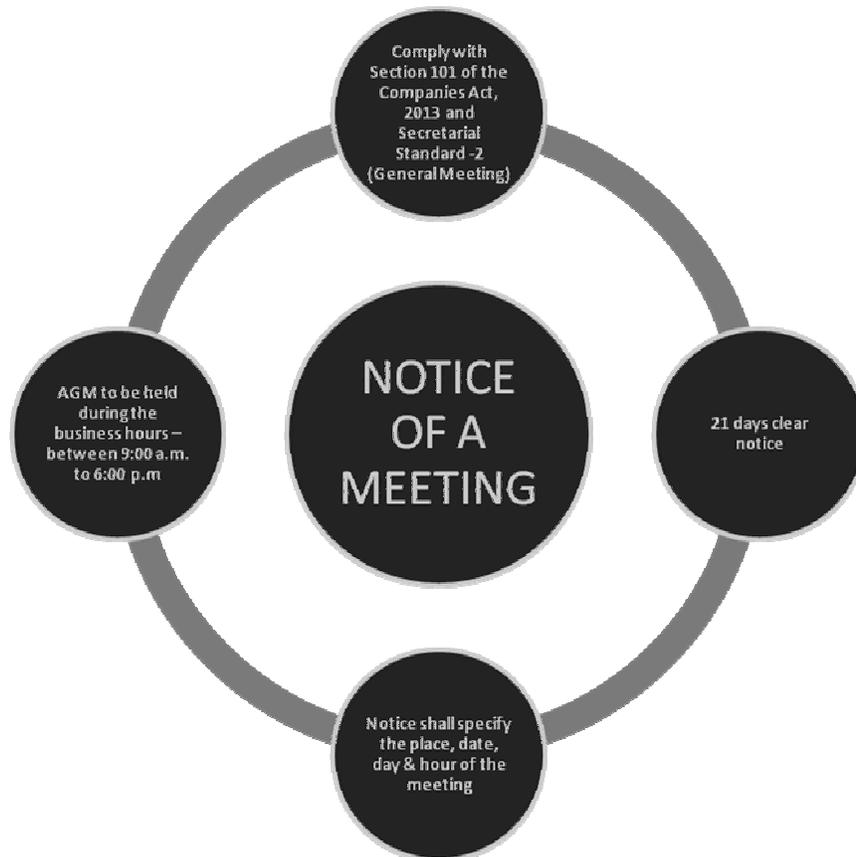
A general meeting of a company may be called by giving not less than 21 clear days' notice either in writing or through electronic mode. Notice through electronic mode shall be given in such manner as may be prescribed. In case of section 8 company, 14 days' clear notice is required instead of 21 days.

'Clear days' means days exclusive of the day of the notice of service and of the day on which the meeting is held.

Where a notice of general meeting is sent by post, it shall be deemed to be served at the expiration of 48 hours after the letter containing the same is posted (Rule 35(6) of the Companies (Incorporation) Rules, 2014). Each of the 21 days must be full or complete days. The day on which the notice is deemed to be served on the member, and the day of the general meeting have to be in addition to the 21 days.

In case a valid special notice under the Act has been received from Member(s), the company shall give Notice of the Resolution to all its Members at least seven days before the Meeting, exclusive of the day of

dispatch of Notice and day of the Meeting, in the same manner as a Notice of any General Meeting is to be given. Where this is not practicable, the Notice shall be published in a vernacular newspaper in the principal vernacular language of the district in which the registered office of the company is situated, and in an English newspaper in English language, both having a wide circulation in that district, at least seven days before the Meeting, exclusive of the day of publication of the Notice and day of the Meeting. In case of companies having a website, such Notice shall also be hosted on the website. **(Para 1.2.6 of SS-2)**



### Illustration

**Question:** ABC Ltd. issued a notice on 1<sup>st</sup> August, 2015 to hold its AGM on 24<sup>th</sup> August, 2015. Check the validity of the notice referring to the provisions of the relevant act, in case it is sent by post.

**Answer:** Date of holding AGM: 24<sup>th</sup> August, 2015

Date of dispatch of notice: 1<sup>st</sup> August, 2015

Days to be excluded: (a) Day of holding AGM i.e 24<sup>th</sup> August, 2015

(b) Day of dispatch of notice i.e. 1<sup>st</sup> August, 2015

(c) 2 days for service of notice i.e 2<sup>nd</sup> & 3<sup>rd</sup> August, 2015

Number of days notice given: 20 days

Number of days notice required under section 101 of the Act is 21 days. Therefore it is not a case of valid notice. However, shortfall of 1 day can be condoned if consent is given for such shorter notice by at least 95% of the members entitled to vote at such AGM.

**Shorter notice**

A general meeting may be called after giving a shorter notice also if consent is given in writing or by electronic mode by not less than 95% of the members entitled to vote at such meeting.

A general meeting may be called after giving shorter notice than that specified in this sub-section if consent, in writing or by electronic mode, is accorded thereto—

- (i) in the case of an annual general meeting, by not less than ninety-five per cent. of the members entitled to vote thereat; and
- (ii) in the case of any other general meeting, by members of the company—
  - (a) holding, if the company has a share capital, majority in number of members entitled to vote and who represent not less than ninety-five per cent 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 ninety-five per cent. of the total voting power exercisable at that meeting:

Where any member of a company is entitled to vote only on some resolution or resolutions to be moved at a meeting and not on the others, those members shall be taken into account for the purposes of this sub-section in respect of the former resolution or resolutions and not in respect of the latter.

**Secretarial Standard on calling of General Meeting on shorter notice:**

Para 1.2.7 of SS-2 provides that notice and accompanying documents may be given at a shorter period of time if consent in writing is given thereto, by physical or electronic means, by not less than ninety-five per cent of the Members entitled to vote at such Meeting.

The request for consenting to shorter notice and accompanying documents shall be sent together with the Notice and the Meeting shall be held only if the consent is received **prior** to the date fixed for the Meeting from not less than ninety five per cent of the Members entitled to vote at such Meeting.

**Contents of Notice**

Section 101(2) provides that every notice of a meeting shall specify the place, date day and the hour of the meeting and shall contain a statement of the business to be transacted at such meeting.

**Place of meeting (Section 96)**

The notice should state the place where the general meeting is scheduled to be held. In case of an annual general meeting, the place of the meeting has to be either the registered office of the company or some other place within the city, town or village in which the registered office of the company is situated. Explanation to Rule 17(2) of Companies (Management and Administration) Rules 2014 states that requisitionists should convene meeting at Registered Office or in the same city or town where the Registered Office is situated and such meeting should be convened on working day.

Annual general meeting of an unlisted company may be held at any place in India if consent is given in writing or by electronic mode by all the members in advance.

The Central Government may exempt any company from the provisions of this sub-section subject to such conditions as it may impose.

In case of government company, AGM may be held at registered office of the company or such other place within the city, town or village in which the registered office of the company is situated or such other place as

the central government may approve in this behalf.

Para 1.2.4 of SS-2 provides Annual General Meetings shall be held either at the registered office of the company or at some other place within the city, town or village in which the registered office of the company is situated, whereas other General Meetings may be held at any place within India.

Notice shall contain complete particulars of the venue of the Meeting including route map and prominent land mark for easy location. **(SS 1.2.4)**

***Day of meeting (Section 96)***

The day and date of the meeting should be clearly stated in the notice. In case of an annual general meeting, the day should be one that is not a National Holiday. An extraordinary general meeting can however be held on any day. However, as per Para 1.2.4 of SS-2 a Meeting called by the requisitionists shall be convened **only on a working day.**

*Explanation.*—For the purposes of this sub-section, "National Holiday" means and includes a day declared as National Holiday by the Central Government.]

As explained earlier National Holiday means National Holiday means Republic Day i.e. 26th January, Independence Day i.e. 15th August, Gandhi Jayanti i.e. 2nd October and such other day as may be declared as National Holiday by the Central Government.

***Time of meeting [(Section 96(2))]***

Exact time of holding the meeting should be given in the notice. An annual general meeting can be called during business hours only, i.e. between 9:00 a.m. and 6:00 p.m. There is no restriction of timings in case of an extraordinary general meeting.

In case of Section 8 Company, the time, date and place of each AGM are decided upon before-hand by the directors having regard to directions, if any, given in this regard by the company in its general meeting.

***Agenda (Section 102)***

A statement of the business to be transacted at the general meeting should be given in the notice. In case, the meeting is to transact a special business, an explanatory statement should be attached about such item.

***Proxy clause with reasonable prominence [Section 105(2)]***

Every notice calling a meeting of a company which has a share capital, or the articles of which provide for voting by proxy at the meeting, should carry with reasonable prominence, a statement that a member entitled to attend and vote is entitled to appoint a proxy, or, where that is allowed, one or more proxies, to attend and vote instead of himself, and that a proxy need not be a member.

**Notice through Electronic Mode (Rule 18 of Companies (Management and Administration) Rules 2014)**

According to the Companies (Management and Administration) Rules, 2014, the company may serve the notice in electronic mode in following manner.

- (1) A company may give notice through **electronic mode**. The expression "electronic mode" shall mean any communication sent by a company through its authorized and secured computer programme which is capable of producing confirmation and keeping record of such communication addressed to the person entitled to receive such communication at the last electronic mail address

provided by the member.

- (2) A notice may be sent through **e-mail** as a text or as an attachment to e-mail or as a notification providing electronic link or Uniform Resource Locator for accessing such notice.
- (3) (i) The e-mail shall be **addressed to the person entitled to receive such e-mail** as per the records of the company or as provided by the depository:
- The company shall provide an advance opportunity at least once in a financial year, to the member to register his e-mail address and changes therein and such request may be made by only those members who have not got their email ID recorded or to update a fresh email ID and not from the members whose e-mail IDs are already registered.
- (ii) The **subject line in e-mail** shall state the name of the company, notice of the type of meeting, place and the date on which the meeting is scheduled.
- (iii) **If notice is sent in the form of a non-editable attachment to e-mail**, such attachment shall be in the Portable Document Format or in a non-editable format together with a 'link or instructions' for recipient for downloading relevant version of the software.
- (iv) When **notice or notifications of availability of notice are sent by e-mail**, the company should ensure that it uses a system which produces confirmation of the total number of recipients e-mailed and a record of each recipient to whom the notice has been sent and copy of such record and any notices of any failed transmissions and subsequent re-sending shall be retained by or on behalf of the company as "proof of sending".
- (v) The **company's obligation shall be satisfied when it transmits the e-mail** and the company shall not be held responsible for a failure in transmission beyond its control.
- (vi) If a **member entitled to receive notice fails to provide or update relevant e-mail address to the company**, or to the depository participant as the case may be, the company shall not be in default for not delivering notice via e-mail.
- (vii) The **company may send e-mail** through in-house facility or its registrar and transfer agent or authorise any third party agency providing bulk e-mail facility.
- (viii) The **notice made available on the electronic link or uniform resource locator** has to be readable, and the recipient should be able to obtain and retain copies and the company shall give the complete Uniform Resource Locator or address of the website and full details of how to access the document or information.
- (ix) The notice of the general meeting of the company shall be simultaneously placed on the **website of the company** if any and on the website as may be notified by the Central Government.

*Explanation.-* For the purpose of this rule, it is hereby declared that the extra ordinary general meeting shall be held at a place within India.

#### **Secretarial Standard on issuance of notice:**

Para 1.2.2 of SS-2 provides that Notice shall be sent by hand or by ordinary post or by speed post or by registered post or by courier or by facsimile or by e-mail or by any other electronic means. 'Electronic means' means any communication sent by a company through its authorized and secured computer programme which is capable of producing confirmation and keeping record of such communication addressed to the person entitled to receive such communication at the last electronic mail address provided by the Member.

Notice shall be sent to Members by registered post or speed post or courier or e-mail and not by ordinary post in the following cases:

- (a) if the company provides the facility of e-voting ;
- (b) if the item of business is being transacted through postal ballot;

If a Member requests for delivery of notice through a particular mode, other than one of those listed above, he shall pay such fees as may be determined by the company in its Annual General Meeting and the Notice shall be sent to him in such mode.

Notice shall be sent to Members by registered post or speed post or email if the Meeting is called by the requisitionists themselves and where the Board had not proceeded to call the Meeting.

### **Persons entitled to receive Notice**

In terms of Section 101(3), notice of every meeting of the company must be given to:

- (a) every member of the company, legal representative of any deceased member or the assignee of an insolvent member;
- (b) the auditor or auditors of the company; and
- (c) every director of the company.

A private company, which is not, a subsidiary of a public company may prescribe, by its Articles, persons to whom the notice should be given.

It does not always follow that all the members of a company are entitled to receive notice of meetings of the company; the Articles frequently provide that preference shareholders shall not be entitled to receive notice of and vote at general meeting of the company, except in certain circumstances. There is a statutory obligation to send notice to preference shareholders when their dividend is in arrears for more than a certain period [Section 47(2)]. This obligation arises from the fact that preference shareholders whose dividends are in arrears are entitled to attend and vote at the meeting.

The non-receipt of notice or accidental omission to give notice to any member shall not invalidate the proceedings in the meeting [Section 101(4)]. However, omission to serve notice of meeting on a member on the mistaken ground that he is not a shareholder cannot be said to be an accidental omission [*Musselwhite Vs. C.H. Musselwhite & Sons Ltd.*(1962) 32 Comp. Cas 804]. 'Accidental omission' means that the omission must be not only designed but also not deliberate [*Maharaja Export Vs. Apparels Exports Promotion Council* (1986) 60 Comp. Cas 353.].

### **Notice to Directors, Auditors & other specified persons:**

Para 1.2.1 of SS-2 provides that notice in writing of every meeting shall be given to every member of the company. Such Notice shall also be given to the Directors and Auditors of the company, to the Secretarial Auditor, to Debenture Trustees, if any, and, wherever applicable or so required, to other specified persons. Court may direct issuance of Notice to some other persons such as Court-appointed Chairman or observers or persons whose entitlement is under challenge. Considering that Preference Shareholders are Members of the company, Notice of general meetings should also be given to them.

In the case of Members, Notice shall be given at the address registered with the Company or depository. In the case of shares or other securities held jointly by two or more persons, the Notice shall be given to the person whose name appears first as per records of the Company or the depository, as the case may be. In the case of any other person who is entitled to receive Notice, the same shall be given to such person at the

address provided by him.

Notice shall be given to:

- (a) Every member of the Company
- (b) Legal representative of any deceased member
- (c) Assignee of an insolvent member
- (d) The auditor or auditors of the company
- (e) Every director of the company
- (f) Secretarial Auditor of the Company
- (g) Debenture trustee
- (h) To other specified persons

**Secretarial Standard on entitlement to receive notice:**

Para 1.2.1 of SS-2 provides that where the company has received intimation of death of a Member, the Notice of Meeting shall be sent as under:

- (a) where securities are held singly, to the Nominee of the single holder;
- (b) where securities are held by more than one person jointly and any joint holder dies, to the surviving first joint holder;
- (c) where securities are held by more than one person jointly and all the joint holders die, to the Nominee appointed by all the joint holders;
  - (i) In the absence of a Nominee of member or joint members, the notice shall be sent to the legal representative of the deceased Member or joint members.
  - (ii) In case of insolvency of a Member, the Notice shall be sent to the assignee of the insolvent Member.
  - (iii) In case the Member is a company or body corporate which is being wound up, Notice shall be sent to the liquidator.

**Statement to be annexed to Notice– Explanatory Statement (Section 102)**

Section 102 requires that a statement detailing the material facts of the businesses to be transacted as special business be annexed to the notice of the general meeting.

**Secretarial Standard on annexure to notice of General Meeting:**

Para 1.2.5 of SS-2 requires that notice shall clearly specify the nature of the Meeting and the business to be transacted thereat. In respect of items of Special Business, each such item shall be in the form of a Resolution and shall be accompanied by an explanatory statement which shall set out all such facts as would enable a Member to understand the meaning, scope and implications of the item of business and to take a decision thereon. **In respect of items of ordinary business, resolutions are not required to be stated in the Notice except where the auditors or directors to be appointed are other than the retiring auditors or directors, as the case may be.**

**Contents of Explanatory Statement:**

In case of special business items to be transacted at a general meeting, a statement setting out the following material facts, shall be annexed to the notice calling the meeting:

- (l)(a) the nature of concern or interest, financial or otherwise, if any, in respect of each item of:

- every director and the manager, if any;
  - every other key managerial personnel; and
  - relatives of every director, manager and key managerial person.
- (b) any other information and facts that may enable members to understand the meaning, scope and implications of the items of business and to take decision thereon.

Where any item of special business to be transacted at a meeting of the company relates to or affects any other company, the extent of shareholding interest in that other company of every promoter, director, manager, if any, and of every other key managerial personnel of the first mentioned company shall, if the extent of such shareholding is not less than 2% of the paid-up share capital of that company, also be set out in the statement.

- (II) Where any item of business refers to any document, which is to be considered at the meeting, the time and place where such document can be inspected shall be specified in the explanatory Statement.

**Effect of non-disclosure:** Where as a result of the non-disclosure or insufficient disclosure in any statement referred as above, being made by a promoter, director, manager, if any, or other key managerial personnel, any benefit which accrues to such promoter, director, manager or other key managerial personnel or their relatives, either directly or indirectly, the promoter, director, manager or other key managerial personnel, as the case may be, shall hold such benefit in trust for the company, and shall, without prejudice to any other action being taken against him under this Act or under any other law for the time being in force, be liable to compensate the company to the extent of the benefit received by him.

If the explanatory statement is vague and tricky, or insufficient and misleading, the resolution passed, is bad in law. [*Central Industrial Alliance Ltd. Vs. Pravin Kantilal Vakil* (1985) 57 Com. Cases 12 (Bom)].

### Quorum for Meetings [Section-103]

Quorum refers to the minimum number of members required to constitute a valid meeting. Following are the minimum numbers provided in section 103, for various categories of companies. However the Articles of Association of the company may provide for a higher number.

- (a) *Public company:*
- 5 members personally present if the number of members as on the date of meeting is not more than 1000;
  - 15 members personally present if the number of members as on the date of meeting is more than 1000 but up to 5000;
  - 30 members personally present if the number of members as on the date of the meeting exceeds 5000.
- (b) *Private company:*
- 2 members personally present, shall be the quorum for a meeting of the company.

#### Secretarial Standard on Quorum:

Para 3.1 of SS-2 provides that where the quorum provided in the Articles is higher than that provided under the Act, the quorum shall conform to such higher requirement. Members need to be personally present at a meeting to constitute the quorum. Proxies shall be excluded for determining the quorum.

Para 3.2 of SS-2 provides that a duly authorized representative of a body corporate or the representative of

the President of India or the Governor of a State is deemed to be a Member personally present and enjoys all the rights of a Member present in person.

One person can be an authorized representative of more than one body corporate. In such a case, he is treated as more than one member present in person for the purpose of quorum. However, to constitute a meeting, at least two individuals shall be present in person. Thus, in case of a public company having not more than 1000 members with a quorum requirement of five members, an authorized representative of five bodies corporate cannot form a quorum by himself but can do so if at least one more member is personally present.

members who have voted by remote e-voting have the right to attend the General Meeting and accordingly their presence shall be, counted for the purpose of quorum.

A member who is not entitled to vote on any particular item of business being a related party, if present, shall be counted for the purpose of quorum.

The stipulation regarding the presence of a quorum does not apply with respect to items of business transacted through postal ballot.

Let us remember the concept through a table:

(a) in case of a **public company**,—

Quorum for the meeting	Number of members
5 members personally present	Not more than one thousand
15 members personally present	More than one thousand but upto five thousand
30 members personally present	Exceeds five thousand

(b) In the case of a **private company**, two members personally present, shall be the quorum for a meeting of the company.

**Consequences of no quorum-** If the quorum is not present within half-an-hour from the time appointed for holding a meeting of the company—

- (a) the meeting shall stand adjourned to the same day in the next week at the same time and place, or to such other date and such other time and place as the Board may determine; or
- (b) the meeting, if called by requisitionists (under section 100), shall stand cancelled:

### ADJOURNED MEETINGS

**Notice of an adjourned meeting-** Where the meeting stands adjourned to the same day in the next week at the same time and place, or to such other day, not being a National Holiday, or at such other time and place as the Board may determine, there the company shall give at least 3 days notice to the members either individually or by publishing an advertisement in 2 newspapers (one in English and one in vernacular language).

**No quorum in an adjourned meeting-** If at the adjourned meeting also, a quorum is not present within half-an-hour from the time appointed for holding meeting, **the members present, being not less than two in numbers, will constitute the quorum.**

If a Meeting is adjourned sine-die or for a period of thirty days or more, a Notice of the adjourned Meeting shall be given in accordance with the provisions contained hereinabove relating to Notice.

If a Meeting is adjourned for a period of less than thirty days, the company shall give not less than three days' Notice specifying the day, date, time and venue of the Meeting, to the Members either individually or by publishing an advertisement in a vernacular newspaper in the principal vernacular language of the district in which the registered office of the company is situated, and in an English newspaper in English language, both having a wide circulation in that district.

If a Meeting, other than a requisitioned Meeting, stands adjourned for want of Quorum, the adjourned Meeting shall be held on the same day, in the next week at the same time and place or on such other day, not being a National Holiday, or at such other time and place as may be determined by the Board.

The words, personally present exclude proxies. However, the representative of a body corporate appointed under Section 113 or the representative of the President or a Governor of a State under Section 112 is a member 'personally present' for purpose of counting a quorum [*Re. Kelantan Coconut Estate Ltd.*, 1920 W.N. 274].

In case two or more corporate bodies who are members of a company are represented by single individual, each of the bodies corporate will be treated as personally present by the individual representing it. If, for instance, he represents three corporate bodies, his presence will be counted as three members being present in person for purposes of quorum.

It has been held in a Scottish case that one individual may count as more than one member if he attends the meeting in more than one capacity, e.g. as a member holding shares in his own right and as a member entitled to vote in person in respect of a trust holding (*Neil McLeod & Sons Ltd.*, Petitioners, 1976 SC 16).

Para 3.1 of SS-2 requires that quorum shall be present not only at the time of commencement of the Meeting but also while transacting business.

### Illustration

**Question:** The articles of association of XYZ Ltd. having 700 members as on cut off date, prescribe for physical presence of 7 members to constitute quorum of general meetings. Following are the status of persons present in a general meeting of XYZ Ltd to consider the appointment of MD. Check the quorum of the meeting.

- (a) Mr. A, the representative of Governor of Maharashtra.
- (b) Mr. B & Mr. C are preference shareholders
- (c) Mr. D representing ABC Ltd. and SKY Ltd.
- (d) Mr. E, Mr. F, Mr. G and Mr. H are proxies of shareholders

**Hint:** (a) Since Mr. A is the representative of the Governor of Maharashtra, shall be treated as a member personally present (Section 112).

(b) Preference shareholders can vote only in relation to such matters which directly affect their rights. In this case, meeting was called to take decision on appointment of MD, which does not affect their rights. Therefore, Mr. B & Mr. C are not members personally present.

(c) Since Mr. D represents two body corporates, he would be treated as two members personally present. (Section 113)

(d) Since Mr. E, Mr. F, Mr. G and Mr. H are proxies of shareholders and members are not personally present. They are not considered while counting quorum.

From the above analysis, it can be concluded that only 3 members are personally present and they do not constitute proper quorum as fixed by the company.

Note: The quorum required in respect of general meeting of a public company is 5 and the quorum can be increased by the articles of the company.

As per Section 116 where a resolution is passed at an adjourned meeting of a company; or the holders of any class of shares in a company; or the Board of Directors, the resolution shall be treated as passed on the day it was actually passed and not on any earlier date.

**Secretarial Standard on adjournment of meetings (Para-15 of SS-2):**

(1) A duly convened Meeting shall not be adjourned unless circumstances so warrant. The Chairman may adjourn a Meeting with the consent of the Members, at which a Quorum is present, and shall adjourn a Meeting if so directed by the Members.

Meetings shall stand adjourned for want of requisite Quorum. The Chairman may also adjourn a Meeting in the event of disorder or other like causes, when it becomes impossible to conduct the Meeting and complete its business.

(2) At an adjourned Meeting, only the unfinished business of the original meeting shall be considered.

Any Resolution passed at an adjourned Meeting would be deemed to have been passed on the date of the adjourned Meeting and not on any earlier date.

**Chairman of Meetings (Section 104)**

Unless the articles of the company otherwise provide, the members personally present at the meeting shall elect one of themselves to be the Chairman thereof on a show of hands.

If a poll is demanded on the election of the Chairman, it shall be taken forthwith in accordance with the provisions of this Act and the Chairman elected on a show of hands shall continue to be the Chairman of the meeting until some other person is elected as Chairman as a result of the poll, and such other person shall be the Chairman for the rest of the meeting.

**Secretarial Standard on appointment and role of Chairman:**

Para 5 of SS-2 provides that the Chairman of the Board shall take the chair and conduct the Meeting.

If the Chairman is not present within fifteen minutes after the time appointed for holding the Meeting, or if he is unwilling to act as Chairman of the Meeting, or if no Director has been so designated, the Directors present at the Meeting shall elect one of themselves to be the Chairman of the Meeting.

If no Director is present within fifteen Minutes after the time appointed for holding the Meeting, or if no Director is willing to take the chair, the Members present shall elect, on a show of hands, one of themselves to be the Chairman of the Meeting, unless otherwise provided in the Articles.

If a poll is demanded on the election of the Chairman, it shall be taken forthwith in accordance with the provisions of the Act and the Chairman elected on a show of hands shall continue to be the Chairman of the Meeting until some other person is elected as Chairman as a result of the poll, and such other person shall be the Chairman for the rest of the Meeting.

The Chairman shall ensure that the Meeting is duly constituted in accordance with the Act and the Articles or any other applicable laws, before it proceeds to transact business. The Chairman shall then conduct the Meeting in a fair and impartial manner and ensure that only such business as has been set out in the Notice is transacted. The Chairman shall regulate the manner in which voting is conducted at the Meeting keeping in view the provisions of the Act.

Para 5.2 of SS-2 requires that the Chairman shall explain the objective and implications of the Resolutions before they are put to vote at the Meeting.

The Chairman shall provide a fair opportunity to Members who are entitled to vote to seek clarifications and/or offer comments related to any item of business and address the same, as warranted.

Para 5.3 of SS-2 provides that in case of public companies, the Chairman shall not propose any Resolution in which he is deemed to be concerned or interested nor shall he conduct the proceedings for that item of business.

If the Chairman is interested in any item of business, without prejudice to his Voting Rights on Resolutions, he shall entrust the conduct of the proceedings in respect of such item to any Dis-Interested Director or to a Member, with the consent of the Members present, and resume the Chair after that item of business has been transacted.

Para 4.1.1 of SS-2 provides that if any Director is unable to attend the Meeting, the Chairman shall explain such absence at the Meeting.

Para 4.1.2 of SS-2 requires that Directors who attend General Meetings of the company and the Company Secretary shall be seated with the Chairman.

### **PRESENCE OF STATUTORY AUDITOR AND SECRETARIAL AUDITOR**

Section 146 of the Act requires the presence to Auditors in general meetings unless otherwise exempted, either himself or through his authorized representative, who shall also be qualified to be an auditor and shall have right to be heard at such meeting on any part of the business which concerns him as the auditor.

Para 4.2 of SS-2 requires that the Auditors, unless exempted by the company, shall, either by themselves or through their authorised representative, attend the General Meetings of the company and shall have the right to be heard at such Meetings on that part of the business which concerns them as Auditors.

The authorized representative who attends the General Meeting of the company shall also be qualified to be an Auditor.

Similarly, para 4.3 of SS-2 requires the secretarial auditor, unless exempted by the company shall, either by himself or through his authorized representative, attend the Annual General Meeting and shall have the right to be heard at such Meeting on that part of the business which concerns him as Secretarial Auditor.

The authorized representative who attends the General Meeting of the company shall also be qualified to be a secretarial auditor.

### **Proxies (Section 105)**

A person who is appointed by a member to attend and vote at a meeting in the absence of the member at the meeting is termed as proxy. Thus proxy is an agent of the member appointing him. The term 'proxy' is also used to refer to the instrument by which a person is appointed as proxy. Section 105 of the Companies Act, 2013 provides that a member, who is entitled to attend to vote, can appoint another person as a proxy to attend and vote at the meeting on his behalf. This section also provides the manner of appointing proxy. The provisions are as follows.

- (1) Who can appoint a proxy:** Any member of a company who is entitled to attend and vote at a meeting of the company shall be entitled to appoint another person as a proxy to attend and vote at the meeting on his behalf.

The SS added that where allowed, one or more proxies, to attend and vote instead of himself and a

Proxy need not be a Member.

However, a Proxy shall be a Member in case of companies with charitable objects etc. and not for profit registered under the specified provisions of the Act.

A Proxy can act on behalf of Members not exceeding fifty and holding in the aggregate not more than ten percent of the total share capital of the company carrying Voting Rights.

However, a Member holding more than ten percent of the total share capital of the company carrying Voting Rights may appoint a single person as Proxy for his entire shareholding and such person shall not act as a Proxy for another person or shareholder.

If a Proxy is appointed for more than fifty Members, he shall choose any fifty Members and confirm the same to the company before the commencement of specified period for inspection. In case, the Proxy fails to do so, the company shall consider only the first fifty proxies received as valid.

- (2) **Disabilities of proxy:** A proxy shall not have the right to speak at the meeting. A proxy cannot vote on a show of hands. A proxy is not counted for the purpose of quorum.
- (3) **Rights of proxy:** A proxy has the right to attend the meeting. A proxy has the right to vote only on a poll. A proxy, if eligible under section 109, has the right to demand a poll.
- (4) **Restriction on proxy:** A member of a company registered under section 8 (Not for Profit company) shall not be entitled to appoint any other person as his proxy unless such other person is also a member of such company.

A person appointed as proxy shall not act as proxy on behalf of more than fifty members and members holding in the aggregate more than ten percent of the total share capital of the company carrying voting rights.

A member holding more than 10% of the total share capital of the company carrying voting rights may appoint a single person as proxy, provided that such person shall not act as proxy for any other person or shareholder.

- (5) **Time limit for deposit of proxy forms:** The instrument appointing the proxy must be deposited with the company, 48 hours before the meeting. Any provision contained in the articles, requiring a longer period than 48 hours shall have effect as if a period of 48 hours had been specified.

#### **Secretarial standard of proxies:**

- (1) **Deposit of proxies:** Para 6.6.1 of SS-2 provides that proxies shall be deposited with the company either in person or through post not later than forty-eight hours before the commencement of the Meeting in relation to which they are deposited and a Proxy shall be accepted even on a holiday if the last date by which it could be accepted is a holiday.
- (2) **Records of proxies:** Para 6.9.1 of SS-2 requires that all Proxies received by the company shall be recorded chronologically in a register kept for that purpose.

Para 6.9.2 of SS-2 provides that in case any Proxy entered in the register is rejected, the reasons therefor shall be entered in the remarks column.

- (3) The prescribed form for appointing a proxy is Form No. MGT. 11. It needs to be in writing and signed by the appointer or his attorney duly authorised in writing. If the appointer is a body corporate, the instrument should be under its seal or be signed by an officer or an attorney duly authorised by the body corporate. An instrument appointing a proxy, if in MGT-11, shall not be

questioned on the ground that it fails to comply with any special requirement specified for such instrument by the article of a company.

Para 6.2.1 requires that an instrument appointing a Proxy shall be either in the Form specified in the Articles or in the Form set out in the Act.

The instrument of Proxy shall be signed by the appointer or his attorney duly authorized in writing, or if the appointer is a body corporate, be under its seal or be signed by an officer or an attorney duly authorized by it.

Para 6.2.2 requires that an instrument of Proxy duly filled, stamped and signed, is valid only for the Meeting to which it relates including any adjournment thereof.

Para 6.3 provides that an instrument of Proxy is valid only if it is properly stamped as per the applicable law. Unstamped or inadequately stamped Proxies or Proxies upon which the stamps have not been cancelled are invalid.

Para 6.4.1 requires that the Proxy-holder shall prove his identity at the time of attending the Meeting.

Para 6.4.2 provides that an authorized representative of a body corporate or of the President of India or of the Governor of a State, holding shares in a company, may appoint a Proxy under his signature.

Para 6.5.1 states that a Proxy form which does not state the name of the Proxy shall not be considered valid.

Para 6.5.2 states that undated proxy shall not be considered valid.

Para 6.5.3 provides that if a company receives multiple proxies for the same holdings of a Member, the Proxy which is dated last shall be considered valid; if they are not dated or bear the same date without specific mention of time, all such multiple Proxies shall be treated as invalid.

**Let us Remember:**

The prescribed proxy form is Form No. MGT 11

- (4) **Inspection of proxy:** Every member entitled to vote at a meeting of the company, or on any resolution to be moved thereat, is entitled to inspect the proxies lodged with the company, if at least 3 days notice in writing is given to the company. Such notice shall be received at least three days before the commencement of the Meeting. Such inspection can be taken during the period beginning 24 hours before the time fixed for the commencement of the meeting, during the business hours of the company, and ending with the conclusion of the meeting. Such inspection should be allowed between 9:00 am and 6:00 pm during such period.

A fresh requisition confirming to the above requirements, shall be given for inspection of Proxies in case the Original Meeting is adjourned.

- (5) **Revocation of proxy:** If after appointment of proxy, the member himself attends the meeting, it amounts to automatic revocation of proxy. But once the proxy has voted, it cannot be revoked.

Para 6.7.1 provides that if a Proxy had been appointed for the original meeting and such meeting is adjourned, any Proxy given for the adjourned Meeting revokes the Proxy given for the original Meeting.

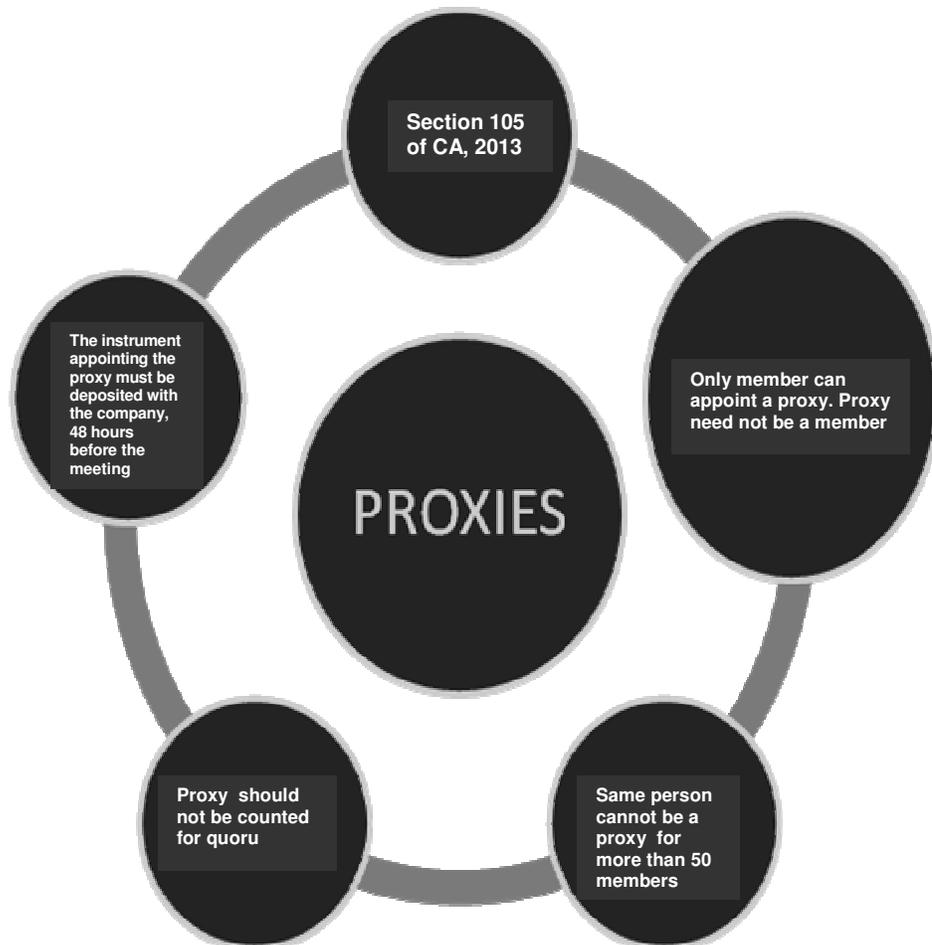
Para 6.7.2 provides that a proxy later in date revokes any Proxy/Proxies dated prior to such Proxy.

Para 6.7.3 provides that a Proxy is valid until written notice of revocation has been received by the

company before the commencement of the Meeting or adjourned Meeting, as the case may be.

An undated notice of revocation of Proxy shall not be accepted. A notice of revocation shall be signed by the same Member (s) who had signed the Proxy, in the case of joint Membership.

A Proxy need not be informed of the revocation of the Proxy issued by the Member.



**Illustrations**

**Question:** Annual General Meeting of a Public Company was scheduled to be held on 15.12.2015. Mr. A, a shareholder, issued two Proxies in respect of the shares held by him in favor of Mr. 'X' and Mr. 'Y'. The proxy in favor of 'Y' was lodged on 12.12.2015 and the one in favor of Mr. X was lodged on 15.12.2015. The company rejected the proxy in favor of Mr. Y as the proxy in favor of Mr. Y was of dated 12.12.2015 and thus in favor of Mr. X was of dated 15.12.2015. Is the rejection by the company in order?

**Hint:** As per Section 105 of the Companies Act, 2013 a proxy should be deposited 48 hours before the time of the meeting. In the given case, the proxies should have, therefore, been deposited on or before 13.12.2015 (the date of the meeting being 15.12.2015). X deposited the proxy on 15.12.2015.

Therefore, proxy in favour of Mr. X has become invalid. Thus, rejecting the proxy in favour of Mr. Y is unsustainable. Proxy in favor of Y is valid since it is deposited in time.

**Question:** The Chairman of the meeting of a public company received a Proxy 54 hours before the time fixed for the start of the meeting. He refused to accept the Proxy on the ground that the Articles of the

company provided that a Proxy must be filed 60 hours before the start of the meeting. Decide, under the provisions of the Companies Act, 2013 whether the Proxy holder can compel the Chairman to admit the Proxy?

Hint: As per Section 105 of the Companies Act, 2013 proxy shall be deposited with the company within 48 hours before the meeting.

Any provisions contained in the Articles of a company that requires a longer period than 48 hours before a meeting of the company for depositing a proxy shall be void. Thus contention of Mr X is valid.

Question: Mr. A, a member of XYZ Limited, appoints Mr. B as his proxy to attend the general meeting of the company. Later he (Mr. A) also attends the meeting. Both Mr. A (the member) and Mr. B (the proxy) voted on a particular resolution in the meeting. Mr. A's vote was declared invalid by the chairman stating that since he has appointed the proxy and Mr. B's vote has been considered as valid. Mr. A objects to the decision of the Chairman. Decide, under the provisions of the Companies Act, 2013 whether Mr. A's objection shall be taxable.

Hint: Decision by Chairman is invalid. Since Mr. A i.e. a member himself attended a meeting and voted on resolution, it will amount to revocation of proxy. Thus any vote put by Mr. B i.e. proxy shall be invalid.

## **VOTING**

### **Restriction on Voting Rights (Section 106)**

The articles of a company may provide that a member shall not exercise any voting right in respect of any shares registered in his name on which any calls or other sums presently payable by him have not been paid or on which company has exercised any right or lien. No member can be prohibited from exercising his voting right on any other ground.

### **Voting by Show of Hands (Section 107)**

At any general meeting, a resolution put to the vote of the meeting shall in the first instance be decided on a show of hands, unless-

- (a) A poll is demanded under section 109 of the Act.
- (b) Voting is carried out electronically under section 108 of the Act.

A declaration by the Chairman of the meeting of the passing of a resolution (that the resolution has been passed or failed, as the case may be) on show of hands and an entry to that effect in the minutes book shall be conclusive evidence of the fact of passing of such resolution. No proof of numbers of votes casts in favor of and against the resolution is required.

### **Voting through Electronic Means (Section 108)**

General meetings of companies are held at their registered offices and it is not possible for every member specially members holding minor shares to travel up to the registered office of the company and participate in the general meetings of the company.

To eliminate this type of difficulty and to enhance the participation of minority members, concept of e-voting has been introduced by the Companies Act 2013. Now a member can cast his vote easily through electronic mode without physically attending the general meeting.

E-voting do not eliminate members right to physically attend and vote at the general meeting. However member can cast his vote through one mode only. A member after casting his vote through e-voting can go and attend the general meeting but cannot cast vote in that general meeting.

The facility of Remote e-voting does not dispose with the requirements of holding a General Meeting by the company.

**Applicability:** Section 108 of the Act shall apply to such companies as may be prescribed by the Central Government. The prescribed class of companies, for this purpose, are-

- (i) All companies whose equity shares are listed on a recognized stock exchange; and
- (ii) All companies having 1000 or more members.

However, the provisions of section 108 shall not apply to a company referred to in chapter XB (Companies listed on SME exchange) or chapter XC (Companies listed on institutional trading platform without IPO) of the SEBI (Issue of Capital and Depository Receipt) Regulations, 2009.

Following companies are out of ambit of e-voting:-

1. Companies having whose debenture/preference shares are only listed.
2. Companies listed on SME trading platform.
3. Companies listed on institutional trading platform.

**Legal Requirement:**

- (a) A company to which section 108 is applicable, shall provide to its members facility to exercise their right to vote on resolution proposed at general meetings by electronic means.
- (b) a resolution proposed to be considered through voting by electronic means shall not be withdrawn.

**Meaning of certain terms:**

Rule 20 of Companies (Management and Administration) Amendment Rules, 2015 defines some of the terms relating to voting through electronic means as follows:

- (i) “cut-off date” means a date not earlier than seven days before the date of general meeting for determining the eligibility to vote by electronic means or in the general meeting;
- (ii) “cyber security” means protecting information, equipment, devices, computer, computer resource, communication device and information stored therein from unauthorised access, use, disclosures, disruption, modification or destruction;
- (iii) “electronic voting system” means a secured system based process of display of electronic ballots, recording of votes of the members and the number of votes polled in favour or against, in such a manner that the entire voting exercised by way of electronic means gets registered and counted in an electronic registry in a centralised server with adequate cyber security;
- (iv) “remote e-voting” means the facility of casting votes by a member using an electronic voting system from a place other than venue of a general meeting;
- (v) “secured system” means computer hardware, software, and procedure that
  - (a) are reasonably secure from unauthorised access and misuse;
  - (b) provide a reasonable level of reliability and correct operation;
  - (c) are reasonably suited to performing the intended functions; and
  - (d) adhere to generally accepted security procedures;
- (vii) “voting by electronic means” includes “remote e-voting” and voting at the general meeting through an electronic voting system which may be the same as used for remote e-voting .

**The Board shall:**

**(a) appoint one or more scrutinisers for e-voting or the ballot process,**

The scrutiniser (s) may be a Company Secretary in Practice, a Chartered Accountant in Practice, a Cost Accountant in Practice, or an Advocate or any other person of repute who is not in the employment of the company and who can, in the opinion of the Board, scrutinise the e-voting process or the ballot process, as the case may be, in a fair and transparent manner.

The scrutiniser (s) so appointed may take assistance of a person who is not in employment of the company and who is well-versed with the e-voting system.

Prior consent to act as a scrutiniser(s) shall be obtained from the scrutiniser(s) and placed before the Board for noting.

**(b) appoint an Agency – NSDL, CDSL or other such agency;**

**(c) decide the cut-off date for the purpose of reckoning the names of Members who are entitled to Voting Rights;**

The cut-off date for determining the Members who are entitled to vote through Remote e-voting or voting at the meeting shall be a date not earlier than seven days prior to the date fixed for the Meeting.

Only Members as on the cut-off date, who have not exercised their Voting Rights through Remote e-voting, shall be entitled to vote at the Meeting.

**(d) authorise the Chairman or in his absence, any other Director to receive the scrutiniser's register, report on e-voting and other related papers with requisite details.**

The scrutiniser(s) is required to submit his report within a period of three days from the date of the meeting.

The Chairman or any other director so authorized shall countersign the scrutiniser's report so received.

The notice of the meeting shall clearly state that:-

- (i) the company is providing facility for voting by electronic means and the business may be transacted through such voting.
- (ii) the facility for voting, either through voting by electronic means or ballot/polling paper shall also be made available at the meeting and members attending the meeting who have not already cast their vote by remote e-voting shall be able to exercise their right at the meeting.
- (iii) that the members who have cast their vote by remote e-voting prior to the meeting may also attend the meeting but shall not be entitled to cast their vote again.

**(A) Additional Disclosures in notice:**

The notice shall –

- (i) indicate the process and manner for voting by electronic means;
- (ii) indicate the time schedule including the time period during which the votes may be cast by remote e-voting;
- (iii) provide the details about the login ID;

- (iv) specify the process and manner for generating or receiving the password and for casting of vote in a secure manner.

**(B) Public notice by way of advertisement:**

- (i) The company shall cause a public notice by way of an advertisement to be published, immediately on completion of dispatch of notice of general meeting.
- (ii) The public notice shall be published at least twenty-one days before the date of general meeting, at least once in a vernacular newspaper in the principal vernacular language of the district in which the registered office of the company is situated, and having a wide circulation in that district, and at least once in English language in an English newspaper having country-wide circulation.
- (iii) The public notice shall specify the following matter in the said advertisement
  - (a) a statement that the business may be transacted through voting by electronic means;
  - (b) The date and time of commencement of remote e-voting;
  - (c) The date and time of end of remote e-voting;
  - (d) Cut-off date;
  - (e) The manner in which persons who have acquired shares and become members of the company after the dispatch of notice may obtain the login ID and password;
  - (f) A statement that –
    - (i) remote e-voting shall not be allowed beyond the said date and time;
    - (ii) the manner in which the company shall provide for voting by members present at the meeting; and
    - (iii) a member may participate in the general meeting even after exercising his right to vote through remote e-voting but shall not be allowed to vote again in the meeting; and
    - (iv) a person whose name is recorded in the register of members or in the register of beneficial owners maintained by the depositories as on the cut-off date only shall be entitled to avail the facility of remote e-voting as well as voting in the general meeting;
  - (g) Website address of the company, if any, and of the agency where notice of the meeting is displayed; and
  - (h) Name, designation, address, email id and phone number of the person responsible to address the grievances connected with facility for voting by electronic means.

The public notice shall be placed on the website of the company, if any, and of the agency;

Such notice shall remain on the website till the date of general meeting.

**(C) Remote e-voting:**

- (i) The facility for remote e-voting shall remain open for not less than three days and shall close at 5.00 p.m. on the date preceding the date of the general meeting.
- (ii) During the period when facility for remote e-voting is provided, the members of the company, holding shares either in physical form or in dematerialised form, as on the cut-off date, may opt for remote e-voting.
- (iii) Once a member has cast his vote on a resolution, he shall not be allowed to change it subsequently

or cast the vote again.

- (a) A member may participate in the general meeting even after exercising his right to vote through remote e-voting but shall not be allowed to vote again.
- (b) At the end of the remote e-voting period, the facility shall forthwith be blocked.

**(D) Appointment of scrutinizer:**

- (i) The Board of Directors shall appoint one or more scrutinizer(s).
- (ii) The scrutinizer(s) may be a Chartered Accountant in practice, Cost Accountant in practice, or Company Secretary in practice or an Advocate, or any other person who is not in employment of the company and is a person of repute who, in the opinion of the Board can scrutinise the voting and remote e-voting process in a fair and transparent manner. At least one of the scrutinisers shall be a member who is present at the Meeting provided such members is available and willing to be appointed.
- (iii) The scrutinizer may take assistance of a person who is not in employment of the company and who is well-versed with the electronic voting system.
- (iv) The scrutinizer shall be willing to be appointed and be available for the purpose of ascertaining the requisite majority. For this purpose, prior consent to act as scrutiner(s) shall be obtained from the scrutinizer(s) and placed before the Board for noting.
- (v) The scrutinizer(s) shall maintain a register to record the assent or dissent received, mentioning the particulars of members.
- (vi) The register and all other papers relating to voting by electronic means shall remain in the safe custody of the scrutinizer(s) until the Chairman considers, approves and signs the minutes and thereafter, the scrutinizer(s) shall hand over the register and other related papers to the company.

**(E) Voting at General Meeting:**

- (i) During general meeting, a company may opt to provide the same electronic voting system as used during remote e-voting. In such a case, the members attending the general meeting and who have not exercised their right to vote through remote e-voting, shall be entitled to vote using the electronic voting system.
- (ii) At the general meeting, after conclusion of the discussion, the chairman shall, with the assistance of scrutiners, allow voting on the resolutions, by use of polling paper or by using an electronic voting system for all those members who are present at the general meeting but have not cast their votes by availing the remote e-voting facility.

**(F) Declaration of result of voting:**

- (i) The scrutinizer shall, immediately after the conclusion of voting at the general meeting, first count the votes cast at the meeting, thereafter unblock the votes cast through remote e-voting in the presence of at least two witnesses not in the employment of the company.
- (ii) The scrutinizer shall make, not later than three days of conclusion of the meeting, a consolidated scrutiner's report of the total votes cast in favor or against, if any, to the Chairman or a person authorized by him in writing who shall countersign the same.
- (iii) The Chairman or a person authorized by him in writing shall declare the result of the voting forthwith.

- (iv) The result of the voting, with details of the number of votes cast for and against the Resolution, invalid votes and whether the Resolution has been carried or not shall be displayed on the Notice Board of the company at its Registered Office and its Head Office as well as Corporate Office, if any, if such office is situated elsewhere. Further, the results of voting alongwith the scrutinizer's report shall also be placed on the website of the company, in case of companies having a website and of the Agency, immediately after the results are declared.
- (v) The scrutinizers' register, report and other related papers received from the scrutinizer(s) shall be kept in the custody of the Company Secretary or any other person authorised by the Board for this purpose.
- (vi) The manner in which members have cast their votes, that is, affirming or negating the resolution, shall remain secret and not available to the Chairman, scrutinizer or any other person till the votes are cast in the general meeting.
- (vii) If the requisite number of votes are cast in favor of the resolution, the resolution shall be deemed to be passed on the date of relevant general meeting.
- (viii) The results declared along with the report of the scrutinizer shall be placed on the notice board of the company at its registered office and its head office as well as corporate office, if any, if such office is situated elsewhere and on the website of the company, if any, and on the website of the agency immediately after the result is declared by the Chairman.
- (ix) In case of companies whose equity shares are listed on a recognized stock exchange, the company shall, simultaneously, forward the results to the concerned stock exchange or exchanges where its equity shares are listed and such stock exchange or exchanges shall place the results on its or their website.

### **Demand for Poll (Section 109)**

Before or on the declaration of the result of the voting on any resolution on show of hands, a poll may be ordered to be taken by the Chairman of the meeting on his own motion, and shall be ordered to be taken by him on a demand made in that behalf by the following person(s):

- (a) in the case a company having a share capital: by the members present in person or by proxy, where allowed, and having not less than one-tenth of the total voting power or holding shares on which an aggregate sum of not less than Rs.5,00,000/- or such higher amount as may be prescribed, has been paid-up; and
- (b) in the case of any other company: by any member or members present in person or by proxy, where allowed, and having not less than one-tenth of the total voting power.

The Chairman shall get the validity of the demand verified.

The demand for a poll may be withdrawn at any time by the persons who made the demand.

#### *Time for taking poll and declaring the result*

A poll shall be taken forthwith, if it is demanded for adjournment of the meeting or appointment of Chairman of the meeting.

A poll shall be taken at such time, not being later than 48 hours from the time when the demand was made on any other question. The Chairman shall announce the date, venue and time of taking the poll to enable members to have adequate and convenient opportunity to exercise their votes. Further, the Chairman may permit any member who so desires to be present at the time of counting the votes. The Chairman shall

inform the members, the modes and the time of such communication, which shall in any case be within 24 hours of closer of meeting in case the date, venue not announced.

Where a poll is to be taken, the Chairman of the meeting shall appoint such number of persons, as he deems necessary, to scrutinise the poll process and votes given on the poll and to report thereon to him in the manner as may be prescribed.

The result of the poll shall be deemed to be the decision of the meeting on the resolution on which the poll was taken.

### **Manner to get poll process scrutinized**

*Rule 21 of Companies (Management and Administration) Rules, 2014 provides that the chairman of a meeting shall ensure that –*

- The Scrutinizers are provided with the Register of Members, specimen signatures of the members, Attendance Register and Register of Proxies.
- The Scrutinizers are provided with all the documents received by the Company.
- The Scrutinizers initial the Polling papers and distribute them to the members and proxies present at the meeting. In case of joint shareholders, the polling paper shall be given to the firstnamed holder or in his absence to the joint holder attending the meeting as appearing in the chronological order in the folio. The Polling paper shall be in Form No. MGT.12.
- The Scrutinizers keep a record of the polling papers issued.
- The Scrutinizers lock and seal an empty polling box in the presence of the members and proxies.
- The Scrutinizers open the Polling box in the presence of two persons as witnesses after the voting process is over.
- In case of ambiguity about the validity of a proxy, the Scrutinizers decide the validity in consultation with the Chairman.
- The Scrutinizers shall ensure that if a member who has appointed a proxy has voted in person, the proxy 's vote shall be disregarded.
- The Scrutinizers count the votes cast on poll and prepare a report thereon addressed to the Chairman.
- Where voting is conducted by electronic means, the company shall provide all the necessary support, technical and otherwise, to the Scrutinizers in orderly conduct of the voting and counting the result thereof.
- The Scrutinizers' report state total votes cast, valid votes, votes in favour and against the resolution including the details of invalid polling papers and votes comprised therein.
- The Scrutinizers submit the Report to the Chairman who shall counter-sign the same.
- The Chairman declare the result of Voting on poll. The result may either be announced by him or a person authorized by him in writing.

The scrutinizer/s appointed for the poll, shall submit a report to the Chairman of the meeting in Form No. MGT No. 13 within 7 days from the date the poll is taken. The report shall be signed by the scrutinizer / all the scrutinizers, in case there is more than one scrutinizer.

### Voting by Poll in General Meeting

In case of Companies for which e-voting is mandatory, poll may be the only other method left out to cast vote by remaining shareholders

For AGM, e-voting to be kept open for 1-3 days & to close at least 3 days before the day of AGM.

#### Mandatory E-Voting

Section 108 of Companies Act, 2013 read with Rule 20 of company (Management & Administration) Rules, 2014

- ✓ Listed Companies
- ✓ Companies having 1,000 or more Shareholders

All Companies has to pass all the resolution of the meeting electronically as per SEBI

**Note:** Sections 102, 103, 104, 105, 106, 107 and 109 shall apply in case of private company unless otherwise specified in respective sections of articles of the company provided otherwise.

#### Postal Ballot (Section 110)

**Meaning of postal ballot:** As per section 2(65) "postal ballot" means voting by post or through any electronic mode. It includes voting by shareholders by postal or electronic mode instead of voting personally for transacting businesses in a general meeting of the company.

Each item proposed to be passed through postal ballot shall be in the form of a Resolution and shall be accompanied by an explanatory statement which shall set out all such facts as would enable a Member to understand the meaning, scope and implications of the item of business and to take a decision thereon.

A company shall send a notice and draft resolution by registered post to all shareholders explaining the reasons and requesting them to send their assent or dissent in writing on a postal ballot. If a resolution is assented to by the requisite majority of the shareholders by means of postal ballot, it shall be deemed to have been duly passed at a general meeting convened in that behalf.

**Meaning of requisite majority:** Requisite majority with regard to special resolution means votes cast in favor of the business is three times more than the votes cast against, with regard to ordinary resolution, votes cast in favor is more than the votes cast against.

- (a) Company may transact such items of business as the Central Government may, by notification, declare to be transacted only by means of postal ballot. In case of companies which are required to provide facility to members to vote by electronic means under section 108, the Act now makes it non-mandatory for these companies to transact business through postal ballot.
- (b) A company may use postal ballot for transacting any item of business, other than
  - (i) Ordinary business and

- (ii) Any business in respect of which directors or auditors have a right to be heard at any meeting.

**Business to be transacted through postal ballot: [Rule 22 of Companies (Management and Administration) Rules, 2014]**

The following items of business shall be transacted only by means of voting through postal ballot:

- (a) Alteration of the objects clause of the memorandum and in the case of the company in existence immediately before the commencement of the Act, alteration of the main objects of the memorandum;
- (b) Alteration of articles of association in relation to insertion or removal of provisions defining a private company.
- (c) Change in place of registered office outside the local limits of any city, town or village.
- (d) Change in objects for which a company has raised money from public through prospectus and still has any unutilized amount out of the money so raised.
- (e) Issue of shares with differential rights as to voting or dividend or otherwise.
- (f) Variation in the rights attached to a class of shares or debentures or other securities.
- (g) Buy-back of shares by a company.
- (h) Election of a 'small shareholders' director.
- (i) Sale of the whole or substantially the whole of an undertaking of a company.
- (j) Giving loans or extending guarantee or providing security exceeding 60% of its paid up share capital, free reserves and securities premium account or 100% of its free reserves and securities premium account.
- (k) any other resolution prescribed under any applicable law, rules or regulations.

*Any item of business required to be transacted by means of postal ballot (as stated above), may be transacted at a general meeting by a company which is required to provide the facility to members to vote by electronic means under section 108, in the manner provided in that section.*

Following companies are not required to transact any business through postal ballot.

- (i) One person company
- (ii) All other companies having members up to 200.

**Secretarial Standard on postal ballot:**

Para 16.1 of SS-2 provides that every company, except a company having less than or equal to two hundred Members, shall transact items of business as prescribed, only by means of postal ballot instead of transacting such business at a General Meeting. Ordinary Business shall not be transacted by means of a postal ballot.

**Rule 22 of the Companies (Management and Administration) Rules, 2014** lay down the procedure to be followed for conducting business through postal ballot.

**(1) Notice to all shareholders:** The company shall send a notice to all the shareholders, along with a draft resolution explaining the reasons therefore and requesting them to send their assent or dissent in writing on a postal ballot because postal ballot means voting by post or through electronic means within a period of thirty days from the date of dispatch of the notice.

**(2) Mode of sending documents:** The notice shall be sent

- (a) By Registered Post or speed post, or
- (b) Through electronic means like registered e-mail id or
- (c) Through courier service

**Secretarial Standard on Notice of postal ballot (Para 16):**

Notice of the postal ballot shall be given in writing to every Member of the company. Such Notice shall be sent either by registered post or speed post, or by courier or by e-mail or by any other electronic means at the address registered with the company.

The Notice shall be accompanied by the postal ballot form with the necessary instructions for filling, signing and returning the same. In case the Notice and accompanying documents are sent to Members by e-mail, these shall be sent to the Members' e-mail addresses, registered with the company or provided by the depository, in the manner prescribed under the Act.

Such Notice shall also be given to the Directors and Auditors of the company, to the Secretarial Auditor, to Debenture Trustees, if any, and, wherever applicable or so required, to other specified recipients.

Notice shall specify the day, date, time and venue where the results of the voting by postal ballot will be announced and the link of the website where such results will be displayed.

Notice shall also specify the mode of declaration of the results of the voting by postal ballot.

Notice of the postal ballot shall inform the Members about availability of e-voting facility, if any, and provide necessary information thereof to enable them to access such facility.

In case the facility of e-voting has been made available, the provisions relating to conduct of e-voting shall apply, *mutatis mutandis*, as far as applicable.

Notice shall describe clearly the e-voting procedure.

Notice shall also clearly specify the date and time of commencement and end of e-voting, if any and contain a statement that voting shall not be allowed beyond the said date and time. Notice shall also contain contact details of the official responsible to address the grievances connected with the e-voting for postal ballot.

Notice shall clearly specify that any Member cannot vote both by post and e-voting and if he votes both by post and e-voting, his vote by post shall be treated as invalid.

**(3) Publishing of an advertisement:** The company shall issue an advertisement to be published at least once in a vernacular newspaper in the principal vernacular language of the district in which the registered office of the company is situated, and having a wide circulation in that district, and at least once in English language in an English newspaper having a wide circulation in that district, stating that the ballot papers have been dispatched.

The advertisement shall specify the following matters, namely:-

- (a) A statement to the effect that the business is to be transacted by postal ballot which includes voting by electronic means;
- (b) The date of completion of dispatch of notices;
- (c) The date of commencement of voting (postal and e-voting);

- (d) The date of end of voting (postal and e-voting);
- (e) A statement that any postal ballot received from the member beyond the said date will not be valid and voting whether by post or by electronic means shall not be allowed beyond the said date; For this purpose the SS-2 provides that the advertisement shall include a statement that any posted ballot form received from the member after thirty days from the date of dispatch of Notice will not be valid.
- (f) A statement to the effect that members, who have not received postal ballot forms may apply to the company and obtain a duplicate thereof;
- (g) The Contact details of the person responsible to address the grievances connected with the voting by postal ballot including voting by electronic means; and
- (h) day, date, time and venue of declaration of results and the link of the website where such results will be displayed.

Notice and the advertisement shall clearly mention the record date as on which the right of voting of the Members shall be reckoned and state that a person who is not a Member as on the record date should treat this Notice for information purposes only.

**(4) Notice to be placed on the website:**

The notice of the postal ballot shall also be placed on the website of the company forthwith after the notice is sent to the members.

Such notice shall remain on such website till the last date for receipt of the postal ballots from the members.

**(5) Appointment of scrutinizer:** The Board of directors shall appoint one scrutinizer, who is not in employment of the company and who, in the opinion of the Board can conduct the postal ballot voting process in a fair and transparent manner.

The scrutinizer may be a Company Secretary in Practice, a Chartered Accountant in Practice, a Cost Accountant in Practice, an Advocate or any other person of repute who is not in the employment of the company and, who can in the opinion of the Board, scrutinise the postal ballot process in a fair and transparent manner.

The scrutinizer shall however not be an officer or employee of the company.

The scrutinizer so appointed may take assistance of a person who is not in employment of the company and who is well-versed with the e-voting system.

Prior consent to act as a scrutinizer shall be obtained from the scrutinizer and placed before the Board for noting.

**(6) Safe custody of registers and papers:** Postal ballot received back from the shareholders shall be kept in the safe custody of the scrutinizer and after the receipt of assent or dissent of the shareholder in writing on a postal ballot, no person shall deface or destroy the ballot paper or declare the identity of the shareholder.

**(7) Submission of report of the scrutinizer:** The scrutinizer shall submit his report as soon as possible after the last date of receipt of postal ballots but not later than seven days thereof.

**(8) Maintenance of register by the Scrutinizer:** The scrutinizer shall maintain a register either manually or electronically to record their assent or dissent received, mentioning the particulars of the shareholder and details of postal ballots which are received in defaced or mutilated form and postal ballot forms which are

invalid.

**(9) Preservation of postal ballots:** The postal ballot and all other papers relating to postal ballot including voting by electronic means, shall be under the safe custody of the scrutinizer till the chairman considers, approves and signs the minutes and thereafter, the scrutinizer shall return the ballot papers and other related papers or register to the company who shall preserve such ballot papers and other related papers or register safely.

**(10) Reply from members:** The assent or dissent received after thirty days from the date of issue of notice shall be treated as if reply from the member has not been received.

**(11) Declaration of result:** The results shall be declared by placing it, along with the scrutinizer's report, on the website of the company.

**(12) Resolution deemed to be passed in general meeting:** The resolution shall be deemed to be passed on the date of at a meeting convened in that behalf.

**(13) Applicability of Rule 20:** The provisions of Rule 20 of Companies (Management and Administration) Rules, 2014 regarding voting by electronic means shall apply, as far as applicable, with the necessary changes to this rule in respect of the voting by electronic means.

**A postal ballot form shall be considered invalid if:**

- (a) A form other than one issued by the company has been used;
- (b) It has not been signed by or on behalf of the Member;
- (c) Signature on the postal ballot form doesn't match the specimen signatures with the company
- (d) It is not possible to determine without any doubt the assent or dissent of the Member;
- (e) Neither assent nor dissent is mentioned;
- (f) Any competent authority has given directions in writing to the company to freeze the Voting Rights of the Member;
- (g) The envelope containing the postal ballot form is received after the last date prescribed;
- (h) The postal ballot form, signed in a representative capacity, is not accompanied by a certified copy of the relevant specific authority;
- (i) It is received from a Member who is in arrears of payment of calls;
- (j) It is defaced or mutilated in such a way that its identity as a genuine form cannot be established;
- (k) Member has made any amendment to the Resolution or imposed any condition while exercising his vote. (Para 16.5.3 of SS-2)

**Rescinding the Resolution**

A Resolution passed by postal ballot shall not be rescinded otherwise than by a Resolution passed subsequently through postal ballot. **(Para 16.8 of SS-2)**

**Modification to the Resolution**

No amendment or modification shall be made to any Resolution circulated to the Members for passing by means of postal ballot. **(Para 16.9 of SS-2)**

### Procedure for Postal Ballot

1. Rule 22 of the Companies (Management and Administration) Rules 2014 lay down procedural details.
2. Where a company decides to pass any resolution by way of postal ballot, it shall send a notice to all the shareholders, along with a draft resolution explaining the reasons there for. The Company shall request members them to send their assent or dissent in writing on a postal ballot within a period of thirty days from the date of dispatch of the notice. Postal ballot means voting by post or through electronic means. [Rule 22(1)]
3. The notice shall be sent either
  - (a) by Registered Post or speed post, or
  - (b) through electronic means like registered e-mail id or
  - (c) through courier service

for facilitating the communication of the assent or dissent of the shareholder to the resolution within the said period of thirty days. [Rule 22(2)]
4. An advertisement shall be published at least once in a vernacular newspaper in the principal vernacular language of the district in which the registered office of the company is situated, and having a wide circulation in that district, and at least once in English language in an English newspaper having a wide circulation in that district, about having dispatched the ballot papers and specifying therein, inter alia, the following matters, namely:
  - (a) a statement to the effect that the business is to be transacted by postal ballot which includes voting by electronic means;
  - (b) the date of completion of dispatch of notices;
  - (c) the date of commencement of voting;
  - (d) the date of end of voting;
  - (e) the statement that any postal ballot received from the member beyond the said date will not be valid and voting whether by post or by electronic means shall not be allowed beyond the said date;
  - (f) a statement to the effect that members, who have not received postal ballot forms may apply to the company and obtain a duplicate thereof; and
  - (g) contact details of the person responsible to address the grievances connected with the voting by postal ballot including voting by electronic means. [Rule 22(3)]
5. The notice of the postal ballot shall also be placed on the website of the company forthwith after the notice is sent to the members and such notice shall remain on such website till the last date for receipt of the postal ballots from the members. [Rule 22(4)]
6. The Board of directors shall appoint one scrutinizer, who is not in employment of the company and who, in the opinion of the Board can conduct the postal ballot voting process in a fair and transparent manner. [Rule 22(5)]
7. The scrutinizer shall be willing to be appointed and be available for the purpose of ascertaining the requisite majority. [Rule 22(6)]
8. Postal ballot received back from the shareholders shall be kept in the safe custody of the scrutinizer and after the receipt of assent or dissent of the shareholder in writing on a postal ballot, no person shall deface or destroy the ballot paper or declare the identity of the shareholder. [Rule 22(8)]

9. The scrutinizer shall submit his report as soon as possible after the last date of receipt of postal ballots but not later than seven days thereof. [Rule 22(9)]
10. The scrutinizer shall maintain a register either manually or electronically to record their assent or dissent received, mentioning the particulars of name, address, folio number or client ID of the shareholder, number of shares held by them, nominal value of such shares, whether the shares have differential voting rights, if any, details of postal ballots which are received in defaced or mutilated form and postal ballot forms which are invalid. [Rule 22(10)]
11. The postal ballot and all other papers relating to postal ballot including voting by electronic means, shall be under the safe custody of the scrutinizer till the chairman considers, approves and signs the minutes and thereafter, the scrutinizer shall return the ballot papers and other related papers or register to the company who shall preserve such ballot papers and other related papers or register safely. [Rule 22(11)]
12. The assent or dissent received after thirty days from the date of issue of notice shall be treated as if reply from the member has not been received. [Rule 22(12)]
14. The results shall be declared by placing it, along with the scrutinizer's report, on the website of the company. [Rule 22(13)]
15. The provisions of rule 20 regarding voting by electronic means shall apply, as far as applicable, *mutatis mutandis* to this rule in respect of the voting by electronic means. [Rule 22(15)]

**Sample Postal Ballot Form**

**(On the letterhead of the Company)**

1. Name and Registered Address of the: sole / first named Member

2. Name(s) of Joint-Holder(s), if any :

3. Registered Folio No. /DP ID No.\* : /Client ID No.\* (\*Applicable to Members holding shares in dematerialized form)

4. Number of equity shares held :

5. I/We hereby exercise my / our vote in respect of the under mentioned resolutions to be passed through Postal Ballot as stated in the Notice dated February 20, 2015 of the Company by sending my / our assent or dissent to the said Resolution by placing the tick (√) mark in the appropriate box below:

Item No.	Brief Particulars of the Resolution	No. of Shares	I / We assent to the Resolution (FOR)	I / We dissent to the Resolution (AGAINST)

Place: \_\_\_\_\_

Date: \_\_\_\_\_

Signature of Shareholder

**Circulation of Members' Resolution (Section 111)**

As per Section 111, a company shall, on requisition in writing of certain number of members, give notice to members of any proposed resolution intended to be moved in the meeting or circulate any statement with

respect to matters referred in proposed resolution. The company shall be bound to give notice of resolution only if the requisition is deposited not less than six weeks before the meeting. In case of other requisition not less than 2 weeks before the meeting. The statement need not be circulated if the Central Government declares that the right conferred is being abused to secure needless publicity for defamatory matters. If default is made the company and every officer of the company shall be punishable with fine.

### **Maintenance of Minutes of Meetings**

The minutes refer to a written record of business transacted at a meeting. Section 118 provides that every company shall prepare, sign and keep minutes of proceedings of every general meeting, including the meeting called by the requisitionists and all proceedings of meeting of any class of shareholders or creditors or Board of Directors or committee of the Board and also resolution passed by postal ballot within thirty days of the conclusion of every such meeting concerned. In case of meeting of Board of Directors or of a committee of Board, the minutes shall contain name of the directors present and also name of dissenting director or a director who has not concurred the resolution. The chairman shall exercise his absolute discretion in respect of inclusion or non-inclusion of the matters which is regarded as defamatory of any person, irrelevant or detrimental to company's interest in the minutes. Minutes kept shall be evidence of the proceedings recorded in a meeting and containing fair and correct summary of the proceeding thereat.

*As per 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.*

### **Secretarial Standard on Minutes**

**Procedure of maintenance of minutes:** Minutes shall be recorded in books maintained for that purpose. **(Para 17.1.1 of SS-2)**

A distinct Minutes Book shall be maintained for Meetings of the Members of the company, creditors and others as may be required under the Act. **(Para 17.1.2 of SS-2)**

Resolutions passed by postal ballot shall be recorded in the Minutes book of General Meetings.

#### **Precautions to be taken while preparing the minutes:**

**(1) Uniformity in the manner of maintaining minutes:** Minutes may be maintained in electronic form in such manner as prescribed under the Act and as may be decided by the Board. Minutes in electronic form shall be maintained with Time stamp. (Para 17.1.3 of SS-2). Time stamp under SS-2 has been defined to mean the current time of an event that is recorded by a secured computer system and is used to describe the time that is printed to a file or other location to help keep track of when data is added, removed, sent or received.

Every company shall, however, follow a uniform and consistent form of maintaining the Minutes. Any deviation in such form of maintenance shall be authorized by the Board.

**(2) Page Numbering:** The pages of the Minutes Books shall be consecutively numbered. **(Para 17.1.4 of SS-2)**

This shall be followed irrespective of a break in the Book arising out of periodical binding in case the Minutes are maintained in physical form. This shall be equally applicable for maintenance of Minutes Book in electronic form with Time stamp.

In the event any page or part thereof in the Minutes Book is left blank, it shall be scored out and initialled by

the Chairman who signs the Minutes.

Minutes shall not be pasted or attached to the Minutes Book, or tampered with in any manner. (Para 17.1.5 of SS-2)

(1) Binding of minutes: Minutes of Meetings, if maintained in loose-leaf form, shall be bound periodically depending on the size and volume. (Para 17.1.6 of SS-2)

There shall be a proper locking device to ensure security and proper control to prevent removal or manipulation of the loose leaves.

(2) Place of keeping minutes: Minutes Books shall be kept at the Registered Office of the company or at such other place, as may be approved by the Board. (Para 17.1.7 of SS-2)

### **Para 17.2 of SS-2 prescribes for Contents of Minutes**

#### **(i) General Contents**

Minutes shall state, at the beginning the Meeting, name of the company, day, date, venue and time of commencement and conclusion of the Meeting. In case a Meeting is adjourned, the Minutes shall be entered in respect of the original Meeting as well as the adjourned Meeting. In respect of a Meeting convened but adjourned for want of Quorum a statement to that effect shall be recorded by the Chairman or any Director present at the Meeting in the Minutes.

Minutes shall record the names of the Directors and the Company Secretary present at the Meeting.

The names of the Directors shall be listed in alphabetical order or in any other logical manner, but in either case starting with the name of the person in the Chair.

#### **(ii) Specific Contents**

Minutes shall, inter alia, contain:

- (a) The Record of election, if any, of the Chairman of the Meeting.
- (b) The fact that certain registers, documents, the Auditor's Report and Secretarial Audit Report, as prescribed under the Act were available for inspection.
- (c) The Record of presence of Quorum.
- (d) The number of Members present in person including representatives.
- (e) The number of proxies and the number of shares represented by them.
- (f) The presence of the Chairmen of the Audit Committee, Nomination and Remuneration Committee and Stakeholders Relationship Committee or their authorised representatives.
- (g) The presence if any, of the Secretarial Auditor, the Auditors, or their authorised representatives, the Court/Tribunal appointed observers or scrutinisers.
- (h) Summary of the opening remarks of the Chairman.
- (i) Reading of qualifications, observations or comments or other remarks on the financial transactions or matters which have any adverse effect on the functioning of the company, as mentioned in the report of the Auditors.
- (j) Reading of qualifications, observations or comments or other remarks as mentioned in the report of the Secretarial Auditor.
- (k) Summary of the clarifications provided on various Agenda Items.

- (l) In respect of each Resolution, the type of the Resolution, the names of the persons who proposed and seconded and the majority with which such Resolution was passed. Where a motion is moved to modify a proposed Resolution, the result of voting on such motion shall be mentioned. If a Resolution proposed undergoes modification pursuant to a motion by shareholders, the Minutes shall contain the details of voting for the modified Resolution.
- (m) In the case of poll, the names of scrutinisers appointed and the number of votes cast in favour and against the Resolution and invalid votes.
- (n) If the Chairman vacates the Chair in respect of any specific item, the fact that he did so and in his place some other Director or Member took the Chair.
- (o) the time of commencement and conclusion of the Meeting.

**Minutes of E-Voting and postal ballot:**

Para 17.2.2.2 of SS-2 provides that in respect of Resolutions passed by e-voting or postal ballot, a brief report on the e-voting or postal ballot conducted including the Resolution proposed, the result of the voting thereon and the summary of the scrutiniser's report shall be recorded in the Minutes Book and signed by the Chairman or in the event of death or inability of the Chairman, by any Director duly authorised by the Board for the purpose, within thirty days from the date of passing of Resolution by e-voting or postal ballot.

**17.3. Recording of Minutes**

Minutes shall contain a fair and correct summary of the proceedings of the Meeting. The Company Secretary shall record the proceedings of the Meetings. Where there is no Company Secretary, any other person authorised by the Board or by the Chairman in this behalf shall record the proceedings.

The Chairman shall ensure that the proceedings of the Meeting are correctly recorded.

The Chairman has absolute discretion to exclude from the Minutes, matters which in his opinion are or could reasonably be regarded as defamatory of any person, irrelevant or immaterial to the proceedings or which are detrimental to the interests of the company.

**Para 17.3.2 of SS-2 provides** that minutes shall be written in clear, concise and plain language.

Minutes shall be written in third person and past tense. Resolutions shall however be written in present tense. Minutes need not be an exact transcript of the proceedings at the Meeting.

Para 17.3.3 of SS-2 provides that each item of business taken up at the Meeting shall be numbered.

Numbering shall be in a manner which would enable ease of reference or cross-reference.

**Para 17.4 of SS-2 prescribes for entry in the Minutes Book**

Minutes shall be entered in the Minutes Book within thirty days from the date of conclusion of the Meeting. In case a Meeting is adjourned, the Minutes in respect of the original Meeting as well as the adjourned Meeting shall be entered in the Minutes Book within thirty days from the date of the respective Meetings.

The date of entry of the Minutes in the Minutes Book shall be recorded by the Company Secretary. Where there is no Company Secretary, it shall be entered by any other person authorised by the Board or the Chairman. Minutes, once entered in the Minutes Book, shall not be altered.

**Para 17.5 of SS-2 prescribes for Signing and Dating of Minutes**

Minutes of a General Meeting shall be signed and dated by the Chairman of the Meeting or in the event of

death or inability of that Chairman, by any Director who was present in the Meeting and duly authorised by the Board for the purpose, within thirty days of the General Meeting.

The Chairman shall initial each page of the Minutes, sign the last page and append to such signature the date on which and the place where he has signed the Minutes. Any blank space in a page between the conclusion of the Minutes and signature of the Chairman shall be scored out.

If the Minutes are maintained in electronic form, the Chairman shall sign the Minutes digitally.

Rule 25 of Companies (Management and Administration) Rules, 2014 contains provisions with regards to minutes of meetings.

**(A) Distinct minute book for each type of meeting:** A distinct minute book shall be maintained for each type of meeting namely:

- (i) general meetings of the members;
- (ii) meetings of the creditors;
- (iii) meetings of the Board; and
- (iv) meetings of the committees of the Board.

It may be noted that resolutions passed by postal ballot shall be recorded in the minute book of general meetings as if it has been deemed to be passed in the general meeting. In no case the minutes of proceedings of a meeting or a resolution passed by postal ballot shall be pasted to any such book.

**(B) Manner of maintenance of minutes:** Minutes of proceedings of each meeting shall be entered in the books maintained for that purpose along with the date of such entry within thirty days of the conclusion of the meeting.

In case of every resolution passed by postal ballot, a brief report on the postal ballot conducted including the resolution proposed, the result of the voting thereon and the summary of the scrutinizer's report shall be entered in the minutes book of general meetings along with the date of such entry within thirty days from the date of passing of resolution.

**(C) Manner of signing of minutes:** Each page of every minute book shall be initialled or signed and the last page of the record of proceedings of each meeting or each report in such books shall be dated and signed by:

- in the case of minutes of proceedings of a meeting of the Board or of a committee thereof, by the chairman of the said meeting or the chairman of the next succeeding meeting;
- in the case of minutes of proceedings of a general meeting, by the chairman of the same meeting within the aforesaid period of thirty days or in the event of the death or inability of that chairman within that period, by a director duly authorized by the Board for the purpose;
- in case of every resolution passed by postal ballot, by the chairman of the Board within the aforesaid period of thirty days or in the event of there being no chairman of the Board or the death or inability of that chairman within that period, by a director duly authorized by the Board for the purpose.

**(D) Preservation of minutes book:** Minute books of general meetings shall be kept at the registered office of the company. Minutes of the Board and committee meetings shall be kept at the registered office or at such other place as may be approved by the Board.

**Minutes of all Meetings shall be preserved permanently in physical or in electronic form with Timestamp.**

Where, under a scheme of arrangement, a company has been merged or amalgamated with another company, Minutes of all Meetings of the transferor company, as handed over to the transferee company, shall be preserved permanently by the transferee company, notwithstanding that the transferor company might have been dissolved.

Minutes books shall be preserved permanently and kept in the custody of the company secretary of the company or any director duly authorized by the Board for the purpose and shall be kept in the registered office or such place as the members may decide by passing special resolution pursuant to requirement of section 88 read with section 94 of the Act.

**Duties of Company Secretaries before, during and after General Meeting**

**(A) Before the General Meeting:**

1. To convene a Board meeting, after giving notice as per Section 173(3), as soon as the final accounts are ready, invite the Auditors for their report and transact the following business (in case of listed company, give advance notice to stock exchange):
  - (a) To consider and discuss the report of Audit Committee on the Annual accounts.
  - (b) To approve the accounts and authorise signing of accounts.
  - (c) To secure Auditor's report on the accounts.
  - (d) To approve the draft of the Board's Report in compliance with the provisions of Section 134 of the Act and to authorise the Chairman to sign the Report on behalf of the Board.
  - (e) To consider the payment of dividend, if any, in case it is to be declared in the Annual General Meeting

*(Notes: 1. In case of listed company prior intimation have to be sent to stock exchange of the Board meeting where recommendation of dividend is proposed to be considered vide Regulation 29 of SEBI (Listing Obligations and Disclosure Requirements) Regulation, 2015 .*

2. Listed entity to disclose the audit qualifications of any other audit reservations along with financial results in addition to explanatory statement as to how audit qualifications of previous accounting year have been addressed in financial results).
  - (a) To fix time, date and place for the annual general meeting, approve the draft notice and also authorise the Secretary to issue Notice for the meeting. The Notice must contain Ordinary Business in accordance with the provisions of Section 102 of the Act, While fixing the time, date and place for the annual general meeting, care should be taken that the time should be during 9 am to 6 pm, the date should not be a National holiday, and the place should be either the registered office of the company or some other place within the same city, town or village in which the registered office of the company is situated.
  - (b) To consider the closure of the Register of Members and the Share Transfer Books of the Company in compliance with the provisions of Section 91 of the Act and to authorise the Secretary to arrange for its publication in a newspaper. In case of listed company, a notice in advance of at least 7 working days should be sent to the stock exchange(s) about the proposed dates for such closure and also to comply with the requirement of stock exchange for book closure.

2. Listed entity shall give prior intimation to stock exchange atleast 5 days in advance (excluding date of intimation and date of meeting) about Board meeting in which financial results are due to be considered [Regulation 29 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015].
3. To arrange for the publication in a newspaper of at least 7 days previous notice of closure of the Register of Members and the Share Transfer Books as per Section 91 of the Act. [Regulation 42 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015]
4. In case of listed company, close the registers for the period as advertised and inform the all the stock exchanges by giving a notice in advance of at least 7 working days.
5. To arrange for the printing of the balance sheet, profit and loss account, reports of the directors and of the auditors and the notice for the meeting.
6. To issue notice to the shareholders, for at least 21 clear days before the date of annual general meeting and where it is to be sent by post, it should be posted 48 hours still earlier in terms of section 101. Notice of the meeting must also be send to the directors (whether member or not), auditors and stock exchanges. In case of section 8 companies 14 clear days notice is sufficient for general meeting.
7. If the directors decide for the publication of the Chairman's statement, make arrangements for the same.
8. Check proxies with the Register of Members as and when they are received, from day to day, so that an up-to-date position is available till the date of the meeting.
9. To arrange for the printing of attendance slips or attendance register and ballot papers.
10. In consultation with the chairman or the Managing Director, prepare a detailed agenda for the meeting.
11. To prepare Dividend List from the Register of Members/beneficial owners, as on the last date of the closure of the Register of Members and the Share Transfer Books.
12. To make arrangement for the printing of a combined document containing "Notice of Dividend" and "Dividend Warrant"

**(B) At the Meeting:**

- (1) To arrange for the collection of admission slips or in the alternative to get the Attendance Register signed by the shareholders, and to make them comfortable in their seats, and to look to the comfort and convenience of the directors and the chairman.
- (2) To help the Chairman in ascertaining quorum.
- (3) To read out the notice of the meeting if advised by the Chairman.
- (4) To read out the Auditor's Report, if advised by the Chairman, when the item relating to adoption of accounts is taken up for consideration.
- (5) To produce copies of Memorandum and Articles of Association of the company.
- (6) To help the Chairman in the conduct of the meeting, particularly in the conduct of poll, counting of votes etc.
- (7) To supply to the Chairman any information which he may require in connection with the queries

raised by the shareholders relating to accounts and other connected matters.

- (8) Give advance information to the members who are to propose and second the resolutions to be passed at the meeting.
- (9) To take notes of the proceedings for the purpose of preparing minutes thereof.
- (10) To keep at the meeting Register of Members, Minutes Book of the general meeting containing minutes of the previous annual general meeting(s), copies of the accounts, notice of the meeting and reports of the directors and of the auditors.
- (11) To ensure that the Chairman of the Audit Committee is present at annual general meeting to provide any clarification on matters relating to audit and to answer shareholder queries;

**(C) After the Meeting:**

- (1) To prepare minutes of the proceedings.
- (2) To record the minutes of the meeting and get them signed by the Chairman within thirty days of the meeting.
- (3) To send intimation of appointment/re-appointment of directors. File Form DIR-12 with the Registrar of Companies within 30 days of appointment along with filing fee.
- (4) To send intimation of appointment/re-appointment of auditors.
- (5) To file copies of the special and other resolutions, if any, passed at the meeting, along with Form MGT14 with the Registrar of Companies, within thirty days of the meeting.
- (6) To file balance sheet, profit and loss account, reports of the directors and the auditors and the notice of the meeting in Form AOC-4 within thirty days of the meeting. In case of companies covered under XBRL filing, it should be ensured that the annual accounts are filed in XBRL format. Ensure that a copy of Secretarial Audit Report obtained from a Secretary in whole time practice as required under Section 204(1) of the Act, if any, is filed with Registrar of Companies within 30 days from the date of annual general meeting. Listed entity shall submit the annual report to stock exchange within 21 working days of it being approved and adopted in AGM [Regulation 34 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015]
- (7) Deposit dividend distribution tax at the applicable rate within the prescribed time limit under Income-tax Act, 1961.
- (8) Where the company has invited public deposits, a copy of the Balance sheet shall be forwarded to the RBI.
- (9) To open a separate bank account known as "Dividend Account for the year....." and to deposit the total amount of dividend within five days from the date of declaration of dividend.
- (10) To get the Dividend Warrants and Notice of Dividend signed by authorised persons.
- (11) To despatch Dividend Warrants together with the Notice of Dividend to the shareholders within thirty days of the declaration of dividend after making arrangement with the banker for payment of dividend warrants at prescribed number of branches at par.
- (12) To file along with the prescribed filing fee, Annual Return in Schedule V to the Companies Act as an attachment to Form MGT-7 with the Registrar of Companies within sixty days of the meeting prepared as at the date of the annual general meeting, as required by Section 92 of the Companies Act, 2013. The Certificate of Company Secretary shall be in Form MGT-8 and extract of annual

return shall be attached with Board Report in Form MGT-9. However, a Specified IFSC public and private company shall not attach extract of annual return with the Board Report. Ensure that in the case of listed company, the annual return is also signed by a Company Secretary in whole time practice.

- (13) To take action on other decisions of the shareholders.
- (14) If the company is listed then to submit to the stock exchange, within 48 hours of conclusion of annual general meeting, details regarding the voting results in the following format specified by Board (Regulation 44 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015].

### LESSON ROUND-UP

- An annual general meeting is required to be held every year by every company whether public or private, limited by shares or by guarantee, with or without share capital or unlimited company.
- In case of default is made in holding the annual general meeting of a company under section 96, the Tribunal may call or direct the calling of an annual general meeting.
- Class meetings are those meetings which are held by holders of a particular class of shares e.g. preference shares.
- For a General Meeting to be valid, it must be duly convened, properly constituted and the business must be validly transacted.
- In case of public company the quorum shall depend on number of members as on the date of meeting:-
  - If members not more than 1000—quorum shall be 5
  - If members more than 1000 but less than 5000- quorum shall be 15
  - If members more than 5000- quorum shall be 30
- In case of private company 2 members personally present shall be the quorum of the meeting.
- The central government is vested with the power to prescribe a class or classes of companies whose members shall not be entitled to appoint another person as a proxy.
- Chairman plays a very important role in a meeting as he is responsible for successful conduct of a meeting
- A motion becomes a resolution only after the requisite majority of members have adopted it.
- Various methods which may be adopted for taking votes on a motion properly placed before a meeting are by show of hands, by poll, by postal ballot and by electronic voting.
- There are three kinds of resolutions under the Act (a) Ordinary Resolution(S. 114), (b) Special Resolution (S. 114) (c) Resolution requiring special notice (S. 115)
- In accordance with Section 117 of the Act, certain resolutions are required to be filed with the Registrar for its recording within 30 days of its passing at the meeting.
- Every company is required to keep minutes of the proceedings of general meetings and of the meetings of Board of Directors and its Committees.

### GLOSSARY

Book Closure	Book closure refers to the time period when a company will not handle adjustments to the register, or requests to transfer shares. The book closure date is often used to identify the cut-off date determining which investors of
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record will be sent a given dividend payment or the issue of right or bonus shares or issue of shares for conversion of debentures. This is more relevant in case of physical shares. Also refer Section 91 of Companies Act, 2013.

*Suomotu*

It is a Latin legal term meaning "on its own motion"

*Mutatis mutandis*

It is a Latin term meaning "the necessary changes having been made" or "once the necessary changes have been made"

### SELF-TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

1. What are the items that constitute Ordinary Business in an Annual General Meeting of a company?
2. Who shall be chairman of a general meeting of a company? What are the provisions of the Companies Act, 2013 regarding his election?
3. Every Annual General Meeting of a company shall be called on a day which is not a National holiday. Can an adjourned Annual General Meeting of a company be called on a National holiday?
4. A shareholder having given proxy, personally attends and votes at the meeting. Comment, illustrating a case law.
5. At a general meeting, two joint holders voted on a resolution. Will the votes of both the joint holders be accepted?
6. What are the provision of the Companies Act, in regard to the holding of aExtra Ordinary General Meeting?
7. Write short notes on:  
(i) Proxy; (ii) Special Business; (iii) Quorum; (vi) Scrutinizer.
8. Can any company pass some resolutions through postal ballot? If yes, what are the Rules in connection to it.

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# Lesson 20

## Virtual Meetings

### LESSON OUTLINE

- Virtual Meeting - Meaning
- Virtual Board Meeting
- Procedure of Board meeting through video or audio conferencing
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

As a professional a company secretary is expected to be well versed with the technological advancements effecting their profession. “Virtual meetings” are the meetings that do not involve a physical gathering, but which take place in an electronic form.

Board meetings as permitted under law can be held through video conferencing, a company secretary has an important role to play in such meetings.

On the other hand electronic voting has also been permitted by law for the shareholders meeting in certain cases, but that’s not a virtual shareholders meeting, its only one way interaction, the shareholders cannot question the directors.

The chapter takes you through the modalities of holding a virtual meeting.

## INTRODUCTION

Chapter XII of the Companies Act 2013 deals with Board Meeting. Section 173(1) stipulates that every company shall hold the first meeting of the Board of Directors within thirty days of the date of its incorporation and thereafter hold a minimum number of four meetings of its Board of Directors every year in such a manner that not more than one hundred and twenty days shall intervene between two consecutive meetings of the Board.

Subsection (2) of the section specifies that, the participation of directors in a meeting of the Board may be either in person or through video conferencing or other audio visual means, as may be prescribed, which are capable of recording and recognizing the participation of the directors and of recording and storing the proceedings of such meetings along with date and time. The Central Government may, by notification, specify such matters which shall not be dealt with in a meeting through video conferencing or other audio visual means.

Similarly, Section 108 of the Companies Act, 2013 provides for Voting through electronic means by the members of the companies.

## Virtual Meeting - Definition

A meeting held totally by means of either Video conferencing or other audio-visual means is known as Virtual Meeting. A virtual meeting is when people around the world, regardless of their location, use video, audio, and text to link up online. Virtual meetings allow people to share information and data in real-time without being physically located together. In virtual meeting there is no physical presence of participants and there is no designated venue for the purpose of meetings. Participants located at different places participate in the meeting either by teleconference or video conference or combination of them at predetermined time.

Virtual meetings are becoming an increasingly common aspect at corporate world when it comes to professional communication and the way business are done, for most company's Virtual meetings is the fact of life. Companies today operate across multiple time zones from different countries and continents. Employees, Board Members, stakeholders and investors are not from any particular region, city or country, in fact they are spread wide and far. By using Virtual technology, it is possible to replace physical meetings which require the presence of people at the designated place and time.

With rapid change in technology and wide spread of internet and audio and video combination, which is readily available, affordable and reliable, many companies and organizations are adopting and favoring virtual meetings. The use of audio and video conferences, webinars and web meetings via computers, telephones or other devices is more frequent. The potential gains are in terms of reduced travel costs, timesaving, efficiency improvements, and less environmental impact in terms of savings on fuel and transport.

Virtual Meetings are held at a distance in real time basis with the help of digital technology. The meetings are mainly 1) audio- and/or video based, such as audio conferencing, video conferencing, and on-line meetings or webinars, often they are supported by other forms like chat, white boards, document sharing, etc. 2) Audio conferencing means conference calls with three or more participants, either by connecting the different participants by using a conference phone, or both. 3) Video conferencing, a technology now a day commonly used in board meetings.

## Types of Meeting

<p><b>Same Time, Same Place</b></p> <p>Conventional Meetings</p>	<p><b>Different Time, Same Place</b></p> <p>Project Meetings</p> <p>Organizational Meetings</p>
<p><b>Same Time, Difference Place</b></p> <p>Conference Calls</p> <p>Video Conferences</p> <p>Online Meetings</p> <p>Web Conferences</p>	<p><b>Different Time, Difference Place</b></p> <p>Email</p> <p>Recordings</p> <p>Discussion Forum</p> <p>Social Media</p>

The main economic benefits of virtual meetings are efficiency, improvements, direct savings through reduced travel costs.

Success of virtual meetings depends on technical equipment, the software used and trained manpower which should work well and be operated with ease. Virtual Equipment should be simple and easy to use and understand by the users with little instruction or training. The Commonly used software for Virtual meeting are Microsoft's Skype for Business, Adobe's Connect, Google's Hangouts, or WebEx to name a few. The development of new technologies such as VOIP telephony (voice over internet protocol, an example of which is Skype) and shared computer screens. All the major providers provide for a website address where participants can click to join the meeting. Hence a virtual meeting is a "room" set up online through a website host that allows people from anywhere to "meet" with each other to share information and network in real-time. As understood a meeting can take the form of audio, video, instant-message chat, and apps that can be shared among attendees, such as for taking notes or polls. Virtual meetings can also be recorded so that attendees or those who missed the meeting can review the meeting and its chat transcripts at a later date. A virtual meeting space works through a Web browser plug-in and by a host's local or remote server. Participants usually must log in, and they can see a list of other participants. Webcams are used for those participating in video, and "Voice over Internet protocol," or VoIP, allows the audio to work.

## Brief Requirements for Virtual Meeting

- Meeting rooms
- Software, which can be either purchased or can be provided by vendor for a fee on yearly rental basis.
- Hardware equipment like Monitor or LED screen, Webcams.
- High quality mike system.
- Projectors.
- Document scanners.
- Leased Lines.
- High speed wireless internet.

- Recording & Storage Equipment for recording the proceeding and Proper storage for future reference as many be required under law.
- Have trial run before the meeting to ensure all the systems are working properly.
- Ensure that the proper arrangements are made in the Meeting room.

A virtual meeting room is a unique identifier that allows a meeting organizer to invite attendees from disparate geographical locations to collaborate in real time over the Internet. A virtual meeting room is also known as a virtual meeting space.

### **Virtual Board Meetings**

Present day Directors' who are professional have busy schedules which makes it difficult for them to attend board meetings of the companies in which they are directors especially for those who are living and working in different cities and countries. Teleconferencing, videoconferencing, and meeting online benefit boards and directors to enable them to attend the meetings from any location. Virtual meetings help the directors to participate in meetings where ever they are despite their busy schedule and make valuable contributions by their participation. Virtual attendance can also make board participation more attractive and appealing especially for independent directors as they are not be expected attend every meeting in person and it is not practically possible as they sit on many boards of company which are located in different cities countries and due to statutory requirements most the board meetings of the companies especially listed entities are held around the same time making it more difficult for the Independent professional directors to be physically present and participate in the meetings. By holding virtual meetings, Boards with members around the country and globe will benefit from wider participation and it would be very convenient for the directors to attend through virtual media from their respective location and also it helps from reduced travel and reimbursement of costs.

The use of technology can present its own challenge, including directors' reluctance, lack of technical proficiency, lack of access to data and material. However, modern tools like board portals and board management software and help in solving some of the concerns.

**The Section 173 of Companies Act, 2013 read with Rule 3 & 4 of Companies (Meetings of Board and its Powers) Rules, 2014 and Secretarial Standards on Board meetings give a much wanted platform for holding virtual meetings.**

**SS-1 defines electronic mode as “Electronic Mode”** in relation to Meetings means Meetings through video conferencing or other audio-visual means. “Video conferencing or other audiovisual means” means audio visual electronic communication facility employed which enables all the persons participating in a Meeting to communicate concurrently with each other without an intermediary and to participate effectively in the Meeting.

**“Secured Computer System”** means computer hardware, software, and procedure that –

- (a) are reasonably secure from unauthorized access and misuse;
- (b) provide a reasonable level of reliability and correct operation;
- (c) are reasonably suited to performing the intended functions; and
- (d) adhere to generally accepted security procedures.

**“Timestamp”** means the current time of an event that is recorded by a Secured Computer System and is used to describe the time that is printed to a file or other location to help keep track of when data is added,

removed, sent or received. Words and expressions used and not defined herein shall have the meaning respectively assigned to them under the Act.

Provisions in detail are as under:

**Any Director may participate through Electronic Mode in a Meeting unless the Act or any other law specifically prohibits such participation through Electronic Mode in respect of any item of business.**

Directors shall not participate through Electronic Mode in the discussion on certain restricted items. Such restricted items of business include approval of the annual financial statement, Board's report, prospectus and matters relating to amalgamation, merger, demerger, acquisition and takeover. Similarly, participation in the discussion through Electronic Mode shall not be allowed in Meetings of the Audit Committee for consideration of annual financial statement including consolidated financial statement, if any, to be approved by the Board.

It means that directors can participate in a board meeting through video conference or by teleconference and can be counted for the purpose of quorum except for those items which are under law, Audit Committee meetings and their presence shall not be counted for the purpose of quorum.

**Notice in writing of every Meeting shall be given to every Director by hand or by speed post or by registered post or by facsimile or by e-mail or by any other electronic means.**

The Notice shall be sent to the postal address or e-mail address, registered by the Director with the company or in the absence of such details or any change thereto, any of such addresses appearing in the Director Identification Number (DIN) registration of the Director.

Even if the notice is sent by e-mail or by any electronic means to the email id provided by the Director, then such notice sent through electronic platform shall be constituted as valid notice served on the director.

**The Notice shall inform the Directors about the option available to them to participate through Electronic Mode and provide them all the necessary information.**

If a Director intends to participate through Electronic Mode, he shall give sufficient prior intimation to the Chairman or the Company Secretary to enable them to make suitable arrangements in this behalf.

The Director may intimate his intention of participation through Electronic Mode at the beginning of the Calendar Year also, which shall be valid for such Calendar Year. Though such declaration shall not debar him from participation in the meeting in person, in such case a sufficient intimation of attending in person is required to be sent to the company.

The Notice shall also contain the contact number or e-mail address(es) of the Chairman or the Company Secretary or any other person authorized by the Board, to whom the Director shall confirm in this regard. In the absence of an advance communication or confirmation from the Director as above, it shall be assumed that he will attend the Meeting physically.

Every notice served on the director shall clearly specify that proper arrangements have been made for video or tele conferencing and the director has option of participating in the meeting through such means. The Director should be sent the link through which he can log in and attend the meeting. The Director should inform the Chairman or the Secretary of the Company his option regarding participating the meeting through Electronic mode.

**Directors participating through Electronic Mode in a Meeting shall be counted for the purpose of**

**Quorum, unless they are to be excluded for any items of business under the provisions of the Act or any other law.**

Directors participating through Electronic mode are counted for quorum unless prohibited as per law. The chairperson shall ensure that the required quorum is present throughout the meeting

### **The attendance registers.**

**The attendance register shall be deemed to have been signed by the Directors participating through Electronic Mode, if their attendance is recorded in the attendance register and authenticated by the Company Secretary or where there is no Company Secretary, by the Chairman or by any other Director present at the Meeting, if so authorized by the Chairman and the fact of such participation is also recorded in the Minutes.**

In case of Directors participating through Electronic Mode, the Chairman shall confirm the attendance of such Directors. For this purpose, at the commencement of the Meeting, the Chairman shall take a roll call. The Chairman or Company Secretary shall request the Director participating through Electronic Mode to state his full name, location from where he is participating, confirm that he has received the agenda and other relevant material and that no one other than the concerned director is attending or having access to the proceedings of the meeting at the location. This shall also be recorded in the Minutes. The proceedings of such Meetings shall be recorded through any electronic recording mechanism and the details of the venue, date and time shall be mentioned.

### **Venue of the meeting**

With respect to every meeting conducted through video conferencing or other audio visual means authorised under these rules, the scheduled venue of the meeting as set forth in the notice convening the meeting shall be deemed to be the place of the said meeting and all recordings of the proceedings at the meeting shall be deemed to be made at such place.

### **Role of Chairperson and Company Secretary**

The Chairperson of the meeting and the company secretary shall take due and reasonable care with respect to the following:

- (a) to safeguard the integrity of the meeting by ensuring sufficient security and identification procedures;
- (b) to ensure availability of proper video conferencing or other audio visual equipment or facilities for providing transmission of the communications for effective participation of the directors and other authorised participants at the Board meeting;
- (c) to record proceedings and prepare the minutes of the meeting;
- (d) to store for safekeeping and marking the tape recording(s) or other electronic recording mechanism as part of the records of the company at least before the time of completion of audit of that particular year.
- (e) to ensure that no person other than the concerned director are attending or have access to the proceedings of the meeting through video conferencing mode or other audio visual means; and
- (f) to ensure that participants attending the meeting through audio visual means are able to hear and see the other participants clearly during the course of the meeting. The persons, who are differently abled, may be facilitated by the Board to allow a person to accompany him.

### **Procedures for Convening and Conducting Board's Meetings through video or Audio Visual Means (Rule 3 of Companies (Meetings of Board and its powers) rules, 2014**

Directors may participate in the meeting either in person or through video conferencing or other audio visual means.

Rule 3 of the Companies (Meetings of Board and its Powers) Rules, 2014 provides for the requirements and procedures, in addition to the procedures required for Board meetings in person, for convening and conducting Board meetings through video conferencing or other audio visual means:

- (1) Every Company shall make necessary arrangements to avoid failure of video or audio visual connection.
- (2) The Chairperson of the meeting and the company secretary, if any, shall take due and reasonable care, the same has been discussed above.
- (3) (a) The notices of the meeting shall be sent to all the directors in accordance with the provisions of sub-section (3) of section 173 of the Act.
- (b) The notice of the meeting shall inform the directors regarding the option available to them to participate through video conferencing mode or other audio visual means, and shall provide all the necessary information to enable the directors to participate through video conferencing mode or other audio visual means.
- (c) A director intending to participate through video conferencing mode or audio visual means shall communicate his intention to the Chairman or the company secretary of the company.
- (d) If the director intends to participate through video conferencing or other audio visual means, he shall give prior intimation to that effect sufficiently in advance so that company is able to make suitable arrangement in this behalf.
- (f) In the absence of any such intimation from the director, it shall be assumed that the director will attend the meeting in person.
- (4) At the commencement of the meeting, a roll call shall be taken by the Chairperson when every director participating through video conferencing or other audio visual means shall state, for the record, the following namely:
  - (a) name;
  - (b) the location from where he is participating;
  - (c) that he can completely and clearly see, hear and communicate with the other participants;
  - (d) that he has received the agenda and all the relevant material for the meeting; and
  - (e) that no one other than the concerned director is attending or having access to the proceedings of the meeting at the location mentioned in (b) above.
- (5) (a) After the roll call, the Chairperson or the Secretary shall inform the Board about the names of persons other than the directors who are present for the said meeting at the request or with the permission of the Chairman and confirm that the required quorum is complete.

*Explanation:* It is clarified that a director participating in a meeting through video conferencing or other audio visual means shall be counted for the purpose of quorum, unless he is to be excluded for any items of business under any provisions of the Act or the Rules.

- (b) The roll call shall also be made at the conclusion of the meeting and at the re-commencement of the meeting after every break to confirm the presence of a quorum throughout the meeting.
- (6) With respect to every meeting conducted through video conferencing or other audio visual means authorised under these rules, the scheduled venue of the meeting as set forth in the notice convening the meeting, shall be deemed to be the place of the said meeting and all recordings of the proceedings at the meeting shall be deemed to be made at such place.
- (7) The statutory registers which are required to be placed in the Board meeting as per the provisions of the Act shall be placed at the scheduled venue of the meeting and where such registers are required to be signed by the directors, the same shall be deemed to have been signed by the directors participating through electronic mode if they have given their consent to this effect and it is so recorded in the minutes of the meeting.
- (8) (a) Every participant shall identify himself for the record before speaking on any item of business on the agenda.
  - (b) If a statement of a director in the meeting through video conferencing or other audio visual means is interrupted or garbled, the Chairperson or company secretary shall request for a repeat or reiteration by the director.
  - (9) If a motion is objected to and there is a need to put it to vote, the Chairperson shall call the roll and note the vote of each director who shall identify himself while casting his vote.
- (10) From the commencement of the meeting until the conclusion of such meeting, no person other than the Chairperson, directors, Secretary and any other person whose presence is required by the Board shall be allowed access to the place where any director is attending the meeting either physically or through video conferencing without the permission of the Board.
- (11) (a) At the end of discussion on each agenda item, the Chairperson of the meeting shall announce the summary of the decision taken on such item along with names of the directors, if any, dissented from the decision taken by majority
  - (b) The minutes shall disclose the particulars of the directors who attended the meeting through video conferencing or other audio visual means.
- (12) (a) The draft minutes of the meeting shall be circulated among all the directors within fifteen days of the meeting either in writing or in electronic mode as may be decided by the Board.
  - (b) Every director who attended the meeting, whether personally or through video conferencing or other audio visual means, shall confirm or give his comments, about the accuracy of recording of the proceedings of that particular meeting in the draft minutes, within seven days or some reasonable time as decided by the Board, after receipt of the draft minutes failing which his approval shall be presumed.
  - (c) After completion of the meeting, the minutes shall be entered in the minute book as specified under section 118 of the Act and signed by the Chairperson.

*Explanation* - For the purposes of this rule, 'video conferencing or other audio visual means' means audio-visual electronic communication facility employed which enables all the persons participating in a meeting to communicate concurrently with each other without an intermediary and to participate effectively in the meeting.

**Summarised procedure of Video conferencing:**

- Roll call by chairperson
- Directors to introduce themselves at each and every time they speak on matters
- Presence will be counted for quorum
- No unauthorized access.
- Differently abled Director may have person accompanying them
- Directors to repeat if there is any disturbances
- Chairperson to announce summary at the end of the Meeting
- Minutes of the meeting to contain the names of Directors who participated through Video conference.

**Matters not to be dealt with in a Meeting through Video Conferencing or other Audio Visual Means**

Rule 4 prescribe restriction on the following matters, which shall not be dealt with in any meeting held through video conferencing or other audio visual means:

- (i) the approval of the annual financial statements;
- (ii) the approval of the Board's report;
- (iii) the approval of the prospectus;
- (iv) the Audit Committee Meetings for consideration of financial statement including consolidated financial statement, if any, to be approved by the Board under sub-section (1) of Section 134 of the Act; and
- (v) the approval of the matter relating to amalgamation, merger, demerger, acquisition and takeover.

The above restricted items cannot be dealt through video-conference meeting. SS however clarifies that any Director participating through Electronic Mode in respect of restricted items with the express permission of Chairman shall however, neither be entitled to vote nor be counted for the purpose of Quorum in respect of such restricted items.

**Virtual AGM/EGMs**

Section-108 of the Companies Act, 2013 provides for Voting through electronic means. —The Central Government may prescribe the class or classes of companies and manner in which a member may exercise his right to vote by the electronic means

General meetings, particularly when large numbers of shareholders are involved, can be very expensive and are not considered to be a cost-effective.

Virtual meetings of members have advantages for companies and their shareholders. When compared to couple of decade back present-day shareholders are spread across the country and also in different countries, and as the AGMs can only conducted in the city or place in which the registered office of the company is located, it makes it more difficult for the shareholders located in faraway locations and cites to attend the meetings as it involves lot of travel time and cost. With less participation, the agenda items are

often passed without any discussion with fewer members. Virtual meetings will help in increasing shareholder participation as compared to physical meetings because of improved access, shareholders who cannot attend in person due to location or other reasons can attend virtually and do not have to incur the time and costs of travel to a physical meeting.

Similarly, companies may find virtual meetings help to achieve wider shareholders participation. Virtual annual meetings offer benefits to both companies and shareholders. With companies and investors becoming increasingly global, virtual meetings can save travel time and costs for shareholders, avoid traffic and other logistical delays and be easier to schedule. It will also eliminate the costs of an in-person meeting, including travel for shareholders and a company's directors and management, thereby allowing shareholders more time to attend more meetings in which they hold shares, as well as minimizing the amount of time that directors and management must spend at meetings. This in turn will increase the participation of shareholders who would otherwise not attend the meetings.

### **Advantages of Virtual AGM/EGMs**

- Increase shareholder participation in meetings,
- Save time on travel and cost because of remote voting.
- Encourages more participation by investors across the world.
- Provides greater accessibility to shareholders who cannot be physically present due to distance.
- Enables institutional investors to attend more than one meeting in a day and protect shareholders interest.
- Reduce the cost of holding and conducting shareholder meeting, including the costs of the venue, stationary, transport and refreshments.
- Saves time of the Company's personal.

### **Difficulties in holding Virtual Meetings of Members:**

- Security of the systems used.
- Streaming with quality without interruption.
- Providing with secure login and shareholder authentication for attendance, with ease of access for shareholders, and remote voting.
- Combined registration, voting and reporting software.
- Customized instant results screen and detailed audit reporting.
- Data Security of Logins and Passwords.
- Allowing the shareholders, the choice of device.
- the technology used must give all shareholders a reasonable opportunity to participate
- the technology must be secure and must provide reasonable measures for verifying/validating those allowed to attend and vote at the meeting
- The company must provide a digital record of the meeting.

***As of today, holding of total virtual shareholder meeting is not allowed, at present Hybrid meeting are permitted. “hybrid” to refer to those meetings are combination of online participation as well as option of attending the meeting in-person. “virtual meetings” are those conducted wholly online with no physical meeting of shareholders.***

Voting by electronic means is a facility given to the members of a company to cast their votes on the resolutions through electronic mode. It provides an opportunity to shareholders residing in far-flung area to take part in the decision making process of the company. They may or may not attend the meeting physically. Boards in their fiduciary capacity are now looked upon for greater accountability and transparency for the effectiveness of their overall governance process. E-Voting is a further step to encourage corporate democracy and to promote good corporate governance.

E-voting allows a voter to record his or her secure and secret ballot electronically. E-voting are generally used in government elections like general elections, state legislative assembly elections etc. and considered as a tool of effective governance in voting infrastructure. E-voting is a common Internet infrastructure that enables the investors to vote electronically on resolution of companies. Shareholders normally exercised their votes on resolutions proposed by companies through postal ballot. If a company decides to pass any resolution by resorting to postal ballot, it will send a notice to all the shareholders, requesting them to send their assent or dissent in writing on a postal ballot. The Companies Act, 2013 had ushered in the concept of e-voting to ensure wider shareholder participation in the decision-making process in companies. The concept has been discussed in earlier chapter.

## LESSON ROUND UP

- A virtual meeting is when people around the world, regardless of their location, use video, audio, and text to link up online.
- virtual meeting is a "room" set up online through a website host that allows people from anywhere to "meet" with each other to share information and network in real-time.
- Directors shall not participate through Electronic Mode in the discussion on certain restricted items. (Rule 4)
- The Director may intimate his intention of participation through Electronic Mode at the beginning of the Calendar Year also, which shall be valid for such Calendar Year.
- Directors participating through Electronic mode are counted for quorum unless prohibited as per law. The chairperson shall ensure that the required quorum is present throughout the meeting

## GLOSSARY

Roll Call	A roll call is nothing but identifying and confirming the attendance of the director.
VoIP	VoIP (voice over IP) is the transmission of voice and multimedia content over Internet Protocol (IP) networks. VoIP compresses and encapsulate audio into data packets, transmit the packets across an IP network and unencapsulate the packets back into audio at the other end of the connection.



# Lesson 21

## Legal Framework Governing Company Secretaries

### LESSON OUTLINE

- Associate and Fellow Company Secretaries
- Disciplinary mechanism
- Provisions relating to misconduct under Company Secretary Act, 1980
- Lesson Round up
- Glossary
- Self-Test Questions

### LEARNING OBJECTIVES

Professionals are expected to conduct themselves in such a manner so as to uphold the grace, dignity and professional standing of their respective Institutes. Any commitment to complete a particular assignment as agreed by the person himself should be completed in a professional manner.

The purpose of this chapter is to explain to the students, expectation as a member with respect to various aspects of the ethical conduct. This lesson has been designed to assist in defining appropriate personal and professional conduct, to provide guidance in the identification and resolution of ethical issues, and to help the prospected company secretaries to maintain the culture of honesty, integrity, transparency and accountability.

## INTRODUCTION

The need to have a profession of Company Secretaries was first felt in early 50's, when the business environment had started changing, that had necessitated the services of a professional to bring Corporate Discipline.

The Government set up an Advisory Board on a non-statutory basis, to help it in standardising the basic qualifications needed for manning the position of Company Secretaries and to hold the qualifying examination.

Subsequently, the Department of Company Affairs conducting examination leading to Government Diploma in Company Secretaryship (GDSCS), marked the beginning of the profession of Company Secretaries in an organised manner. Later in the wake of substantial increase in the number of candidates for GDSCS, the Institute of Company Secretaries of India was set up and registered as a company on 4th October, 1968 under Section 25 of the Companies Act, 1956 (i.e. not for profit company) with its registered office at New Delhi. The work relating to Company Secretaries' Examination and all allied matters were taken over by the Institute with effect from 1st January 1969.

In 1980, the Government moved the Company Secretaries Bill, 1980 to convert the Institute into a statutory body.

While moving the Company Secretaries Bill, 1980 for consideration by the Lok Sabha on 16th June, 1980, the then Minister of Law, Justice and Company Affairs, Shri P. Shiv Shankar had said, "An essential ingredient in the healthy growth of the corporate sector is the induction of professional management. The Government attaches special importance to the development of professional management, so that the corporate sector can evolve and function in tune with the changing needs of the times, and the social responsibilities that this important segment of the economy has to shoulder. The profession of Company Secretaries has an important part to play in the introduction of professionalism in the area of corporate management."

### Legal framework

S.No.	Acts/Regulations/Rules
1	The Company Secretaries Act, 1980
2	The Company Secretaries Regulations, 1982

### Some legal terminologies and interpretation

According to section 2(1)(c) of the Company Secretaries Act, 1980 "**Company Secretary**" means a person who is a member of the Institute of Company Secretaries of India.

The role of the Company secretary is defined in various other legal enactments.

Under the Companies Act, 2013 Company Secretary has been defined under section 2(24) as: 'Company Secretary' or 'Secretary' means a Company Secretary as defined in clause (c) of sub section (1) of Section 2 of the Company Secretaries Act, 1980 who is appointed by a company to perform the functions of the Company Secretary under the Companies Act, 2013.

Functions have been well discussed in earlier chapters.

## Associates and Fellows

The members of the Institute shall be divided into two classes designated respectively as Associates and Fellows.

Any person whose name is entered in the Register of members maintained by Institute of Company Secretaries of India shall be deemed to have become an Associate and as long as his name remains so entered, shall be entitled to use the letters “A.C.S.” after his name to indicate that he is an Associate.

A person, being an Associate who has been in continuous practice in India as a Company Secretary for at least five years and a person who has been an Associate for a continuous period of not less than five years and who possesses such qualifications or practical experience as the Council may prescribe with a view to ensuring that he has experience equivalent to the experience normally acquired as a result of continuous practice for a period of five years as a Company Secretary shall, on payment of fees, be entered in the Register as a Fellow.

## Certificate of practice

A member is entitled to continue the practice of Company Secretary, whether in India or elsewhere, only after obtaining a Certificate of Practice.

## Deemed “to be in practice”

A member of the Institute 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 recognised 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, reorganisation or winding up of companies; or
- (c) offers to perform or performs such services as may be performed by—
  - (i) an authorised 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 matters
  - (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;

## Register of Members

The Council shall maintain in the prescribed manner a Register of the members of the Institute.

The Register shall include the following particulars about every member of the Institute, namely:—

- (a) his full name, date of birth, domicile, residential and professional addresses;
- (b) the date on which his name is entered in the Register;
- (c) his qualifications;
- (d) whether he holds a certificate of practice; and
- (e) any other particulars which may be prescribed.

The Council shall cause to be published in the list of members of the Institute as on the 1st day of April of each year. Every member of the Institute shall, on his name being entered in the Register, pay annual membership fee as may be decided by the council from time to time.

## Removal from the Register of Members

(1) in the following cases the Council may remove from the Register the name of any member of the Institute—

- (a) who is dead; or
- (b) from whom a request has been received to that effect; or
- (c) who has not paid any prescribed fee required to be paid by him; or
- (d) who is found to have been subject at the time when his name was entered in the Register, or who at any time thereafter has become subject, to any of the disabilities mentioned in section 8, or who for any other reason has ceased to be entitled to have his name borne on the Register.

The Council shall remove from the Register the name of any member in respect of whom an order has been passed under this Act removing him from membership of the Institute.

## Disciplinary Mechanism

The member of the Institute is subject to the Disciplinary mechanism provided for under Chapter V of the Company Secretaries Act, 1980 (the Act).

## Disciplinary Directorate

Section 21 of the Act provides for the establishment of a Disciplinary Directorate headed by an officer of the Institute designated as Director (Discipline) and such other employees for making investigations in respect of any information or complaint received by it. On receipt of any information or complaint along with the prescribed fee, the Director (Discipline) shall arrive at a prima facie opinion on the occurrence of the alleged misconduct. The Disciplinary Directorate shall follow such procedure as may be specified to make investigations under the Act.

Where the Director (Discipline) is of the opinion that a member is guilty of any professional or other misconduct mentioned in the First Schedule, the matter shall be placed before the Board of Discipline.

Where the Director (Discipline) is of the opinion that a member is guilty of any professional or other

misconduct mentioned in the Second Schedule or in both the Schedules, the matter shall be placed the Disciplinary Committee.

### **Board of Discipline**

The Board of Discipline shall be constituted by the Council of the Institute under section 21A of the Companies Act, 1980. The Board of Discipline shall follow summary disposal procedure in dealing with all the cases before it.

Where the Board of Discipline is of the opinion that a member is guilty of a professional or other misconduct mentioned in the First Schedule, it shall afford to the member an opportunity of being heard before making any order against him and may thereafter take any one or more of the following actions, namely:—

- (a) reprimand the member;
- b) remove the name of the member from the Register up to a period of three months;
- (c) impose such fine as it may think fit which may extend to rupees one lakh.

The Director (Discipline) shall submit before the Board of Discipline all information and complaints where he is of the opinion that there is no prima facie case and the Board of Discipline may, if it agrees with the opinion of the Director (Discipline), close the matter or in case of disagreement, may advise the Director (Discipline) to further investigate the matter.

### **Disciplinary Committee**

According to Section 21B a Disciplinary Committee shall be constituted by the Council. The Disciplinary Committee shall consist of the President or the Vice-President of the Council as the Presiding Officer and two members to be elected from amongst the members of the Council and two members to be nominated by the Central Government from amongst the persons of eminence having experience in the field of law, economics, business, finance or accountancy:

The Council may constitute more Disciplinary Committees as and when it considers necessary. The Disciplinary Committee, while considering the cases placed before it, shall follow such procedure as may be specified.

Where the Disciplinary Committee is of the opinion that a member is guilty of a professional or other misconduct mentioned in the Second Schedule or both the First Schedule and the Second Schedule, it shall afford to the member an opportunity of being heard before making any order against him and may thereafter take any one or more of the following actions, namely:—

- (a) Reprimand the member;
- (b) Remove the name of the member from the Register permanently or for such period, as it thinks fit;
- (c) impose such fine as it may think fit, which may extend to rupees five lakhs.

### **Authority, Disciplinary Committee, Board of Discipline and Director (Discipline) to have powers of civil court**

Section 21C provides that for the purposes of an inquiry under the provisions of this Act, the Authority, the Disciplinary Committee, Board of Discipline and the Director (Discipline) shall have the same powers as are vested in a civil court under the Code of Civil Procedure, 1908, in respect of the following matters, namely:—

- (a) summoning and enforcing the attendance of any person and examining him on oath;

- (b) the discovery and production of any document; and
- (c) receiving evidence on affidavit.

*Explanation* – For the purposes of sections 21, 21A, 21B, 21C and 22, “member of the Institute” includes a person who was a member of the Institute on the date of the alleged misconduct although he has ceased to be a member of the Institute at the time of the inquiry.

### **Appeal to Authority**

Under section 22A of the Act the Appellate Authority constituted under sub-section (1) of section 22A of the Chartered Accountants Act, 1949, shall be deemed to be the Appellate Authority for the purposes of this Act, subject to certain modifications.

Accordingly, any member of the Institute aggrieved by any order of the Board of Discipline or the Disciplinary Committee imposing on him any of the penalties referred to in section 21A and section 21B, may within ninety days from the date on which the order is communicated to him, prefer an appeal to the Authority:

The Director (Discipline) may also appeal against the decision of the Board of Discipline or the Disciplinary Committee to the Authority if so authorised by the Council, within ninety days:

The Authority may entertain any such appeal after the expiry of the said period of ninety days, if it is satisfied that there was sufficient cause for not filing the appeal in time.

(2) The Authority may, after calling for the records of any case, revise any order made by the Board of Discipline or the Disciplinary Committee under sub-section (3) of section 21A and sub-section (3) of section 21B and may —

- (a) confirm, modify or set aside the order;
- (b) impose any penalty or set aside, reduce, or enhance the penalty imposed by the order;
- (c) remit the case to the Board of Discipline or Disciplinary Committee for such further enquiry as the Authority considers proper in the circumstances of the case; or
- (d) pass such other order as the Authority thinks fit:

Provided that the Authority shall give an opportunity of being heard to the parties concerned before passing any order.

### **Certain Provisions Relating to Misconduct under the Company Secretaries Act, 1980**

Professional misconduct in relation to members of the Institute is broadly structured under Schedule I and Schedule II of the Act:

- (a) Professional misconduct in relation to Company Secretaries in Practice. (Part I of the First Schedule)
- (b) Professional misconduct in relation to members of the Institute in service. (Part II of the First Schedule)
- (c) Professional misconduct in relation to members of the Institute generally. (Part III of the First Schedule)
- (d) Other misconduct in relation to members of the Institute generally (Part IV of the First Schedule)
- (e) Professional misconduct in relation to Company Secretaries in practice requiring action by

disciplinary committee (Part I of the Second Schedule)

- (f) Professional misconduct in relation to members of the Institute generally, requiring action by disciplinary committee (Part II of the Second Schedule).
- (g) Other misconduct in relation to members of the Institute generally (Part III of the Second Schedule)

The detailed provisions relating to misconduct and disciplinary mechanism are contained in Sections 21, 21A, 21B, 21C, 21D & 22 and the First and the Second Schedules to the Act and the Rules

### **a. Professional misconduct in relation to Company Secretaries in Practice (Part I of the First Schedule to the Act)**

Part I of the First Schedule to the Act deals with professional misconduct in relation to Company Secretaries in practice. It contains eleven clauses in all. The implications of various clauses in Part I are briefly explained herein below.

#### **Clause (1)**

provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“allows any person to practice in his name as a Company Secretary unless such person is also a Company Secretary in Practice and is in partnership with or employed by him.”

This rule is intended to ensure that the professional work is done by a qualified professional so as to protect the client's/public interest. The rule permits another person to practice in the name of a Company Secretary in Practice provided such other person is also a Company Secretary in Practice and is in partnership with or is employed by the Company Secretary in Practice in whose name the work is to be carried out.

This clause read with clause 11 of Part I of the First scheduled does not permit PCS to allow any person to practice in his name as a Company Secretary or to allow any person to sign as PCS, unless such person is also a Company Secretary in Practice or is in partnership with or employed by him;

On a question as to how CA / CWA can become partner(s) of PCS, council has opined that though for the time being CA/CWA etc. cannot become partners of a PCS but after the amendments to the relevant provisions, person(s) who are non members, may become partners of PCS and may be allowed to provide non-attestation services.

Two persons are said to be in Partnership when they work together on mutual faith and agency. Sharing of remuneration does not make them partners. Thus an associate who is not a part of decision making process does not become a partner. Following tests if fulfilled cumulatively may make two persons partners of each other.

- i. Sharing of profits and or losses.
- ii. Taking decisions together.
- iii. Sharing the responsibilities of such decision making.
- iv. Acting on behalf of each other and binding other person with one own acts of commission or omission.

Sharing of common infrastructure at same or different geographical location are not relevant at all to decide the relationship.

**Clause (2)**

provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“pays or allows or agrees to pay or allow, directly or indirectly, any share, commission or brokerage in the fees or profits of his professional business to any person other than a member of the Institute or a partner or a retired partner or the legal representative of a deceased partner or a member of any other professional body or with such other persons having such qualifications as may be prescribed, for the purpose of rendering such professional services from time to time in or outside India.

*Explanation* — in this item, ‘partner’ includes a person residing outside India with whom a Company Secretary in Practice has entered into partnership which is not in contravention of item (4) of this part.”

This clause does not prohibit a Company Secretary in Practice from sharing fees, commission or brokerage in the fees or profits of his professional business, with any other member of the Institute or a partner or a retired partner or the legal representative of a deceased partner. Such sharing of fees, commission or brokerage in the fees or profits of professional business is also permissible with members of such professional bodies or with such other persons having such qualifications as may be prescribed from time to time. This provision is made primarily to encourage multi-disciplinary partnership.

In terms of clause (2) of Part II of the First Schedule to the Act, a member of the Institute in service shall be deemed to be guilty of professional misconduct, if he being an employee of any company, firm or person, accepts or agrees to accept any part of fees, profits, or gains from a lawyer, a Company Secretary or broker engaged by such company firm or person or agent or customer of such company, firm or person by way of commission or gratification. Accordingly a Practising Company Secretary cannot share fees with an employee Company Secretary. Therefore, words ‘who is in practice’ are to be read in Clause 2 of the Part I of the First Schedule, after the word “institute”.

The term ‘partner’ used in this rule would include ‘ipso facto’ another Company Secretary in Practice or a member of any other recognised profession under Section 2(2) of the Act. In regard to sharing of fees with the legal representative of a deceased partner it is desirable that the partnership deed contains a suitable covenant in this behalf. In the case of a sole proprietorship firm, on the death of the proprietor of the firm, there cannot be any sharing of fees between the purchaser of the goodwill of the firm and the legal representative of the proprietor. Payment of goodwill is permissible, which can be in installments as provided in the agreement of sale of goodwill. The payment of goodwill shall, in no circumstances be linked with participation in the earnings of the firm of the buyer of the goodwill.

It may appear that this Clause permits sharing of fees by PCS with members of the Institute who are not employed but are practicing as CA / CWA or an Advocate. However this does not appear to be the intention. The term “Professional Business” used may be understood as professional activities.

CA/CWA may become partners of PCS only for non attestation services i.e. only for the purposes as contemplated by clause nos. 2, 3, 4 & 5 of the First Schedule and CA / CWA cannot become full fledged partners as contemplated by Clause 1 of Part I of the First Schedule. That is to say a PCS even if he is allowed to be a partner of a Chartered Accountant, will not be able to sign the Auditors report on behalf of the multidisciplinary firm.

In other words, a CA or CWA who does not hold CP of ICSI, can not issue Secretarial Audit Report by a multidisciplinary firm even if such CA/ CWA is a partner of PCS for the purposes of Clause 2, 3, 4, & 5 of the First Schedule.

Council in its 177th meeting held on 27th November 2007 has passed following resolution:

**“168A. Other Professional bodies.—**

(1) For the purposes of clauses (2), (3) and (5) of Part I of the First Schedule to the Act, a person has to be member of any of the following, namely:

- (a) The Institute of Chartered Accountants of India established under the Chartered Accountants Act, 1949 (No.38 of 1949);
- (b) The Institute of Cost and Works Accountants of India established under the Cost and Works Accountants Act, 1959 (No. 23 of 1959);
- (c) The Bar Council of India established under the Advocates Act, 1961 (No.25 of 1961);.
- (d) The Indian Institute of Architects established under the Architects Act, 1972(No.20 of 1972);
- (e) The Institute of Actuaries of India established under the Actuaries Act, 2006 (No.35 of 2006);
- (f) the membership of the professional bodies or institutions whose qualifications relating to Company Secretaryship are recognized by the Council under sub-section (2) of Section 38 of the Act

(2) For the purposes of clauses (2), (3) and (5) of Part I of the First Schedule to the Act, the following shall be the persons qualified in India, namely:

- (a) Chartered Accountant within the meaning of the Chartered Accountants Act, 1949;
- (b) Cost Accountant within the meaning of the Cost and Works Accountants Act, 1959;
- (c) Actuary within the meaning of the Actuaries Act, 2006;
- (d) Bachelor in Engineering from a University established by law or an institution recognized by law;
- (e) Bachelor in Technology from a University established by law or an institution recognized by law;
- (f) Bachelor in Architecture from a University established by law or an institution recognized by law;
- (g) Bachelor of Law from a University established by law or an institution recognized by law;
- (h) Master in Business Administration from Universities established by Law or Technical Institutions recognized by All India Council for Technical Education.”

The resolution amends the Company Secretaries Regulations, 1982. The amendment was notified in the Gazette of India Extraordinary dated 26th of July 2010.

**Clause (3)**

provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“accepts or agrees to accept any part of the profits of the professional work of a person who is not a member of the Institute:

Provided that nothing herein contained shall be construed as prohibiting a member from entering into profit sharing or other similar arrangements, including receiving any share commission or brokerage in the fees, with a member of such professional body or other person having qualifications, as is referred to in item (2) of this part.”

This is the converse of clause (2) discussed (supra at para 4.3) wherein a Company Secretary in Practice can partake of his profits with other members of the Institute and with members of any other professional bodies specified in this regard or with such other persons having such qualifications as may be prescribed, under clause (3) a Company Secretary in Practice as recipient can enter into profit sharing arrangement with a member of the Institute and/or with a member of such other professional body or other person having qualifications, as is referred to in clause (2)

#### Clause (4)

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“enters into partnership, in or outside India, with any person other than a Company Secretary in Practice or such other person who is a member of any other professional body having such qualifications as may be prescribed, including a resident who but for his residence abroad would be entitled to be registered as a member under clause (e) of sub-section (1) of section 4 - or whose qualifications are recognised by the Central Government or the Council for the purpose of permitting such partnerships .”

This clause prohibits a Company Secretary in Practice entering into partnership with any person other than a Company Secretary in Practice or a member of any other recognised profession. Even entering into partnership with persons, who are not members of the Institute, for the purposes of carrying on a business and not the profession of Company Secretaries, would attract the mischief of the clause.

Also, partnership with any other person residing outside India but possessing qualifications recognised by the Central Government or the Council under section 4(1)(e) of the Act, is permitted. The purpose behind clause (4) is that a Company Secretary in Practice should not enter into partnership with any non-recognised professionals. In recognising any other profession for partnership, the compatibility of the other profession with the Company Secretaries' profession would be a relevant factor. The other professions referred to in this clause cannot be any different from those as may be recognised under section 2(2) of the Act. Practicing Company Secretary may share the fees or profits of the partnership both within and outside India

The council has passed the resolution by inserting the following regulation in CS regulations, 1982.

**“168B. Membership of Professional body for Partnership** — (1) For the purposes of entering into partnership under clauses (4) and (5) of Part I of the First Schedule to the Act, a person shall be a member of any of the following professional bodies, namely:

- (a) The Institute of Chartered Accountants of India established under the Chartered Accountants Act, 1949 (No. 38 of 1949);
- (b) The Institute of Cost and Works Accountants of India established under the Cost and Works Accountants Act, 1959 (No. 23 of 1959);
- (c) Bar Council of India established under the Advocates Act, 1961 (No.25 of 1961);
- (d) The Institute of Engineers or Engineering from a University established by law or an institution recognized by law;
- (e) The Indian Institute of Architects established under the Architects Act, 1972 (No.20 of 1972);
- (f) The Institute of Actuaries of India established, under the Actuaries Act, 2006 (No. 35 of 2006);
- (g) Professional bodies or institutions outside India whose qualifications relating to Company Secretary recognized by the Council under sub-section (2) of Section 38 of the Act.”;

The resolution amends the Company Secretaries Regulations, 1982. The amendment was notified in the Gazette of India Extraordinary dated 26th July 2010.

### Clause (5)

provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“secures, either through the services of a person who is not an employee of such Company Secretary or who is not his partner or by means which are not open to a Company Secretary, any professional business.

Provided that nothing herein contained shall be construed as prohibiting any arrangement permitted in terms of items (2), (3) and (4) of this part.”

This clause frowns upon discreditable practices in securing professional work. The clause covers instances of obtaining professional work by unethical means and by means which are not open to a Company Secretary.

Council has issued guidelines for advertisement by PCS. These guidelines were approved by the council in its 178th Meeting held on 29th of December, 2007. A PCS can therefore, within the parameters of the above guidelines issue advertisement / launch his own website and such action on the part of PCS would not be treated as violation of Clause 5 as well as Clause 6 of the Part I of the First Schedule.

Clause 5 of part I of first schedule is very clear that no member in practice should secure any professional business through propagation, etc., the member in practice have to be cautious that any kind of wording or message in the website created by them shall not indicate or imply securing/solicitation of business/client.

However any act of omission or commission beyond the permitted methods as per the guidelines would amount to misconduct. Text of the Advertisement Guidelines is placed as Annexure to this chapter.

### Clause (6)

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“solicits clients or professional work, either directly or indirectly, by circular, advertisement, personal communication or interview or by any other means: Provided that nothing herein contained shall be construed as preventing or prohibiting

- (i) any Company Secretary from applying or requesting for or inviting or securing professional work from another Company Secretary in practice; or
- (ii) a member from responding to tenders or enquires issued by various users of professional services a organisations from time to time and securing professional work as a consequence.”

This clause further fortifies the proposition under clause (5) supra about securing clients or professional work. Solicitation of clients or solicitation of professional work or both, are prohibited. Such a solicitation may be direct or indirect and such a solicitation may further be by means of a circular, advertisement, personal communication or interview or any other means. The bedrock of this rule is that a professional should gain recognition by rendering expert services, to a few though in the beginning, who would themselves lead others to him. A true professional should command honour and not demand it. The conduct of the member is noted all the times by the society at large and their ethics and integrity towards the profession itself is

sufficient for growth. So, the purpose of this clause is, to ensure that a professional secures work by his credibility, reliability and integrity in the public eyes and not by advertisement adversely affecting the image of the professional and also the profession.

The word 'solicit' has various shades of meaning. According to Legal Thesaurus, it means bait, (lure) desire, importune, inquire, lobby, petition, plead (implore), apply (request), pray, pressure, pursue, (strive to gain), urge. 'Solicit' means 'ask for' or 'seek'. Means of solicitation may be a circular, advertisement, personal communication or by any other means. The phrase 'by any other means' used in this clause would perhaps exhaust other means like telephonic conversation, mail, electronic means and messages/social media or even third party solicitation.

The word 'indirectly' used in this clause suggests that even innuendos would not be tolerated under this clause. If the overall message of the alleged act is solicitation of clients or professional work, though this lurks or lies beneath what has apparently been done, clause 6 would stand attracted.

(1) Circular or advertisement in newspapers indicating the range of services offered by him.

(2) A circular letter offering secretarial services and professional work.

(3) Any circular, advertisement or communication which creates an impression that certain professional work would be done much more expeditiously than is normally the case. Like for instance, registration of a company in, say, two days' time or registration of a charge in one day's time, etc.

(4) Circular, advertisement or personal communication highlighting any provision of any law, to person other than existing clients, which provides for certification/ authentication by a Company Secretary in Practice of any form/return/application/document.

(5) Issuing hand bills covering matters in (1) to (4) above.

(6) Publication in the telephone directory, name and address in extra bold typeface or opting for more than one listing. However, where separate sections are devoted in the telephone directory (yellow pages, for instance) for a classified list, publishing the name and address by a member in such sub-section in the directory would not be treated as misconduct. But any kind of message or writing which indicates tall claims, supremacy and superiority in professional attainments will tantamount to solicitation of clients, indirectly.

(7) Communicating or holding out, as being prepared to provide professional services at fees that are less than reasonable and appropriate in the circumstances, in order to obtain professional work.

(8) Communicating or describing himself as a 'specialist' in any branch of law/work or knowingly permitting himself to be so described.

(9) A member allowing a company to carry in its prospectus or other circular letters that 'Mr. X a specialist in corporate laws is the adviser to the company' would offend clause (6). However printing the name of Practising Company Secretary as Secretarial Auditor in Annual Report will not violate the provisions of the Act.

(10) Requesting his client(s) to recommend his/their acquaintances to him for professional work.

(11) Frequent press announcements or circulars about his not being available for professional work for a certain period at the place whereat he normally has his office.

(12) Highlighting or causing to be highlighted in public interviews over the television, AIR, etc. their professional attainments, more than just necessary or warranted by the circumstances of such an interview,

making tall claims, indicating supremacy over other professional colleagues, etc. However sending bio data to organizers of the programmes/seminars, etc., where they have been invited as a faculty, is not violative of this clause.

(13) Writing to any institution/agency that though, he is in the panel; no work has been allotted to him. Even approaching through a third person is violative of this clause.

(14) Approaching any trade association/chamber of commerce/ business forum, communicating his ready availability for rendering any professional service to the constituents of any association or chamber.

(15) Sending his profile to persons/companies/firms without any requisition for the same.

(16) Including names of other professionals in his profile circulated to various persons.

The Professional Development Committee of the Council of the Institute has opined that listing of services by a Company Secretary with a group for creation of network of affiliates which is non-professional and not a group of company secretaries would amount to commercialization of the profession and therefore such listing would amount to violation of the Code of Conduct.

However, the following would not fall into the mischief of clause (6):

(1) publishing in the journal of the Institute or newspaper any change in the professional address;

(2) publishing in professional journals, newspapers and magazines in any classified column, any advertisement for recruitment of staff without in any way giving an impression about the services that he can render, or in other manner smacking of solicitation of work;

(3) publishing information regarding changes in the constitution of firm, provided the information contained therein is limited to bare facts and consideration given to appropriateness of the area in which the newspaper or magazine is circulating and the number of insertions

(4) sending New Year or any other seasonal greetings without narrating the list of services, professional attainments, supremacy or any kind of indication seeking clients.

(5) appearance in AIR, TV or any stage in private capacity as a speaker, actor or otherwise on programmes having no nexus with his profession. Any reference to him only as a Company Secretary and nothing beyond that in such programmes would not offend clause (6);

(6) appearance or participation in professional capacity in the AIR/TV or other forums where a reasonable amount of biographical material may be given without in any way referring to the member as specialist in any branch of work;

(7) editing/publishing any professional journal, newspaper and magazines;

(8) writing articles/comments in professional journals, magazines and newspapers;

(9) associating with charitable, other welfare associations and trade associations without in any way using such position to solicit clients/ professional work;

(10) writing to his existing clients about implications/interpretations of any law or amendments thereof by way of any circular, newsletter or any personal communication or by way of print/electronic means of communication.

The Council of the Institute in a case held that the Conduct of the member in practice by mentioning against

his name 'Company Secretary' in the issue of 'Secretarial Aid' a journal edited by him was violative of Clause (6) of Part I of First Schedule to the Act. It was observed that the words 'for further clarification please contact the Editor' was an indirect attempt to solicit professional work.

Responding to a specific letter or a follow up of personal discussions and sending a profile of a firm/individual to specific addresses is not prohibited.

(11) Stating the assignments handled by him in his profile. However, the name of the clients should be supplied only against specific request of the client for the same.

(12) Issuing advertisement in Chartered Secretary for opening branch or seeking partnership with other members.

(13) Issuing advertisement or launching website within the frame work of guidelines issued by the council about advertisement by PCS.

(14) Securing professional work from another PCS is now expressly permitted

(15) Responding to tenders or enquires issued by various users of professional services and securing professional work as a consequence is now expressly permitted.

### **Clause (7)**

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“advertises his professional attainments or services, or uses any designation or expressions other than Company Secretary on professional documents, visiting cards, letterheads or signboards, unless it be a degree of a University established by law in India or recognised by the Central Government or a title indicating membership of the Institute of Company Secretaries of India or of any other institution that has been recognised by the Central Government or may be recognised by the Council.

Provided that a member in practice may advertise through a write up setting out the services provided by him or his firm and particulars of his firm subject to such guidelines as may be issued by the Council.”

This clause covers two aspects –

- (i) advertisement of professional attainments or services by a Company Secretary in Practice and
- (ii) using the designation 'Company Secretary'.

As regards the ban on advertisement of professional attainments or services, almost all the professions all over the world had this type of restriction at least to start with. The idea behind this restriction was that advertisement by professionals is incompatible with the qualities of integrity and independence which a professional is expected to possess, especially when these acts are motivated by a desire for personal gain. The advertisement of professional attainment or services under this clause is completely prohibited except where the Company Secretary in Practice advertises as per the guidelines issued by the council, through a write up setting forth services provided by him or his firm.

A PCS cannot include in his advertisement following particulars like the infrastructure available in his own office, details of Associate PCS, details of his networking in other places within & outside India, infrastructure at such networked offices, number of trainees who have completed training from his office, certain landmark achievements like number of companies incorporated since he started his practice, number of appearances made before CLB/NCLT, CBDT, Tribunals, Regulatory Authorities, Commissions, number

of Foreign Collaborations handled, number of Merger & Acquisitions handled, Number of due diligence carried out etc.

Council is of the view that a PCS can be permitted to allow his clients to use his name in their brochure/hoardings etc. e.g. Builders invariably write the names of Architects, RCC Consultants, legal advisors on the Board at the construction site. Similarly the name of PCS may also be written. Certain software companies desire to use the name of PCS in their marketing brochure for their products while giving a list of satisfied customers. A PCS is permitted to allow his name to be used as one of the satisfied customers of particular software.

What amounts to advertisement of professional attainments or services is to be decided on a case to case basis, having regard to the attendant facts. For instance, where in the visiting card or name board or letterhead, a member in practice mentions that he is a specialist or expert in company law, tax law, etc. it would amount to advertisement of professional attainments or services.

Where a member in practice furnishes upon a specific request by a prospective client, a list of companies for whom he is a consultant/retainer or writes his specific subjects of specialisation, it may not be objectionable.

Where in the letterhead or visiting card, a member in practice mentions that he was or is holding directorships in any company; it would be offending this clause.

Advertisement by a Practising member for staff for his office in the press should in no way savour of any advertisement of professional attainments or services. The use of certain adjectives like “a reputed firm”, “a well-known firm”, etc. may be treated as inconsistent with the spirit of this clause. Similarly, announcement in the press by a Practising member in regard to certain attainments like having been named for certain public awards, acquisition of merit in other professional examinations and other recognitions in any important committee, commission, governing body, etc. should be suitably modified so as not to be construed as amounting to advertisement of professional attainments or services. Advertisement for part-time assignments fall under the mischief of this clause.

Circulars or announcement regarding change of address, or change in the constitution of the firm should be very cautiously worded to tell just the minimum necessary facts.

Where a Company Secretary in Practice has been appointed as retainer/consultant by certain companies, it would not be proper to either list the names of such companies in letterheads, visiting cards or signboards or to circulate the list among prospective clients by way of circular. However, including such names, while sending individual profile in response to a specific enquiry is permitted.

Where a Company Secretary in Practice takes up the position of a director in a company, it is incumbent on his part to exercise great care in regard to references in any explanatory statement in notice of the general meeting reappointing the Practising Company Secretary brochure or circular brought out in connection with an issue of securities of the company etc. The member concerned is to ensure personally that laudatory statements in such literature about his professional competence, while highlighting the Board's competence as a whole, are avoided; otherwise liability under clause (7) would attract.

The Council held a member guilty of professional misconduct for misusing the Institute's letter head, brochures, circulars, etc. mentioning his name with designation, description and the Practising field other than as prescribed and thus misleading the readers by not mentioning his whole time employment.

This clause also speaks of using the designation 'Company Secretary' on professional documents, visiting cards, letterheads, sign-boards, etc. This requirement fortifies the provisions of section 7 of the Act and in fact is an extension of the requirement in regard to the use of proper designation. Designations like

Company Law Consultant, Income Tax Consultant, Corporate Adviser, Investment Adviser, Management Consultant etc. are prohibited. The use of descriptions indicating membership of the Institute of Chartered Accountants of India, The Institute of Cost and Works Accountants of India and the Bar Councils is permitted provided members are not holding certificate of practice issued by the Institute or using the description 'Company Secretary'. The use of the designation "Practicing Company Secretary". "Company Secretary in whole-time practice", etc. is not violative of this clause.

Where a member in practice had described himself in visiting cards and letter heads as "Company Secretary & Advocate, High Court", the Council held the member guilty of professional misconduct under this clause.

### **Clause (8)**

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“accepts the position of a Company Secretary in Practice previously held by another Company Secretary in Practice without first communicating with him in writing.”

The primary requirement under this clause is of prior communication with the previous incumbent. This is intended for reasons of professional courtesy. The clause is not intended to prevent a client from changing over to another Company Secretary for his own reasons. The client as of right, has full freedom to change over to another Company Secretary.

It would be desirable for the new incumbent to obtain a letter from the company letting him know the name of the earlier incumbent or that no other Company Secretary has been appointed for the same assignment.

It is expressly clarified that the communication mentioned in this clause does not mean that no-objection or consent of the previous incumbent is a prerequisite of accepting the said assignment.

In regard to certification of Annual Return under Section 92 and for all exclusive attestation assignments, it is incumbent on the Company Secretary; to ascertain if any other Company Secretary had been appointed previously by the company concerned for certification of Annual Return or for issuance of compliance certificate, as the case may be. The appointee shall take positive steps to ascertain if anyone has been engaged earlier, for the same year, for the certification work. In such cases it is not only necessary for the Company Secretary to communicate with the earlier incumbent, but it is desirable to seek his consent in order to uphold the dignity and independence of the profession. It is further clarified that though communication is a must, obtaining consent will not apply in cases of certification of Annual Returns for different years.

It would be necessary that the communication, in order to be effective, shall be by a registered letter or by hand with an acknowledgement so that there is positive evidence of the communication having been complete. In a case under a similar rule of conduct under the Chartered Accountants Act, 1949, the Rajasthan High Court in *J S Bhati v. Council of ICAI* (S.B. Civil Misc. Appeal No. 136 of 1973) observed that mere obtaining a certificate of posting does not fulfill the requirements of clause (8) of Schedule I as the presumption under section 114 of the Evidence Act that the letter in due course reached the addressee cannot replace that positive degree of proof of delivery of letter to the addressee which letters of the law in this case require.

The expression 'in communication with' when read in the light of the instructions contained in the booklet 'Code of Conduct' cannot be interpreted in any other manner but to mean that there should be positive evidence of the fact that the communication addressed to the outgoing auditor by the incoming auditor

reached his hands. Certificate of posting of a letter cannot, in the circumstances, be taken as positive evidence of its delivery to the addressee. The Court, therefore, has expressed the view that the communication by a certificate of posting cannot be taken as a positive evidence of its delivery to the addressee. A communication sent by hand which has been properly acknowledged by the addressee would be effective communication.

With the advent of use of the technology, it would proper communication in this regard made by any other electronic medium viz., SMS, Whats App and such other Messenger apps is also permitted, provided the sender (the PCS taking up the assignment) is able to establish that the message is delivered to the recipient before he or she takes up the assignment. Needless to mention, that a reasonable time should be given to the previous incumbent to offer his response, if any, and it is not just a kind of formality. For sake of better clarity, the new incumbent should express clearly in the communication the details of assignment being taken up by him.

Members have been held guilty of professional misconduct under this clause for having accepted and commenced the certification of Annual Return of a company without first communicating with the earlier incumbent in writing. It has been concluded that mere posting of the letter is not sufficient to comply with the requirements of clause (8) of Part I of First Schedule to the Act, but the delivery of the message to the addressee of the same is essential. Oral communication is no communication as far as this clause is concerned.

To a question about whether communication 'with' contemplates a dialogue, the council is of the view that use of the preposition 'with ' instead of 'to ' does not make it mandatory for the PCS to obtain 'no objection' from the earlier incumbent. What is critical for PCS (new incumbent) is to prove that he has sent a written communication to the earlier incumbent before accepting a position of PCS.

It has been observed that majority of the Disciplinary cases were in respect of this clause about not sending written intimation by the new incumbent (PCS).

While clarifying the scope of the words " accepting a position of Company Secretary in Practice" Council has expressed a view that need for sending a previous communication to the earlier incumbent arises only in relation to exclusive area of practice under the Act. Therefore, in respect of following it shall not be mandatory (though desirable) to send a prior written communication to the earlier incumbent:

- a. certifying e-forms for various companies.
- b. giving Due Diligence Certificate for consortium borrowers.
- c. holding assignment as retainer for a company or group of companies .
- d. issuing search reports.
- e. Issuing certificates as contemplated under SEBI (LODR) Regulation, 2015.
- f. Giving legal opinion

In respect of the following, it shall be mandatory to send a prior written communication (including means mentioned above in 4.9.8) to the earlier incumbent:

- (i) Signing / Certification of Annual Return
- (ii) Issuance of Secretarial Audit Report in terms of Section 204 of the Companies Act, 2013
- (iii) Issuance of Certificate of Securities Transfers.
- (iv) Certificate of reconciliation of capital, updation of Register of Members, etc. as per the Securities &

Exchange Board of India's Circular D & CC/Cir-16/2002 dated December 31, 2002.

- (v) Conduct of Internal Audit of Operations of the Depository Participants.
- (vi) Certification of corporate governance under SEBI (LODR) Regulation, 2015.

### **Clause (9)**

provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“charges or offers to charge, accepts or offers to accept, in respect of any professional employment, fees which are based on percentage of profits or which are contingent upon the findings or results of such employment, except in cases which are permitted under any regulations made under this Act.”

which determine remuneration based on results. For instance, if the Company Secretary in Practice were to quote remuneration in an Excise Refund case, as a percentage of the final amount of refund that may be ordered by an appellate authority, it would be hit by this clause. The fundamental is that the fee should be more related to the expertise required and the time spent on a particular case without in any way linking the fee with the final results.

### **Clause (10)**

provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“engages in any business or occupation other than the profession of Company Secretary unless permitted by the Council so to engage:

Provided that nothing contained herein shall disentitle a Company Secretary from being a director of a company except as provided in the Companies Act.”

This clause is intended to ensure that a PCS does not engage in vocations which are not compatible with the profession of Company Secretary. This has been provided with a view to ensure the profession develops in its true sense. Pursuant to the Company Secretaries Regulations, 1982, the Council has decided not to issue certificate of practice to members engaged in other professions such as Chartered Accountants, Cost Accountants and Advocates and also to members in employment. The said decision was taken by the Council to give an independent identity and status to the profession and a thrust to the concept of Company Secretary in whole-time practice.

The Council held a member guilty of professional misconduct under this clause for engaging himself in employment while holding a certificate of practice from the Institute.

The Council in an another case held a member guilty of professional misconduct under this clause for holding the certificate of practice of both the Institutes, i.e., ICAI & ICSI without the permission of the Council of the latter and also Practicing both the professions on whole-time bases simultaneously.

Regulation 168(2) of the Regulations provides that a Company Secretary may act as a secretary, trustee, executor, administrator, arbitrator, receiver, appraiser, valuer, internal auditor, management consultant or as a representative of financial matters including taxation and may take up appointment that may be made by the Central or any State Government, Courts of Law, labour tribunals, or any authority. From the reading of Regulation 168, it is clear that the various occupations provided in sub-regulation (2) thereof do not require a specific resolution to be passed by the Council.

It is pertinent to refer to Regulation 168(1) which provides that the prior permission of the Council by a resolution is required for a Company Secretary to engage in any business or occupation other than the profession of Company Secretary. The Council has expressly permitted a PCS to take up following vocations:

- (i) Acting as Private tutor.
- (ii) Authoring Books and Articles.
- (iii) Holding of Life Insurance Agency License for the limited purpose of getting renewal commission.
- (iv) Holding of public elective offices such as M.P., M.L.A., M.L.C. and others.
- (v) Honorary office-bearership of charitable, educational or other non-commercial organisations.
- (vi) Acting as Justice of Peace, Special Executive Magistrate and the like
- (vii) Teaching assignment under the Coaching Organisation of the Institute and other Institutes such as the Institute of Cost & Works Accountants of India, the Institute of Chartered Accountants of India, Management Institutes, Universities and any college affiliated to a University, and such other organisation as may be recognised by the Council of the Institute from time to time, so long as the hours during which a member in practice is so engaged in teaching do not exceed average three hours in a day irrespective of the manner in which such assignment is described or the remuneration receivable (whether by way of fixed amount or on the basis of any time scale of pay or in any other manner) by the member in practice for such assignment.
- (viii) carrying out valuation of papers, acting as a paper-setter, head examiner or a moderator, for any examination.
- (ix) Acting as editor of professional journals

#### Permission to be granted specifically

Members of the Institute in practice may engage in the following categories of business or occupation, after obtaining the specific and prior approval of the Executive Committee of the Council in each case:

1. Interest or association in family business enterprises even when he does not hold substantial interest in such enterprises.
2. Office of Managing Director or whole-time Director of a body corporate within the meaning of the Companies Act, 2013. The Council may refuse permission in individual cases though covered under any of the above categories.

For the purpose of the above, a member shall be deemed to have a “substantial interest” in a concern:

- (i) in a case where the concern is a company, if its shares (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) carrying not less than twenty-five per cent of voting power at any time during the previous year, are owned beneficially by such member.
- (ii) in the case of any other concern, if such member is entitled at any time during the previous year, to not less than 25% of the profits of such concern.

A PCS can function as a non-executive director of a company. This does not require any prior approval

**Clause (11)**

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“allows a person not being a member of the Institute in practice or a member not being his partner to sign on his behalf or on behalf of his firm anything which he is required to certify as a Company Secretary, or any other statements related thereto.”

This clause further fortifies clause (1) discussed already. It is not permissible for a Company Secretary in Practice to allow any person to sign on his behalf or on behalf of his firm anything which he is required to certify as a Company Secretary or any other statement related thereto. The purpose is not to allow a member to have his judgment and expertise substituted by the judgment of any other person who is not a member in practice or his partner in the firm. To take an instance, the annual return under Section 92 of the Companies Act, 2013 has to be certified by a Company Secretary in Practice himself. It is not possible to have the certification done by a Company Secretary, say, through a power of attorney holder, even though the holder of the power of attorney is an employee (of the Company Secretary) who has been associated with the checking up of various details furnished in the Annual Return.

PCS who is not a partner of another PCS can not sign on behalf of such other PCS on Annual Returns or Secretarial Audit Report or any other certificates.

In e-governance era, a PCS on many occasions attaches his Digital Signature to various forms / statements. Due care has to be taken that such digital signature is attached only by the PCS himself. It would be the exclusive duty and obligation of PCS to prevent any unauthorized use of his Digital signature. PCS is not expected to part with the password of his Digital signature.

**b. Professional misconduct in relation to members of the Institute in service (Part II of the First Schedule)**

Part II of First Schedule to the Act deals with professional misconduct of a member of the Institute (other than a member in practice) if he is an employee of any company, firm or person.

Part II of the First Schedule recognises the need for a member in employment also to observe a certain code of conduct. To be in ‘employment’ connotes to be in a ‘contract of service’ and not ‘contract for service’. There are four indicia of a contract of service, namely :

- (a) master’s power of selection of his servant;
- (b) payment of wages or other remuneration;
- (c) master’s right to control the method of doing the work; and
- (d) the master’s right of suspension or dismissal.

Lord Denning pointedly observed, “under a contract of service, a man is employed as part of a business, and his work is done as an integral part of the business; whereas under a contract for services, his work although done for the business is not integrated into it but is only accessory to it.”

One important issue which very frequently comes up is, the conflict that may arise between the employer’s interest and the interest of the member to uphold professional values and broader public interest. The code of conduct formulated by the Institute originally in 1977 emphasised the importance of a member in employment exercising professional independence in relation to his work as well as his endeavor to provide the highest quality of service attainable by him, without reference to the monetary compensation. The idea

being, a member must have courage of conviction to express candidly his considered professional opinion to his employer.

The Royal Commission in its Final Report on legal services submitted to the British Parliament in October, 1979 categorically observed that the standards of professional conduct and integrity which a member of the legal profession in employment has to abide by are the same as those who practice on their own account. Even though the difference is that a salaried lawyer acts for only one client, unlike a lawyer in practice who acts for several clients, the former must uphold the same standards of honour and etiquette, observed the Royal Commission. The Report recognised the continuing conflict between loyalty to the employer and loyalty to the external body enforcing the code of conduct. Nevertheless, whether a member is in employment or in practice, his duty to uphold professional values shall gain precedence over all other exigencies.

Part II and Part III of the First Schedule to the Act specify certain instances of misconduct to which a Company Secretary in employment may stand attracted. It has been mentioned earlier that under section 21 of the Act, the Council's power to direct enquiry is not limited only to those contained in the Schedule to the Act, in view of the fact that the phrase 'other misconduct' used in section 21 is sufficiently broad enough to cover instances not enumerated in the Schedule.

Clause (1) of Part II of the First Schedule provides that a member of the Institute (other than member in practice) shall be deemed to be guilty of professional misconduct, if he, being an employee of any company, firm or person—

“pays or allows or agrees to pay, directly or indirectly, to any person any share in the emoluments of the employment undertaken by him.”

This clause is analogous to clause (2) of Part I of the First Schedule in some respects. A member in employment shall not share emoluments of the employment with any other person, not even a member. Both direct and indirect sharing of the emoluments is prohibited. However, it may be noted that under Part I of the First Schedule, a member in practice can share the fee, commission or brokerage or profits with any other member of the Institute who is his partner.

Clause (2) of Part II of the First Schedule provides that a member of the Institute (who is in service) shall be deemed to be guilty of professional misconduct, if he, being an employee of any company, firm or person—

“accepts or agrees to accept any part of fees, profits or gains from a lawyer, a Company Secretary or broker engaged by such company, firm or person or agent or customer of such company, firm or person by way of commission or gratification.”

This clause vindicates the confidence and trust that an employer reposes in an employee while the latter deals with any outsider on matters relating to business. It is an implied term of any employment that the employee concerned shall not secretly benefit from the employment.

This clause is also analogous in some respects to clause (3) of Part I of First Schedule.

### **c. Professional misconduct in relation to members of the Institute generally (Part III of the First Schedule to the Act)**

Part III of the First Schedule to the Act covers cases of professional misconduct in relation to members of the Institute generally. Under this Part, three specific instances have been categorised as professional misconduct.

Clause (1) of Part III of the First Schedule provides that a member of the Institute whether in practice or not

shall be deemed to be guilty of professional misconduct, if he—

“not being a Fellow of the Institute, acts as a Fellow of the Institute.”

This clause prohibits the practice of styling oneself as a Fellow, while in fact he is not a Fellow member. A person is entitled to have his name entered in the Register as a Fellow as per regulation 4(2) of the Regulations. The Fellowship of the Institute suggests a certain degree of status and seniority and obviously any wrongful representation of such seniority amounts to breach of code of conduct.

Clause (2) of Part III of the First Schedule provides that a member of the Institute whether in practice or not, shall be deemed to be guilty of professional misconduct, if he—

“does not supply the information called for or does not comply with the requirements asked for by the Institute, Council or any of its Committees, Director ( Discipline ) Board of Discipline, Disciplinary Committee, Quality Review Board or the Appellate Authority.”

It is the duty of a member to supply information called for or to supply the requirements asked for by the Council or any of its Committees and other authorities. Non-compliance with this clause would tantamount to breach of code of conduct.

The Council of the Institute in a case of professional misconduct, held a member guilty of professional misconduct under this clause for failure to disclose the fact of holding of the certificate practice of the Institute of Chartered Accountants of India to the Council of ICSI which was required to be made at the time of renewal of Certificate of Practice.

A member of ICSI bound to give any and every kind of information called from him since not providing information is a misconduct under clause (2) of Part III of the First Schedule. It is presumed that the concerned authorities would call only relevant information.

Clause (3) of Part III of the First Schedule provides that a member of the Institute, whether in practice or not, shall be deemed to be guilty of professional misconduct, if he—

“while inviting professional work from another Company Secretary or while responding to tenders or enquiries or while advertising through a write up, or anything as provided for in items (6) and (7) of Part I of this Schedule, gives information knowing it to be false.”

#### **d. Other Misconduct in relation to members of the Institute generally(Part IV of the First Schedule)**

##### **Clause 1 of Part IV**

A member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he is held guilty by any civil or criminal court for an offence which is punishable with imprisonment for a term not exceeding six months;

##### **Clause 2 of Part IV**

A member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if in the opinion of the Council, he brings disrepute to the profession or the institute as a result of his action whether or not related to his professional work.

Clause 2 of Part IV of the First Schedule provides that it shall be misconduct if in the opinion of the Council, a member of ICSI brings disrepute to the profession or the institute as a result of his action whether or not related to his professional work. Making an exhaustive list of such misconduct may not be possible.

Following may amount to misconduct under Clause 2 of Part IV of the First Schedule;

- Sending an e-mail to number of members (e-groups ) criticizing the decisions of the Council in derogatory and filthy language.
- Discussing through e forums failures of the Council/ president/ secretary by using derogatory and filthy language.
- Writing letter(s) in an aggressive, loud and filthy language to the Ministry of Corporate Affairs, about working of ROC offices/ MCA site, inability to upload forms etc.
- Arranging DHARANA/ agitations at the gates of the Govt. Offices/Institute's offices in a manner not befitting a professional.
- Instigating Students or other members by creating a pandemonium in or around Institute's offices by raising issues pertaining to syllabus, training, examination or any other reason what so ever.
- Misusing the confidential data available with the offices of the Institute for personal purposes.
- Inviting Govt. Officers for Chapter's / Regional Council's Programs by spending heavily on their travel & stay arrangements, with an intention to get personal mileage.
- Tampering with the Books of Accounts/ Minutes of the meetings of the Managing Committees of Chapter/ Regional Councils.

**e. Part I of the Second Schedule to the Act Section 21(3), 21(B)(3) and 22) where the matters are to be dealt with by the disciplinary committee constituted by the Council**

Part I of the Second Schedule to the Act deals with ten instances of professional misconduct in relation to members in practice, which require action by a Disciplinary Committee. The implications of various clauses in Part I of the Second Schedule are briefly explained herein below:

**Clause (1)**

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“Discloses information acquired in the course of his professional engagement to any person other than the client so engaging him, without the consent of such client, or otherwise than as required by any law for the time being in force.”

This clause indicates the position of trust and confidence reposed by the client in a Company Secretary in practice. A Company Secretary in Practice in the course of his professional engagement may come into possession of vital information. Such information has to be kept confidential unless consent of the client has been obtained to disclose the same or the disclosure is required by any law. In the case of a sole proprietor client, consent must be from the sole proprietor. In case the client is a partnership firm, consent has to be given by all partners if the partnership deed so provides; if the deed is silent, any partner can give the consent on behalf of the firm in view of his implied authority. In the case of Board-managed companies, the Board has to give the consent unless it has specifically resolved to delegate the power to any executive. Where the company is managed by a managing director, he may give consent.

It is necessary to bear in mind that any communication acquired by a Company Secretary in Practice in the course of his professional engagement on behalf of his client, any communication or any advice given by him to his client in the course and for the purpose of his engagement is a privileged communication and should

not be disclosed by him without the express consent of his client. Similarly, the Company Secretary in Practice should not disclose, without written consent of his client, the contents or conditions of any document with which he has become acquainted in the course and for the purpose of his professional engagement.

It is observed these days that PCS retains the digital signature of his client along with the password for the administrative convenience of uploading the forms from the office of PCS. It is suggested that in such a situation PCS should retain a formal letter signed by his client authorising PCS to make use of his Digital signature. The reason being once the forms are uploaded they appear on MCA portal and come to public domain. In order to avoid any future possible controversy, such authority letter would come handy for PCS.

### **Clause (2)**

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“certifies or submits in his name or in the name of his firm a report of an examination of the matters relating to Company Secretarial practice and related statements unless the examination of such statements has been made by him or by a partner or any employee in his firm or by another Company Secretary in practice.”

This clause is intended to imbibe in a member in practice, a higher degree of responsibility and care while certifying any fact or a statement. Either he himself or his partner or any employee of his firm should have examined what is being certified. The words “or by another Company Secretary in Practice” used in this clause envisage a situation where the responsibility for the certification is undertaken by a Company Secretary in Practice, who is neither a partner nor an employee of the Company Secretary concerned, for an examination done by another member in Practice.

This clause prohibits PCS from certifying or submitting in his name a report of an examination of the matters relating to company secretarial practice unless the examination of such statements has been made by him or by a partner or an employee in his firm or by another Company Secretary in Practice. Trainees working in the office of PCS are not to be considered as his employees for the purpose of this item . Reference to “another Company Secretary in Practice” at the end of paragraph refers to any PCS who may or may not be his partner. Thus a PCS would be justified in relying on the search report / examination done by another PCS and such reliance would not violate Clause 1 of the First Schedule.

### **Clause (3)**

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“permits his name or the name of his firm to be used in connection with any report or statement contingent upon future transactions in a manner which may lead to the belief that he vouches for the accuracy of the forecast.”

This clause underlines the duty of a Company Secretary in Practice to exercise utmost care in associating his name with any report or statement about future happenings or contingencies. A Company Secretary in Practice has to clearly disclose in the report or statement, as the case may be, the sources of his information and the premises on which the forecast is based. He shall further take care that he does not vouch for the accuracy of the forecast. Restraint is therefore required in subscribing to reports/statements, the contents of which may or may not turn out to be true.

The future is always uncertain and there is always an element of contingency. PCS can not become a

fortune teller. PCS should not certify any possible happening or non happening or give a report about the future e.g. it would be improper for a PCS to certify the future earning capacity, future shareholding pattern, future profitability or similar future figures and numbers. If at all there is any occasion for a PCS to sign such document he should clearly insert appropriate disclaimer clause.

#### **Clause (4)**

provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“expresses his opinion on any report or statement given to any business enterprise in which he, his firm or a partner in his firm has a substantial interest;”

This clause ensures that a professional has to be independent while expressing any opinion. He should not have any substantial interest in the business enterprise to which the report or statement pertains. That would create a conflict with his duty. Expressing opinion or giving any report with appropriate disclosures about his interest in the report was permitted earlier. However under the new clause there is a total ban on expressing opinion or giving any report about any business enterprise in which he, his firm or a partner in his firm has a substantial interest. ‘Substantial interest’ used in this clause is not limited to financial interest only.

In this connection it may be stated that the Council has, pursuant to Regulation 168 of the Regulations passed a resolution in which ‘substantial interest’ has been defined to mean an interest to the extent of 25%. The same guideline is relevant under the above clause also. If the business enterprise does not have a share capital, say a sports club, which may be a company limited by guarantee without Capital, the question whether PCS has substantial interest in such Club would be a question of fact.

#### **Clause (5)**

provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“fails to disclose a material fact known to him in his report or statement but the disclosure of which is necessary in making such report or statement, where he is concerned with such report or statement in a professional capacity.”

This clause deals with the paramount duty of a member in practice towards the user of any statement or report. The clause underlines the need for full and complete disclosure as to make any statement or report with which he is associated, true in every possible respect. The aiding or abetting must be with reference to a material fact known to him. If the member in practice does not know a material fact, or he has no reason to come to know a material fact by any means, there cannot arise any liability under this clause; also where a material fact is known to him but in his considered opinion, there is no reason to disclose them, the onus of defense would be on him to prove that the non-disclosure of the material fact has not made the statement misleading.

The expectation provided in this clause is something similar to the golden rule in respect of prospectus. The report/statement signed by PCS should contain truth, whole truth and nothing but the truth. Half truth at times is more disastrous. For example: making a statement that company has continuous track record of dividend declaration since incorporation, when the facts are that for last three years dividend was being declared from accumulated profits and not from current year’s profit. Making a statement that company has continuous track record of dividend declaration since incorporation would be half truth. The reader would be made to believe that the company has sound financial health. Thus the full facts should be disclosed by PCS by mentioning the fact that company has continuous track record of dividend declaration since incorporation, however since last three years dividend is being declared out of reserves.

### Clause (6)

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“fails to report a material misstatement known to him and with which he is concerned in a professional capacity.”

This clause deals with non-disclosure by a member in practice of a material misstatement known to him in any report with which he is concerned.

### Clause (7)

provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“does not exercise due diligence, or is grossly negligent in the conduct of his professional duties.”

This clause deals with due care that a member in practice has to exercise in the discharge of his professional duties. The words used in this clause “grossly negligent” imply that purely clerical errors or an omission to give more details in any recommended course of action will not fall within the sweep of this clause. What constitutes gross negligence would depend upon the facts and circumstances of each case.

The ICAI in their booklet ‘Code of Conduct’ have quoted the following extract from the judgment of the Karnataka High Court, in reference to an identical clause under the Chartered Accountants Act, 1949:

“It is the duty of an auditor to bring to bear on the work he has to perform that skill, care and caution which a reasonably competent and cautious auditor would use. What is reasonable skill, care and caution must depend on the particular circumstances of each case. An auditor is not bound to be a detective, or, as was said, to approach his work with suspicion or with a foregone conclusion that there is something wrong. He is a watch dog but not a blood-hound. 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. Professional misconduct is a term of fairly wide import but generally speaking, it implies fairly serious cases of misconduct of gross negligence. Negligence per se would not amount to gross negligence. In the case of minor errors and lapses, which do not constitute professional misconduct and which, therefore, do not require a reference to the disciplinary committee, the Council would nevertheless, bring the matter to the attention of its members so that greater care may be taken in the future in avoiding errors and lapses of a similar type“.

In *NemiChand v. Commissioner, Nagpur Division* ILR (1947 Nag 256 at 265 ,AIR 1948 24 at 27) it was held that gross negligence imports high degree of careless conduct.

Where, for instance, a Company Secretary who is not in wholtime practice under Companies Act, 2013, certifies Annual Return pursuant to section 92 of Companies Act, he would be guilty of being grossly negligent under this clause. Similarly, where a member in practice gives a certificate to a financial institution regarding necessary powers of a company and its directors to enter into an agreement without thoroughly verifying the Memorandum and Articles of Association of the Company, he would be guilty of misconduct under this clause. So also failure to check the resolutions as contained in the minutes book while certifying copies of resolutions would attract liability under this clause.

The difference in between the two expressions “Not exercising due diligence” and “being grossly negligent”-

is of degree. In both the situations it would amount to professional misconduct.

### Clause (8)

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“fails to obtain sufficient information which is necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion.”

The first limb of this clause deals with the duty of a member in practice to obtain sufficient information to warrant expression of an opinion. Issuing of a wrong consumption certificate under the Import Export Regulations for instance, without obtaining all necessary information required for the purpose, would get attracted to this clause. The second limb of this clause requires that any opinion expressed by a Company Secretary in Practice may be subject to certain exceptions. But, where the exceptions are sufficiently material, he should refrain from expressing an opinion, in other words, the second limb of this clause gives scope for making minor exceptions which are not important /material as to negate the very expression of opinion itself.

### Clause (9)

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“fails to invite attention to any material departure from the generally accepted procedure relating to the secretarial practice.”

This clause deals with the duty of a member in practice to invite attention to material departure from generally accepted secretarial practice. As of now, there have evolved certain widely accepted sound practices in regard to, say, share issue and transfers, share transmission, servicing of corporate securities, meetings procedure and other approvals, which are generally accepted as good secretarial practices. Until the time the standard secretarial practices in respect to any matter are recommended by the Institute for adoption are made mandatory, a member in practice has to, by and large, conform to existing well-recognised secretarial practices and invite attention to departures which are material. 8.11

### Clause (10)

Provides that a Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he—

“fails to keep moneys of his client other than fees or remuneration or money meant to be expended in a separate banking account or to use such moneys for purposes for which they are intended within a reasonable time.”

The purpose of this clause is firstly to ensure that the client's money is separately accounted for and secondly such money is specifically used only for the purpose for which it is paid by the client.

Advance received from clients for expenses like traveling, conveyance to be incurred by PCS need not be kept in a separate account, however advance received from a client for payment of Statutory / filing fees, Stamp duty to be paid by PCS on Client's behalf , must be kept in a separate account. In case client has paid advance for certain specific purpose, say for payment of fees and stamp duty for incorporation of the company or for increase in authorized capital such amount should be used in reasonable time. If the decision to incorporate a company or increase in capital is postponed/ cancelled, PCS should promptly return such

advance and should not adjust his fees from the amount so received for services rendered , if any, by him, unless such adjustment is authorised by the client.

**f. Professional misconduct in relation to members of the Institute generally (Part II of the Second Schedule to the Act)**

Part II of Second Schedule to the Act covers professional misconduct in relation to members of the Institute generally. The implications of the four clauses included in this Part are explained herein below:

**Clause (1) of Part II of Second Schedule**

Provides that a member of the Institute whether in practice or not, shall be deemed to be guilty of professional misconduct, if he—

“contravenes any of the provisions of this Act or the regulations made there under or any guidelines issued by the Council.”

This clause requires every member to pay due obedience to the Act, the Regulations and Guidelines issued by the council from time to time. For instance, a member of the Institute not having a certificate of practice representing that he is in practice (under section 24) or any violation of the rules relating to the conduct of elections (under Rule 42 of the Rules) would become guilty under this Clause; besides becoming liable for prosecution under section 24 of the Act.

The Council of the Institute, found a member guilty of professional misconduct under this clause for contravention of Section 6 of the Act as he certified an Annual Return of a company without holding a certificate of practice.

Following guidelines have been issued by the council so far

1. Display of particulars on website
2. Approving firm's name
3. Compulsory attendance at PDP
4. Dress Code
5. Issuing Compliance Certificate
6. Maintenance of Register of attestation services
7. Issue of advertisement by PCS
8. Change of Name of a Concern/Firm
9. Guideline for use of own Logo by PCS

It is necessary for all the members to understand the guidelines and follow the same in spirit and letter. It is also necessary to mention here that contravention of any of the provisions of the Company Secretaries Act, 1980 or the Company Secretaries Regulations, 1982 made there under or any guidelines issued by the council falls within the ambit of clause (1), part II of the Second Schedule to the Company Secretaries Act, 1980 and invites sterner actions.

**Clause (2) of Part II of Second Schedule**

Provides that a member of the Institute whether in practice or not, shall be deemed to be guilty of professional misconduct, if he—

“being an employee of any company, firm or person, discloses confidential information acquired in the

course of his employment, except as and when required by any law for the time being in force or except as permitted by the employer.”

The employer and employee relationship is of trust and confidence. This principle is embodied in this clause. The confidential information may pertain to technical secrets, important policy decisions, business strategies or any matter having a bearing on the interest of the employer.

Confidential information is a valuable asset for any employer. Confidentiality has to be maintained about members, customers, employees, suppliers, product mix, future plans, proposals, list of associates, affiliates, stake holders, dealers and financial information. All confidential information must be used for the benefit and best interest of the employer. Employee member must maintain the confidentiality of the information which comes to his knowledge / custody except when disclosure is authorized or legally required. Confidential information includes all non-public information that might be harmful or may have potential to cause harm to the employer, if disclosed.

The confidential information, discussions, documents and data should be dealt with utmost care and should not be shared or passed on to undesirable persons / outsiders under any circumstances, directly or indirectly.

### **Clause (3) of Part II of Second Schedule**

Provides that a member of the Institute whether in practice or not, shall be deemed to be guilty of professional misconduct, if he—

“includes in any information, statement, return or form to be submitted to the Institute, Council or any of its Committees, Director (Discipline), Board of Discipline, Disciplinary Committee, Quality Review Board or the Appellate Authority any particulars knowing them to be false.”

This clause covers situation where a member includes in any statement, return or form to be submitted to the Council any particulars knowing them to be false. The purpose of this clause is to ensure that a member submits accurate particulars, as are required to be furnished by him to the Council. It is pertinent to know that the clause is attracted only when the particulars furnished are known to the member to be false. It was held in Metropolitan Life Insurance Co. vs. S. Adam that the word ‘false’ has two distinct and well recognized meanings—

- (i) intentionally or knowingly or negligently untrue;
- (ii) untrue by mistake or accident after the exercise of reasonable care.

It is in the former sense that the term ‘false’ is to be understood in this clause. This is abundantly made clear by the qualifying words, ‘knowing them to be false’. The word false itself implies something more than mere untruth; it would even connote an intention to deceive.

Where for instance, while submitting the application for the issue/ restoration of certificate of practice under Regulation 10(1) of the Regulations, a member does not disclose that he is engaged in any business/occupation other than the profession of company secretaries when in fact he was so engaged, this clause would be attracted.

### **Clause (4) of Part II of Second Schedule**

Provides that:

“a member of the Institute whether in practice or not, shall be deemed to be guilty of professional misconduct, if he defalcates or embezzles moneys received in his professional capacity.”

This clause covers defalcation and embezzlement of moneys received in professional capacity by a member and not in any other capacity. The professional capacity referred to here would cover situations contemplated under Section 2(2) of the Act and those specifically covered under Regulation 168 of the Regulations. In as much as the Act deals with professional misconduct, logically the misconduct must be something having a nexus, direct in that, with the discharge of professional duties. However, this does not mean that other cases of embezzlement are not misconduct. Section 21 of the Act is wide enough to cover other acts not befitting to the member of the Institute.

#### **g. Part III of the Second Schedule**

This part is about other misconduct in relation to members of the Institute generally if a member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he is held guilty by any civil or criminal court for an offence which is punishable with imprisonment for a term exceeding six months.

Part III does not get attracted at the very first instance of being held guilty but it is attracted only after the final appeal, as it may be, is disposed off and the member is held guilty.

It may be observed that this clause does not provide that the offence for which a member is held guilty by any civil or criminal court for an offence which is punishable with imprisonment for a term exceeding six months involves moral turpitude. Therefore even for an imprisonment for a term exceeding six months in an offence which does not involve moral turpitude would attract the consequences

#### **Complaints and Enquiries Relating To Professional or Other Misconduct of Members**

(1) Subject to the provisions of this regulation, any complaint received against a member of the Institute under Section 21 shall be investigated, and any enquiry relating to misconduct of such member shall be held, by the Disciplinary Committee.

Provided that if the subject matter of a complaint is, in the opinion of the President, substantially the same as or has been covered in any previous information of complaint received, the Secretary may file the complaint without any further action or inform the complainant, accordingly, as the case may be.

(2) A complaint under Section 21 shall be made to the Council in the appropriate form, duly verified as required therein.

(3) Every complaint shall contain the following particulars, namely-

- (a) the acts or omissions which, if proved, would render the member complained against guilty of any professional or other misconduct;
- (b) the oral and/or documentary evidence relied upon in support of the allegations made in the complaint.

(4) Every complaint other than a complaint made by or on behalf of the Central or any State Government, shall be accompanied by a deposit of rupees fifty which shall be forfeited, if the Council, after considering the complaint, comes to the conclusion that no prima facie case is made out and, moreover, that the complaint is either frivolous or has been made with *mala fide* intention.

(5) The Secretary shall return a complaint which is not in the proper form or which does not contain the aforesaid particulars or which is not accompanied by the deposit of rupees fifty to the complainant for resubmission after compliance with such requirements and within such time as the Secretary may specify.

- (6) Ordinarily within sixty days of the receipt of a complaint under Section 21 the Secretary shall,-
- (a) if it is against an individual member send particulars of the acts of omissions alleged or a copy of the complaint, as the case may be, to such member at his address as entered in the Register;
  - (b) if it is against a firm, send particulars of the acts or omissions or a copy of the complaint, as the case may be, to the firm concerned at the address of the head office of the firm as entered in the Register of offices and firms which a notice calling upon the firm to disclose the name(s) of the member(s) concerned and to send particulars of acts or omissions or a copy of the complaint, as the case may be to member(s).

*Explanation-*A notice shall be deemed to be a notice to all the members who are partner or employees of that firm.

(7) A member who has been intimated of the complaint made against him under sub-regulation (6) (hereinafter referred to as the respondent) shall, within fourteen days of issue of such intimation or within such further time as the Secretary may allow, forward to the Secretary a written statement in his defence verified in the same manner as the complaint.

(8) On a perusal of the complaint and written statement in any, the Secretary may call for such additional particulars or documents connected therewith either from the complainant or the respondent, as he may consider necessary or as may be directed by the President, for perusal of the Council.

(9) Where on a perusal of the complaint, the written statement, if any, of the respondent and other relevant documents and papers, the Council is prima facie of opinion that any member has been guilty of professional or other misconduct, the Council shall cause an enquiry to be made in the matter by the Disciplinary Committee and where the Council is prima facie of opinion that there is no case against the respondent, the case shall be dismissed and the complainant, if any, and the respondent shall be informed accordingly.

Provided that the Council may, if deemed necessary, call for any additional particulars or documents connected therewith from the complainant, if any, or the respondent.

- (10)(i) Every notice issued by the Secretary or by the Disciplinary Committee under this Regulation shall be sent to the member or the firm concerned by registered post with acknowledgement due.
- (ii) If the notice is returned unserved with an endorsement to the effect that the addressee had refused to accept the notice, it shall be deemed to have been served.
- (iii) If the notice is returned with an endorsement indicating that the addressee cannot be found at the address given, the Secretary shall ask the complainant to supply to him the correct address to the member or firm concerned and send a fresh notice to the member or firm at the address so supplied.

(11) The provision relating to a notice shall apply mutatis mutandis to a letter.

### **Procedure in enquiry before the Disciplinary committee**

Applicable to the complaint or information pending before the Council or any inquiry initiated by the Disciplinary Committee or any reference or appeal made to a High Court prior to 17.11.2006.

(1) It shall be the duty of the Secretary to place before the Disciplinary Committee all facts brought to his

knowledge which are relevant for the purpose of any enquiry by the Disciplinary Committee.

(2) The Disciplinary Committee shall have the power to regulate its procedure in such manner as it considers necessary and during the course of enquiry, may examine witnesses on oath and receive evidences on affidavits and any other oral or documentary evidence, exercising its powers as provided in Sub-section (8) of Section 21.

(3) The Disciplinary Committee shall give the complainant and respondent a notice of the meeting at which the case shall be considered by the Committee.

(4) Such complainant and respondent may be allowed to defend themselves before the Disciplinary Committee either in person or through a legal practitioner or any other member of the Institute.

(5) Where, in the course of a disciplinary enquiry, a change occurs in the composition of the Disciplinary Committee, unless any of the parties to such enquiry makes a demand within fifteen days of receipt of a notice of a meeting of such Disciplinary Committee, that the enquiry be made de novo report of the Disciplinary Committee shall be called in question on the ground that any member of the Disciplinary Committee did not possess sufficient knowledge of the facts relating to such inquiry.

(6) The Disciplinary Committee shall after investigation report the result of its enquiry to the Council for its consideration

### **Procedure in a hearing before the Council**

(1) The Council shall consider the report of the Disciplinary Committee and if in its opinion, a further enquiry is necessary, may cause such further enquiry to be made and a further report submitted by the Disciplinary Committee.

(2) After considering such report or further report of the Disciplinary Committee, as the case may be, where the Council finds that the respondent is not guilty of any professional or other misconduct, it shall record its findings accordingly and direct that the proceedings shall be filed or the complaint shall be dismissed as the case may be.

(3) After considering such report or further report of the Disciplinary Committee, as the case may be, where the Council finds that the respondent has been guilty of a professional or other misconduct, it shall record its findings accordingly and shall proceed in the manner as laid down in the succeeding sub-regulations.

(4) Where the finding is that the member of the Institute has been guilty of a professional or other misconduct, the Council shall afford to the member an opportunity of being heard before orders are passed against him in the case. The Council after hearing the respondent, if he appears in person or after considering the representations, if any, made by him, pass such orders as it may think fit, as provided under Subsection (4) of Section 21.

(5) The orders passed by the Council shall be communicated to the complainant and the respondent.

**GUIDELINES FOR ADVERTISEMENT BY COMPANY SECRETARY IN PRACTICE**

**THE INSTITUTE OF COMPANY SECRETARIES OF INDIA**

*(Constituted under the Company Secretaries Act, 1980)*

**ICSI Guideline No. 4 of December, 2007**

*In exercise of the powers conferred by Clause (1) of Part II of the Second Schedule to the Company Secretaries Act, 1980 (56 of 1980), as amended by the Company Secretaries (Amendment) Act, 2006, the Council of the Institute of Company Secretaries of India hereby issues the following guidelines:-*

**1. Introduction**

- 1.1 The Institute of Company Secretaries of India, (the Institute) constituted under the Company Secretaries Act, 1980 (the Act) is a statutory body to develop and regulate the profession of company secretaries in India. Members of the Institute who hold the Certificate of Practice issued by it are authorised to practise the profession of Company Secretaries and these members are known as Company Secretaries in Practice.
- 1.2 The areas in which the Company Secretaries in Practice can and do render their services and the names, addresses and other particulars of Company Secretaries in Practice are displayed on the website of the Institute.
- 1.3 Members of the Institute are required under the Act to maintain high standards of professional conduct.
- 1.4 Part I of the First schedule of the Company Secretaries Act, 1980, enumerates professional misconduct in relation to a member in practice and inter-alia includes if such a member:

(6) solicits clients or professional work, either directly or indirectly, by circular, advertisement, personal communication or interview or by any other means:

Provided that nothing herein contained shall be construed as preventing or prohibiting—

- (i) any company secretary from applying or requesting for or inviting or securing professional work from another Company Secretary in Practice; or
- (ii) a member from responding to tenders or enquiries issued by various users of professional services or organizations from time to time and securing professional work as a consequence;

(7) advertises his professional attainments or services, or uses any designation or expressions other than Company Secretary on professional documents, visiting cards, letterheads or sign boards, unless it be a degree of a University established by law in India or recognized by the Central Government or a title indicating membership of the Institute of Company Secretaries of India or of any other institution that has been recognized by the Central Government or may be recognized by the Council :

Provided that a member in practice may advertise through a write up setting out

- the services provided by him or his firm and
- particulars of his firm subject to such guidelines as may be issued by the Council;

- 1.5 The Council of the Institute of Company Secretaries of India at its 178th meeting held on 29th December, 2007 approved the following Guidelines for Advertisement by Company Secretary in Practice.
- 1.6 The Guidelines herein, as issued by the Central Council of the Institute on 29<sup>th</sup> December, 2007 deal with the manner in which a Company Secretary in Practice can advertise the services provided by him or his firm and the particulars of his firm through a write-up.
- 1.7 Any non compliance or violation of these Guidelines as may be in force from time to time in any manner whatsoever shall be deemed to be an act of professional misconduct and the concerned member shall be liable to disciplinary proceedings under the Act.

## **2. Key Definitions**

For the purposes of these Guidelines,

- 2.1 The “Act” means the Company Secretaries Act, 1980.
- 2.2 “Institute” means the Institute of Company Secretaries of India.
- 2.3 “Advertisement or advertising” means advertisement or advertising in any mode including written, recorded, displayed communication through print or electronic mode or otherwise including in newspapers, journals, internet, online, websites, banners, letters, circulars issued, circulated or published in accordance with these guidelines.
- 2.4 “Company Secretary in Practice” means a member of the Institute who holds a Certificate of Practice issued to him by the Institute.
- 2.5 “Firm of Company Secretaries” means sole proprietorship concern, the sole proprietor of which is a Company Secretary in Practice or a firm, wherein all partners are Company Secretaries and such firm is approved by the Council.
- 2.6 “write up” includes any writing or display setting out services rendered by a Company Secretary in Practice or firm of company secretaries and any writing or display of the particulars of the Company Secretary in Practice or of firm of company secretaries issued, circulated or published in accordance with these guidelines.

The terms not defined herein have the same meaning as assigned to them in the Company Secretaries Act, 1980 and the rules and regulations made thereunder.

## **3. Prohibition to Advertise**

- 3.1 No Company Secretary or a firm of Company Secretaries is permitted to advertise the services as specified in the Act, rules, regulations framed thereunder except through a write-up as defined in Clause 2.6.

## **4. The Write-up shall be made in compliance with the following:**

### **4.1 Applicability**

These guidelines shall apply to advertisements issued by a Company Secretary in Practice not only in India but would also apply to those circulated, communicated, published, issued or allowed to be issued abroad.

### **4.2 Permitted list of information**

- 4.2.1 Name of Company Secretary, Membership number, Certificate of Practice  
Number and date of issue (for each partner in case of firm)
- 4.2.2 Address and website (if any), telephone, mobile, e-mail, fax number of the member
- 4.2.3 Name of the firm in which the member is a partner
- 4.2.4 Year of Establishment
- 4.2.5 Date and place of Issue of Advertisement
- 4.2.6 Age
- 4.2.7 Gender
- 4.2.8 Additional recognized qualifications
- 4.2.9 Languages spoken by the partner(s)
- 4.2.10 Honours or awards in the field of teaching, research, authorship etc. conferred by nationally accredited institutions
- 4.2.11 Current teaching or research appointments at a university or college of advanced education or professional Institute
- 4.2.12 Name of firm in case of partnership
- 4.2.13 Details of networking through own office or through formal association in other places within & outside India
- 4.2.14 Number, name of employees of the firm and their qualifications and other particulars
- 4.2.15 Business address, telephone numbers (including email, fax and other details) of the firm
- 4.2.16 Office hours and after office hours availability
- 4.2.17 Advertisement about setting up of certified filing centers
- 4.2.18 Frequently Asked Questions (FAQs) in conformity to these guidelines
- 4.2.19 Declaration indicating
  - (a) willingness to accept work, either generally or in particular areas of practice;
  - (b) unwillingness to accept work in particular areas;
  - (c) willingness or unwillingness to accept work directly from clients, either generally or in particular areas of practice.
- 4.2.20 The write-up may display the passport size photograph of the member or partners of the firm of Company Secretaries
- 4.2.21 Fees:
  - (a) Willingness to give written estimates of fees;
  - (b) Methods for determining fees;
  - (c) Mode of Acceptance of Fees.
- 4.2.22 Speed of Service

- (a) willingness to give written estimates concerning completion of particular work;
- (b) maximum time within which specific services will be completed.

4.2.23 Write-up may include the names of clients and services rendered

4.2.24 Particulars of Services

- (i) The write-up to be circulated, distributed, published, issued by or on behalf of Company Secretary in Practice shall set out the professional services rendered or to be rendered by the advertiser.
- (ii) The write-up may explain the nature and usefulness of the professional services rendered by the Company Secretary in Practice.
- (iii) The write-up may include the names of clients and services rendered provided that the Company Secretary in Practice shall maintain record of his having provided such professional services.

4.2.25 In case of advertisement through website :

- (a) A Company Secretary or a firm of Company Secretaries may display photograph of the Company Secretary or partners of the firm of Company Secretaries in Practice.
- (b) While designing and/or hosting the particulars on the website, certain keywords should be provided so as to enable the search engine/s to locate the website and these keywords will not be visible or displayed on the website. Any one of the following key words may be used for this purpose. Company Secretary/Company Secretary in Whole-time Practice/Company Secretary in Practice/Practising Company Secretary/Indian Chartered Secretary/Indian Certified Corporate Secretary/Indian CS/Indian Company Secretary/Corporate Advisor / Company Law Consultant/Secretarial Auditor/Secretarial Consultant/Indian Certified Public Secretary/CS/ ACS/FCS/PCS/CSP.  
  
However, the keywords shall not be materially different from the designations used for a Company Secretary.
- (c) The website may provide a hyperlink to the website of ICSI, its Regional Councils and Chapters and other regulatory bodies of the Government, after obtaining necessary permission from the concerned body.
- (d) A Company Secretary in Practice may provide online advice to their clients or other members/ firms of Company Secretaries who specifically request for the same.
- (e) A Company Secretary or a firm of Company Secretaries may disclose the fact that he/she or their firm has been Peer Reviewed. Any such disclosure shall clearly state the period for which the Peer Review has been conducted and in case the member has more than one office or place of practice, then it shall be mentioned that the Peer Review has been done for which branch office.\*

4.2.26 Changes in any of the above particulars.

**4.3 Restrictions**

The write-up shall:

- (i) not be false or misleading ;

\* Inserted by the Council at its 216th Meeting held at New Delhi on June 21-22,2013.

- (ii) not claim superiority over any or all other Company Secretaries in Practice;
- (iii) not be indecent, sensational or otherwise of such nature as to be likely to bring the profession into disrepute;
- (iv) not contain testimonials or endorsements concerning the Company Secretary in Practice.
- (v) not refer the Company Secretaries in practice in terms such as “specialists” or “experts”.
- (vi) In case of advertisement through website:
  - (a) A Company Secretary in Practice or a firm of Company Secretaries shall ensure that no information contained in the website is circulated to other websites/email accounts etc. through e-mail or otherwise without the same having been specifically requested for.
  - (b) A Company Secretary in Practice or a firm of Company Secretaries shall not use logo(s) unless otherwise permitted by the Institute.

#### 4.4 Declaration

The Advertiser shall declare that the contents of the advertisement are true to the best of his knowledge and belief and are in conformity with these Guidelines.

#### 4.5 Disclaimer

The Advertiser shall also include the following Statement of Responsibility and Disclaimer in the Advertisement :

**Disclaimer:** The contents or claims in the Advertisement issued by the advertiser are the sole and exclusive responsibility of the Advertiser. The Institute of Company Secretaries of India does not own any responsibility whatsoever for such contents or claims by the Advertiser.

#### 5. Responsibility for the observance of these Guidelines

5.1 The responsibility for the observance of these guidelines lies with members who commission, create, place or publish any advertisement or assist in the creation or publishing of any advertisement covered under these guidelines. Members are expected not to commission, create, place or publish any advertisement which is in contravention of these Guidelines. This is a self-imposed discipline required to be observed by all those involved in the commissioning, creation, placement or publishing of advertisements.

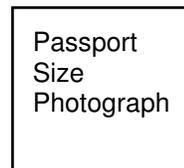
#### 6. Effective Date

6.1 These guidelines become effective from 1st January, 2008 and consequently the existing Guidelines for Display of Particulars on Website by Company Secretaries in Practice stand repealed.

#### Annexure

##### MODEL ADVERTISEMENT

- (i) Name of Company Secretary
- (ii) Membership number
- (iii) Certificate of Practice number and date of issue



- (iv) Website (if any)
- (v) Name of the sole proprietary concern under which the member is practicing/Name of the partnership in which the member is a partner
- (vi) Age
- (vii) Gender
- (viii) Languages spoken
- (ix) Number, name of employees and their qualifications and other particulars
- (x) Business address telephone numbers (including email, fax and other details)
- (xi) Office hours and after office hours availability
- (xii) Additional recognized qualifications
- (xiii) Current teaching or research appointments at a university or college of advanced education or professional Institute
- (xiv) Honours or awards conferred
- (xv) Frequently Asked Questions (FAQs)
- (xvi) Declaration indicating:
  - willingness to accept work, either generally or in particular areas of practice;
  - unwillingness to accept work in particular areas;
  - willingness or unwillingness to accept work directly from clients, either generally or in particular areas of practice.
- (xvii) Fees:
  - Mode of Acceptance of Fees
  - Methods for determining fees
  - Willingness to give written estimates of fees
- (xviii) Speed of Service:
  - willingness to give written estimates concerning completion of particular work;
  - maximum time within which specific services will be completed.
- (xix) Particulars of Services:
- (xx) Declaration : I ..... declare that the contents of the advertisement are true to the best of my knowledge and belief and are in conformity with these Guidelines.
- (xxi) Disclaimer : The contents or claims in the Advertisement issued by the advertiser are the sole and exclusive responsibility of the Advertiser. The Institute of Company Secretaries of India does not own any responsibility whatsoever for such contents or claims by the Advertiser.
- (xxii) Date and Place of Issue of Advertisement: .....

## LESSON ROUND UP

- The members of the Institute shall be divided into two classes designated respectively as Associates and Fellows.
- The member of the Institute is subject to the Disciplinary mechanism provided for under Chapter V of the Company Secretaries Act, 1980 (the Act).
- Professional misconduct in relation to members of the Institute is broadly structured under Schedule I and Schedule II of the Act.
- On receipt of any information or complaint along with the prescribed fee, the Director (Discipline) shall arrive at a prima facie opinion on the occurrence of the alleged misconduct.
- Where the Director (Discipline) is of the opinion that a member is guilty of any professional or other misconduct mentioned in the First Schedule, the matter shall be placed before the Board of Discipline.
- Where the Director (Discipline) is of the opinion that a member is guilty of any professional or other misconduct mentioned in the Second Schedule or in both the Schedules, the matter shall be placed the Disciplinary Committee.

## GLOSSARY

Associate Member	The person whose name is entered in the register of members of the Institute of Company Secretaries of India shall be deemed to be the Associate Members
Fellow Member	A person, being an Associate who has been in continuous practice in India as a Company Secretary for at least five years and a person who has been an Associate for a continuous period of not less than five years and who possesses such qualifications or practical experience as the Council may prescribe with a view to ensuring that he has experience equivalent to the experience normally acquired as a result of continuous practice for a period of five years as a Company Secretary shall, on payment of fees, be entered in the Register as a Fellow. Such person shall be a Fellow member.

## SELF TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

1. What is the Disciplinary Mechanism in case of misconduct of clause 5 of Part I of First Schedule of Company Secretaries Act, 1980?
2. Write short notes on:
  - (a) Board of Discipline
  - (b) Fellow member
  - (c) Appellate authority

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# Lesson 22

## Secretarial Standards Board

### LESSON OUTLINE

- Function of SSB of ICSI
- Need and Scope of Secretarial Standards
- Process of making of Secretarial Standards
- Lesson Round up
- Self-Test Questions

### LEARNING OBJECTIVES

A company is mandatorily required to comply with the Secretarial Standards under Section 118(10). A company secretary in whole time employment is required to guide the Board of Directors of the company on the compliances of the secretarial standards.

Further, it is also a function of company secretary under Section 205 that the Company complies with the applicable secretarial standards.

On the other hand a practicing company secretary while conducting secretarial audit has to ensure the compliance.

This chapter shall give the readers a broader perspective of how the standards are formulated and developed.

## INTRODUCTION

The Institute of Company Secretaries of India (ICSI), recognising the need for integration, harmonisation and standardisation of diverse secretarial practices prevalent in the corporate sector, has constituted the Secretarial Standards Board (SSB) with the objective of formulating Secretarial Standards.

SSB was constituted in the year 2000. The formulation of SSB is a unique and pioneering step by the Institute of Company Secretaries of India (ICSI) since there was no such Board or body throughout the world. The purpose of constituting this Board was for long-term benefits for the growth and enhanced visibility of the profession and setting up international benchmarks.

The SSB comprises of representatives from major industry associations viz, The Federation of Indian Chambers of Commerce and Industry (FICCI), Confederation of Indian Industry (CII), The Associated Chambers of Commerce & Industry of India (ASSOCHAM), PHD Chamber of Commerce and Industry, representatives of regulatory authorities, such as the Ministry of Corporate Affairs, Securities & Exchange Board of India, Reserve Bank of India, Bombay Stock Exchange, National Stock Exchange of India Ltd. and the sister professional bodies viz. the Institute of Chartered Accountants of India and the Institute of Cost Accountants of India and eminent members of the Institute of Company Secretaries of India in employment and in practice.

The scope of SSB is to identify the areas in which Secretarial Standards need to be issued by the Council of ICSI and to formulate such Standards. SSB also clarify issues, if any, arising out of such Standards and issue guidance notes for the benefit of members of ICSI, corporates and other stakeholders.

## Functions of the Secretarial Standards Board

The main functions of SSB are:

- (i) Formulating Secretarial Standards;
- (ii) Clarifying issues arising out of the Secretarial Standards;
- (iii) Issuing Guidance Notes; and
- (iv) Reviewing and updating the Secretarial Standards / Guidance Notes at periodic intervals.

## Need of Secretarial Standards

Companies follow diverse secretarial practices and, therefore, there is a need to integrate, harmonise and standardise such practices so as to promote uniformity and consistency.

SSB formulates Secretarial Standards taking into consideration the applicable laws, business environment, practical applicability and the best secretarial practices prevalent.

Secretarial Standards are developed in a transparent manner after extensive deliberations, analysis, research and after considering the views of corporates, regulators and the public at large.

## Scope of Secretarial Standards

Secretarial Standards do not seek to substitute or supplant any existing laws or rules and regulations framed thereunder but, in fact, seek to supplement such laws, rules and regulations.

Secretarial Standards are issued in conformity with the provisions of the applicable laws. However, if, due to subsequent changes in the law, a particular Standard or any part thereof becomes inconsistent with such law, the provisions of the said law shall prevail.

## Process of making Secretarial Standards

The following procedure is adopted for formulating and issuing Secretarial Standards:

- (i) SSB, in consultation with the Council, determine the areas in which Secretarial Standards need to be formulated and the priority thereof.
- (ii) In the preparation of Secretarial Standards, SSB may constitute Working Groups to formulate preliminary drafts of the proposed Standards.
- (iii) The preliminary draft of the Secretarial Standard prepared by the Working Group shall be circulated amongst the members of SSB for discussion and shall be modified appropriately, if so required.
- (iv) The preliminary draft will then be circulated to the members of the Central Council, as well as to Regional Councils/ Chapters of ICSI, various professional bodies, Industry Association/Chambers of Commerce, regulatory authorities such as the Ministry of Corporate Affairs, the Securities and Exchange Board of India, Reserve Bank of India, Department of Public Enterprises and to such other bodies/organisations as may be decided by SSB, for ascertaining their views, specifying a time-frame within which such views, comments and suggestions are to be received.
- (v) On the basis of suggestions received on the preliminary draft, an Exposure Draft of proposed Secretarial Standard will be prepared and published in the “Chartered Secretary”, the journal of ICSI, and placed on the Website of ICSI for inviting suggestions/comments from public at large.

The exposure draft will also be circulated to:

- (a) All Council Members
  - (b) Regional Council/Chapters
  - (c) Professional Bodies (ICAI/ICoAI).
  - (d) Chambers of Commerce/Industry Associations
  - (e) MCA/SEBI/RBI and such other bodies/organisations as may be decided by SSB
  - (f) All members of the Institute through bulk e-mail/website link etc.
- (vi) After taking into consideration the comments received, the draft of the proposed Secretarial Standard will be finalised by SSB and submitted to the Council of ICSI.
  - (vii) The Council will consider the final draft of the proposed Secretarial Standard and finalise the same in consultation with SSB. The Secretarial Standard on the relevant subject will then be issued under the authority of the Council.

Section 118 (10) of Companies Act, 2013 provides that 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.

Hence ICSI has so far issued the following Standards:

- Secretarial Standards on Meetings of Board of Directors(SS-1)
- Secretarial Standards on General Meetings(SS-2)
- Secretarial Standard on Dividend (SS-3)( adoption of the same is voluntary)



# Lesson 23

## MEGA FIRMS

### LESSON OUTLINE

- Adoption of Mode of Practice
- Applicable Rules, Regulations and Guidelines for PCS or Firm of PCS
- What is Multidisciplinary/Mega firm?
- Pre-requisites of Mega Firm
- Benefits of Mega Firm
- Risks of Mega Firm
- Process of Constitution
- Management of Firms
- Revenue Sharing Models
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

The first exclusive recognition for Practising Company Secretaries (PCSs) came in 1988 in the form of Annual Return Certification for listed companies. Thereafter in last about twenty five years, CS profession obtained many more recognitions.

Firms and practices are not what they used to be. In fact, they have had to adapt to the changes in the corporate world. Every business requires multifarious professional services and it is common knowledge that a business entity invariably approaches multiple agencies for different services, for which they are qualified or considered proficient. Mega firm or a Multi Disciplinary Firm is intended to build the capacity of any professional firm in terms of ability to render multifarious services. Many clients need services such as accounting, auditing and assurance, secretarial, legal, systems controls and audit, valuation, risk assessment and management, so on and so forth.

This chapter gives an overview of having a multidisciplinary / mega firm its scope, benefits and expertise required.

## INTRODUCTION

In a rapidly changing economy, industrial environment and emergence of the need for corporate governance and ethical business practices of voluntary disclosures, role of a practicing company secretary has also changed substantially over last three decades. Company Secretary in Practice has become a crucial player. The stakeholders are becoming vigilant towards the compliances. It is the prime duty of a professional to meet the expectations of the stakeholders at any given point of time.

The Company Secretaries profession has also obtained new dimensions from being conscience keeper to compliance officer, governance professionals, Advisor, strategist for the growth of corporate. Presently the Company Secretaries profession has achieved a significant position in corporate world to step in a leadership role in guiding the corporates for the success and sustainable growth. The Company Secretaries to assume the leadership position with new role, values and approach. It is now imperative for Company Secretaries to act as catalyst for change and, help decision makers in setting the direction of corporate to achieve excellence.

The Companies Act, 2013, so also Insolvency and Bankruptcy Code 2016, has considerably enhanced the role and responsibilities of company secretaries both in employment and in practice. Company secretary is a key managerial person in a company, responsible to ensure the effective and efficient administration of the company and certifying the company's compliance with the provision of the Act.

This is challenging.

## ADOPTION OF MODE OF PRACTICE

To meet the expectation and to survive competition, moulding, changing and upgrading oneself is a must. For stability as well as growth one needs to join hands with professional fraternity and have synergy. Synergy is possible by way of establishing big firms, putting minds, hands and intelligence together. Such flow of synergies would enable the Practicing community as a whole to grow big, achieve higher goals and maintain highest degree of quality which otherwise one would not be able to achieve as a sole proprietor.

Before we talk about big firms let us understand the features of being in practice.

Decision whether to join a company as whole time secretary or to start one's own practice itself is a tough decision to make. Features (Limitations) of a single practicing professional are enumerated as under:

1. Irregular Cash flows;
2. Capital investment. (Fixed as well as Working);
3. No limit on working hours , clients expect PCS to be available 24\*7;
4. No work no pay— ---is a rule;
5. Need to continuously update oneself;
6. No body to protect your mistakes, PCS is directly exposed to all kinds of acts of omission & commission;
7. Has to create his own infrastructure – right from acquiring office premises, PCs, Computer networking, Office furniture, hardware, software, its maintenance;
8. Has to have staff, their appointments, promotions, incentives, salaries, HR management;
9. Cannot directly or indirectly solicit clients.

10. No pension, no provident fund, no gratuity, no perquisites, no fringe benefits;
11. May not afford air travel or even train travel in first class, on the first day;
12. No paid leave, no leave travel concession, No casual leave, No sick leave;
13. Encroachment on family time.

Of course there are lots of positive aspects of being in practice the most important being, *Quid Pro Co* i.e. more you work more you get. PCS is his own master, he generates employment, has flexibility of working hours, has reasonable assurance of sustained earnings in long run, no fear of losing employment at advanced age.

Lets now discuss certain features of the two forms of enterprise a practicing professional may choose i.e. Partnership Firm (including LLP) & Sole Proprietor:

No.	Firm with several partners	Proprietor
1	Various avenues of practice, un-trodden areas can be explored.	Likely to get restricted to the "Routine" procedural matters.
2	Knowledge management becomes easier as partners can help each other in their respective areas of expertise.	Knowledge management becomes difficult being the only person. No other person is available to support /guide. Keeping track of latest developments, case law, notifications, circulars becomes a daunting task.
3	Inherent risks associated with the practice are shared with others.	Risk bearing has to be shouldered by one person. No one available to share the risks.
4	Several partners can render multi-dimensional services.	Difficult for a single individual to provide multiple services say under GST, Income Taxes, FEMA along with Company Law.
5	Partners inter-se should have full faith & trust	Not relevant since it is 'one man show'
6.	Frequencies of the partners should match. It is desirable that their family background, culture, political thinking should be more or less similar.	Not relevant since it is 'one man show'.
7.	Freedom of decision making gets restricted.	Not required Proprietor is his own master. No need to consult others
8.	All partners should be mentally prepared to share revenues.	Not required Proprietor is his own master. No need to share revenues.
9.	One is responsible to the wrongs & liabilities of his partners	Not relevant since it is 'one man show'

10.	There should not be communication gap inter-se	Not relevant since it is 'one man show'
11	One of the partners can afford to become Resolution professional (RP ) / valuer .	It is very difficult for a proprietor to act as RP / Valuer while simultaneously handling is routine Practice as PCS.

### Applicable Rules, Regulations and Guidelines for PCS or Firm of PCS

Whether a Company Secretary in Practice or a Firm of Company Secretaries they are subject to Rules, Regulations and Guidelines enumerated as under:

- (i) Company Secretaries Regulations, 1982
- (ii) Schedule I and III of Company Secretaries Act, 1980 in relation to Professional misconduct
- (iii) Guidelines for requirement of maintenance of a register of attestation certification services rendered by practising company secretary/firm of practising company secretaries
- (iv) Guidelines for issuing compliance certificate and signing of annual return
- (v) Guidelines framed by the council relating to approval of proprietorship concern/firm's name under regulation 169 of the company secretaries Regulations, 1982
- (vi) Guidelines for advertisement by Company Secretary in Practice
- (vii) Guidelines for compulsory attendance of Professional development programmes by the members
- (viii) Mechanism for maintenance of attendance records of members at professional development programmes and issuance of Certificates for programme credit hours (PCH)
- (ix) Guidelines for peer review of attestation services by Practising Company Secretaries
- (x) Guidelines for professional dress of Company Secretaries
- (xi) Guidelines for setting up and Conversion of Firms of PCS into LLP.

### WHAT IS MULTIDISCIPLINARY/MEGA FIRM?

Mega Firm can be described as a Partnership firm with more than twenty five partners. A firm which provides core professional service of a particular profession along with the allied and ancillary service with equal competence under one roof is a multidisciplinary firm. For example, company and corporate law is core knowledge for company secretaries, however, they can acquire expertise in any other area like direct-indirect taxation, labour laws, economic laws, finance, accounting, insurance, international business and IPRs and they may be in position to provide single window business solutions.

Regulation 168B of Company Secretaries Regulations, 1982 determines the membership of professional body for partnership, accordingly For the purposes of entering into partnership under clauses (4) and (5) of Part I of the First Schedule to the Act, a person shall be a member of any of the following professional bodies, namely:-

- The Institute of Chartered Accountants of India established under the Chartered Accountants Act, 1949 (No. 38 of 1949);
- The Institute of Cost and Works Accountants of India established under the Cost and Works Accountants Act, 1959 (No.23 of 1959);

- Bar Council of India established under the Advocates Act, 1961 (No. 25 of 1961);
- The Institute of Engineers or Engineering from a University established by law or an institution recognized by law;
- The Indian Institute of Architects established under the Architects Act, 1972 (No. 20 of 1972);
- The Institute of Actuaries of India established, under the Actuaries Act, 2006 (No. 35 of 2006);
- Professional bodies or institutions outside India whose qualifications relating to Company Secretary recognized by the Council under Sub-section (2) of Section 38 of the Act

This actually introduces the concept of multi disciplinary firms or mega firms.

### Why such firms?

Keeping in view of the present needs of the corporate and multi dimensional growth of CS profession especially in the areas of practicing in the areas of Corporate Laws, Labour laws, RBI/ FEMA, acting as Secretarial Audit, Resolution Professional Insolvency Bankruptcy Code, GST Practitioner there is a need to structure and build the Multidisciplinary(MDF)/mega firms. There is a huge demand and scope for a multifunctional firm, where several services are provided under one roof. Clients always have a comfort level in dealing with such firms. They are assured of timely and quality service since even if one of the Partners is not available for consultancy they can bank on the others.

Unless there are MDF/Mega firms, it may not be possible to cater to the bigger assignments.

### PRE REQUISITES

MDF is a joint or collaborative venture amongst independent individuals. Therefore, every one wishing to join hands should understand that:

1. All minds should work together and in unison;
2. Say go to ego;
3. Mutual faith and respect lays strong foundation;
4. Unanimity shall be the rule on important policy decisions;
5. Financial discipline is a must;
6. Founder partners shall be given equal status;
7. Income of the firm shall be distributed at short regular intervals;
8. One shall not put undue influence on the others or show that he is king pin of the association.

Even the small crack in the above stated pre requisites ruin the things.

### BENEFITS

The nature of a multidisciplinary firm fosters collaboration. The common office space, with professionals working in close proximity to one another, provides each professional with a strong set of resources in the firm. In addition, this spirit of working together creates greater opportunity for collaboration so the total needs of the client are best met.

- Working in a team environment: The concept of MDF will have an opportunity to work with team members who share interests, expertise, ideas, and work ethically.

- Exposure to various and different works: Every client has different expectations, needs, audience, products and services, so consultants get to oversee projects of all kinds. In MDF being more than two partners having different experience in different fields the apprentice and employee will have an exposure to various and different works. With each partners specialized knowledge the MDF may venture into new areas of practice.
- Cost effective: the With large investment budgets, the MDF have not only create state-of-the-art training facilities, they also may have much more developed infrastructure, processes and tools which can make your life less stressful when trying to sell or deliver a project. The overheads and the risks get distributed amongst the partners.
- Exceptional training and on-boarding: MDF provides an opportunity to have a good training facilities whether on job training or off job training to get things started off on the right foot. The goal of on job training or off job training is to set you up for success, so during this training you can expect to receive the resources, knowledge, and tools to do so.
- Continuous learning: The partners of MDF having multi dimensional experience they can impart continuous training by adapting to new trends in the Profession. The great thing about staying on your toes is that clients appreciate it because you'll be able to develop relevant and successful ideas. Though it might sound overwhelming to always be on top of news and trends, it will eventually become habit – and the results are worth it!
- Big growth opportunities: With the right work ethic and dedication, MDF can experience professional growth early compared to the other small firms. MDF may attract big multinationals. They get comfort about availability of at least one of the partners, if they are dealing with a firm rather than an individual. Senior partners can concentrate on critical assignments which obviously are more lucrative.
- The MDF have an international or global scope and reach, offer diversified services and can draw from a large pool of consultants, skills and expertise, and hence become a Mega Firm.
- Revenue sharing: By appropriate revenue sharing model a PCS who himself may not have subject expertise can get a share from the assignments of that subject being executed by others.
- Structure & Processes: The structure for execution of works or assignments will be more systematic and the process will be cost effective due to the standard processes and procedure. The hiring and training of people will be more systematic there by productivity of the company will be improved
- Corporate or Industry perception: When considering different professional firms, the corporate client may be preferring to one of the familiar, renowned MDF having brand image. The MDF may appear like a known quantity and can draw from a large pool of partners and associates.
- Reputation & risk-adjusted value: Many of the bigger client's organizations may prefer that "you never go wrong when hiring one of the MDF", since the renowned brands of the MDF are perceived as proxy for high levels of professionalism, quality and reputation. Credibility of the firm and brand gets established in long term.

## RISKS

Lack of understanding and multiplicity of directions to the staff could be disastrous.

1. More cost on infrastructure and technology.
2. Dominance of senior partners over the younger partners.
3. Defining exit route is difficult.

4. Lack of transparency may lead to disputes.
5. If crack develops in mutual faith & trust, very difficult to cure.
5. Communication gap between partners

## PROCESS OF CONSTITUTION

The process of formation of MDF shall be an outcome of conscious and sincere decision and it is essential that the like minded professional should deliberate and take this decision. It shall be ensured that the proposed constituents have expertise in different disciplines. There could be series of meetings before MOU is reached. It is advisable to work under MOU for one year. This works as a cooling period and for better understanding each other such trial period help in getting acclimatised. Mutual faith and understanding is *sine qua non*. Time has to be given to understand the compatibility of the individuals to each other. Once the initial bridge is successfully crossed then formal partnership may be constituted on the agreed terms. It will be in the long term interest of the MDF to have all the founder partners on equal footing. Their intellectual level shall be at par. During the reasonable period individual practice existing if any, shall be introduced in the firm. When it is proposed to add new partner, apart from settling commercial terms, it is suggested that the MDF shall enter into MOU effective at least for one year with the proposed partner and after understanding each others compatibility he or she may be admitted to the MDF.

## Agreement between partners

Partners must enter into a partnership agreement defining *inter alia* the process of decision making, allocation of duties, responsibilities, delegation of authorities, revenue sharing and exit route.

## Management of Firms

The mega firm requires effective management skills including skills for handling finance, dealing with human resources and day to day administration of the office. The management of a MDF is in itself a major challenge.

### (a) Operational functions

Operational functions are for providing services by the firms, the operational functions requires expertise in the domain areas by each of the partners

### (b) administrative functions

Partners should allocate different administrative functions required for day to day functionality of the firm. For example infrastructure availability- right from acquiring office premises, handling reception, attending to calls, inward-outward, record keeping, PCs, library, computer networking, office furniture, hardware, software, its maintenance, brand building, etc.

### (c) Human resources

The Mega firms over a period of time creates aa large pool of talented people. They need to be offered extremely competitive salaries and benefits, career and learning opportunities. Right from appointment of staff, promotions, incentives, salaries, HR management, require proper knowledge of human resources skills

### (d) Client relationship

Michael R. Caplan, chief operating officer of Goodwin Procter, argues the benefits of a multi-disciplinary, full-

service model in the New York Law Journal: “When law firms treat client relationships as strategic partnerships, flexibility, transparency, and communication are paramount, investment in risk and reward is shared, and all firm resources are leveraged for the client’s benefit. Only then does the relationship grow and prosper.”

*(e)Public Relationship and Brand building:*

Admittedly a PCS firm cannot advertise or solicit clients . The only way to grow is rendering excellent timely and quality service to the client who certainly recommend the name of a good consultants to their peers. There cannot be a marketing department in MDF but there has to be PR department which ensures cordial relations with the existing and probable clients.

## **Revenue Sharing Models**

In the long term success of the MDF the revenue sharing model has to be designed to suit the given situation. Partners may adopt simple revenue sharing model to share profits and losses equally. In this model it is assumed that each one is bringing equal business and generating equal revenue. However, in reality if it doesn’t happen it may give rise to sense of discomfort against the person who is continuously showing less contribution but at the same time getting equal share of profits.

Therefore, it is essential to device “performance, contribution and efficiency based” revenue sharing model. Assume a situation where A,B,C,D and E are the partners expert in different disciplines. The revenue sharing model could be the following:

1. Partner bringing new client shall be given referral or induction share, say, @ 15% of the fees settled and received; it can be for the first year or for given number of years;
2. Certain percentage of fees, say 15% shall be retained in business in common pool for meeting expenses;
3. 70% of the fees shall be given to the partner or partners who actually work on the assignment (assignment share). When more than one partners are involved in an assignment their share can be determined based on respective role;
4. At the year end after meeting expenses resultant profit shall be shared in proportion of contribution of individual in the gross earnings/ net profit of the firm.
5. Internally, different verticals can be created and surplus generated by each one can be assessed as an independent cost centre.

This model motivates each partner to bring more and more business into the firm and also to work for maximization of his share and wealth of the firm.

There could be more tailor made revenue sharing models, however, the model based on performance, contribution and efficiency is likely to work better.

## **Conclusion**

One stop or single window solutions or services always attract clients or customers. We can witness that conventional shops are being replaced by big shopping malls. In the same manner there is need for corporate and business sector to have “service malls”. It always works better for a business enterprise to have handy team of consultants, both from cost and management point of view. It is most likely that MDF giving professional advice considers all angles and dimensions rather than an advice only from one point of view. Well considered advice by MDF can add value to their clients. Off late, business enterprises have

become professionally shroud and they always like to have a professional firm who is willing to invest in improving their knowledge of the industries they serve. MDF is the right platform that caters to the requirement of the business enterprises. With specialized partner, “knowledge management” becomes easier and less costlier.

MDF is a step towards mega firm. It is paradigm shift from traditional approach of 10X10 offices to a global office. MDF will put the professionals in general and company secretaries in particular on fast track. Large firms will still become larger and one day the global business enterprise will call them a “Mega Firm”.

## **ANNEXURE I**

### **Frequently Asked Questions**

1. Can there be a Partnership firm in between CA, CS, CWA, Advocate?

CA/CWA may become partners of PCS only for non attestation services i.e. only for the purposes as contemplated by clause nos. 2, 3, 4 & 5 of the First Schedule and CA / CWA cannot become full fledged partners as contemplated by Clause 1 of Part I of the First Schedule. That is to say a PCS even if he is allowed to be a partner of a Chartered Accountant, will not be able to sign the Auditors report on behalf of the multidisciplinary firm. (See Regulation 168 A & B of Company Secretaries Regulations, 1982, discussed in earlier chapter)

2. How many Partners a PCS Partnership Firm can have ?

According to section 464(1) of the Companies Act,2013, no association or partnership consisting of more than such number of persons as may be prescribed shall be formed for the purpose of carrying on any business that has for its object the acquisition of gain by the association or partnership or by the individual members thereof, unless it is registered as a company under this Act or is formed under any other law for the time being in force: Provided that the number of persons which may be prescribed under this sub-section shall not exceed one hundred. Further, the Companies (Miscellaneous) Rules, 2014, provides that no association or partnership shall be formed, consisting of more than 50 persons for the purpose of carrying on any business that has for its objects the acquisition of gain by the association or partnership or by individual members thereof, unless it is registered as a company under the Act or is formed under any other law for the time being in force.

3. Can there be a PCS LLP in between CA, CS, CWA, Advocate?

Yes, there can be a PCS LLP in between CA, CS, CWA, Advocate. (See Regulation 168 A & B of Company Secretaries Regulations, 1982, discussed in earlier chapter)

4. How many Partners LLP of Practicing professional can have ?

The minimum number of members of LLP under LLP Act, 2008 is two, there is no restriction on a maximum number of members.

5. Are there any restrictions on sharing fees with members/ non-members of ICSI ?

A Company Secretary in Practice can partake of his profits with other members of the Institute and with members of any other professional bodies specified in this regard or with such other persons having such qualifications as may be prescribed. A Company Secretary in Practice as recipient can enter into profit sharing arrangement with a member of the Institute and/or with a member of such other professional body or other person having qualifications. (See clause 3 of Part I of the First Schedule to the Companies Secretaries Act, 1982).

6. Can MEGA firm charge fees to the clients based on the result of the matter/ success of the litigation?

Fees shall be charged for the professional work done

7. Can a Mega Firm have branches within / outside India? What regulations guide operations of such Branch office?

As per Section 37(1) of the Company Secretaries Act, 1980 where a Company Secretary in Practice or a firm of such Company Secretaries has more than one office in India, each one of such offices must be in the separate charge of a member of the Institute.

Applications for opening of Branch Office without a member in the separate charge at places where there are few or no Company Secretaries in Practice are decided by the Council on the merits of each case subject to the following general conditions:

The branch office shall be an independent office and not in the office of some other professional.

One of the partners of the firm shall attend the branch office atleast 100 days in a financial year. However, if a candidate who has passed Intermediate examination of the Institute and also completed Management/Apprenticeship Training or has passed the Final Examination of the Institute is posted at the said branch office, one of the partners of the firm shall attend the branch office atleast 60 days in the financial year.

The approval shall be valid for a period of two years within which a member must be appointed in the separate charge of the branch office.

Section 37(2) requires every Company Secretary in Practice or firm of such Company Secretaries maintaining more than one office to send to the Council a list of offices and the persons in charge thereof and also to intimate any change therein. Regulation 163 of the Company Secretaries Regulations, 1982, requires the changes to be intimated to the Council within one month of such change(s).

## LESSON ROUND-UP

- PCS is his own master, he generates employment, has flexibility of working hours, has reasonable assurance of sustained earnings in long run, no fear of losing employment at advanced age.
- The process of formation of MDF shall be an outcome of conscious and sincere decision and it is essential that the like minded professional should deliberate and take this decision.
- Partners must enter into a partnership agreement defining *inter alia* the process of decision making, allocation of duties, responsibilities, delegation of authorities, revenue sharing and exit route.
- The mega firm requires effective management skills including skills for handling finance, dealing with human resources and day to day administration of the office.
- In a MDF Partners may adopt simple revenue sharing model to share profits and losses equally.





EXECUTIVE PROGRAMME  
COMPANY LAW

**EP-CL**

TEST PAPER

**A Guide to CS Students**

To enable the students in achieving their goal to become successful professionals, Institute has prepared a booklet 'A Guide to CS Students' providing the subject specific guidance on different papers and subjects contained in the ICSI curriculum. The booklet is available on ICSI website and students may download from <http://www.icsi.edu/Portals/0/AGUIDETOCSSSTUDENTS.pdf>

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In the event of any misconduct by a registered student or a candidate enrolled for any examination conducted by the Institute, the Council or the Committee concerned may suo motu or on receipt of a complaint, if it is satisfied that, the misconduct is proved after such investigation as it may deem necessary and after giving such student or candidate an opportunity to state his case, suspend or debar the person from appearing in any one or more examinations, cancel his examination result, or studentship registration, or debar him from future registration as a student, as the case may be.

Explanation - Misconduct for the purpose of this regulation shall mean and include behaviour in a disorderly manner in relation to the Institute or in or near an Examination premises/centre, breach of any regulation, condition, guideline or direction laid down by the Institute, malpractices with regard to postal or oral tuition or resorting to or attempting to resort to unfair means in connection with the writing of any examination conducted by the Institute".

EXECUTIVE PROGRAMME  
**COMPANY LAW**

**TEST PAPER**

*(This Test Paper is for recapitulate and practice for the student. Student need not submit responses/Answers to this Test Paper)*

*Time Allowed: 3 hours*

*Maximum Marks: 100*

*Total number of questions: 6*

(All references to the sections relate to Companies Act 2013, unless stated otherwise)

**PART I (50 marks)**  
**(Company Law, Principles & Concepts)**

1. (i) The name of X is found entered in the register of a company. But X contends that he is not a member of the company. The company maintains that X had orally agreed to become a member and hence his name was entered in the register and so he is a member. Is the contention of the company valid? *(4 marks)*
- (ii) RB Arora & Co. a proprietary firm of Rahulbajaj, a Chartered Accountant in practice, has been appointed as the statutory auditor of ABCpvt.ltd. Subsequently, it came to light Mrs. Rahul has been holding less than 1% of the shares of that company. Comment on the appointment of the statutory auditor? *(4 marks)*
- (iii) Issuance of duplicate share certificate can be delegated to the committee. Comment. *(4 marks)*
- (iv) What is the role of Debenture Trustee? *(4 marks)*
- (v) Is section 135 relating to Corporate Social Responsibility applicable to OPCs? Also explain the tax benefits which can be availed under CSR? *(4 marks)*
2. (i) Jagsir is the elder son of Raj? Raj was holding 5000 equity shares of Dreams Limited and died. As the Company Secretary of the company, how will you guide Jagsir to claim the shares of Raj? He has one brother, 2 sisters and mother. Raj had not made any nomination? *(5marks)*
- (ii) Mr. 'A' a press reporter by profession, holding merely 1% shares of the company, wishes to inspect the Register of members of the company. Company has declined such demand taking the base that he may use the information for creating some news. Is the contention of the company valid? *(5 marks)*
- (iii) List the disclosures to be made with the board's report under the Companies Act, 2013 under section 134 of the Act? *(5 marks)*
3. (i) Your company, is a public limited company which wishes to make investments in the shares of another company. The total investment exceeds the statutory limit stipulated by the Act. What are the formalities to be complied with in this regard? *(5 marks)*
- (ii) A 100% subsidiary of a public company, having a paid-up share capital of ₹10 crore, is unable to get a qualified Company Secretary; however, the managing director of the subsidiary is a

qualified Company Secretary and a fellow member of the Institute of Company Secretaries of India? Can he be appointed as company secretary of the subsidiary? (5 marks)

(iii) Explain in brief the procedure of issue of bonus shares? (5 marks)

**Part – II (40 Marks)**

**(Company administration and meetings- Law and Practices)**

4. (i) When is a person disqualified for appointment as a director of the company? (5 marks)
- (ii) Explain Special Resolution? Is there any difference between Special Notice and special resolution? If yes, then explain in brief? (5 marks)
- (iii) Discuss the role of Nomination and Remuneration Committee? (5 marks)
- (iv) Discuss in brief the benefits of virtual board meetings? (5 marks)
- 5 (i) Draft an agenda for the very first meeting of Board of Directors? (5 Marks)
- (ii) Draft the board resolution to appoint Company Secretary under the Companies Act, 2013. (5 Marks)
- (iii) Discuss the concept e-voting? (5 Marks)
- (iv) The Board of Directors of Panja limited had five directors. One of them died and the board appointed Rajat in his place to fill –up the casual vacancy. However, Rajat resigned from the board after two months of his appointment. The Board wishes to appoint Bhagat in place of Rajat to fill-up the casual vacancy. As a Company Secretary of that company, what would you advice to the board and why? (5 Marks)

**PART III (10 marks)**

**(Company Secretary as a profession secretaries)**

6. (a) What are the functions of Secretarial Standards Board? (4marks)
- (b) Who is fellow member of Institute of Company Secretaries of India? How a member becomes FCS from ACS? (3 marks)
- (c) Explain whether Secretarial standards is mandatorily applicable on every company? (3 marks )

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