

Answer to MTP_Final_Syllabus 2012_Jun 2014_Set 2

Paper-13: CORPORATE LAWS AND COMPLIANCE

Time Allowed: 3 hours

Full Marks: 100

Section A (Corporate Laws)

Answer **Question No.1** (carrying 15 marks) which is compulsory and answer **any four** (carrying 15 marks each) from the rest in this section

1. (a) India Bank, a National Bank, acquired on 1st January 2014 a building, fully occupied by various tenants, from Mr. Raj, who is the owner of the building. In discharging of a Term Loan advanced to Mr. Raj, who had mortgaged the said building as security with the said Bank and failed to repay the Loan. The said Bank wants to keep the Building permanently with it and earn the rent from tenants. You are required to state with reference to the provisions of the Banking Regulation Act, 1949 whether the said Bank can do so. [4]

- (b) Nisha Textiles Ltd. is a company engaged in manufacture of fabrics. The Company has investments in shares of other bodies corporate including shares in Nisha Cotton Co. Ltd. and it has also advanced loans to other bodies corporate. The aggregate of all the investments made and loans granted by Nisha Textiles Ltd. exceeds 60% of its paid up share capital and free reserves and also exceeds 100% of its free reserves. In course of its business requirements, Nisha textiles Ltd. has obtained a term loan from Industrial Development Bank of India (a Public Financial Institution within the meaning of section 4A of the companies Act, 1956) and the same is still subsisting. Now the company wants to increase its holding from 70% to 80% of the equity share capital in Nisha Cotton Co. Ltd. by purchase of additional 10% shares from other existing shareholders.

State the legal requirements to be complied with by Nisha Textiles Ltd. under the provisions of the companies Act, 1956 to give effect to the above proposal.

Will your answer be different if Nisha Textiles Ltd. would have defaulted in payment of matured fixed deposits accepted by it from the public? [5]

- (c) M/s Raja Limited was wound up by the court. The official liquidator invited claims from the creditors which stood as under:

Income Tax dues	₹ 11.00 lakhs
Sales Tax dues	₹ 5.00 lakhs
Dues of workers	₹ 25.00 lakhs
Unsecured loans payable to directors	₹ 25.00 lakhs
Trade creditors who supplied raw material	₹ 15.00 lakhs
Secured creditors being the bankers of the company	₹ 75.00 lakhs
Total	₹ 156.00 lakhs

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Official Liquidator could realize only ₹80.00 lakhs by sale of the assets and realization made from company's debtors, which is not sufficient to pay to all the creditors. Please decide the order of priority for payment to creditors explaining the relevant provisions of the Companies Act, 1956. [6]

Answer: 1. (a)

As per section 9, no banking company shall hold any immovable property howsoever acquired, except such as is required for its own use, for any period exceeding 7 years from the acquisition thereof or any extension of such period as in this section provided, and such property shall be disposed of within such period or extended period, as the case may be.

As per Proviso to Section 9, the Reserve Bank may in any particular case extend the aforesaid period of 7 years by such period not exceeding 5 years where it is satisfied that such extension would be in the interests of the depositors of the banking company.

In the given case, India Bank proposes to keep the building for earning rent from tenants, and not for its own use. In view of the provisions of section 9, India Bank of India cannot keep the building permanently with it for the purpose of earning rent from tenants. It shall have to dispose of the Building within 7 years from the date of its acquisition, i.e. on or before 31st December, 2021.

However, if the approval of the Reserve Bank is obtained, it may continue to hold the Building till such extended period as is sanctioned by the Reserve Bank. The Reserve Bank shall not permit the Union Bank to hold the property beyond 31st December, 2026.

Answer: 1. (b)

As per section 372A (8), any loans, investments etc. made by a holding company in its wholly owned subsidiary are outside the preview of Section 372A. However, Nisha Cotton Co. Ltd. is not a wholly owned subsidiary of Nisha Textiles Ltd. and hence investment in Nisha Cotton Co. Ltd. is not covered by the exemption under section 372 (8).

The aggregate of loans and investments already made by Nisha Textiles Ltd. exceeds the two limits of 60% and 100% specified under section 372A. Therefore, the company can make new inter-corporate investments only by passing a special resolution.

The proposed investment can be made as follows:

- (a) A resolution shall be passed at a Board meeting with the consent of all the directors present.
- (b) A special resolution shall be passed in the general meeting. The notice of special resolution must indicate clearly the specific limits, the particulars of the body corporate in which the investment is proposed to be made, the purpose of the investment, specific source of funding and other similar details.
- (c) IDBI is a Public Financial Institution within the meaning of section 4A. Since, the aggregate investments exceed the limit of 60%, prior approval of IDBI shall be obtained.
- (d) The company shall enter the prescribed particulars of the investment in the register maintained for this purpose within 7 days of making the investment.
- (e) The company shall ensure that no default in compliance with section 58A (relating to public deposits) is subsisting.

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If the company has defaulted in repayment of public deposits, the company cannot make any investments even if special resolution and resolution of Board is passed. The investments can be made only after the default has been made good.

Answer: 1. (c)

Section 529A(1) provides that in the winding-up of a company, the following dues shall be paid in priority to all other debts irrespective of anything contained in any other provision of this Act or any other law for the time being in force:

- (a) Workmen's dues; and
- (b) Debts due to secured creditors to the extent such debts rank under clause (c) of the proviso to sub-section (1) of section 529 pari passu with such dues, shall be paid in priority to all other debts.

The debts listed under section 529A shall be paid in full unless the assets are insufficient to meet them, in which case they shall abate in equal proportions.

The order of payment of liabilities adopted by the liquidator shall be as under:

1. Overriding preferential payments under section 529A (i.e., workmen's dues and debts due to secured creditors).
2. Costs and expenses of winding up.
3. Preferential payments under section 530.
4. Creditors secured by a floating charge.
5. Unsecured creditors.

In the present case, ₹80 lakhs have been realised by the sale of all the assets of the company. The amount due to secured creditors is ₹75 lakhs and the workmen's dues are ₹25 lakhs. Overriding preferential payments (workmen's dues and secured creditors) amount to ₹100 lakhs.

Therefore, the workmen's dues and dues payable to secured creditors shall abate in equal proportions, i.e., payments to workmen and secured creditors shall be made in the proportion of amount owed by the company to them (i.e., in the ratio of 75:25). Accordingly, the workers shall be paid ₹20 lakhs and the secured creditors shall be paid ₹ 60 lakhs. No payment shall be made to the Government authorities for income tax dues, sales tax dues, unsecured loans payable to directors or to trade creditors who supplied raw material.

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2. (a) A Public Company has been declaring dividend at the rate of 20% on equity shares during the last 5 years. The company has not made adequate profits during the year ended 31st March, 2013, but it has got adequate reserves which can be utilised for maintaining the rate of dividend at 20%.

Advise the Company as to how it should go about if it wants to declare dividend at the rate of 20% for the year 2012-13.

Would your answer be different if the company utilised only the profits made in the previous years and retained in the profit and loss account for the purpose of payment of dividend at the rate of 20% for the year 2012-13? [5]

- (b) Following is the latest audited Balance Sheet of ABC Ltd.

Capital and liabilities	₹	₹	Assets	₹
Equity Share Capital (10000 shares of 100 each)	10,00,000		Goodwill	1,00,000
Less: Calls unpaid	10,000	9,90,000	Land and Buildings	10,50,000
Preference Share Capital		1,50,000	Plant and machinery	20,25,000
Securities Premium A/c		1,50,000	Equity shares in A Ltd.	1,25,000
Capital Redemption Reserve		2,25,000	Preference shares in B Ltd.	50,000
General Reserve		5,00,000	Debentures in C Ltd.	1,00,000
Profit & Loss A/c		2,20,000	Shares in P Ltd.	2,25,000
Sinking Fund Reserve		1,10,000	Capital in Z & Co.	1,00,000
Dividend Equalisation Reserve		60,000	Current Assets	55,000
Loan from TIIIC		10,00,000		
Deposits from S Ltd.		2,00,000		
Current Liabilities		1,25,000		
Provision for Taxation		1,00,000		
		38,30,000		38,30,000

The following is the additional relevant information:

- (i) Of the equity shares capital, 3,000 shares have been issued as rights shares and 2,000 shares as bonus shares.
- (ii) B Ltd. is subsidiary of ABC Ltd. with 90% shareholding, whereas A Ltd. is wholly owned subsidiary of ABC Ltd.
- (iii) Z & Co. is a partnership firm. The directors seek advice as to whether the following additional investments can be made by a decision taken in a Board Meeting:
 - a. Loan to A Ltd. ₹10,00,000
 - b. Debentures in B Ltd ₹2,25,000
 - c. Purchase of shares of Shree Ltd. in the open market ₹95,000

State reasons.

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- (c) Mr. Ghanshyam goes abroad for four months from 04.11.2013 and an alternate director has been appointed in his place. Therefore, advice as to sending of notice as required under section 286 of the Companies Act, 1956. [2]

Answer: 2. (a)

The fundamental principle with respect to payment of dividend is that dividend is to be paid only out of profits. In other words, the dividend can be paid only out of the following sources:

- (a) Profits of current financial year
- (b) Undistributed profits of previous financial years, i.e., accumulated profits of previous years
- (c) Moneys provided by the Central Government or State Government in pursuance of guarantee given by it.

Payment of dividend out of reserves

Dividend can be declared out of the profits transferred to the reserves only if:

- (a) previous approval of the Central Government is obtained; or
- (b) such payment is made in accordance with such rules as may be prescribed by the Central Government in this behalf, i.e., The Companies (Declaration of Dividend out of Reserves) Rules, 1975, which are detailed hereunder:

In the event of inadequacy or absence of profits in any year, a company may declare dividend out of the accumulated profits earned by it in previous years and transferred by it to the reserves, subject to the following conditions:

- (a) The rate of dividend must not exceed the lower of:
 - (i) average of the rates of dividend declared by the company in immediately preceding 5 financial years; or
 - (ii) 10%.
- (b) The amount to be withdrawn from reserves must not exceed 1/10th of aggregate of paid up capital & free reserves. Further, the amount so withdrawn shall be first utilised to set off the losses incurred in the financial year, and the balance amount can only be utilised for the declaration of dividend.
- (c) The balance of reserves, after such withdrawal, shall not fall below 15% of paid up share capital. In the present case, the company intends to distribute dividend at the rate of 20%. But as per the provisions discussed in point (a) above, the rate of dividend declared cannot exceed 10%, i.e. the rated dividend declared out of reserves can be a maximum of 10%. Thus, the company cannot declare dividend @ 20% out of reserves.

Answer: 2. (b)

Step 1: Calculation of paid up capital and free reserves:

Paid Up Capital: Equity Share Capital	10,00,000
Less: Calls Unpaid	10,000
	9,90,000
Preference Share Capital	1,50,000
Total	11,40,000

NOTE: Preference Share Capital is to be included for calculating paid up capital.

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Free Reserves: Securities Premium	1,50,000
General Reserve	5,00,000
Profit & Loss Account	2,20,000
Dividend Equalisation Reserve	60,000
Total	9,30,000

NOTE: Capital Redemption Reserve and Sinking Profit Reserve are not available for distribution as dividend and therefore shall not be considered for computing free reserves.

Step 2: Calculation of the limits:

- (A) 60% of Paid up Capital and free reserves
= 60% of (11,40,000 + 9,30,000)
= 60% of (20,70,000)
= 12,42,000
- (B) 100% of Free Reserves as computed above ₹9,30,000
- (A) or (B) whichever is higher ₹12,42,000

Step 3: Computation of Value of transactions as per Balance Sheet:

Preference Shares in B Ltd	50,000
Debentures In C Ltd	1,00,000
Shares in P Ltd	2,25,000
	3,75,000

NOTE:

1. Equity Shares in A Ltd is not considered as acquisition of shares by a holding company in its wholly owned subsidiary is exempted from the provisions of 372 A. The shares are not to be considered while computing Limits.
2. As Z & Co., is a partnership firm the capital therein is not considered.

Step 4: Computation of Proposed Investments:

Debentures in B Ltd	2,25,000
Purchase of shares in Shree Ltd	95,000
	3,20,000

- The aggregate of the investments already made ₹ (3,75,000) together with the proposed investments of ₹(3,20,000) amounts to ₹6,95,000.
- This is well within the ceiling limit of ₹12,42,000 computed in step 2 above.
- Therefore there is no requirement as to previous approval by way of special resolution.
- The Board of directors should approve the proposed transactions at a meeting of the board by passing a resolution agreed to by all the directors present at the meeting.
- Previous approval of M/s. TIIC a PFI is not required as:
 - (a) There is no default towards TIIC and
 - (b) The aggregate of the value of the transactions (₹6,95,000) does not exceed 60% paid up capital and free reserves i.e. ₹12,42,000.

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Answer 2. (c)

Notice of every Board meeting shall be given in writing to every director for the time being in India and to every other director at his usual address in India (Section 286).

As can be seen, section 286 does not specifically state that notice to an alternate director shall be served. However, an alternate director is a director in his own right. He is not a proxy or representative of the original director. The grounds of vacation of office also apply to him as these apply to the original director, e.g., an alternate director shall vacate office if he does not attend the Board meetings as contemplated by section 283(1)(g). As such, it is implied that notice to an alternate director is to be given. Thus, notice should be served to both, the alternate director as well as the original director. Notice to Mr. Ghanshyam, who is outside of India, shall be served at his usual address in India.

3. (a) **Divya, a resident in India is likely to inherit an immovable property in USA from her father, who is a resident outside India. Advise Divya about the restrictions, if any, in this regard. Will your answer be different if she is likely to inherit foreign securities? [4]**

(b) **Best Automobiles Limited intends to make a public issue of 2,00,00,000 equity shares of ₹10 each through the 100% book building process indicating a price band.**

You are required to answer the following with reference to the SEBI (Disclosure and Investor Protection) guidelines:

- (i) **What is the price band that can be indicated in the red herring prospectus, if the floor price is proposed to be fixed at ₹300 per equity share?**
- (ii) **What are the restrictions, if the company wants to revise the price band during the bidding period?**
- (iii) **How the shares are to be allocated to different categories of investors like Qualified Institutional Buyers, Retail Individual Investors, etc.? [8]**

(c) **Mr. Nihar holding 3% Shares in Super Ltd., became a Director of this Company on 01.05.2011. The Company prior to his appointment as Director, had commenced transactions with A Ltd. in the next Board Meeting to be held on 10.05.2011, the Board proposes to discuss about price revisions sought for by A Ltd. Briefly explain –**

- (i) **Whether Mr. Nihar should make a disclosure of his interest in A Ltd, assuming that the Company is going to have transactions with A Ltd. on a continuous basis, if yes, when and how? When should it be renewed?**
- (ii) **Can he vote in the price revision resolution in the Board Meeting?**

You are informed that Mr. Nihar holds 1.5% of the Share Capital of A Ltd and that his wife holds another 3% of the Share Capital of A Ltd. [3]

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Answer 3 (a):

Holding of Currency, Security and Property [Sec. 6(4) & 6(5)]:

- (a) A person resident in India may hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India, if such currency, security or property was:
- Acquired, held or owned by such person when he was resident outside India, or
 - Inherited from a person who was resident outside India.
- (b) A person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India, if such currency, security or property was:
- Acquired, held or owned by such person when he was resident in India, or
 - Inherited from a person who was resident in India.

Note: However, Current Income on such assets like rent, dividend, interest etc. have to be repatriated to India within the prescribed time limit as specified in Regulation 5(i) of FEMA (Realisation, Repatriation and Surrender of Foreign Exchange), 2000.

There are no restrictions with regard to inheritance of either immovable property situated outside India or of foreign security, from a person resident outside India. Further, such inheritance does not require approval of RBI. Hence, Divya can hold the immovable property/foreign security, after such inheritance.

Answer 3 (b):

The provisions relating to book building are contained in Part A of Schedule XI to the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009. The relevant Clauses of Schedule XI are discussed below:

As per Sub-Clause (b) of Clause (8), where the issuer decides to opt for price band instead of floor price, the issuer shall also ensure compliance with the following conditions:

- (i) The cap of the price band should not be more than 20%, of the floor of the band; i.e. cap of the price band shall be less than or equal to 120% of the floor of the price band;
- (ii) The price band can be revised during the bidding period in which case the maximum revision on either side shall not exceed 20% i.e. floor of price band can move up or down to the extent of 20% of floor of the price band disclosed in the red herring prospectus and the cap of the revised price band will be fixed in accordance with clause (i) above;
- (iii) Any revision in the price band shall be widely disseminated by informing the stock exchanges, by issuing press release and also indicating the change on the relevant website and the terminals of the syndicate members.
- (iv) In case the price band is revised, the bidding period shall be extended as per provisions of sub-regulation (2) of regulation 46.

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Applying the provisions of the said Clause to the given case:

- (i) The price band that can be indicated in the red herring prospectus shall be ₹300 to ₹360.
- (ii) The price band can be revised during the bidding period. However, the maximum revision on either side shall not exceed 20% of the floor price. Thus, floor of the price band can move up or down to the extent of 20% of the floor price disclosed in the red herring prospectus, and the cap of the price band shall not be more than 20% of the revised floor price. Accordingly, in the given case, the revised price band can be ₹240 to ₹288 on the lower side, or ₹360 to ₹432 on the upper side.
Any revision in the price band shall be widely disseminated by informing the stock exchange, by issuing press release and also indicating the change on the relevant website and terminals of the syndicate members. Also, the bidding period shall be extended for a further period of 3 days, subject to the total bidding period not exceeding 13 days.
- (iii) As per Regulation 43 of Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009, in an issue made through the book building process, the allocation in the net offer to public category shall be made as follows:
 - (a) not less than 35% to retail individual investors;
 - (b) not less than 15% to non-institutional investors;
 - (c) not more than 50% to qualified institutional buyers, 5% of which shall be allocated to mutual funds.

Answer 3 (c):

1. Disclosure of Interest: Mr. Nihar should disclose his interest as required u/s 299.

- The words 'becomes concerned or interested' occurring in the provision denotes a present state of thing.
- In case of a person who was actually concerned or interested in the contract or arrangement, the liability for disclosure arises the moment he accepts office as Director.
- If a Director acquired interest in a running transaction of the Company, he should disclose this fact at the next Board Meeting held after he becomes so interested.

2. Voting at Board Meeting:

- (a) U/s 300, an Interested Director shall not vote on the resolution in respect of the contract in which he is interested.
- (b) However, provisions of Sec. 300 are not applicable if the interest of the Director consists solely of his holding only Qualification Shares, or less than 2% of the Paid-Up Capital in the other Company.
- (c) In the given case, Mr. Nihar holds 1.5% of the Share Capital of A Ltd, and his wife holds another 3% in the Share Capital of A Ltd, and therefore it cannot be said that he is interested only to the extent of less than 2% of the Paid-Up Share Capital of A Ltd.
- (d) Hence, Mr. Nihar should not participate and vote in the Board Meeting to be held on 10.05.2011, in the matter pertaining to A Ltd.

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4. (a) Mr. SOURAV is a director of M/s ASHEEKA Ltd. He has approached M/s Housing Finance Co. Ltd. for the purpose of obtaining a loan of ₹50 lacs to be used for construction of building his residential house. The loan was sanctioned subject to the condition that M/s ASHEEKA Ltd. should provide the guarantee for repayment of loan installments by Mr. SOURAV. Advise Mr. SOURAV. [5]

(b) M/s Ahana Private Limited was incorporated in the year 2001 under the Companies Act, 1956 by 3 brothers, namely, Amit, Anil and Akhlesh. All the three were Promoter-directors named in the Articles of Association and subscribed for 100 shares each in the company through Memorandum of Association. Thereafter, from time to time, further shares were allotted in proportion of one-third to each of them and in due course, the company started earning substantial profits. Due to greed of money, the two brothers, namely, Amit and Anil, joined hands together to assume complete control of the company, leaving their brother, Akhlesh in lurch. Both the brothers got further shares allotted to themselves, thereby their joint shareholding increased from 66 2/3% to 90%, while the shareholding of Akhlesh got reduced from the erstwhile 33 1/3% to 10%. No notice of any Board Meeting was sent to Akhlesh, who was sidelined and was also removed as a Director.

Aggrieved by the decisions taken by his two brothers at his back, Akhlesh seeks your advice for taking out appropriate proceedings before the court or judicial authority of competent jurisdiction. Also suggest the nature of reliefs he may claim while filing his case. [4]

(c) Amit, Biswajit, Shyam and Tarak are Directors of XYZ Ltd. Shyam and Tarak did not attend the Board Meeting which was properly convened. At the said Board Meeting, two Additional Directors were appointed. They are the wife and brother of Amit and Biswajit respectively, the Directors who attended the Board Meeting. Explain whether the Directors who attended the Board Meeting are entitled to vote on the subject-matter and whether the appointment of Additional Directors is valid. [4]

(d) Smart Banking Company Limited has advanced a sum of ₹25.00 lacs to Mr. Reliable, a director of the company, to meet his personal liabilities but due to some adverse conditions, Mr. Reliable is not in a position to repay the loan. The Board of directors of the company is considering to remit a sum of ₹10.00 lacs. The Board of Directors seeks your advice. [2]

Answer 4(a):

As per section 295, a public company shall not, directly or indirectly, make any loan to a director without obtaining the previous approval of the Central Government. Also, if a company wishes to give a guarantee or provide any security in connection with a loan made by any other person to a director, it requires the previous approval of the Central Government. Moreover, where a company gives a guarantee to a body corporate, it shall comply with the provisions of section 372A.

The following legal requirements must be complied with in the present case:

1. The Board shall consider the contract relating to giving of guarantee to M/s Housing Finance Co. Ltd. Since Mr. SOURAV is interested, he shall disclose his interest, shall not be counted in

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quorum, and shall not vote (Sections 299 and 300). Necessary entries will be made in the register of contracts (Section 301).

2. M/s ASHEEKA Ltd. shall make an application to the Central Government for approval under section 295. Only on receipt of the approval of the Central Government, M/s ASHEEKA Limited will give the guarantee to M/s Housing Finance Co. Ltd (Section 295).
3. Following requirements of section 372A shall also be fulfilled:
 - (a) A resolution shall be passed at a Board meeting with the consent of all the directors present in the meeting.
 - (b) Approval of Public Financial Institution, if applicable, shall be obtained.
 - (c) The company shall ensure that no default in compliance with section 58A (relating to public deposits) is subsisting.
 - (d) If the ceiling limit specified under section 372A (60% of aggregate of paid up capital and free reserves or 100% of free reserves, whichever is higher) is exceeded, a special resolution shall be passed in the general meeting.

Answer: 4. (b)

Issue of further shares amounts to oppression if it is proved that the idea of issuing further shares was to benefit one group to the detriment of the other [Piercy v Mill(s) d Co. (1920) 1 Ch. 77]. Further issue of shares must be made for the benefit of the company. If the directors use their fiduciary power of issuing shares for an extraneous purpose like maintenance or acquisition of control over the affairs of the company, it would amount to oppression [Needle Industries Case]. It is not open to the directors to issue and allot shares in a manner by which an existing majority of shareholders is reduced to a minority. If the issue of shares disturbs the existing majority of the shareholders and if it is not bonafide, it will amount to oppression [Re, Glaco Series (P)Ltd.].

In the given case, further shares have been allotted to Amit and Anil without simultaneous offer to other members (Akhlesh) on pro-rata basis. Such single act of issue of further shares shall have a continuous effect, and so it amounts to oppression, especially if, the Board meeting at which the further shares are allotted is held without complying with the requirements of section 286, and the member who was not offered further shares was also removed from directorship [Bhagirath Agarwala v Tara properties P. Ltd.]. Therefore, Akhlesh should file an application with the Company Law Board for claiming relief from oppression.

Answer: 4. (c)

In view of the opinion of Madras High Court & Tribunal Letter cited below, the appointment of relatives of Amit & Biswajit as Additional Directors is not valid.

The question is whether the appointment of Additional Director would come within the scope of the word "contract or arrangement", in order to consider the Director to be "interested". The Court concluded that appointment as Director does not come within the scope of the expression "contract" (because the position of a Director may be conferred on a person by any method other than "contract"), but it would amount to "arrangement". So, the attending

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Directors became Interested Directors. Appointment of their relatives as Additional Directors was null and void – **Madras Tube Co. Ltd. Vs Harikrishna Somani 1 Comp LJ 195 (Mad)**.

It will be a clearly unsound Company practice if a Director, whose near relative is proposed to be appointed to the Board, were to participate in the discussions at the Board Meeting and vote on the proposal for such appointment – **L.No. 8/46/(300) 64-PR dated 27-01-1965**.

Note: Contrary opinion is taken by Bombay High Court

Appointment as an Additional Director of a person who is related to a Director does not violate the requirements of Sec. 300(1), because such appointment does not constitute any "contract or arrangement" of the Company with the Sitting Director. The Sitting Director is entitled to participate and vote – **Shailesh Harilal Shah Vs. Matushree Textiles Ltd. 82 CC 5 (Bom)**.

Answer 4. (d)

Section 20A of the Banking Regulation Act, 1949 provides that except with the prior approval of RBI, a banking company shall not remit in whole or in part any debt due to it by:

- (a) Any of its Directors, or
- (b) Any firm or company in which any of its Directors is interested as Director, Partner, Managing Agent or Guarantor, or
- (c) Any individual, if any of its Directors, is his Partner or Guarantor.

Sub-section (2) further provides that any remission of debt in contravention of the aforesaid shall be void and of no effect.

5. (a) **The promoters of XYZ Ltd., an Unlisted Company, decide to go for a public issue. They seek your advice in respect of the following matters:**
- (i) **Can equity shares be reserved in Firm Allotment Category for Promoters, at a price different from the price at which shares are offered to Public?**
 - (ii) **Circumstances in which equity shares can be issued in denomination of ₹2 per share.**
 - (iii) **Need for past track record of distributable profits.**
 - (iv) **Requirement of Net Tangible Assets in previous years.** **[4]**
- (b) **On 24th January 2013, the Board of Directors of M/s. Bold Limited appointed Mr. A as the company's Sole Selling Agent for a period of 5 years. At the first general meeting of the company, held after the Board Meeting, on 29th September 2013, the above appointment was disapproved. Referring to the provisions of the Companies Act, 1956:**
- (i) **State the date from which the above appointment comes to an end.**
 - (ii) **What would be your answer in case a clause in the above appointment that "the appointment must be made by the company in General Meeting" was not inserted as a condition?** **[4]**
- (c) **Printed Computer is a Singapore based company having several business units all over the world. It has a unit for manufacturing computer printers with its headquarters in Pune. It has a**

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branch in Dubai which is controlled by the headquarters in Pune. What would be the residential status under FEMA, 1999 of printer units in Pune and that of Dubai branch? [5]

(d) BOD of M/s SK Ltd., in its meeting held on 29th May, 2013 declared an interim dividend payable on paid up equity share capital of the company. In the Board meeting scheduled for 10th June, 2013, the Board wants to revoke the said declaration. You are required to state with reference to the provisions of the Companies Act, 1956 whether the BOD can do so. [2]

Answer 5 (a):

(i) Differential Pricing is a process by which the Shares of the Company are issued at two different prices depending on the type of the allottees.

Such differential pricing shall be allowed in respect of – (a) Higher Price for Firm Allotment Category Applicants, (b) Issue to Retail Individual Investors, (c) Composite Public and rights Issue and (d) Employees in case the issuer opts for the alternate method of book-building in terms of Part D of Schedule XI.

(ii) An issuer making IPO shall determine the face value of shares as follows:

Issue Price	Face Value
Less than ₹500	₹10 per share.
₹500 or more	Can be below ₹10 per share, but shall not be less than ₹1 per share.

(iii) Earlier it was required to maintain a track record of distributable profits in terms of section 205 of the Companies Act, 1956, on both standalone as well as consolidated basis for at least 3 out of the immediately preceding 5 years, but now it has been substituted by SEBI (Issue of Capital and Disclosure Requirements) (Second Amendment) Regulations, 2012, w.e.f. 12.10.2012 as:

“It has a minimum average pre-tax operating profit of rupees fifteen crore, calculated on a restated and consolidated basis, during the three most profitable years out of the immediately preceding five years.”

(iv) Requirement of Net Tangible Assets:

“It should have net tangible assets of at least three crore rupees in each of the preceding three full years (of twelve months each), of which not more than fifty per cent are held in monetary assets:

Provided that if more than fifty per cent of the net tangible assets are held in monetary assets, the issuer has made firm commitments to utilize such excess monetary assets in its business or project:

Provided further that the limit of fifty per cent on monetary assets shall not be applicable in case the public offer is made entirely through an offer for sale.”

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Answer 5 (b):

The legal position

- (a) Where the Board of directors of a company appoints a Sole Selling Agent, such appointment shall be subject to the condition that the appointment shall cease to be valid if it is not approved by the shareholders in the first general meeting held after the date of the appointment.
- (b) If the shareholders in the general meeting disapprove the appointment, the appointment shall cease to be valid with effect from the date of that general meeting.
- (c) The provisions regarding incorporation of this condition are mandatory. If there is no such condition, the agreement will be void ab initio even if the appointment is approved by the general meeting [Arantee Manufacturing Corporation v Bright Bolts Pvt. Ltd. AIR (1967) 37 Comp Cas 758; Department Circular No. 12(11)-CL- VI/68, dated 6.11.1968].

The given case

- (i) Mr. A has been appointed by the Board of Directors on 24th January, 2013. At the first general meeting held after the date of appointment of Mr. A, the appointment of Mr. A has been disapproved. Therefore, the appointment of Mr. A comes to an end with effect from the date of the first general meeting, viz. 29th September, 2013.
- (ii) In case the appointment of Mr. A had been made without any condition regarding approval of his appointment in the first general meeting, the appointment of Mr. A would have been void ab initio. In such a case, the question of cessation of office does not arise at all, since the appointment is altogether void.

Answer 5 (c):

Section 2(u) defines a 'person'. As per this definition, the following shall be covered in the definition of a 'person':

- (a) A company.
- (b) Any agency, office or branch owned by a 'person'.

Section 2(v) defines a 'person resident in India'. As per this definition, the following shall be covered in the definition of a 'person resident in India':

- (a) An office, branch or agency in India owned or controlled by a person resident outside India.
- (b) An office, branch or agency outside India owned or controlled by a person resident in India.

In the given case, Printed Computers (Singapore), its headquarters in Pune as well as Dubai Branch is a 'person'. Therefore, residential status under FEMA shall be determined for each of them separately.

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- Printed Computers (Singapore) does not fall under any of the clauses of the definition of a 'person resident in India'. Therefore, Printed Computers (Singapore) is a person resident outside India.
- The Pune Headquarters of Printed Computers is a 'person resident in India' since it falls under the clause 'an office, branch or agency in India owned or controlled by a person resident outside India'.
- The Dubai branch of Printed Computers (Singapore), though not owned, is controlled by the Pune headquarters. The Dubai branch is a 'person resident in India' since it falls under the clause 'an office, branch or agency outside India owned or controlled by a person resident in India'.

Answer 5 (d):

Any dividend in between two annual general meetings of the company, or before or after the closure of annual accounts for any particular year is referred as interim dividend. Dividend, once declared, becomes a debt payable by the company and after declaration, dividend cannot be cancelled. The Companies (Amendment) Act, 2000 inserted sub-section (1A), (1B) and (1C) in section 205. These new provisions specifically authorize the BOD to declare interim dividend and that the provisions of section 205, 205A, 205C, 206, 206A and 207 shall apply to any interim dividend also as they apply in case of final dividend. Therefore, interim dividend also cannot be cancelled.

In view of the above discussion, it can be concluded since the Board of SK Ltd. has already declared interim dividend, it cannot be revoked.

6. (a) Mr. Boston was appointed as the sole selling agent of M/s Quality Ltd. w.e.f 1st January 2010 for a period of 5 years. Mr. Boston earned his remuneration as following during the years 2010 to 2012:

Year	Amount of remuneration
2010	₹4,41,000
2011	₹6,32,000
2012	₹7,45,000

On and from 1st January 2013, the sole selling agency agreement was terminated by M/s Quality Ltd. You are required to calculate the amount of compensation payable by the said company to Mr. Boston under the provisions of the Companies Act, 1956.

What would be your answer in a case where the said M/s Quality Ltd. was amalgamated with another company with effect from 1st January 2013 and Mr. Boston refused to act as the sole selling agent of the amalgamated company after amalgamation? [3+2=5]

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(b) The Central Govt. acquired a Banking Company. The scheme of acquisition, apart from other matters, provided for the quantum of compensation payable to the shareholders of the acquired Bank. Some Shareholders are not satisfied with the amount of compensation fixed under the scheme of acquisition.

Is there any remedy available to the shareholders under the provisions of the Banking Regulation Act, 1949? [3]

(c) What are the qualifications to be appointed as members of Central Commission as per The Indian Electricity Act, 2003? Also state the functions of the Central Commission. [3+4=7]

Answer: 6. (a)

(i) According to section 294A, where the office of a sole selling agent is vacated for any reason other than those specified under that section then the company shall be liable to pay compensation and the amount of compensation shall not exceed the remuneration which he would have earned if he would have been in office for the unexpired residue 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 his office ceased or was terminated, or where he held his office for a period lesser than three years, then average remuneration actually earned by him during such lesser period.

In the given case, based on the above provision of the Companies Act, 1956 Mr. Boston is entitled to compensation for the remaining term of his office i.e., 2 years. The amount of compensation is to be calculated on the basis of average of preceding three years' remuneration i.e., $(₹4,41,000 + ₹6,32,000 + ₹7,45,000)/3 = ₹6,06,000$. Thus, the amount of compensation shall not exceed ₹12,12,000 i.e. ₹6,06,000 x 2.

(ii) According to section 294A, the company shall not be liable to pay compensation to the sole selling agent for loss of office where the sole selling agent vacates office for facilitating any scheme of compromise or arrangement and he is reappointed in the new company. Since the question Mr. Boston refuses to act as sole selling agent in the amalgamated company, he is not entitled for any compensation. He would have been entitled for compensation had he not been offered to be appointed in the amalgamated company.

Answer: 6. (b)

Compensation to Shareholders of the Acquired Bank [Sec. 36AG]:

1. **Recipient:** The Central Govt. / Transferee Bank shall give the compensation determined in the prescribed manner, to:
 - (a) Registered Shareholder of the acquired Bank, or
 - (b) Where the acquired Bank is a Banking Company incorporated outside India, the acquired Bank

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2. Reference to Tribunal:

(a) Request: If the amount of compensation offered is not acceptable to any person to whom the compensation is payable, the aggrieved person may request the Central Govt. in writing to have the matter referred to the Tribunal. Such a request shall be made before the date notified by the Central Govt.

(b) Eligible Persons: The Central Govt. shall have the matter referred to the Tribunal for decision, if it receives requests from:

- Not less than 1/4th in number of the Shareholders holding not less than 1/4th in value of the Paid up Share Capital of the acquired Bank, or
- Where the acquired Bank is a Banking Company incorporated outside India, from the acquired Bank.

3. Finality of compensation:

If before the notified date, the Central Govt. does not receive requests as required, the amount of compensation offered, and where a reference has been made to the Tribunal, the amount determined by it, shall be the compensation payable and shall be final and binding on all parties concerned.

Answer: 6. (c)

Qualification for appointment of Members of Central Commission [Section 77]:

1. The Chairperson and the Members of the Central Commission shall be persons having adequate knowledge of, or experience in, or shown capacity in, dealing with, problems relating to engineering, law, economics, commerce, finance or, management and shall be appointed in the following manner, namely:

(a) one person having qualifications and experience in the field of engineering with specialisation in generation, transmission or distribution of electricity;

(b) one person having qualifications and experience in the field of finance;

(c) two persons having qualifications and experience in the field of economics, commerce, law or management:

Provided that not more than one Member shall be appointed under the same category under clause (c).

2. Notwithstanding anything contained in sub-section (1), the Central Government may appoint any person as the Chairperson from amongst persons who is, or has been, a Judge of the Supreme Court or the Chief Justice of a High Court:

Provided that no appointment under this sub-section shall be made except after consultation with the Chief Justice of India.

3. The Chairperson or any other Member of the Central Commission shall not hold any other office.

4. The Chairperson shall be the Chief Executive of the Central Commission.

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Functions of Central Commission [Section 79]:

1. The Central Commission shall discharge the following functions, namely:
 - (a) to regulate the tariff of generating companies owned or controlled by the Central Government;
 - (b) to regulate the tariff of generating companies other than those owned or controlled by the Central Government specified in clause (a), if such generating companies enter into or otherwise have a composite scheme for generation and sale of electricity in more than one State;
 - (c) to regulate the inter-State transmission of electricity;
 - (d) to determine tariff for inter-State transmission of electricity;
 - (e) to issue licenses to persons to function as transmission licensee and electricity trader with respect to their inter-State operations;
 - (f) to adjudicate upon disputes involving generating companies or transmission licensee in regard to matters connected with clauses (a) to (d) above and to refer any dispute for arbitration;
 - (g) to levy fees for the purposes of this Act;
 - (h) to specify Grid Code having regard to Grid Standards;
 - (i) to specify and enforce the standards with respect to quality, continuity and reliability of service by licensees;
 - (j) to fix the trading margin in the inter-State trading of electricity, if considered, necessary;
 - (k) to discharge such other functions as may be assigned under this Act.

2. The Central Commission shall advise the Central Government on all or any of the following matters, namely:
 - (a) formulation of National electricity Policy and tariff policy;
 - (b) promotion of competition, efficiency and economy in activities of the electricity industry;
 - (c) promotion of investment in electricity industry;
 - (d) any other matter referred to the Central Commission by that Government.

3. The Central Commission shall ensure transparency while exercising its powers and discharging its functions.

4. In discharge of its functions, the Central Commission shall be guided by the National Electricity Policy, National Electricity Plan and Tariff Policy published under section 3.

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Section B

(Corporate Governance and Responsibilities)

[Answer **any five** questions from Q.No.7 (a) to (f)]

7. (a) What is Corporate Governance? What is the need for Corporate Governance in India?
- (b) State the advantages of Good Corporate Citizenship.
- (c) State the factors influencing Corporate Social Responsibility (CSR).
- (d) Would you advocate the following understandings with relation to CSR? Discuss.
- Businesses invest the money, therefore they decide the modus operandi of the CSR initiative
 - Financial resources alone can meet CSR needs of an enterprise.
 - CSR is interchangeable with corporate sponsorship, donation or other philanthropic activities.
- (e) Can whole life risk be analysed?
- (f) Discuss, "Governance in India – The Path Ahead" [5×5 = 25]

Answer: 7. (a)

Corporate governance is:

- (i) The system by which companies are directed and controlled -The Cadbury Report, 1992.
- (ii) The process of supervision and control intended to ensure that the company's management acts in accordance with the interests of shareholders -Parkinson, 1994.
- (iii) Corporate Governance is the acceptance by management of the inalienable rights of shareholders as the true owners of the corporation and of their own role as trustees on behalf of the shareholders. It is about commitment to values, about ethical business conduct and about making a distinction between personal and corporate funds in the management of a company –Report of N.R.Narayana Murthy Committee on Corporate Governance constituted by SEBI (2003).

Need for Corporate Governance:

Corporate Governance is integral to the existence of the company. It is needed to create a corporate culture of transparency, accountability and disclosure.

- i. **Corporate Performance:** Improved governance structures and processes help ensure quality decision-making, encourage effective succession planning for senior management and enhance the long-term prosperity of companies, independent of the type of company and its sources of finance.
- ii. **Enhanced Investor Trust:** Investors consider Corporate Governance as important as financial performance when evaluating companies for investment.
- iii. **Combating Corruption:** Companies that are transparent, and have sound system that provide full disclosure of accounting and auditing procedures, allow transparency in all business transactions, provide environment where corruption will certainly fade out.

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- iv. **Better Access to Global Market:** A Good Corporate Governance system attracts investment from global investors, which subsequently leads to greater efficiencies in the financial sector.
- v. **Enhancing Enterprise Valuation:** Improved management accountability and operational transparency fulfill investors' expectations and confidence on management and corporations, and return, increase the value of corporations.
- vi. **Accountability:** An Investor relation 'is essential part of good Corporate Governance. Investors have directly/indirectly entrusted management of the company for creating enhanced value for their investment.
- vii. **Easy Finance from Institutions:** Evidence indicates that well-governed companies receive higher market valuations.
- viii. **Reduced Risk of Corporate Crisis and Scandals:** Effective Corporate Governance ensures efficient risk mitigation system in place

Answer: 7. (b)

Business cannot exist in isolation; business cannot be oblivious to societal development. The social responsibility of business can be integrated into the business purpose so as to build a positive synergy between the two.

- i. CSR creates a favourable public image, which attracts customers. Reputation or brand equity of the products of a company which understands and demonstrates its social responsibilities is very high. Customers trust the products of such a company and are willing to pay a premium on its products. Organizations that perform well with regard to CSR can build reputation, while those that perform poorly can damage brand and company value when exposed. Brand equity is founded on values such as trust, credibility, reliability, quality and consistency.
- ii. CSR activities have its advantages. It builds up a positive image encouraging social involvement of employees, which in turn develops a sense of loyalty towards the organization, helping in creating a dedicated work force proud of its company. Employees like to contribute to the cause of creating a better society. Employees become champions of a company for which they are proud to work.
- iii. Society gains through better neighbourhoods and employment opportunities, while the organization benefits from a better community, which is the main source of its workforce and the consumer of its products.
- iv. Public needs have changed leading to changed expectations from consumers. The industry/business owes its very existence to society and has to respond to needs of the society.
- v. The company's social involvement discourages excessive regulation or intervention from the Government or statutory bodies, and hence gives greater freedom and flexibility in decision-making.
- vi. The internal activities of the organization have an impact on the external environment, since the society is an inter-dependent system.
- vii. A business organization has a great deal of power and money, entrusted upon it by the society and should be accompanied by an equal amount of responsibility. In other words, there should be a balance between the authority and responsibility.

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- viii. The good public image secured by one organization by their social responsiveness encourages other organizations in the neighborhood or in the professional group to adapt themselves to achieve their social responsiveness.
- ix. The atmosphere of social responsiveness encourages co-operative attitude between groups of companies. One company can advise or solve social problems that other organizations could not solve.
- x. Companies can better address the grievances of its employees and create employment opportunities for the unemployed.
- xi. A company with its —ear to the ground|| through regular stakeholder dialogue is in a better position to anticipate and respond to regulatory, economic, social and environmental change that may occur.
- xii. Financial institutions are increasingly incorporating social and environmental criteria into their assessment of projects. When making decisions about where to place their money, investors are looking for indicators of effective CSR management.
- xiii. In a number of jurisdictions, governments have expedited approval processes for firms that have undertaken social and environmental activities beyond those required by regulation.

Answer: 7. (c)

Many factors and influences, including the following, have led to increasing attention being devoted to CSR:

- i. Globalization – coupled with focus on cross-border trade, multinational enterprises and global supply chains – is increasingly raising CSR concerns related to human resources management practices, environmental protection, and health and safety, among other things.
- ii. Governments and intergovernmental bodies, such as the United Nations, The OECD and the ILO have developed compacts, declarations, guidelines, principles and other instruments that outline social norms for acceptable conduct.
- iii. Advances in communications technology, such as the Internet, Cellular phones and personal digital assistants, are making it easier to track corporate activities and disseminate information about them. Non-governmental organizations now regularly draw attention through their websites to business practices they view as problematic.
- iv. Consumers and investors are showing increasing interest in supporting responsible business practices and a demanding more information on how companies are addressing risks and opportunities related to social and environmental issues.
- v. Numerous serious and high-profile breaches of corporate ethics have contributed to elevated public mistrust of corporations and highlighted the need for improved corporate governance, transparency, accountability, and ethical standards.
- vi. Citizens in many countries are making it clear that corporations should meet standards of social and environmental care, no matter where they operate.
- vii. There is increasing awareness of the limits of government legislative and regulatory initiatives to effectively capture all the issues that CSR addresses.
- viii. Businesses are recognizing that adopting an effective approach to CSR can reduce risk of business disruptions, open up new opportunities, and enhance brand and company reputation.

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Answer: 7. (d)

In the absence of a universally accepted definition for CSR, there are some myths that surround the concept, and the ones stated are a few of the same. They should be dealt as follows.

Myth # 1: Businesses invest the money, therefore they decide the modus operandi of the CSR initiative

There is a notion that since businesses invest money in society, they are the one who will be deciding upon the modus operandi of the CSR initiative. However this is not true. CSR driven by the mandate of an enterprise alone may not generate desired results. Stakeholders must be involved from the onset in defining an initiative to make it successful. Corporates must not assume that they understand the needs of a community by taking them at face value; stakeholder's needs must be considered within the local context and culture.

Myth # 2: Financial resources alone can meet CSR needs of an enterprise.

In fact, financial resources are only part of the equation. Besides financial resources, it is equally or even more important for the CSR programmes to be well defined and well accompanied by adequate human resources if they are to meet the intended objectives.

Myth # 3: CSR is interchangeable with corporate sponsorship, donation or other philanthropic activities.

The focus of responsible business practices in the profit sector is hitherto largely confined to community charity-based projects.

While this may have been relevant for the historical context in the mid-90s when Carroll's definition was coined, the current thinking of CSR has moved beyond philanthropy to in fact encompass all internal and external segments of business operations: employees, market environment and community.

The rationale for CSR has been articulated in a number of ways. In essence, it is about building sustainable businesses, which need healthy economies, markets and communities.

Answer: 7. (e)

Several methodologies are available to deal with WLCC risk analysis. The techniques that can be used in WLCC risk assessment decision making might be summarised as deterministic, probabilistic and AI. Deterministic methods measure the impact on project outcomes of changing one uncertain key value or a combination of values at a time. In contrast, probabilistic methods are based on the assumption that no single figure can adequately represent the full range of possible outcomes of a risky investment (Fuller & Petersen 1996). Rather, a large number of alternative outcomes must be considered and each possibility must be accompanied by an associated probability from a probability distribution, followed by a statistical analysis to measure the degree of risk. Using a deterministic approach, the analyst determines the degree of risk on a subjective basis. AI methods differ from the above approaches and use historical data to model cost and uncertainty in WLCC analysis. None of these techniques can be applied to every situation. The best method depends on the relative size of the project, availability of data and resources, computational aids and skills, and user understanding of the technique being applied.

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Following the identification, quantification and development of risk responses, the related vulnerabilities of building assets need to be determined and planned for. This provides the basis on which risk management plans and decisions are made. The risk management planning process is concerned with putting in place the procedure for:

- (i) What response actions are needed
- (ii) When these response actions are needed
- (iii) How these actions are implemented
- (iv) Who is responsible for the implementation, control and monitoring of the actual progress of risk responses and management strategies that have been developed to deal with the identified risk.

Answer: 7. (f)

Governance in India: The Path Ahead

The Indian economy on the eve of the Twelfth Plan is characterized by strong macro-fundamentals and good performance over the Eleventh Plan period, though clouded by some slowdown in growth in the current year with continuing concern about inflation and a sudden increase in uncertainty about the global economy. The objective of the Eleventh Plan was faster and inclusive growth and the initiatives taken in the Eleventh Plan period have resulted in substantial progress towards both objectives. Inevitably, there are some weaknesses that need to be addressed and new challenges that need to be faced. Some of the challenges themselves emanate from the economy's transition to a higher and more inclusive growth path, the structural changes that come with it and the expectations it generates. There are external challenges also arising from the fact that the global economic environment is much less favourable than it was at the start of the Eleventh Plan. These challenges call for renewed efforts on multiple fronts, learning from the experience gained, and keeping in mind global developments. We focus on the backdrop of target setting and areas of focus of the Eleventh Plan. India entered the Eleventh Plan period (2007-2012) with an impressive record of economic growth. The vision for the Eleventh Plan prominently included an improvement in governance. Over the years, the governments at the Centre and the States have launched a large number of initiatives at substantial public expense to achieve the objectives of growth with poverty alleviation and inclusiveness. Experience suggests that many of these initiatives have floundered because of poor design, insufficient accountability and also corruption at various levels. Increasingly, there is demand for effective implementation without which expanded government intervention will be infructuous. The strategy for the Eleventh Plan was therefore aimed at bringing about major improvements in governance which would make government-funded programmes in critical areas more effective and efficient. The best possible way of achieving this objective may be by involving communities in both the design and implementation of such programmes, although such involvement may vary from sector to sector. For achieving the vision of the Eleventh Plan, it is extremely important to experiment with programme design to give more flexibility to decision making at the local level. It is especially important to improve evaluation of the effectiveness of how government programmes work and to inject a commitment to change their designs in the light of the experience gained. Evaluation must be based on proper benchmarks and be scientifically designed to generate evidence-

Answer to MTP_Final_Syllabus 2012_Jun 2014_Set 2

based assessment of different aspects of programme design. Along with greater transparency and feedback from community participation, this is particularly important in the case of programmes delivering services directly to the poor. Accountability and transparency are critical elements of good governance. The Right to Information Act (RTI) enacted in 2005 empowers people to get information and constitutes a big step towards transparency and accountability.