PAPER 13 – Corporate Laws and Compliance
SECTION A

[Answer to Q.No.1 is compulsory and attempt any 4 from the rest]

1. **(a) Anita Ltd. and Binita Ltd. entered into a scheme of amalgamation by which Anita Ltd. would transfer its entire undertaking to Binita Ltd. However, the Central Govt. raised an objection that unless the Objects Clause of the companies are similar, and Memorandum empowers to do so, the scheme of amalgamation cannot be permitted. Is the contention of the Central Govt. correct? [3]**

   (b) Mr. Ram, a Director of XYZ Ltd., requested by providing an advance information for leave of absence expressing his inability to attend the next Board meeting. Advise whether notice is required to be sent to him. [2]

   (c) Amal, Vimal, Chapal and Dhabal are Directors of ABCD Ltd. Chapal and Dhabal did not attend the Board Meeting which was properly convened. At the said Board Meeting, two Additional Directors was appointed. They are the wife and brother of Amal and Vimal 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) The board of Directors of GF Projects Ltd. , a company whose Shares are listed on the Delhi Stock Exchange proposes to give loans to a sister Company in excess of the limit prescribed u/s 372A (1). The next AGM of the Company is due only after 6 months. Since the Board is anxious to complete the formalities quickly without waiting for the date of next AGM, advise the board about the steps to be taken to comply with the legal requirements under the Companies Act, 1956. [6]

Answer 1(a):

There is no statutory condition that the Objects Clause of both amalgamating companies should be similar. Infact, the purpose of amalgamation may be to enter into new areas of activity/lines of business (within the powers stipulated by the MoA), without starting a new undertaking afresh. Hence, non-similarity of Objects Clause of amalgamating companies cannot be a valid objection.
In the case of EITA India Ltd. AIR 1997 Cal 208, United Bank of India Vs united India Credit & Devt Co. Ltd. 47 CC 689 Hari Krishna Lohia Vs Hoolungoree Tea Company 47 CC 458, it was held that "To amalgamate with another company" is a power of the company, and not merely an object. This right to amalgamate is derived from the Statute itself, and no separate provision in the Company's MoA is required. Sec. 394 gives full jurisdiction to the Court to sanction amalgamation, even though there may be no power in the objects clause of MoA.
In view of the above discussion, the objections of the Central Govt. are not valid.

Answer 1(b):

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).

Notice is to be sent to a director even if he waives his right to receive the notice [Re, Portuguese Consolidated Copper Mines Ltd. (1889) 42 Ch D 160 (CA)]. Thus, the notice of Board meeting must be sent to Mr. Ram.

Answer 1(c):

In view of the opinion of Madras High Court & Tribunal Letter cited below, the appointment of relatives of Amal & Vimal 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 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 1(d):

Loans above the ceiling limit u/s 372A(1) can be made only with the previous approval by a Special Resolution in the General meeting. So, the following steps are to be taken by the Company:

1. According to Rule 4 of Companies (Passing of the Resolution by postal Ballot) Rules, 2001, Postal Ballot is mandatory in case of a Listed Company for transacting a business relating to giving loans in excess of the limits prescribed u/s 372A(1). As the above Company is a Listed Company, it must take steps for passing a special resolution through postal ballot in accordance with the aforesaid Rules. [Sec. 192A].
2. Notice of such resolution to be sent to members should indicate specific limits, particulars of Company to which loan is to be given, specific sources of funding and such other details.
3. In addition to special resolution, prior approval of the Board of Directors is required u/s 372A. All Directors present at the Board meeting must vote in favour of the resolution.
4. Prior approval should be obtained from Public Financial Institution from whom loans have been taken.
5. Interest Rate to be charged by the Company shall not be less than the prevailing Bank Rate specified by RBI u/s 49 of the RBI Act.
6. Prescribed particulars must be entered in the Register maintained u/s 372A(5), within specified time limits.
7. A copy of the special resolution should be filed with the RoC.

2. (a) One of the members of AB Ltd. has proposed the name of Mr. Fern for appointment as a director of the company in the Annual General Meeting and given a notice under section 257 of the Companies Act, 1956. Mr. Fern is one of the partners of Fern & Fern, Chartered Accountants, who are the retiring auditors of the company. But the audit of the company is being looked after by another partner of the firm. Examine whether Fern & Fern can be reappointed as auditors, if Mr. Fern is appointed as director. [4]

(b) Unique Technologies Ltd. has been wound up and the Official Liquidator has been asked to take charge of the Company. Briefly explain the relevant provisions regarding filing of Statement of Affairs in relation to the Company in liquidation. [8]

(c) Examine the validity of the following appointment made by Board of Dhanavan Ltd. Buddhiman Ltd. is a Subsidiary Company of Dhanavan Ltd. in which Mr. Pratik Sen is a Director. Mr. Pratik Sen has been appointed as Manager – Research & Development in Dhanavan Ltd. on a Monthly Salary ₹2.5 Lakhs per month with effect from 1st April 2013.
What would be your answer is case ABC Ltd. is a Subsidiary of Buddhiman Ltd. [3]

Answer 2(a):

The present problem relates to section 226 of the Companies Act, 1956.

The legal position

1. As per section 226, a person shall be disqualified to be appointed or reappointed as an auditor of the company if he is an officer or employee of the company.
2. As per section 2(30), a director is an officer of the company.
3. As per section 257, any member of a public company can give a notice proposing the appointment of any person (whether a member or not) as a director of the company.

The given case

1. Mr. Fern is a partner in the firm 'Fern & Fern', 'Fern & Fern' are the retiring auditors of the company, and they are seeking reappointment in the forthcoming annual general meeting.
2. The name of Mr. Fern has been proposed as a director by a member by giving a notice under section 257. Mr. Fern has been appointed as a director in the annual general meeting.

Conclusion

On appointment as a director, Mr. Fern becomes an officer of the company. Therefore, Mr. Fern and any firm in which Mr. Fern is a partner, is disqualified to be re-appointed as auditors of the company.

Answer 2(b):

Sec. 454 deals with Statement of Affairs to be made to Official Liquidator, in a compulsory winding-up. The provisions are summarized as under:

1. **Situations:** A Statement of Affairs of the Company shall be made out and submitted to the Official Liquidator, where the Court has:

   (a) made a winding-up order, or
   (b) appointed the Official Liquidator as Provisional Liquidator.

2. **Contents:** The Statement of Affairs shall be in the prescribed form, with the following particulars:

   (a) Assets of the Company [Cash balance in Hand and at Bank, and Negotiable Securities, if any, held by the Company, should be separately stated]
   (b) Debts and Liabilities of the Company,
   (c) Names, Residences and Occupations of its Creditors, with break-up of Secured and Unsecured Debts, [In case of Secured Debts, particulars of securities given, whether by Company or an Officer thereof, their value and dates on which they were given, should

be stated.]
(d) Debts due to the Company, and the Names, Residences and Occupations of the persons from whom they are due and the amount likely to be realised on account thereof,
(e) Such further or other information as may be prescribed, or as the Official Liquidator may require.

3. **Verification:** The Statement shall submitted and verified (by an affidavit) by one or more Directors, Manager, Secretary or other Chief Officer of the Company, on the relevant date. Further, the Official Liquidator may require any of the following persons to verify the statement:

(a) Present or Past Officers of the Company,
(b) Persons who have taken part in the formation of the Company at any time within preceding 1 year,
(c) Present or Past Employees of the Company within preceding 1 year, and are, in the opinion of the Official Liquidator, capable of giving the information required,
(d) Present or Past Officers / Employees of any other Company, which is an Officer of the Company to which the statement relates.

4. **Time Limit:** The statement shall be submitted within 21 days from the relevant date. The Official Liquidator or the Court may, for special reasons, extend this time upto 3 months.

Note: For this purpose, "Relevant Date" means:

Where Provisional Liquidator -	**Relevant Date**
is appointed	Date of appointment of Provisional Liquidator
is not appointed	Date of winding-up order

5. **Reimbursement of Cost**: Any person making, or concurring in making, the Statement and Affidavit u/s 454 shall be entitled to receive the costs and expenses incurred in preparation of the Statement. The amount, as considered reasonable by him, shall be paid by the Official / Provisional Liquidator, out of the assets of the Company.

6. **Default:** Default in complying with Sec.454, without reasonable excuse, is punishable with imprisonment upto 2 years, and /or fine upto ₹1,000 for every day during which the default continues.

7. **Inspection:** Any Creditor or Contributory shall be entitled to inspect the Statement of Affairs, and to a copy thereof or extract therefrom, on payment of the prescribed fee. Any person untruthfully so stating himself to be a Creditor or Contributory shall be guilty of an offence u/s 182 of Indian Penal Code, and shall be punishable accordingly.

8. **Application of Sec.454 to voluntary winding-up [Sec. 511A]:** Provisions of Sec. 454 shall, so far as may be, apply to every voluntary winding-up as they apply to winding-up by the Court except that reference to:
(a) the Court shall be omitted,
(b) the Official Liquidator or Provisional Liquidator shall be construed as reference to the Liquidator, and
(c) the "Relevant Date" shall be construed as reference to the date of commencement of winding-up.

Answer 2(c):

It can be assumed Mr. Pratik sen is a Director either in Dhanavan Ltd. or Buddhiman Ltd., as the same is not clear in the question. The effect of the appointment of Mr. Pratik Sen in Office or place of Profit (OPP) in Dhanavan Ltd. u/s 314(1) is analyzed as follows:

Mr. Pratik sen is a Director in:	Case A: Dhanavan Ltd. – Holding, Buddhiman Ltd. - Subsidiary	Case B: Buddhiman Ltd. – Holding, Dhanavan Ltd. - Subsidiary
Dhanavan Ltd.	Appointment of Mr. Pratik Sen in Dhanavan Ltd. in OPP is covered u/s 314(1). Shareholders approval required u/s 314(1).	Appointment of Mr. Pratik Sen in Dhanavan Ltd. in OPP is covered u/s 314(1). Shareholders approval required u/s 314(1).
Buddhiman Ltd.	Appointment of Mr. Pratik Sen (Director of Subsidiary) in Dhanavan Ltd. (Holding) is not covered by sec. 314(1). Hence, OPP can be held in Holding Company Dhanavan Ltd.	Appointment of Mr. Pratik Sen (Director of Subsidiary) in Dhanavan Ltd. (Holding) is covered by sec. 314(1). Hence, restriction applies. However, restriction will not apply if the remuneration received from the Subsidiary in respect of such OPP (held in the Subsidiary) is paid over to the Subsidiary or its Holding Company.

3. (a) Union Bank of India, a National Bank, acquired on 1st January 2002 a Building, fully occupied by various tenants, from Mr. Rahul, the owner of the Building in discharging of a Term Loan advanced to Mr. Rahul, 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) "Life Policy cannot be questioned after the expiry of 2 years from the date on which it was effected".
Explain with reference to Section 45 of the act. [4]

(c) 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? [7]

Answer 3(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, Union 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, Union 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, 2009.

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, 2014.

Answer 3(b):

Inaccurate or false particulars: An insurer shall not call in question a Life Insurance Policy after the expiry of 2 years from the date on which it was effected on the ground that – (a) a statement made in the proposal for insurance, or (b) in any report of a Medical Officer, or Referee, or Friend of the insured, or in any other document leading to the issue of the policy, was inaccurate or false. [Sec. 45]

Exception: The above provision does not apply if the Insurer shows that such statement was on-

(a) A material matter or suppressed facts which it was material to disclose, and
(b) That it was fraudulently made by the policy-holder, and
(c) That the policy-holder knew at the time of making it that the statement was false or that it suppressed facts which it was material to disclose.

Only if all the 3 conditions are satisfied conjointly the insurer can repudiate after 2 years – **LIC Vs. G.M.Chennabasamma.**

LIC challenged a policy after 2 years after its issue. It was in evidence that the assured fraudulently suppressed facts. It was held that the LIC was not liable – **Mithoolal Vs. LIC (SC 1962).**

Held that "If a period of 2 years has expired from the date on which the policy of life insurance was effected, that policy cannot be called in question by an insurer on the ground that a statement made in the proposal for insurance or on any report of a medical officer or referee, or a friend of the insured, or in any other document leading to the assure of the policy, was inaccurate or false." – **LIC Vs. Janaki Ammal (Mad HC 1968).**

Note:

(a) Policies issued in India shall be subject to law in force in India.
(b) The insurer can notify the Policyholder of the options available to him in case of non-payment of premiums.
(c) The Life Policy Holders have the right to seek for Medical Reports procured by the Insurer.

Answer 3(c):

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.

4. (a) Mr. X is a director of M/s ABC 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 ABC Ltd. should provide the guarantee for repayment of loan installments by Mr. X. Advise Mr. X. [6]

(b) The Board of Directors of M Limited propose to donate ₹3,00,000 to a school established exclusively for the benefit of the children of employees and also donate ₹50,000 to a political party during the financial year ending 31st March 2010. The average net profit determined in accordance with the provisions of section 349 and 350 of the Companies Act, 1956 during the immediately preceding three financial years is ₹40,00,000. Examine with reference to the provisions of the Companies Act, 1956 whether the proposed donations are within the powers of the Board of Directors of the Company. [5]

(c) ABC Limited wants to appoint PQR Private Limited as its sole selling agent for Southern India. Mr. Goodword, director of ABC Limited is also a director in PQR Private Limited. Advise the company about the compliances required under the Companies Act. [4]

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. X is interested, he shall disclose his interest, shall not be counted in quorum, and shall not vote (Sections 299 and 300). Necessary entries will be made in the register of contracts (Section 301).
2. M/s ABC 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 ABC 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 pubic 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):

Charitable Contribution

A contribution by a company is said to be charitable contribution if it is made without any object of availing any benefit for the company or for its employees and the object of contribution does not have any direct relation with the business of the company. In the given case contribution is to be made for the school which is exclusively for the benefit of the employees' children. Therefore, it cannot be considered as charitable contribution within the meaning of section 293(1)(e). It is purely a business decision and the Board of Directors of the company is empowered to take such a decision.

Political Contribution

Limit of political contribution

As per section 293A, an eligible company can make political contribution up to 5% of average net profit of immediately preceding three financial years, in a financial year.

In the given case, average net profit of the company during preceding three financial years is ₹40,00,000. The Board is empowered to make political contribution to the tune of ₹2,00,000 being 5% of the average net profit of preceding three years. Since the political contribution proposed is only ₹50,000, it is well within the powers of the Board to make this contribution.

Procedure

Every political contribution is required to be approved only in a Board meeting by way of a resolution and full disclosure of the name of political party and amount contributed shall be made in the profit and loss account.

Answer 4(c):

In this case applicability of section 297, 299, 300 and 314 needs to be examined.

Section 297 is not attracted because it is applicable in relation to contracts or agreements for sale or purchase of goods. When a person acts as an agent of another, as in the given case, there is no sale/purchase between them.

In accordance with section 299, Mr. Goodword will have to make disclosure of his interest in the Board meeting in which the proposed appointment is discussed and consequently provision of section 300 will also be applicable.

As far as section 314 is concerned, depending upon the detailed terms and conditions, sub-section (1B) may be applicable. If it is applicable, then appointment requires prior approval of members by special resolution. Otherwise, the appointment shall be made in a board meeting by a resolution subject to the approval of members in the next general meeting.

5. (a) 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 662/3% to 90%, while the shareholding of Akhlesh got reduced from the erstwhile 331/3% 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. [6]

(b) Some of the Indian citizens in U.K. joined to commence a business by incorporating a company in U.K. for the purpose of carrying on business there. Examine with reference to the relevant provisions of the Companies Act, 1956 whether it is a "Foreign Company".
What would be your answer in case the U.K. Company was incorporated by a company registered in India? [4]

(c) RBI receives a complaint that an authorized person has submitted incorrect statements and information to the RBI in respect of receipt and utilization of Foreign Exchange. Explain the powers of the RBI with regard to inspection of records of the above authorized person. Also state the duties of the authorized person. [5]

Answer 5(a):

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 5(b):

As per section 591, a company shall be a foreign company if:

(a) it is incorporated outside India; and

(b) it has established a place of business in India.

Thus, for deciding as to whether a company is a foreign company or not, the criterion is to see as to whether the company has established a place of business in India or not, and not the persons who have incorporated the company.

In this case, Indian citizens have formed a company outside India. Since, the company has not established any place of business in India, the company cannot be said to be a foreign company. The fact that Indian citizens have formed a company in a foreign country is immaterial in deciding whether the company is a foreign company or not.

The answer would have remained same even if the U.K. Company had been incorporated by a company registered in India for the same reason as stated above.

Answer 5(c):

RBI's powers of inspection [Sec. 12]: RBI may, at any time, cause an inspection to be made, by any of its officer specially authorized in writing in this behalf, of the business of any Authorised Person as may appear to it to be necessary or expedient for the purpose of:

(a) verifying the correctness of any statement, information or particulars furnished to the RBI,
(b) obtaining any information or particulars which such Authorised Person has failed to furnish on being called upon to do so,
(c) securing compliance with the provisions of this Act or Rules/Regulations/Direction/Order made thereunder.

Duties of Authorised Person:

(a) To produce to any Officer/Inspector, such books, accounts and other documents as may be specified, under the Act/Regulations.
(b) To furnish any information/statement/particulars required by RBI/Authorised Officers under the Act/Regulations.

6. (a) Discuss the powers and role of Audit Committee as per Clause 49 of the Listing agreement. [8]

(b) Sunflower Ltd. decided to terminate the services of Mr. Dinesh, who was employed as Sales Manager. However, the Company feels that the Sales Manager may not vacate the Company's flat at Mumbai. What action can be taken by the Company under the

Companies Act, to regain possession of the flat? Is it necessary to take such action under the Act before terminating the services of Mr. Dinesh? Will it make any difference, if the flat is not owned by the Company, but taken on lease? [7]

Answer 6(a):

As per clause 49 of the Listing Agreement,

Powers of Audit Committee:

The audit committee shall have powers, which should include the following:

1. To investigate any activity within its terms of reference.
2. To seek information from any employee.
3. To obtain outside legal or other professional advice.
4. To secure attendance of outsiders with relevant expertise, if it considers necessary.

Role of Audit Committee:

The role of the audit committee shall include the following:

1. Oversight of the company's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible.
2. Recommending to the Board, the appointment, re-appointment and, if required, the replacement or removal of the statutory auditor and the fixation of audit fees.
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 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 (2AA) of section 217 of the Companies Act, 1956
    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. Qualifications in the draft audit report.
5. Reviewing, with the management, the quarterly financial statements before submission to the board for approval

5A. 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.

6. Reviewing, with the management, performance of statutory and internal auditors, adequacy of the internal control systems.

7. 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.
8. Discussion with internal auditors any significant findings and follow up there on.
9. 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.
10. 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.
11. 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.
12. To review the functioning of the Whistle Blower mechanism, in case the same is existing.

12A. Approval of appointment of CFO (i.e., the whole-time Finance Director or any other person heading the finance function or discharging that function) after assessing the qualifications, experience & background, etc. of the candidate.

13. Carrying out any other function as is mentioned in the terms of reference of the Audit Committee.

Explanation (i): The term "related party transactions" shall have the same meaning as contained in the Accounting Standard 18, Related Party Transactions, issued by The Institute of Chartered Accountants of India.

Explanation (ii): If the company has set up an audit committee pursuant to provision of the Companies Act, the said audit committee shall have such additional functions / features as is contained in this clause.

Answer 6(b):

The given problem relates to sec. 630 of the Companies Act.
As per sec. 630, if any Officer or Employee of a Company:
(a) Wrongfully obtains possession of any property of a Company, or
(b) Having any such property in his possession, wrongfully withholds it or knowingly applies it to purposes other than those expressed or directed in the AoA and authorized by the Act.

On the complaint of the Company or any Creditor/Contributory, he shall be punishable with fine upto ₹10,000.

The court trying the offence may also order such Officer/Employee to deliver up or refund, within a specified time, any such property wrongfully obtained or wrongfully withheld or knowingly misapplied, or in default, to suffer imprisonment for a term upto 2 years. [Sec. 630(2)].

In the given case,

1. **Right of Company:** The Company or any Creditor/Contributory, can file a suit u/s 630 against the Sales Manager, if he refuses to vacate the premises provided by the Company. The Court trying the offence may also order such Officer/Employee to deliver up or refund, within a specified time, any such property wrongfully obtained or wrongfully withheld or knowingly misapplied, or in default, to suffer imprisonment for a term upto 2 years.
2. **Employees include Past Employees also:** In the above case, it is possible to initiate action even after termination of services of Mr. Dinesh.

The term "Officer or Employee" in section 630 applies to both the existing and past Officers or Employees if such Officers or Employees either: (a) wrongfully obtain possession of any property of the Company, or (b) having obtained such property during the course of employment, withhold the same after termination of employment. [Baldev Krishna Sahi Vs. Shipping Corporation of India Ltd. (SC)].

3. **Action permissible for Leasehold Property:** It is not necessary that the property in question should be owned by the company. Even if the Company exercises only a leasehold right, the provisions of Sec. 630 can be invoked. [P.V.George Vs. Jayems Engineering Co (P) Ltd.]

SECTION B

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

7. (a) "Corporate Social Responsibility is to be considered as an investment and not as a charity" – Elaborate the statement. [5]

(b) What is Whole Life-Cycle Costing Risk Management? Why does it fails to embrace WLCC? [5]

(c) What is Corporate Governance? What is the need for Corporate Governance in India? [5]

(d) Mention the core elements of CSR Policy as per the CSR Voluntary Guidelines 2009. [5]

(e) Write short notes on:
(i) Corporate Governance in USA
(ii) Corporate Governance in Japan [2.5*2=5]

(f) "The concept of Memorandum of Understanding (MoU) has been designed to provide flexibility and autonomy to CPSEs such that it facilitates them in pursuing the objectives and purposes, for which the enterprises have been set up."
In the light of the above statement, explain the concept of MoU in India. [5]

Answer 7(a):

The originally defined concept of CSR needs to be interpreted and dimensionalised in the broader conceptual framework of how the corporate embed their corporate values as a new strategic asset, to build a basis for trust and cooperation within the wider stakeholder community.

Though there have been evidences that record a paradigm shift from charity to a long-term strategy, yet the concept still is believed to be strongly linked to philanthropy. There is a need to bring about an attitudinal change in people about the concept.

By having more coherent and ethically driven discourses on CSR, it has to be understood that CSR is about how corporates place their business ethics and behaviors to balance business growth and commercial success with a positive change in the stakeholder community.

Several corporates today have specific departments to operationalise CSR. There are either foundations or trusts or a separate department within an organisation that looks into implementation of practices.

Being treated as a separate entity, there is always a flexibility and independence to carry out the tasks.

But often these entities work in isolation without creating a synergy with the other departments of the corporate. There is a need to understand that CSR is not only a pure management directive but it is something that is central to the company and has to be embedded in the core values and principles of the corporate.

Whatever corporates do within the purview of CSR has to be related to core business. It has to utilise things at which corporates are good; it has to be something that takes advantage of the core skills and competencies of the companies. It has to be a mandate of the entire organisation and its scope does not simply begin and end with one department in the organisation.

Charity means the act of donating money, goods, time or effort to support a charitable cause in regard to a defined objective. Charity can be equated with benevolence and charity for the poor and needy. It can be any selfless giving towards any kind of social need that is not served, underserved, or perceived as unserved or underserved. Charity can be by any individual or by a corporate.

Corporate Social Responsibility is about how a company aligns their values to social causes by including and collaborating with their investors, suppliers, employees, regulators and the society as a whole. The investment in CSR may be on people centric issues and/or planet issues. A CSR initiative of a corporate is not a selfless act of giving; companies derive long-term benefits from the CSR initiatives and it is this enlightened self interest which is driving the CSR initiatives in companies.

Answer 7(b):

Whole life-cycle costing (WLCC) is rapidly becoming the standard method for the long-term cost appraisal of buildings and civil infrastructure projects. With clients now demanding buildings that demonstrate value for money over the long term, WLCC has become an essential tool for those involved in the design, construction, operation and risk analysis of construction projects.

WLCC risk management is one of the important issues facing building assets executives today. As spending on building assets rises, asset owners become increasingly worried about WLCC optimisation throughout the life span of facilities; consequently, they become highly vulnerable to the risk of operational costs. Usually, when decision makers are faced with an investment choice under uncertain conditions, their main concern is to avoid projects whose actual economic outcome might be less favourable than what is acceptable, resulting in the risk of missing out on potential investment opportunities.

Thus, the objective of WLCC risk management should be to assist decision makers in evaluating whole life alternatives so that investment success is maximised. Usually traditional methods are used to optimise this process. However, traditional approaches to risk management have failed miserably because of their demand for mysterious statistical data that the end user does not have (Koller 1999). The key to successful WLCC risk-process and risk modelling is to build a WLCC framework that requires from the user nothing more than they presently can provide. This can be a challenge that can be addressed through the use of a variety of techniques. That is why it is important to use a combination of risk management techniques (depending on the stage of assessment) for risk assessment in WLCC, ranging from simple deterministic approaches to uncertainty assessment (e.g. sensitivity and break even analysis methods which are easy to use and understand and require no additional methods of computation beyond the ones used in LCC analysis), to very sophisticated methods based on probabilities, artificial intelligence (AI) and a hybrid of both techniques.

The reasons why it fails to embrace WLCC are:

- The lack of universal methods and standard formats for calculating whole life costs.

- The difficulty in integration of operating and maintenance strategies at the design phase.
- The scale of the data collection exercise, data inconsistency.
- The requirement for an independently maintained database on performance and cost of building components.

Answer 7(c):

Corporate governance is:

- The system by which companies are directed and controlled - **The Cadbury Report, 1992.**
- The process of supervision and control intended to ensure that the company's management acts in accordance with the interests of shareholders - **Parkinson, 1994.**
- 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.

- **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.
- **Enhanced Investor Trust:** Investors consider Corporate Governance as important as financial performance when evaluating companies for investment.
- **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.
- **Better Access to Global Market:** Good Corporate Governance systems attracts investment from global investors, which subsequently leads to greater efficiencies in the financial sector.
- **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.
- **Accountability:** Investor relations' is essential part of good Corporate Governance. Investors have directly/indirectly entrusted management of the company for creating enhanced value for their investment.
- **Easy Finance from Institutions:** Evidence indicates that well-governed companies receive higher market valuations.
- **Reduced Risk of Corporate Crisis and Scandals:** Effective Corporate Governance ensures efficient risk mitigation system in place.

Answer 7(d):

The CSR Policy should normally cover following core elements:

1. Care for all Stakeholders

The companies should respect the interests of, and be responsive towards all stakeholders, including shareholders, employees, customers, suppliers, project affected people, society at large etc. and create value for all of them. They should develop mechanism to actively

engage with all stakeholders, inform them of inherent risks and mitigate them where they occur.

2. Ethical functioning

Their governance systems should be underpinned by Ethics, Transparency and Accountability. They should not engage in business practices that are abusive, unfair, corrupt or anti-competitive.

3. Respect for Workers' Rights and Welfare

Companies should provide a workplace environment that is safe, hygienic and humane and which upholds the dignity of employees. They should provide all employees with access to training and development of necessary skills for career advancement, on an equal and non-discriminatory basis. They should uphold the freedom of association and the effective recognition of the right to collective bargaining of labour, have an effective grievance redressal system, should not employ child or forced labour and provide and maintain equality of opportunities without any discrimination on any grounds in recruitment and during employment.

4. Respect for Human Rights

Companies should respect human rights for all and avoid complicity with human rights abuses by them or by third party.

5. Respect for Environment

Companies should take measures to check and prevent pollution; recycle, manage and reduce waste, should manage natural resources in a sustainable manner and ensure optimal use of resources like land and water, should proactively respond to the challenges of climate change by adopting cleaner production methods, promoting efficient use of energy and environment friendly technologies.

6. Activities for Social and Inclusive Development

Depending upon their core competency and business interest, companies should undertake activities for economic and social development of communities and geographical areas, particularly in the vicinity of their operations. These could include: education, skill building for livelihood of people, health, cultural and social welfare etc., particularly targeting at disadvantaged sections of society.

Answer 7(e):

(i) CORPORATE GOVERNANCE IN USA

Corporate governance in the U.S. has changed dramatically since 1980. As a number of business and finance scholars have pointed out, the corporate governance structures in place before the 1980s gave the managers of large public U.S. corporations little reason to make shareholder interests their primary focus. Before 1980, corporate managements tended to think of themselves as representing not the shareholders, but rather "the corporation." In this view, the goal of the firm was not to maximize shareholder wealth, but to ensure the growth (or at least the stability) of the enterprise by "balancing" the claims of all important corporate "stakeholders"-- employees, suppliers, and local communities, as well as shareholders.

The external governance mechanisms available to dissatisfied shareholders were seldom used. Raiders and hostile takeovers were relatively uncommon. Proxy fights were rare and didn't have much chance of succeeding. And corporate boards tended to be cozy with and dominated by management, making board oversight weak.

Corporate Governance developments in USA:

- 1977 – The Foreign Corrupt Practices Act
- 1979 – US Securities Exchange Commission
- 1985 – Treadway Commission
- 1992 – COSO issued Internal Control – Integrated Framework
- 2002 – Sarbanes – Oxley Act
- The Dodd-Frank Wall Street Reform and Consumer Protection Act, 2010
- Updates to its U.S. Corporate Governance Policy (the "2013 Updates")

(ii) CORPORATE GOVERNANCE IN JAPAN

Japan's economy developed very rapidly during the second half of the twentieth century. Particularly during the period 1985-89, there was a 'bubble economy', characterized by a sharp increase in share prices and the value of land; the early 1990s saw the bubble burst as share prices fell and land was devalued, as well as shareholders and landowners finding themselves losing vast fortunes, banks found that they had severe problems too. The Japanese government wished to restore confidence in the Japanese economy and in the stock market, and to attract foreign direct investment to help regenerate growth in companies. Improved corporate governance was seen as a very necessary step in this process.
Japan's Corporate Governance System is often likened to that of Germany because banks can play an influential role in companies in both countries. However, there are fundamental differences between the systems, driven partly by culture and partly by the Japanese shareholding structure with the influence of the keiretsu (broadly, associations of companies). Charkham (1994) sums up three main concepts that affect Japanese attitudes towards Corporate Governance: obligation, family, and consensus.

The Japan Corporate Governance Committee published its revised Corporate Governance Code in 2001. The code had six chapters, which contained a total of 14 principles.

Summary of key characteristics influencing Japanese Corporate Governance

Feature	**Key characteristic**
Main business form	Public limited company
Predominant ownership structure	*Keiretsu;* but institutional investor ownership is increasing
Legal system	Civil Law
Board structure	Dual
Important aspect	Influence of *keiretsu*

In 2004, the Tokyo Stock Exchange issued the *Principles of Corporate Governance for Listed Companies.* Charkham (2005) discusses the various changes that have taken place in the context of Corporate Governance in Japan and states:

The important part the banks played has greatly diminished. In its place there are now better structured boards, more effective company auditors, and occasionally more active shareholders, an increase of interest, and, where appropriate, action on their part, might restore the balance that the banks' withdrawal from the scene has impaired.

In 2008, the Asian Corporate Governance Association (ACGA) published its 'White Paper on Corporate Governance in Japan'. It states, while a number of leading companies in Japan have made strides in corporate governance in recent years, we submit that the system of governance in most listed companies is not meeting the needs of stakeholders or the nation at large in three ways:

- By not providing for adequate supervision of corporate strategy;
- By protecting management from the discipline of the market, thus rendering the development of a healthy and efficient market in corporate control all but impossible;
- By failing to provide the returns that are vitally necessary to protect Japan's social safety net- its pension system.

It then advocates six areas for improvement: shareholders acting as owners; utilizing capital efficiently; independent supervision of management; pre-emption rights; poison pills and takeover defences; shareholder meetings and voting.

Answer 7(f):

The Memorandum of Understanding (MoU) System in India was introduced in the year 1986, after the recommendations of the Arjun Sengupta Committee Report (1984). Twenty six years after its inception, the MoU system has evolved and is being strengthened, through regular reviews, to become a management tool that helps in performance evaluation as well as performance enhancement of CPSEs in the country.

The concept of Memorandum of Understanding (MoU) has been designed to provide flexibility and autonomy to Central Public Sector Enterprises (CPSEs) such that it facilitates them in pursuing the objectives and purposes, for which the enterprises have been set up. Accountability has to be understood in a wider sense by associating it with answerability for the performance of the tasks and the achievement of targets negotiated mutually between the Government and the CPSE. The rationale for MoU could be derived from principal/agent theory. The principal (administrative ministry on behalf of real owners - the people) can only observe outcomes and cannot measure accurately the efforts expended by the agent (CPSE managers). Also the Principal can only, to a limited extent, distinguish the effects of influences from other factors, which affect the performance. Therefore extensive intervention by administrators, who might not be too knowledgeable about the nature of problems confronting the enterprises, not only impacts productivity and profitability but also makes it impossible to fix accountability for non-achievement of targets.

A negotiated incentive contract (MoU), hence, is viewed as a device to reveal information and motivate managers to exert effort. Notwithstanding the spectacular performance of CPSEs in several areas, there has been a sense of disillusionment with some aspects of CPSE performance such as low profitability and lack of competitiveness. The extensive regulation of CPSEs by government had stifled the initiative and growth of public sector. The Economic Administration Reforms Commission (Chairman: L. K. Jha) had dwelt on issue of autonomy and accountability. The Commission had recommended a careful re-consideration of extant concepts and instrumentalities relating to the accountability of public enterprises with a view to ensuring (a) that they do not erode the autonomy of public enterprises and thus hampers the very objectives and purposes for which these enterprises have been set up and given corporate shape and for which they are to be accountable; and (b) accountability has to be secured in the wider sense of answerability for the performance of tasks and achievements of results. The adoption of MoU system in India could be seen as an attempt to operationalize this very vital recommendation.

In the backdrop of the dynamic external environment, "world- wide competition" and globalization, it is critical that the MoU system is strengthened such that it facilitates the CPSEs in becoming economically viable through efficient management and control. Hence, the MoU system aims at offering autonomy to CPSEs and is designed such that it can aid in the assessment of the extent to which mutually agreed objectives (Mandal, 2012) are achieved. This section of the report traces the evolution of the MoU system through various committee reports and highlights the major observations, along with the actions taken thereafter. This would act as

an indicator of the developments that have happened in the MoU system in India and, through the study of extant literature, would also highlight the areas of concern raised after each study.

The various committees formed over the years are:

1. Arjun Sengupta Committee Report (1984)
2. National Council of Applied Economic Research (2004)
3. Report of the Working Group (2008)
4. S.K. Roongta Committee Report (2011)
5. Mankad Committee and Task Force (2012)